

BULLETIN OF THE UNIVERSITY OF KANSAS

Vol. XVII

December 1, 1916

No. 18

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Published semi-monthly from January to June and monthly from July to  
December, inclusive, by the University of Kansas

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## HUMANISTIC STUDIES

Vol. II, No. 2

### THE LAND CREDIT PROBLEM

BY

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*Associate Professor of Economics and Commerce  
The University of Kansas*

LAWRENCE, DECEMBER, 1916

Entered as second-class matter December 29, 1910, at the postoffice at  
Lawrence, Kansas, under the act of July 16, 1894.

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*The Land Credit Problem*, by George E. Putnam  
Seventy-five Cents

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## PREFACE

So much has been said and written about the rural credit problem during the past four years, and so little about the specific problems of rural credit, that a great deal of confusion has arisen. With a view to clarifying this discussion so far as the land credit problem is concerned, the present study was undertaken—although not without some hesitancy. Most of the writer's conclusions on the subject have already been summarized in other publications; moreover, the recent findings of the federal Department of Agriculture with regard to land credit in the United States, and the reports of the various commissions appointed to investigate agricultural credit in foreign countries, have been given widespread publicity in government publications. It is hoped, nevertheless, that the organization and method of the present study will have the merit of contributing in some measure to a better understanding of the land credit problem.

The writer wishes to acknowledge his gratitude to the editors of the *American Economic Review* and the *Political Science Quarterly* for their cooperation in allowing him to reprint portions of articles previously published in those journals. Chapter VI is virtually the counterpart of an article prepared for the December issue of the *American Economic Review*, 1916.

GEORGE E. PUTNAM.

The University of Kansas,  
December, 1916.

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# The Land Credit Problem

## CHAPTER I

### INTRODUCTION

Fortunately, the history of the United States is not, like that of some countries, the history of a peasantry struggling for land. In the early agricultural organization of this country the land problem was non-existent. There was not, as in Europe, any feudal system to be broken, concentration in land ownership to foster rural discontent, nor landlord and tenant relations to be adjusted. From the very beginning the supply of unoccupied land was abundant, and it was possible for the man of small means to become his own master, the owner of 160 acres of land, with scarcely any financial assistance.

This free and easy path to land ownership and economic independence was due to the establishment of the public-land system. Shortly after the close of the Revolution, the several states ceded the greater portion of their unsold lands to the federal government, which then began to devise plans for their sale and settlement. At first, the policy adopted by the central government for the disposition of the public lands was actuated by financial considerations. To the West was a boundless stretch of unoccupied territory which was regarded as "an asset to be cashed at once for payment of current expenses of Government and extinguishment of the national debt".<sup>1</sup> Accordingly, land was sold in large tracts at a comparatively low price per acre. From 1785 to 1796 the minimum price was \$1 per acre;<sup>2</sup> from 1796 to 1820, \$2 per acre;<sup>3</sup> and in the latter year the price was reduced to \$1.25 per

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1. Donaldson: *The Public Domain*, p. 196.

2. *Ibid.*, p. 197.

3. *Ibid.*, p. 205.

acre.<sup>4</sup> Irrespective of the motive which first prompted the government to dispose of the public land in this manner, the ownership of land was, at these prices, well within the reach of the young man seeking economic independence.

In the meantime the public-land policy was undergoing a significant change. The plan, fathered by Alexander Hamilton, of disposing of the public land for the sake of the revenue it would yield to the federal government was gradually giving way to a policy which regarded the rapid settlement of the western territory as a factor in national development. From 1801 to 1841 there was developed in sixteen special acts the preëmption system, which gave preference to actual settlers in the sale of land. Under this system a settler was allowed to enter upon a tract of land before it had been offered at public sale. After he had lived upon the tract for a limited period and had improved and cultivated a portion of his holdings, he could acquire a title to the land on payment of \$1.25 per acre.<sup>5</sup>

The climax of the policy of favoring the actual settler was reached with the passage of the Homestead Act in 1862. The law was the result of ten years of agitation for free land. In 1852 the Free Soil Democrats, assembled in National Convention, had resolved "that the public lands of the United States belong to the people, and should not be sold to individuals, nor granted to corporations, but should be held as a sacred trust for the benefit of the people, and should be granted in limited quantities, free of cost, to landless settlers".<sup>6</sup>

Moreover, "the rich and fertile lands of the Mississippi Valley were fast filling up with settlers. Agricultural lands in the Middle States, which, after the year 1824, were bought for \$1.25 per acre, now sold at from \$50 to \$80 per acre. Former purchasers of these Government lands in the Middle, Western, and Southern States were selling their early purchases for this great advance, and moving west, to Iowa, Wisconsin, Minnesota, and Missouri, and there again taking cheap Government lands under the preëmption laws.

"The western emigration caused a rush—a migration of neigh-

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4. *Ibid.*, p. 206.

5. *Ibid.*, p. 214.

6. *Ibid.*, p. 332.

borhoods in many localities of the older Western States. Following the sun, their pillar of fire, these State founders moved westward, a resistless army of agents of American civilization, and there was a demand for homes on the public lands, and a strong pressure for the enactment of a law which should confine locators to small tracts, and require actual occupation, improvement, and cultivation."<sup>7</sup>

The Homestead Act and its amendments marked the third important step in the disposition of the vast public domain. For a nominal fee it gave to "a settler—a man or woman over the age of twenty-one, a citizen of the United States or having declared an intention of becoming such—the right to locate upon 160 acres of unoccupied public land in any of the public-land States and Territories subject to entry at a United States land office, to live upon the same for a period of five years, and upon proof of a compliance with the law, to receive a patent therefor free of cost or charge for the land".<sup>8</sup>

The effect of this generous treatment accorded to the farmer by the federal government was far-reaching in its significance. In the first place, it meant that the farmer was independent of the financial institutions not only in the matter of acquiring a farm but also in its improvement and cultivation. Few improvements, in fact, were needed. With the early settlers, about the only improvement which called for immediate attention was the clearing of a portion of the land and the construction of a shelter. Once a small space had been cleared of trees and forest growth, the work of cultivation was comparatively simple because of the natural fertility of the soil. While nature was thus engaged in the growing of crops the farmer was able to devote his time to the complete conquest of the forest. And later, when the tide of westward expansion had reached the western slope of the Mississippi Valley, the settler was even relieved of the preliminary task of clearing his farm. Here were farms already made, with virgin soil that responded bountifully and immediately to careless and extensive methods of cultivation. Under these conditions, which prevailed generally throughout the Middle West, the business

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7. *Ibid.*, pp. 332-333.

8. *Ibid.*, p. 350.

of farming was practically independent of the commercial banking system.

In the second place, the public-land policy was instrumental in producing a type of American farmer totally different in mode of living and economic status from the agricultural workers of Europe. His life was that of a pioneer, spent in comparative isolation. He seldom saw his neighbors, if he had any, but strangers were always welcome. In his reckoning of character, present worth counted for most, antecedents for least. Moreover, with his Bible and his ax he was well-nigh self-sufficient. He paid no rent to an absentee landlord nor looked to charity when overtaken by misfortune. He was essentially a home builder and a home owner, a farmer rather than a proletarian, who enjoyed the full product of his own labor. "Such men", wrote Jefferson, "are the true representatives of the great American interest, and are alone to be relied on for expressing the proper American sentiments".<sup>9</sup>

No less marked in significance was the effect which the land supply had upon the welfare of the laboring classes. On the farm the labor problem was acute. Few there were who cared to work in the hire of another when it was possible for one to become his own master on his own land. Likewise, the frontier offered a life of independence to those who found the conditions of employment in the factory and workshop unpromising or intolerable. To have been born in the ranks of a wage-earning class was no severe handicap. One could easily rise above the status of "low birth". Laborers had an alternative of economic independence by virtue of which employers were constrained to recognize efficiency as it appeared and to grant an early preferment to those worthy of further employment. Being conscious of their ability to rise, however humble in origin, they had ambition and incentive which in turn reacted favorably upon their productive powers and the scale of labor remuneration.

It is little wonder, therefore, that the passion for freedom and democracy has long been regarded as one of the chief characteristics of the American people. At a very early date the spirit of equality became the rule, not because it was decreed that "all men were created equal", but because the conditions under which men made their living were conducive to the development of that

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9. *Works* (Washington ed.); Vol. IV, p. 197.

spirit. Land was the predominant form of wealth and it was abundant; all were free to become landowners; and while there was undoubtedly a certain inequality in material possessions, there was, nevertheless, an approximate equality in opportunity.

Finally, the large supply of free and fertile land determined in advance the character of agricultural methods. The scarcity of labor and the abundance of land gave rise to methods of tillage which conserved the former and wasted the latter. If the farmer realized a surplus from his farming operations, it was more profitable to invest his funds in additional land and await the natural increase in value than to attempt to increase the productivity of the land he already possessed. Or, if he had gotten all from the land that its fertility would yield, he might abandon his exhausted farm and migrate to newer and fresher territory. Even the immigrants who came from Northern and Western Europe to settle upon the public lands soon abandoned the use of intensive methods, to which they had been accustomed, for the more profitable "cut and cover" methods employed by the American farmer. Thus a premium was placed on waste and soil depletion. The course most profitable to the farmer was the one most wasteful to society. Most unfortunate of all was the fact that farmers were being schooled generation after generation under a demoralizing system, the effects of which still linger.

But whatever may be said as to the merits or demerits of the public-land system, it gave a great impetus to agricultural settlement. Within a century after the time of its inception there remained only a small area of public land available for cultivation. The disposition of the public domain from its origin to June 30, 1880, is estimated by Donaldson at 547,754,483 acres.<sup>10</sup> According to the annual reports of the General Land Office, 578,283,140 acres were disposed of between 1880 and 1915. On July 1, 1915, there were 279,544,494 acres of public land in the United States unappropriated and unreserved<sup>11</sup>—less than one-seventh of the total land area. Most of the land still open for settlement is to be found in Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, and Wyoming.

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10. *The Public Domain*, p. 22.

11. *Report of the Commissioner of the General Land Office*, 1915, p. 120.

The importance of free land in the settlement of the public domain is shown in the following table:<sup>12</sup>

FINAL HOMESTEAD ENTRIES FROM THE PASSAGE OF  
THE HOMESTEAD ACT TO JUNE 30, 1915

Fiscal Year Ended June 30	Number	Acres
1868.....	2,772	355,086.04
1869.....	3,965	504,301.97
1870.....	4,041	519,727.84
1871.....	5,087	629,162.25
1872.....	5,917	707,409.83
1873.....	10,311	1,224,890.93
1874.....	14,129	1,585,781.56
1875.....	18,293	2,068,537.74
1876.....	22,530	2,590,552.81
1877.....	19,900	2,407,828.19
1878.....	22,460	2,662,980.82
1879.....	17,391	2,070,842.39
1880.....	15,441	1,938,234.89
1881.....	15,077	1,928,204.76
1882.....	17,174	2,219,453.80
1883.....	18,998	2,504,414.51
1884.....	21,843	2,945,574.72
1885.....	22,066	3,032,679.11
1886.....	19,356	2,663,531.83
1887.....	19,866	2,749,037.48
1888.....	22,413	3,175,400.64
1889.....	25,549	3,681,708.80
1890.....	28,080	4,060,592.77
1891.....	27,686	3,954,587.77
1892.....	22,822	3,259,897.07
1893.....	24,204	3,477,231.63
1894.....	20,544	2,929,947.41
1895.....	20,922	2,980,809.30
1896.....	20,099	2,790,242.55
1897.....	20,115	2,778,404.20
1898.....	22,281	3,095,017.75
1899.....	22,812	3,134,140.44
1900.....	25,286	3,477,842.71
1901.....	37,568	5,241,120.76
1902.....	31,627	4,342,747.70
1903.....	26,373	3,576,964.14
1904.....	23,932	3,232,716.75
1905.....	24,621	3,419,387.15
1906.....	25,546	3,526,748.58
1907.....	26,485	3,740,567.71
1908.....	29,636	4,242,710.59
1909.....	25,510	3,699,466.79
1910.....	23,253	3,795,862.89
1911.....	25,908	4,620,197.12
1912.....	24,326	4,306,068.52
1913.....	53,252	10,009,285.16
1914.....	48,724	9,291,121.46
1915.....	37,343	7,180,981.62
Total.....	1,063,534	154,327,812.45

Although the free distribution of land has continued steadily down to the present time, final entries had been made on the best lands of the Mississippi Valley during the years before 1890. Thereafter settlers were obliged to enter upon lands greatly inferior in quality or to await the opening of Indian reservations to white

12. *Ibid.*, p. 67.

settlers. In recent years the opening of these reservations has been the big factor in the settlement of the public lands. Since the close of the last century, vast areas have been made available to settlers in Oklahoma, Florida, North Dakota, Wyoming, Montana, New Mexico, and the Pacific Coast States. And in nearly every instance where reserved land has been opened for settlement, the number of applicants registered for homesteads has far exceeded the number of farms available for distribution. This fact suggests that the free and easy path to land ownership was practically closed by 1890, when the best land had been taken up.

The practical exhaustion of the supply of free land in 1890 marked the beginning of a new era in the economic history of the United States of no less significance than the establishment of the public-land system itself. The change became apparent just before the close of the century, following a long period of maladjustment. The rapid settlement of the fertile lands of the Mississippi Valley and the subsequent increase in the volume of farm products caused, after 1873, a gradual decline in the prices of agricultural products. Farmers who were seeking to acquire a title to land under the homestead or preëmption laws cultivated their farms in order to conform to the requirements of the law. Moreover, in the cultivation of their land they made extensive use of farm machinery in order to secure, at the same time, the largest possible reward for their labor. Under these conditions, low prices obtained for agricultural products and agricultural discontent became general. For the time being agriculture had outgrown its proper relation to industry. It had evolved from a self-sufficient to a commercial undertaking which was proving altogether unprofitable.

By 1896, however, prices had reached their lowest ebb and, with the return of business prosperity, began a rapid upward bound which has steadily continued. The general increase in the prices of various farm products during the last twenty years is shown in the following table:<sup>13</sup>

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13. The farm prices of December 1 for each year, as reported by the *Yearbook of the Department of Agriculture*, 1915, pp. 412-463, are averaged by five-year periods.

	1896-1900	1901-1905	1906-1910	1911-1915
Corn, per bushel.....	\$0.28	\$0.46	\$0.52	\$0.60
Wheat, per bushel.....	.66	.72	.86	.89
Oats, per bushel.....	.23	.33	.39	.42
Barley, per bushel.....	.38	.44	.55	.59
Potatoes, per bushel.....	.41	.58	.59	.62
Hay, per ton.....	7.06	9.07	10.73	12.06

No sooner had the rise in the prices of farm products been generally felt than the value of land, which before 1900 had been subject to fluctuation and uncertainty, began rapidly to rise. In 1900 the average value of land per acre exclusive of buildings was \$15.57; by 1910 it had risen to \$32.40.<sup>14</sup> In many of the newer states west of the Mississippi, the price of land more than trebled. Apparently there had come over investors a full realization of the fact that the supply of unoccupied land which could be brought under cultivation was practically exhausted, and that a further rise in agricultural prices was imminently certain. These considerations, coupled with the realization that the rate of interest was gradually falling, led investors to offer exorbitant prices for farms—prices that were, in the vast majority of cases, out of all proportion to the then productive capacity of land. What they failed to realize on their investments in the present they expected to recover with interest in the future. The mere prospect of securing an unearned increment had a cumulative effect on land values.

But while the general rise in the value of farm land was filling the coffers of the landowning classes, it was having an adverse effect on the economic status of the landless man. No longer could the man of small means who aspired to a position of economic independence rely upon the generosity of the federal government. On the contrary, he must needs serve a long period of apprenticeship either as a tenant or laborer before he could acquire sufficient means to purchase a farm of his own. In some of the older agricultural states, where, on account of a certain immobility on the part of farmers, the status of tenancy was deemed preferable to the isolation and hardships of frontier life, an increase in the percentage of tenancy had already begun. In 1880, 25.6 per cent of all the farmers in the United States were tenants. In spite of the fact that home seekers were continually appropriating new farms

14. *Thirteenth Census of the United States*; Vol. V, p. 28.

on the public domain, the percentage of tenancy had risen to 37 by 1910.<sup>15</sup> Manifestly, the status of the home seeker had been altered. The rise in the value of land had, in many cases, rendered ownership by the actual cultivator unprofitable if not altogether impossible. It had destroyed that approximate equality of opportunity which obtained when land was free. In short, a problem of land tenure was gradually developing.

Nor has the welfare of the laboring classes been unaffected. While it is true that the rise in the general level of food prices has been accompanied by a rise in the level of money wages, the latter has not kept pace with the former. In other words, real wages have fallen. There seems to be abundant evidence of a substantial decline. According to a recent computation made by Rubinow, the index of real wages per week rose from 99.4 in 1890, to 104.7 in 1896; but thereafter a decline set in, reaching the low figure of 85.3 in 1912.<sup>16</sup> It is his conclusion that "the American wage-worker, notwithstanding his strenuous efforts to adjust wages to these new price conditions, notwithstanding all his strikes, boycotts, and riots, notwithstanding all the picturesque I. W. W.-ism, new unionism, and the modish sabotage, has been losing surely and not even slowly, so that the sum total of economic progress of this country for the last quarter of a century appears to be a loss of from 10 to 15 per cent in his earning power".<sup>17</sup>

Various explanations might be offered to account for the material decline in real wages, but among these explanations a more prominent place than most writers have conceded should be given to the fact that the land supply, which had always been able to absorb a large share of the labor surplus, was beginning to wane in importance. Moreover, the character of the immigrant population was changing. The earlier immigrants had come from Northern and Western Europe for the purpose of acquiring farm homes; now they were coming from Southern and Eastern Europe expecting to enter the ranks of industrial workers. The effect of their numbers was to augment the labor surplus, overstock the labor market, and weaken the bargaining power of the American laborer.

In the first place, then, the period of rising prices after 1896, itself the product of many factors, called for the strengthening of

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15. *Thirteenth Census of the United States*; Vol. V, p. 102.  
16. *American Economic Review*; Vol. IV, Dec., 1914, p. 811.  
17. *Ibid.*, p. 813.

the laborer's bargaining power if the level of real wages was to be maintained. But the laborer was unable to maintain an even ratio between his bargaining power and his increasing productive capacity, because on account of the rise in the value of land the alternative which he formerly enjoyed of becoming an independent landowner no longer existed. It seems reasonable, therefore, to conclude that if the supply of farm land had remained cheap and plentiful, it would have absorbed a large portion of the labor surplus and those who chose to remain in the field of industry could have secured a larger share of their product.

Of equal significance is the effect which higher land values have had and promise to have upon the character of agricultural methods. The old extensive and soil-depleting system of cultivation has at last become relatively unprofitable. Land must be conserved and its productivity increased if a large product per man is to be obtained. While the time has not yet arrived when the farmer should attempt to "make two blades of grass grow where one grew before", the continued rise in the price of land and farm products will necessitate a complete readjustment of the proportion in which land, labor, and capital are now employed.

Already there is an urgent need for readjustment, but the need is not fully appreciated by most farmers. As a class they are slow to adapt themselves to changing conditions. Having been reared under the old school of waste and independent action they are loath to adopt new methods which would increase the product per acre without lowering the product per man. It is too often the case that farmers lag behind with their farming, content in the knowledge that they have made money in land whether they have grown crops or not. Where this attitude is prevalent and persistent little immediate progress can be expected, and the problem of better farming must be left to the younger generation of farmers.

Nevertheless, some progress has been made during the last fifteen years. Unfortunately, the census of 1890 grouped the value of land and buildings together. In 1900 and 1910, however, the value of buildings was listed separately and a comparison shows an increase per farm of 62.3 per cent.<sup>18</sup> During the same decade the value of implements and machinery per farm increased 65.8 per

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18. *Thirteenth Census of the United States*; Vol. V, p. 28.

cent;<sup>19</sup> while the total amount expended by the American farmer for fertilizer and labor increased 115<sup>20</sup> and 82.3<sup>21</sup> per cent respectively. The increase in the value of these items shows some appreciation on the part of farmers of the imperative need for improved methods—better housing for better stock, the prevention of soil depletion, better equipment and machinery, and more intensive cultivation. Yet with all these expenditures there is no evidence to show that the product per acre has increased in the slightest degree. The present agricultural stage is one of transition, and until the farmer has paid in full the price of his reckless schooling the returns from his capital expenditures will be represented only in the maintenance of the productive capacity of his farm. What prosperity he now enjoys is due entirely to the high level of prices.

As a final effect of the rise in the value of land and the growing demands of agricultural progress, the farmer has been obliged to depend more and more upon his marketing ability and his borrowing power. With the disappearance of the American frontier, the backwoods occupation of farming has at last become a business. As such, it requires a knowledge of three distinct kinds of business practice, *i. e.*, production, marketing, and finance. Although it would be difficult to estimate which one of these departments of farming is most important, leaders in agricultural education have, until recently, been wont to emphasize only the need of reform in the business of growing crops. The advancement of other departments of the business has been generally neglected. As a result of this neglect, the system under which the farmer sells his products and borrows his capital has become uneconomical, ill-adapted, and obsolete.

It is about the problem of agricultural finance that chief interest now centers. In discussing the nature of this problem, the fact should be borne in mind that the capital requirements of farmers are supplied by two forms of loans—the long-term and the short-term. The long-term loan is used in aiding to pay the purchase price of land, in making permanent improvements, and in providing those forms of productive equipment which are too expensive to be met out of the earnings of two successive years. As

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19. *Ibid.*, Vol. V, p. 28.

20. *Ibid.*, Vol. V, p. 561.

21. *Ibid.*, Vol. V, p. 560.

security for such loans, the farmer gives a mortgage on his land.

Just as the long-term or land-mortgage loan is needed for the purchase and improvement of the farm, so the short-term or personal loan is necessary in the growing of crops. From the time the ground is prepared and the seed planted until the crop is harvested a period of six or nine months may have elapsed. In the meantime the farmer's income is small and his expenses heavy. He is obliged to make continual advances for the payment of wages and for the purchase of productive equipment and supplies. Funds are required not only to grow the crops but also to tide him over until his products have been sold. The lender's security for the short-term loan may be in the form of a chattel mortgage or it may consist solely of the farmer's personal integrity.

In the following chapters, attention will be given to only one phase of the farmer's credit problem, *i. e.*, the problem of long-term or land-mortgage credit; not because the problem of personal credit is unimportant but because the two problems are absolutely distinct. The lines of procedure to be followed in dealing with one are totally ill-adapted to deal with the other. Furthermore, it is the writer's firm conviction that much of the land credit legislation already in force is of doubtful character and, for reasons which will subsequently appear, that the solution of the farmer's land credit problem is for the present of far more pressing importance.

## CHAPTER II

### LAND MORTGAGE CREDIT IN THE UNITED STATES

The census of 1890, the first to make any definite inquiry into the extent of farm mortgage indebtedness in the United States, reported a total mortgage debt of \$1,085,995,960<sup>22</sup> on farms operated by their owners and on farms whose owners rented additional land. These figures include an estimate of the mortgage debt on those farms from which incomplete reports were obtained. No attempt was made to ascertain the amount of mortgage debt on farms operated by tenants or hired managers for the obvious reason that these operators are not likely to have accurate information as to whether the farms which they operate are mortgaged, and still less as to the amount of mortgage debt.

Unfortunately, the data secured by the census of 1900 are of little comparative value as they relate only to the number of farm homes mortgaged. But in 1910 the census enumerators again attempted to ascertain the extent of farm mortgage indebtedness, reporting a total of \$1,726,172,851.<sup>23</sup> This amount, however, does not include an estimate of the indebtedness on farms from which incomplete reports were obtained, nor does it include the indebtedness on farms whose owners rented additional land. Of these farms there is a considerable number. The figures for 1890 and 1910 are not, therefore, strictly comparable, but they show conclusively the existence of a growing demand for land credit.

Many have viewed with alarm the growth in the number of mortgaged farms, believing it to be an unmistakable sign of agricultural adversity. But this attitude is not well founded. Although farms are frequently mortgaged on account of poor crops, mismanagement, or unavoidable misfortune, such indebtedness more often represents an unpaid portion of the cost of the farm, expenditures for additional land, buildings, and other permanent improvements. Notwithstanding the increase in the number of

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22. *Thirteenth Census of the United States*; Vol. V, p. 162.

23. *Ibid.*, Vol. V, p. 162.

mortgaged farms from 1890 to 1910, the ratio of the farmer's debt to the value of his land actually declined. While the average amount of mortgage indebtedness per farm increased from \$1,224 in 1890 to \$1,715 in 1910, the owner's equity per farm increased from \$2,220 to \$4,574, or more than doubled. It can scarcely be maintained that farmers as a class were less prosperous in 1910 than in 1890. On the contrary, there is plenty of evidence to show that the most prosperous and progressive agriculture obtains in those states where the mortgage indebtedness is the greatest. In the South, where the percentage of farms free from mortgage debt has been unusually large, agriculture has developed only as the percentage of mortgaged farms increased.

Perhaps the most satisfactory estimate of the extent of mortgage indebtedness in the United States is the one recently made by members of the Department of Agriculture. On the basis of the Thirteenth Census figures, supplemented by actual field study, they have estimated the total mortgage debt on all farms, whether operated by owners, managers, or tenants, to be \$3,598,985,000.<sup>24</sup> In the distribution of this debt among the several states, the proportion is much the same as that reported by the Thirteenth Census. Iowa has the largest farm mortgage debt of any state. It is followed by Illinois, Missouri, Wisconsin, Texas, and Kansas. Of the total mortgage indebtedness for the whole country, 64 per cent is found in the North Central States alone.

The table<sup>25</sup> on page 21, prepared by the Department of Agriculture, shows by states the estimated total farm mortgage debt and the extent to which farm mortgages are held by life insurance companies and banks.

At present, life insurance companies are one of the most important sources of land credit. The data on page 21 show that two hundred and twenty companies with assets representing more than 99 per cent of the total assets of all life companies in the United States had, in October, 1915, when their reports were tabulated, \$695,536,000 invested in farm mortgages. Among these companies, the Northwestern Mutual of Milwaukee is the heaviest single lender on mortgage security. On December 31, 1915, it had outstanding farm mortgage loans to the amount of

24. Tabular statement of O. W. Thompson, *Hearings before the Subcommittee of the Joint Committee on Rural Credits*, 64 Cong., 1 Sess., p. 107.

25. *Ibid.*, p. 107.

QUANTITATIVE DATA RELATIVE TO FARM MORTGAGE LOANS  
(Figures for amounts represent thousands of dollars)

Geographic division: and State	Estimated total farm mortgage debt*	Farm mortgages held by life insur- ance companies**		Farm mortgages held by banks†	
		Amount	Per cent of esti- mated total	Amount	Per cent of esti- mated total
United States.....	3,598,985	695,536	19.3	739,500	20.6
Geographic divisions:					
New England:					
Maine.....	80,544	1,702	2.1	84,900	105.4
Middle Atlantic.....	313,156	556	.2	30,900	9.9
East North Central.....	944,436	121,075	12.8	220,000	23.3
West North Central.....	1,375,903	426,960	31.0	216,400	15.7
South Atlantic.....	153,155	22,930	15.0	40,800	26.6
East South Central.....	127,135	22,871	18.0	33,600	26.4
West South Central.....	299,614	72,685	24.3	27,900	9.3
Mountain.....	101,285	12,532	12.4	19,800	19.5
Pacific.....	203,757	14,225	7.0	65,200	32.0
New England:					
Maine.....	13,727	15	.1	6,000	43.7
New Hampshire.....	6,100			12,500	204.9
Vermont.....	17,113	13	.1	46,700	272.9
Massachusetts.....	24,077	9	††	8,700	36.2
Rhode Island.....	2,514			6,000	238.7
Connecticut.....	17,013	1,665	9.8	5,000	29.4
Middle Atlantic:					
New York.....	168,234	128	.1	18,200	10.8
New Jersey.....	35,610	222	.6	2,600	7.3
Pennsylvania.....	109,312	206	.2	10,100	9.2
East North Central:					
Ohio.....	130,678	17,073	13.1	26,200	20.1
Indiana.....	132,325	48,789	36.9	52,000	39.3
Illinois.....	355,802	51,046	14.3	56,200	15.8
Michigan.....	118,950	1,706	1.4	44,900	37.8
Wisconsin.....	206,681	2,461	1.2	40,700	19.7
West North Central:					
Minnesota.....	145,181	35,577	24.5	43,600	30.0
Iowa.....	469,063	150,150	32.0	104,800	22.3
Missouri.....	223,107	59,699	26.8	34,900	15.6
North Dakota.....	100,364	19,423	19.4	5,000	5.0
South Dakota.....	92,467	31,024	33.6	6,200	6.7
Nebraska.....	165,015	66,614	40.4	10,400	6.3
Kansas.....	180,706	64,473	35.7	11,500	6.4
South Atlantic:					
Delaware.....	6,857	46	.7	1,600	23.3
Maryland.....	32,393	492	1.5	6,000	18.5
Virginia.....	25,007	670	2.7	5,000	20.0
West Virginia.....	8,725	23	.3	1,700	19.5
North Carolina.....	21,005	2,267	10.8	6,900	32.9
South Carolina.....	24,967	3,894	15.6	9,000	36.1
Georgia.....	29,711	15,479	52.1	8,000	26.9
Florida.....	4,490	69	1.5	2,600	57.9
East South Central:					
Kentucky.....	41,305	7,170	17.4	13,300	32.2
Tennessee.....	25,468	10,674	41.9	4,000	15.7
Alabama.....	25,943	1,771	6.8	3,700	14.3
Mississippi.....	34,419	3,256	9.5	12,600	36.6
West South Central:					
Arkansas.....	21,023	4,259	20.3	5,700	27.1
Louisiana.....	21,141	1,500	7.1	9,000	42.6
Oklahoma.....	73,129	29,065	39.7	2,100	2.9
Texas.....	184,321	37,861	20.5	11,100	6.0
Mountain:					
Montana.....	17,111	3,518	20.6	5,200	30.4
Idaho.....	21,566	2,948	13.7	2,200	10.2
Wyoming.....	7,148	487	6.8	1,200	16.8
Colorado.....	36,767	3,135	8.5	2,100	5.7
New Mexico.....	4,585	1,191	26.0	400	8.7
Arizona.....	4,161	376	9.0	1,600	38.5
Utah.....	6,818	862	12.6	6,000	88.0
Nevada.....	3,129	15	.5	1,100	35.2
Pacific:					
Washington.....	43,470	3,087	7.1	5,000	11.5
Oregon.....	35,535	1,091	3.1	4,100	11.5
California.....	124,752	10,047	8.1	56,100	45.0

\* Estimates based on Thirteenth Census figures.

\*\* Figures actually reported by 220 companies, with assets representing more than 99 per cent of the total admitted assets of all life insurance companies in the country.

† Estimates based on reports received from banks.

†† Less than one-tenth of 1 per cent.

\$103,769,238. It was followed by the Mutual Benefit of Newark with \$84,882,136, and the Union Central of Cincinnati with \$80,116,236. The Prudential, whose activities in the farm loan field do not cover as many years, held \$67,146,570, and the Aetna, one of the first companies to begin investing its funds in farm mortgages, had \$58,206,405. These are the five largest investors in farm mortgages among life insurance companies or among any other class of institutions in the United States.

The territory within which these companies make farm loans is carefully selected. Safety is demanded before every other consideration. Since the crop-producing qualities of land are the sustaining element of the farm loan, those sections where a one-crop system prevails are generally avoided. Only with the growth of diversified agriculture have the Southern States come to be included in the investment territory of the large companies. With the exception of Connecticut, the New England and Middle Atlantic States are practically excluded. Widespread investments through the great crop-producing states are naturally the safest for average results. For this reason, the investment territory of insurance companies is found principally in Iowa, Nebraska, Kansas, Missouri, Illinois, Indiana, and Texas. In other agricultural states only those sections are favored which are known to have stable land values and a thrifty rural population.

But selection is not exhausted when a general territory has been determined by a company. A state, a county, or even a township does not contain uniformly good land, and undesirable spots must be eliminated. The art of selection seems to be continuous in the business. In choosing an individual farm as security for a loan, companies exercise the greatest care. The most important considerations affecting their decision in the matter are the productiveness and marketability of the land. The productive quality of the soil is evidenced by the record of the crops harvested over a period of years. If the land is located on a good public road, near a good railroad market, and surrounded by well improved farms, it is not likely to be subject to depreciation in value. Other important considerations affecting the selection of individual tracts for investment purposes are the general topography of the land, the extent and character of farm buildings, and the moral hazard in-

volved. An accurate account of the borrower's financial condition is uniformly required.

Various methods are employed by the insurance companies in placing their farm mortgage investments. The smaller companies whose farm mortgage business is not sufficiently large to justify the maintenance of a separate farm loan department frequently buy their mortgages from well established concerns—state banks, savings banks, brokers, and investment companies—operating in the territory which has been selected. Or they may put at the disposal of their selected agents a constant fund to be loaned under certain conditions to well qualified applicants, reserving the right, however, to reject any loan within a given period of time if the representations of the agent have been found to be inaccurate. On the other hand it is the practice of the larger companies to deal directly with the farmer, either through a local representative who acts as the agent of the borrower or through a district agent having charge of the selection of loans within a certain state or territory.

An illustration of the latter method is afforded by the practice of the Union Central Life Insurance Company. This company operates in thirty-four states and has the unique distinction of having a greater proportion of its assets invested in mortgage loans on farm lands than any other company. "It has a complete organization of its own, which means that it does not buy mortgage paper from brokers or investment companies—but deals directly with the farmer in the original transaction. This branch is managed by the treasurer of the Company and consists of thirty-five financial correspondents with local agents, land examiners, abstracters of title, local attorneys—all operating in the field; together with a financial department at the Home Office equipped with a division to handle each phase of a loan—security, title, final settlements, collection of maturities either principal or interest, taxes and assessments, fire insurance, foreclosures, and real estate.

"The application for loan form contains an exhaustive statement in detail of the character and conditions of the security offered, together with an exhibit of assets and liabilities, income and outgo of applicant. It further contains a sworn appraisalment of the security by two land owners and residents of the county, and a report of personal examination and recommendation of the

amount to be loaned, by the local agent. The financial correspondent makes a personal examination of the security and financial condition of the applicant himself or through his salaried land examiner, and in written report he bases his recommendation of amount to be loaned on statements in the application, verified by personal examination and by his office records of other examinations in that immediate locality. This is the field work done upon every application before it is submitted to the Company. The financial department of the Company assumes a position of absolute independence of the applicant, appraiser, local agent and financial correspondent, and proceeds to investigate the security and the applicant as it deems best. The records at the Home Office of the loans already made in the locality afford a reliable guide, as they are the result of actual examination and the report of subsequent changes in ownership indicating purchase price in sales. If abnormal, a special Home Office agent is sent out if the circumstances warrant such examination. When information from all sources is accumulated, it is abstracted and condensed in a single sheet for each loan and a copy is placed before each member of the Executive Committee—the investing authority of the Company—which finally decides the amount of loan justified by the security.

“During its history of forty-six years, the Company has made 75,102 loans to farmers, amounting to \$133,838,549.44 secured by mortgages on 11,462,363 acres—an average loan of \$1,782.00 to the borrower. \* \* \* \*

“It has been a basic principle not to hold real estate obtained under foreclosure for speculative rise in value, but rather to force the quick sale of it. The test of a mortgage investment is the experience with real estate obtained under foreclosure. During forty-six years the Company has acquired 871 pieces of real estate through foreclosure of mortgage, costing a total of \$2,839,660.27. It has sold 859 pieces, and now has on hand 12 pieces located in five states and costing \$46,331.19. \* \* \* The total loss upon the investment of \$133,838,549.44 during the contingencies of forty-six years has been \$193,485.11.”<sup>26</sup>

The records of such companies as the Union Central, the Northwestern Mutual, and the National Life of Montpelier—companies

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26. Extract from an address delivered by Jesse R. Clark, President of the Union Central Life Insurance Company, at the ninth annual meeting of the Association of Life Insurance Presidents, New York City, December 5, 1912.

which have always been willing to inform the general public about the conduct of their business affairs—bear testimony to the abundant security of farm mortgage investments when properly safeguarded. The growing demand for this class of investments on the part of the old established life insurance companies is evidence that the status of the farm mortgage has changed materially during the last two decades. It is true that some of the companies have been induced to enter the field on account of the relatively higher interest rate which the farm mortgage offers, but for the most part they have proceeded with caution, extending their farm loan territory only when considerations of safety justified such action. One of the noteworthy events in farm loan circles during the year 1913 was the entrance of three New York companies—the Equitable, the Mutual, and the New York Life—into the farm mortgage investment field.

A second important source of land-mortgage credit is the bank. Until the passage of the Federal Reserve Act in 1913, national banks were forbidden by law to lend on the security of real estate. The reason for this limitation on lending power was unquestionably sound. Since the primary function of a commercial bank is to make profitable use of funds which would otherwise be temporarily unemployed, and at the same time to keep the bulk of its investment in liquid form so that it will always be able to meet the demands of its depositors, its loans should be continually maturing. If its assets are invested in short-term paper, having a maturity of thirty, sixty, and ninety days, they are liquid. On the other hand, if it has made long-term loans on the security of real estate, to that extent it will be less able to meet its demand obligations in time of stress. This principle was clearly recognized by the national banking law, but in spite of its good intentions, national banks experienced little difficulty in making mortgage loans indirectly through their directors whenever such loans became relatively profitable.

The Federal Reserve Act empowered any national bank not located in a central reserve city to make loans secured by improved farm land within its district up to 50 per cent of the actual value of the property offered as security, and for a period not exceeding five years. Such loans can be made to an aggregate sum equal to 25 per cent of the bank's capital and surplus, or to  $33\frac{1}{3}$  per cent of its time deposits. A statement given out by the Treasury

Department in June, 1914, indicated that the sum of \$500,000,000 was at that time available for farm mortgage loans under the law. But it is not likely that national banks will lend this amount on mortgage security in competition with the older farm mortgage institutions. The rate of interest that can be obtained on short-term loans is generally higher, and, unless the rediscount privilege afforded by the federal reserve system causes a material reduction in the short-term rate, bankers will instinctively prefer the more liquid commercial loans. However, the new system enables a national bank to invest a larger proportion of its assets in long-term loans without running the risk of being seriously embarrassed.

State banks occupy a position of much greater prominence in financing the farmer's long-term credit needs than do national banks. Owing to the small amount of capital required for their organization, they can be more easily formed in the rural districts and are therefore greater in number. Although they are not prohibited by law from lending on the security of real estate, considerations of safety demand that in the performance of their commercial banking function they limit rigidly the proportion of their assets so invested. Individually the volume of their mortgage loans is small, but on account of the great number of these banks the aggregate of their loans is large. Not infrequently they act as financial agents for insurance companies, private lenders, and other investing classes, thereby making a large quantity of foreign capital available for local needs.

The function of trust companies and savings banks is unlike that of the commercial bank. The funds held in trust by these institutions may safely be invested in long-term loans. As yet the savings banks, outside of New England, are not heavy investors in farm mortgages, preferring urban to rural loans. What farm mortgages they hold have been acquired for the most part from country banks and mortgage companies. Trust companies, however, have shown a certain prominence in the farm mortgage field. In addition to investing their own funds in this class of security, they frequently maintain farm loan departments through which mortgages are made on carefully selected farms and sold to private investors. Sometimes, too, they hold in trust the mortgages deposited by investment companies as security for an issue of

bonds or certificates. In a few instances trust companies issue their own bonds on the security of their unsold mortgages.

According to the estimates prepared by the Department of Agriculture, the total volume of farm mortgages held by banks in the spring of 1914, when the data were gathered, was \$739,500,000<sup>27</sup>—more than one-fifth of the estimated total mortgage indebtedness. Under “banks” are included state banks, trust companies, and savings banks, *i. e.*, banks operating under state law. In addition to the mortgages which these banks held, it is estimated by the Department, on the basis of the reports received from banks, that farm mortgages to the amount of \$486,580,000<sup>28</sup> were negotiated by banks or bank officials acting as agents or correspondents for life insurance companies and other investors. Presumably, this amount represents the total outstanding mortgages which the banks had sold but which had not yet matured. Since a portion of this sum has already been accredited to the holdings of life insurance companies, it cannot be included in the aggregate as a definite addition to the total volume of bank loans.

In the distribution of mortgage loans by states there appears to be little correspondence, except in a few states, notably Indiana and Illinois, between the percentage of loans held by banks and the percentage held by life insurance companies. The high percentage of farm mortgages held by the banks in New Hampshire, Vermont, and Rhode Island, indicates that a great many mortgages of western origin are purchased by eastern institutions, especially savings banks. In other sections of the country the difference in the relative importance of banks and insurance companies as sources of land credit is not so striking, but some interesting contrasts can be found. In general, the relation between bank loans and insurance loans is supplementary. The percentage of bank loans seems to be relatively large where the percentage of insurance loans is small and *vice versa*.

This relation is probably due to the fact that insurance companies seek first the territory where the best security and a fair rate of interest can be obtained and, once their territory has been selected, are able on account of the extent of their funds to control most of the farm mortgage business within the district. On the

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27. *Supra*, p. 21.

28. *Hearings before the Subcommittee of the Joint Committee on Rural Credits*, 64 Cong., 1 Sess., p. 15.

other hand, in those sections where the security of mortgage loans is deemed insufficient for the investment of insurance funds, interest rates are high and the farmer is dependent on local capital.

In view of the fact that life insurance companies and state banks hold approximately 40 per cent of the total farm mortgages outstanding, the question arises, What are the other sources of land credit?

In the first place there are the farm mortgage companies, large and small, scattered all over the United States, but operating chiefly in the Middle West. In Kansas, Missouri, and Nebraska alone there are over twenty-five companies each of which has outstanding mortgage loans varying in amount from \$5,000,000 to \$20,000,000. The Farm Mortgage Bankers' Association to which most of the large companies belong claims to have a membership whose outstanding loans in twenty-five states approximate a total of \$500,000,000.<sup>29</sup> And there are hundreds of unincorporated farm loan agencies throughout the Middle West not included in the membership of this association.

The business of these companies is variously conducted. As a rule the large companies operate in several states. Each has a systematic organization of local agents and a carefully selected territory. On receipt of an application for a loan a salaried examiner is sent to investigate the reliability of the applicant and the character and value of his land. If the applicant, title, and security are approved, the loan is made from the company's capital and the mortgage is sold, usually without recourse, to a life insurance company, savings bank, or private investor. The company collects the interest when due, sees that the taxes are paid, and charges the borrower a commission for its services. In some cases it receives in addition a higher rate of interest than that paid to the ultimate investor.

Formerly, it was the practice of many of these companies to provide their funds by the issuance of debenture bonds bearing a lower rate of interest than the mortgages which secured them. But owing to reckless management and lack of proper legal restrictions they became involved in the real estate collapse of the early nineties and with a few exceptions the practice of issuing

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29. Pamphlet entitled *Recommendations of the Farm Mortgage Bankers' Association of America through its Board of Governors*, Chicago, Feb. 15, 1916, p. 3.

debentures has been abandoned. The issuance of serial bonds or certificates, however, is quite common. When a company has made an individual loan of say \$10,000, too large to be readily sold to one client, it may deposit the mortgage with a trustee as security for the issuance of certificates in convenient denominations of \$100 and \$500. These are generally guaranteed by the company and sold to individual investors.

There is another type of mortgage company which follows the "old-fashioned method" of conducting business. It receives applications from farmers or through its own correspondents and, after making an examination of the security offered, submits the application together with its own recommendation to a prospective investor. If the application is accepted, the loan is made in the name of the lender. The mortgage company merely supervises the loan and receives a commission for its services. In such cases, the farmer may be compelled to wait for his loan until a lender can be found.

A promising source of land credit is the building and loan association. These associations are formed primarily for the promotion of thrift among members. They have a variable capital which they lend to their members for the purpose of building or acquiring homes. Until recently, their activities were generally confined to lending on the security of urban property, but in some states the law has been amended to enable them to extend their operations to the rural districts. The building and loan associations of Ohio have, for several years, been lending on the security of farm lands with conspicuous success. In 1914, they had 8,897 farm loans outstanding, representing a total investment of \$18,262,401.<sup>30</sup> In other states they have only begun to adapt their methods to the needs of farmers. Whether they will succeed in promoting home ownership among the agricultural classes as they have among urban workers is a doubtful matter. But owing to the ease with which they can be formed, and the small expense incident to their management, they ought to become an important source of farm credit.

Some states, moreover, lend their permanent school and educational funds directly to farmers at a low rate of interest. This policy has been followed for a number of years in Idaho, Indiana,

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30. *Ohio Building and Loan Association Report*, 1914, p. xvi.

Iowa, North Dakota, Oklahoma, Oregon, South Dakota, and Utah with fairly successful results.<sup>31</sup> In South Dakota, for instance, loans to the amount of \$6,216,405 were in force on September 30, 1912. In the twenty years during which the state had been making farm loans, only one foreclosure had been necessary. Inasmuch as the systems in vogue in other states have been equally well administered, there appears to be no serious objection to this form of state activity so long as its primary purpose is to provide a safe investment for a limited amount of idle funds. Recently, however, a number of states have been contemplating a radical extension of their loan systems so that they will be able to supply farmers with an unlimited quantity of capital at low interest rates.

A final source of land credit is the individual lender. Collectively, these individual investors hold more farm mortgages than any single class of institutions. Nearly every bank, trust company, and mortgage company engaged in the business of negotiating farm mortgages has among its regular clients a large number of individuals of small means who will buy farm mortgages in preference to railroad and public utility securities on account of the higher interest rate that the mortgage investment offers. Furthermore, it is a growing practice in the older agricultural communities, where the laws of the state do not inadvertently discriminate against the investment of local capital in farm mortgages, for one farmer to lend to another or for a private individual to lend directly to a farmer. In such cases the borrower and lender are brought into close contact with one another and the borrower may be relieved of many incidental expenses which would otherwise be paid to a middleman. But in a number of states this immediate contact between borrower and lender is impossible or, if possible, is unprofitable to the lender on account of prejudicial laws. For various reasons the lender usually prefers to buy his mortgages from well established banks and mortgage companies.

The rate of interest received on farm mortgage loans varies from about 5 to 10 per cent. With the exception of a few states which make a limited number of mortgage loans at 5 per cent, the lowest rates are probably received by life insurance companies. According

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31. For fuller details in regard to the mortgage investments of these states see the report of W. M. Duffus to the Wisconsin State Board of Public Affairs on *State Loans to Farmers*, pp. 80-102.

to a report<sup>32</sup> submitted by Robert Lynn Cox at the ninth annual meeting of the Association of Life Insurance Presidents, the average rate of interest obtained in 1914 by 126 American life insurance companies on farm mortgage loans, representing 97 per cent of all farm mortgages held by American companies, was 5.5 per cent. The states in which more than \$10,000,000 of insurance funds were invested and the average rate of interest reported in each were as follows: Iowa, 5.32 per cent; Nebraska, 5.34 per cent; Kansas, 5.46 per cent; Missouri, 5.35 per cent; Illinois, 5.16 per cent; Indiana, 5.31 per cent; Minnesota, 5.36 per cent; Texas, 6.99 per cent; Oklahoma, 5.91 per cent; South Dakota, 5.44 per cent; North Dakota, 5.88 per cent; Ohio, 5.30 per cent; and Georgia, 6.28 per cent. The states in which the highest average rates were obtained were Idaho and Utah. There the reported averages were 8.53 and 8.74 respectively. But these rates are not generally sought except by domestic companies. The most conservative life insurance companies are content to realize an interest rate of 5 or 5½ per cent on well secured mortgage loans. No loan is granted in excess of 50 per cent of the appraised value of a farm and, so far as possible, loans are limited to 40 per cent of the appraised land value.

The rates received by other classes of lenders scarcely admit of accurate generalization but, like the rates received by life insurance companies, are generally lower than the actual rate paid by the farmer. Various middlemen are required to bring the borrower and lender in touch with one another, and for their services they are paid a commission which must be included in any estimate of the farmer's rate. Manifestly this rate varies from section to section and, within a given community, from one farm to another. But over the country as a whole there are a few regions within which fairly accurate generalization is possible. Taking into account the middlemen's commission charge, the farmer's rate of interest is lowest in the New England and Middle Atlantic States, varying from 5 to 6 per cent. In that portion of the North Central division which lies between Pennsylvania and the 98th meridian, the rate varies from 6 to 7 per cent. Westward from this meridian the rate rises to 10 per cent in the arid and

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32. See *Proceedings of the Ninth Annual Meeting of the Association of Life Insurance Presidents*, 1915. The essentials of this report are reprinted in *Bulletin of the Farm Mortgage Bankers' Association of America*, Vol. II, Jan., 1916, p. 50.

Mountain States, falling to approximately 8 per cent on the Pacific Coast. To the south of Pennsylvania and the Ohio river, the rate gradually rises from 6 per cent in Maryland and 7 per cent in Kentucky to about 9 per cent in the Gulf States.

The table<sup>33</sup> on page 33 shows by states the average rates for interest and commissions together with the percentage of farm mortgage business on which a commission is paid.

The facts shown in the table below emphasize the necessity of considering the charge for commissions in making any estimate of the farmer's rate of interest. In general, the commission charge is highest in those states where farmers are dependent on foreign capital. The average annual commission of 1.8 per cent in Oklahoma and North Dakota may well be contrasted with the low commission rates obtaining in eastern states where the supply of local capital is more than sufficient to meet the requirements of the farmer. Moreover, the commission charge may be affected by the laws of a given state. It is commonly used as a means of evading the spirit of a usury law. In North Carolina, for instance, where the legal rate of interest is 6 per cent, the average annual commission charge is 1.4 per cent; whereas in South Carolina, where the legal rate of interest is 7 per cent with the right under contract to make it 8 per cent, the average yearly commission is only 0.6 per cent.

Within a given community, however, the actual rate of interest paid by farmers offering equal security is determined by competitive forces, and it makes little difference, so far as the total cost of borrowing is concerned, whether a loan is obtained from an insurance company, a bank, or a mortgage company. For, the amount of commission paid by the borrower varies inversely with the rate of interest received by the lender and consequently has an equalizing effect on the actual rates. In an investigation<sup>34</sup> conducted by the writer in Kansas in 1914, it was found that on five-year loans made by life insurance companies at  $5\frac{1}{2}$  per cent, the loan agents charged a commission of 5 per cent, making an addition of 1 per cent to the rate recorded in the mortgage instrument. On the other hand, when banks made a competitive farm loan for the

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33. Arranged from data prepared by C. W. Thompson of the Department of Agriculture. *Hearings before the Subcommittee of the Joint Committee on Rural Credits*, 64 Cong., 1 Sess., pp. 98-99.

34. See article entitled *Farm Credit in Kansas*, *American Economic Review*, Vol. V, March, 1915, p. 28.

Geographic division and State	Average inter- est rate	Average annual com- mis- sion*	Inter- est plus com- mis- sion	Percentage with commission		
				Total	With com- mis- sion paid in ad- vance	With com- mis- sion paid in in- stal- ments
<b>New England:</b>						
Maine.....	6.1	0.1	6.2	8.9	5.0	3.9
New Hampshire.....	5.3	†	5.3	3.4	3.4	.....
Vermont.....	5.6	†	5.6	5.9	4.8	1.1
Massachusetts.....	5.6	†	5.6	2.8	2.7	.1
Rhode Island.....	5.7	.2	5.9	21.7	11.7	10.0
Connecticut.....	5.7	†	5.7	1.3	1.3	.....
<b>Middle Atlantic:</b>						
New York.....	5.5	.1	5.6	13.4	9.6	3.8
New Jersey.....	5.5	.3	5.8	27.7	18.7	9.0
Pennsylvania.....	5.5	.3	5.8	18.6	10.1	8.5
<b>East North Central:</b>						
Ohio.....	5.9	.2	6.1	26.3	17.9	8.4
Indiana.....	5.8	.4	6.2	45.5	36.2	9.3
Illinois.....	5.7	.3	6.0	47.3	39.1	8.2
Michigan.....	6.3	.3	6.6	23.2	18.0	5.2
Wisconsin.....	5.7	.1	5.8	14.9	10.4	4.5
<b>West North Central:</b>						
Minnesota.....	6.3	.5	6.8	47.7	20.0	27.7
Iowa.....	5.6	.3	5.9	64.0	51.3	12.7
Missouri.....	6.2	.6	6.8	54.9	28.0	26.9
North Dakota.....	6.9	1.8	8.7	79.8	17.0	62.8
South Dakota.....	7.0	1.0	8.0	68.2	45.5	22.7
Nebraska.....	6.3	.8	7.1	69.3	53.5	15.8
Kansas.....	6.1	.8	6.9	67.8	30.6	37.2
<b>South Atlantic:</b>						
Delaware.....	5.6	†	5.6	1.9	1.9	.....
Maryland.....	5.7	.4	6.1	35.7	28.5	7.2
Virginia.....	6.1	.7	6.8	34.1	26.2	7.9
West Virginia.....	6.2	0.2	6.4	11.1	8.8	2.3
North Carolina.....	6.3	1.4	7.7	40.9	27.5	13.4
South Carolina.....	7.8	.6	8.4	35.3	26.0	9.3
Georgia.....	7.6	1.1	8.7	66.1	54.1	12.0
Florida.....	9.0	.6	9.6	29.8	18.6	11.2
<b>East South Central:</b>						
Kentucky.....	6.7	.4	7.1	23.3	14.2	9.1
Tennessee.....	7.3	.6	7.9	35.4	23.9	11.5
Alabama.....	8.7	.7	9.4	37.2	25.2	12.0
Mississippi.....	8.0	.5	8.5	25.5	15.7	9.8
<b>West South Central:</b>						
Arkansas.....	9.0	.6	9.6	33.1	18.6	14.5
Louisiana.....	8.2	.4	8.6	23.2	16.3	6.9
Oklahoma.....	6.6	1.8	8.4	91.6	36.7	54.9
Texas.....	8.4	.6	9.0	43.0	27.1	15.9
<b>Mountain:</b>						
Montana.....	8.4	1.6	10.0	68.9	28.4	40.5
Idaho.....	8.2	.7	8.9	64.2	45.6	18.6
Wyoming.....	9.2	.8	10.0	40.1	28.1	12.0
Colorado.....	8.3	.6	8.9	58.3	47.0	11.3
New Mexico.....	9.7	.8	10.5	41.0	32.8	8.2
Arizona.....	9.1	.3	9.4	19.5	9.5	10.0
Utah.....	8.6	.4	9.0	33.0	18.3	14.7
<b>Pacific:</b>						
Washington.....	7.9	.8	8.7	58.2	46.4	11.8
Oregon.....	7.7	.3	8.0	31.6	23.6	8.0
California.....	7.4	.2	7.6	19.0	15.1	3.9

\* Where the report shows a commission paid once for all in advance on a loan running more than one year, the equivalent annual commission is used.

† Less than one-tenth of 1 per cent.

same term of years, the lowest rate was usually 6 per cent, with an extra charge of 2 or 3 per cent for commission. In other words, the competitive farm mortgage rate was approximately  $6\frac{1}{2}$  per cent.

The commission charge is thus a variable factor and, whenever the lender's rate of interest is sufficiently low, can be exacted as a separate charge to make the borrower's rate correspond to the competitive rate. It is an exceptionally convenient device for making the farmer's rate of interest appear to be lower than it really is. Its subtle effect upon the actual rate is due partly to the method in which the commission is paid. In the majority of cases, the borrower pays the commission at the time the loan is made by having it deducted from the principal. For instance, a commission of 3 per cent deducted from a loan of \$1,000, maturing in five years and bearing 6 per cent interest, leaves the borrower a net loan of \$970. When he has paid interest charges of \$60 per annum and repaid the principal, his actual rate has been 6.8 per cent. If the commission had been paid in equal yearly instalments, the borrower's actual rate would have been 6.6 per cent. On larger loans, the agent frequently takes a second mortgage for the amount of the commission.

The term of the loan has an important bearing on the cost of borrowing. Until about twenty-five years ago mortgage loans were not made for longer periods than five years, and could not be paid off in whole or in part until the date of maturity. Since that time, however, severe competition and renewed confidence in the farm mortgage have caused more liberal privileges to be granted to borrowers. Although the customary term of mortgage loans is now five years, life insurance companies make loans for terms of seven or ten years in some of the favored sections where first class security can be offered. Only with the smaller institutions such as state banks is a term of three years common.

As regards the repayment of loans, nearly every mortgage instrument provides for the voluntary repayment of a certain percentage of the principal annually, or some multiple of \$100 on any interest-paying date. These privileges enable many borrowers to repay their loans in full before maturity, but for the great majority of borrowers the term of loans is far too short and renewal at maturity is a common practice. This necessitates the payment of

renewal commissions and other incidental fees all of which figure in the borrower's actual rate. Furthermore, if a loan matures during a period of financial stringency, the borrower may be obliged to pay a higher rate of interest on the renewed loan. Only a few companies have found it possible to extend the term of loans beyond the customary five years and provide for the repayment of the principal by amortization.

Finally, the borrower must pay the recording fee and the expenses that arise in connection with the perfection of his land title. Sometimes, too, he pays the notary's fee, the inspector's charges, and a fee for having the mortgage released. These are not insignificant items. The cost of establishing a title prior to the granting of a loan may be especially burdensome to the small borrower. The title must be carefully searched every time the property is sold or mortgaged. Even the findings of a reliable abstract company are subject to review if the farmer attempts to convert his loan by borrowing from a new source. Only in those states where the Torrens system has been successfully adopted is it possible for a farmer to escape this recurrent charge.

From the foregoing account it is evident that the present system of land credit is defective. The specific defects may be summarized as follows: first, the customary term of farm loans is far too short a period for the repayment of a loan out of the product of land; second, the method of repayment is haphazard; third, the possibility and conditions of renewal are uncertain; and fourth, the expenses in the way of interest charges, commissions, etc., are much higher than farm mortgage security under a specialized and mobile system of land credit would warrant.

One reason for the existence of high rates can be found in the legislation of the states themselves. In many of the states the investment of local capital in farm mortgages is adversely affected by the general property tax law which subjects real and personal property to the same kind of taxation. To the local investor the tax is extremely annoying. It scales down an interest rate of 6 per cent on a mortgage loan to an actual rate of 4 or 5 per cent. Rather than suffer this loss of income the individual lender is

wont to invest his capital in foreign enterprises and withhold from the tax assessor a full declaration. Thus an enormous volume of local capital annually seeks investment beyond the boundaries of those states in which mortgages and real property are taxed at the same rate. The withdrawal of these loanable funds compels the farmer to pay commission charges on foreign capital, *i. e.*, a higher rate of interest than would be necessary under more lenient laws.

That the burden of a heavy mortgage tax is borne partly by the borrower in the form of a higher commission may be inferred from the findings of the Department of Agriculture.<sup>35</sup> In California, Arizona, and Utah where mortgages are exempt from taxation, in Massachusetts, New Jersey, and Wisconsin where they are treated as interest in the land, or in New York and Michigan where they are subject to mortgage registration taxes, the commission charge is relatively low because it is possible for borrowers and individual lenders to have direct dealings with one another. Some exceptions will be found to this principle here and there on account of the existence of other factors. In some states where mortgages are subject to the regular property tax rate, the commission charge is low because the law in regard to the taxation of personalty is laxly administered. In others, notably Oklahoma and Montana, the commission charge is exceedingly high—notwithstanding the fact that mortgages in these states are subject only to recording taxes—because of the small quantity of local capital available for investment.

Another phase of state legislation which affects the rate of interest on long-term loans is the privilege accorded in most states to the mortgagor who has defaulted on interest payments of regaining title to his land by redeeming his obligations within a given period after foreclosure sale. A common period allowed for redemption is eighteen months. Until the expiration of this redemption period, the mortgagor may reside upon the land and derive all the income it yields without being subject to the ordinary fixed expenses. The conditional owner, moreover, is exposed to a possible loss not only on account of taxes and interest but also on account of the wilful negligence of the occupier in caring for the property. Under these conditions, it is little wonder that conservative lenders must limit their loans to 40 and 50 per cent of the

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35. *Supra*, p. 33.

appraised value of the property to be mortgaged. Invariably the long-term redemption privilege detracts from the security of a mortgage loan. A shorter period allowed for redemption would virtually lower the borrower's rate of interest by enabling him to secure larger loans on his property with less risk to the lender.

After making due allowance for the effect which obnoxious state laws have upon the farmer's rate of interest, it does not appear that the farmer's net rate—the rate received by the lender—is inordinately high compared with the rates paid by other small business men. It is the commission charge and other incidental expenses rather than the lender's rate that seems in most cases to be excessive. There is, however, one class of borrowers, *i. e.*, those of small means who aspire to land ownership, to whom the lender's rate *is* excessive. At present the value of land is high, out of all proportion in fact to the capitalization of its rent at the current rate of interest. In order to become an independent landowner, the tenant must first be able to pay one-half the purchase price; in addition, he must borrow the remainder at an interest rate of possibly 6 per cent and be subject to other charges which may increase the actual rate to 7 per cent. In view of the small return from land at the present scale of values, these requirements offer little encouragement to the young man to become a landowner. The margin of security demanded is too large and the rate of interest is unprofitably high. Until special provision has been made for this class of borrowers, the land credit system will continue to be defective.

A final and fundamental defect in the existing system of agricultural finance is to be found in the character of the institutions on which the farmer is dependent. The state and national banks particularly are ill-adapted to his needs. These institutions were established to meet the needs of the commercial and industrial classes at a time when land was free, when loans for agricultural purposes were secondary in importance. In the performance of the commercial function for which they were designed, they are unable to extend to the farmer on the most advantageous terms the kind of credit he requires. It is largely because the farmer has been dependent on commercial banking institutions that the specific defects, already indicated, have arisen.

Nor are the life insurance companies wholly satisfactory as

sources of land credit. Although they have accomplished more than any other single class of institutions in meeting the growing demand for better land credit machinery, they operate at a great distance from the borrower and the cost of placing their loans may completely offset the advantages that would otherwise be derived from the low rate of interest they are content to receive. They naturally prefer the large loans and follow a practice similar to that established by banks in fixing the term of loans and the method of repayment. For various reasons it is impossible for them to observe the standards to which an ideal land credit institution should conform.

The farm mortgage companies—the only real specialists in the business of negotiating land-mortgage loans—are open to similar criticism. Their primary function is to bring borrowers and lenders together for mutual benefit. In the performance of this function they have succeeded, like the life insurance companies, in directing a large flow of capital to agricultural channels. But their methods have not kept pace with the needs of agricultural progress, nor have they succeeded in accomodating the large number of small investors whose savings are insufficient to warrant the purchase of individual mortgages. Until new machinery has been devised that will enable the farm mortgage companies to reach this class of investors, capital for agricultural development will be ineffectively mobilized.

## CHAPTER III

### THE RURAL CREDIT MOVEMENT

There is nothing new in the general complaint that the farmer's rate of interest is high. On the frontier, high rates have always caused a certain amount of complaint, especially during periods of falling prices. It is only recently, however, that the fundamental defects in the rural credit system have received recognition. Much credit for the general awakening should be given to the National Monetary Commission, created in 1907, which brought to light certain stimulating facts in regard to the European systems of farm credit. Moreover, the Country Life Commission, created in the following year, found that among the causes contributing to the deficiencies of country life was the "lack of any adequate system of agricultural credit, whereby the farmer may readily secure loans on fair terms",<sup>36</sup> and suggested that "a method of coöperative credit would undoubtedly prove of great service".<sup>37</sup> This view was favorably received by those who saw in the rural problem an economic cause—who believed that the conditions of country life could be made more attractive only by the adoption of a program that would promote the prosperity of the agricultural worker.

Public interest in the possibilities of coöperative credit was immediately aroused. At the annual meetings of the various bankers' associations, the European systems of agricultural credit afforded a recurrent topic for discussion. In furthering this interest, the American Bankers' Association played a prominent role. At its annual meeting, held in New Orleans, November 24, 1911, a Committee on Agricultural and Financial Development and Education was created to undertake a study of agricultural credit at home and abroad. The action of this association was quickly followed by minor organizations until the interest in the movement became nation-wide.

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36. Sen. Doc. 705, 60 Cong., 2 Sess., p. 15.

37. *Ibid.*, p. 59.

At length President Taft, in March, 1912, directed Secretary Knox to instruct the American ambassadors to Germany, France, and Italy, and the American ministers to Belgium and the Netherlands to investigate the agricultural credit systems in operation in their respective countries. On the basis of the data gathered by these investigations, Myron T. Herrick, American Ambassador to France, was instructed to prepare a general report which would "place the Department in possession of all data necessary to the President for the formulation of some practical scheme which may be worked out to bring the desired benefits to agricultural communities in the United States".<sup>38</sup>

This report, known as the *Preliminary Report on Land and Agricultural Credit in Europe*, was published October 11, 1912, and copies were sent to the governors of all the states with a personal letter from President Taft. In the course of the letter the President said: "The interest rate paid by the American farmer is considerably higher than that paid by our industrial corporations, railroads or municipalities. Yet, I think, it will be admitted that the security offered by the farmer in his farm lands is quite as sound as that offered by industrial corporations. Why, then, will not the investor furnish the farmer with money at as advantageous rates as he is willing to supply it to the industrial corporations? Obviously, the advantage enjoyed by the industrial corporation lies in the financial machinery at its command, which permits it to place its offer before the investor in a more attractive and more readily negotiable form. The farmer lacks this machinery and, lacking it, he suffers unreasonably".<sup>39</sup>

In the meantime, Mr. David Lubin of the International Institute of Agriculture, who had been gathering data for a number of years on the European rural credit systems, brought the matter to the attention of Senator Fletcher, president of the Southern Commercial Congress. Mr. Lubin attended the annual convention of this organization in Nashville in the spring of 1912, presented his data on European systems of agricultural credit, and a resolution was promptly adopted calling upon the Southern Commercial Congress to assemble a commission composed of two representatives from each state for the purpose of studying at first hand and

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38. Herrick and Ingalls: *How to Finance the Farmer*, p. 2.  
39. Sen. Doc. 967, 62 Cong., 3 Sess., p. 4.

of popularizing the methods employed by the coöperative credit and coöperative marketing organizations of Europe.

The movement soon took on a political aspect. The three political parties, assembled in national convention in 1912, adopted planks favoring the improvement of agricultural credit facilities. With a view to paving a way for remedial legislation, the Republican and Democratic platforms recommended authoritative investigations of the European credit associations. On March 4, 1913, President Taft approved the Agricultural Appropriation bill which carried an amendment providing for the appointment of a United States Commission of seven members "to investigate and study in European countries coöperative land-mortgage banks, coöperative rural credit unions, and similar organizations and institutions devoting their attention to the promotion of agriculture and the betterment of rural conditions".<sup>40</sup> This commission was instructed to work in conjunction with the American Commission which was being assembled by the Southern Commercial Congress. President Wilson, on his accession to office, promptly appointed Senator Duncan U. Fletcher, Senator Thomas P. Gore, Congressman Ralph W. Moss, Col. Harvie Jordan, Dr. John Lee Coulter, Dr. Kenyon L. Butterfield, and Dr. Clarence J. Owens as members of the United States Commission. Senator Fletcher was made chairman of both commissions.

The American Commission—consisting of seventy members, and representing twenty-nine states, the District of Columbia, and four Canadian provinces—and the United States Commission sailed for Europe April 26, 1913. The commissions as a body or through subcommittees visited Italy, Egypt, Hungary, Austria, Russia, Germany, Switzerland, Belgium, Holland, Denmark, Norway, France, Spain, England, Wales, Scotland, and Ireland. In gathering material for their reports they visited banks, coöperative institutions and farms, and held conferences with government officials, heads of agricultural organizations, and individuals.

The agricultural data thus obtained were published in a report known as *Information and Evidence*.<sup>41</sup> Each commission, however, made a separate report. Of these the report of the United States Commission on *Land-Mortgage or Long-Term Credit*<sup>42</sup> is the most

40. Sen. Doc. 380, 63 Cong., 2 Sess., p. 3.

41. Sen. Doc. 214, 63 Cong., 1 Sess.

42. Sen. Doc. 380, 63 Cong., 2 Sess.

noteworthy on account of its bearing on the course of subsequent events. That report was confined to a consideration of rural credit. The general conclusions recorded by the commission were that the same institution could not properly supply the farmer's long-term and short-term credit requirements, that reform in the long-term facilities should come first, and that with the establishment of suitable machinery under strict federal supervision private initiative could be depended upon to reduce the farmer's rate of interest and improve the methods of making loans.<sup>43</sup> Although the commission recognized the "value of coöperative effort and the wisdom of permitting coöperative institutions to be organized", it found that the landschaft form was unsuited to the conditions and requirements of American agriculture.<sup>44</sup> Furthermore, it recorded its firm conviction "that not only was government aid unnecessary, but that it would be unwise".<sup>45</sup>

The Moss-Fletcher bill,<sup>46</sup> one of the early<sup>47</sup> rural credit bills to be introduced, embodied the specific recommendations of the commission. It provided for the voluntary organization of decentralized farm land banks, either as coöperative or non-coöperative institutions, under a federal charter, with a capital stock of at least \$10,000. The organization and management of the banks were to be supervised by a Commissioner of Farm Land Banks in charge of a bureau in the Department of the Treasury. They were empowered to receive deposits, to make long-term loans, repayable by amortization, up to 50 per cent of the value of improved farm land, and to issue and sell their debenture bonds. The amount of bonds so issued by any one bank could at no time exceed fifteen times its capital and surplus, nor could the farmer's rate of interest exceed by more than one per cent the rate paid on the last series of bonds. Each bank was empowered to make loans only in the state where it was located.

To give the bonds an investment standing, provision was made for the appointment of a federal fiduciary agent for each bank who was to have control of the mortgages deposited as security for

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43. *Ibid.*, pp. 12 and 21.

44. *Ibid.*, p. 31.

45. *Ibid.*, p. 31.

46. S. 4246, introduced January 29, 1914.

47. Another bill (S. 2909) previously introduced by Senator Fletcher provided for the formation of a central bank at Washington with power to issue bonds on the security of mortgages turned over to it and guaranteed by central state banks. At the time, this bill was supposed to embody the opinions of the United States Commission but it was subsequently withdrawn in favor of the Moss-Fletcher bill.

bonds and whose duty it was to certify that each bond issue was properly secured by first mortgages of equal value. The bonds were made available as security for the deposit of postal savings funds in all banks authorized to receive such deposits, and as security for loans from national banks to farm land banks and individuals. Furthermore, they were made legal investments for trust funds and estates under the charge of a United States court, and for time deposits of national banks and of savings banks organized in the District of Columbia. Finally, the land banks and their debenture bonds were to be exempt from all federal, state, and local taxation except taxes on real estate.

Numerous other land credit bills were introduced during this session of Congress. Of these the Bathrick bill,<sup>48</sup> introduced at about the same time as the Moss-Fletcher bill, is worthy of note. It provided for the issuance of government bonds bearing an interest rate of  $3\frac{1}{2}$  per cent or less. The funds obtained from the sale of bonds were to be loaned to farmers up to 60 per cent of the value of their lands at an interest rate of not more than  $4\frac{1}{2}$  per cent. No individual loan could exceed \$15,000. Provision was made for lending to farmers through farm credit associations on condition that such associations become surety for the mortgages they accepted. The administration of the system was to be under the control of a bureau in the Department of Agriculture.

The Senate and House Committees on Banking and Currency created subcommittees on rural credits which held joint meetings from February 16 to July 23, 1914. In the course of the hearings before the subcommittees, the Moss-Fletcher bill was severely criticized. On the whole it was generally regarded with suspicion. The charge was persistently made that it placed too much reliance on private initiative, that it was a banker's rather than a farmer's measure, that it would not only lead to unnecessary centralization in banking power but would also fail to afford the needed relief to the debtor farmer. Moreover, in the course of the extensive hearings it was found that the framers of the bill were not wholly agreed as to the wisdom of its provisions; and that the Bathrick bill, which provided for direct government loans at a low rate of interest, had the stronger support of the farmers' organizations.

Accordingly, no favorable action was reported on either bill.

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48. H. R. 11,897, 63 Cong., 2 Sess.

Instead, the Hollis-Bulkley bill<sup>49</sup> was drafted and introduced by the chairmen of the subcommittees. This bill formed the basis of the present law. It provided for the appointment of a Farm Loan Commissioner by the newly created Federal Reserve Board to supervise the organization and management of national farm loan associations. These associations could be formed under a federal charter with a capital stock of not less than \$10,000, to be subscribed, if the board of directors so authorized, after the manner followed by building and loan associations. When fully organized, they could make long-term loans to farmers up to 50 per cent of the value of their land and 25 per cent of the value of farm buildings at a rate of interest not exceeding the legal rate current in the state where the association was located. Borrowers were required to subscribe for stock in an association up to 5 per cent of the amount of their loans and to reside upon the land offered as security. No association could lend to a single individual more than \$4,000, nor a larger sum than 25 per cent of its capital and surplus.

The bill authorized the Federal Reserve Board to divide the country into twelve districts, the boundaries of which corresponded so far as possible with state boundary lines, and to establish in each district a federal land bank having a capital stock of \$500,000. National farm loan associations were required to subscribe at least 10 per cent of their capital to the capital of the land bank located in their district. If their subscriptions were insufficient to provide the land banks with their minimum capital requirements, the Secretary of the Treasury was authorized to subscribe for the balance.

Federal land banks were to have power to purchase first farm mortgages from the national farm loan associations within their respective districts and, under certain conditions, from institutions organized under state laws. On the security of these mortgages they could issue bonds, bearing an interest rate of 5 per cent or less, to an amount equal to twenty times their capital and surplus. The bonds were to be exempt from all taxation and were made legal investments for the funds withdrawn from postal savings depositaries if the bonds could be purchased at par or below. Finally, upon the recommendation of the Federal Reserve Board,

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49. H. R. 16,478, 63 Cong., 2 Sess.

the Secretary of the Treasury might be required to purchase land bank bonds to an amount not exceeding \$50,000,000 in any one year. No less administrative authority was given to the Federal Reserve Board than that conferred by the Federal Reserve Act of 1913.

Manifestly, the Hollis-Bulkley bill was a drastic attempt to meet the objections that had been urged against the Moss-Fletcher bill. It was far from being a banker's bill as it carefully removed all possibility of private gain; and the federal assistance for which it provided should have satisfied those who favored a program of government loans. But its paternalistic guise failed to win the enthusiastic support of the administration and, as Congress was busily engaged on other pressing matters, all attempts to enact a rural credit law were temporarily abandoned.

At length when the Agricultural Appropriation bill came up for consideration in the House, Representative Bulkley, in a last desperate effort to save the Hollis-Bulkley bill, proposed it as an amendment. In this attempt he was partly successful as the amendment passed the House March 1, 1915. Meanwhile, the McCumber amendment,<sup>50</sup> also proposed as a rider on the Agricultural Appropriation bill, had passed the Senate February 25, 1915. This measure provided for the establishment of a bureau in the Treasury Department with power to issue bonds and to purchase farm mortgages from state and national banks so long as its bonds could be disposed of at par. No objection was made to this amendment by the supporters of the Hollis-Bulkley bill because they expected the latter to be adopted in conference.<sup>51</sup> But owing to a lack of time for proper consideration, the two riders were stricken out and replaced by a clause authorizing the formation of a joint committee of twelve members of the Senate and House to prepare and report to Congress a bill or bills providing for the establishment of a system of rural credits adapted to American needs and conditions. This action was approved March 4, 1915, and the joint committee was immediately organized.

On January 3, 1916, the Joint Committee on Rural Credits submitted the report<sup>52</sup> of its subcommittee on land-mortgage loans

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50. Subsequently introduced as S. 831, 64 Cong., 1 Sess.

51. See *Congressional Record*, Vol. 52, pp. 5195-5196.

52. Printed as House Doc. 494, 64 Cong., 1 Sess.

together with the draft of a proposed bill<sup>53</sup> which differed but slightly from the Hollis-Bulkley bill. It was introduced two days later by Senator Hollis, was favorably reported by the Senate Committee on Banking and Currency with amendments February 15, and passed the Senate with scarcely any opposition May 4. The same bill somewhat changed passed the House May 15 and was approved by the President July 17.<sup>54</sup>

In the meantime, while Congress was attempting to work out a practical program for rural credit reform, the state legislatures had been attacking the problem with characteristic initiative.<sup>55</sup> In 1913, the Wisconsin legislature passed a law on land-mortgage associations. Similar laws were passed in Massachusetts and Utah in 1915. In 1914, the New York legislature provided for the organization of the Land Bank of the State of New York, a central institution, to be owned and controlled by local savings and loan associations. In the following year, Missouri, Montana, and Oklahoma, abandoning all hope of solving the rural credit problem through private initiative, adopted modified programs of state loans.

These measures are not altogether dissimilar. Although there is considerable difference in the proposed machinery for administration and supervision, all contain plans looking toward a longer term of loans, repayable by amortization, and the issuance of bonds on the collective security of farm mortgages. The chief differences are to be found in the effect which these measures are expected to have upon the farmer's rate of interest. From this

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53. S. 2986, known as the Hollis bill, or the Federal Farm Loan bill.

54. The detailed provisions of the Federal Farm Loan Act together with a criticism of the measure may be found *infra*, Chapter VI.

55. The history of state rural credit measures may be sketched briefly as follows: Massachusetts passed a law on credit unions in 1909; Texas on rural credit unions in 1913; Wisconsin on coöperative credit associations in 1913; and New York on credit unions in 1914. In 1913 a law was passed in Wisconsin providing for the incorporation and regulation of land-mortgage associations. The associations were authorized to make long-term loans to farmers on first mortgage security and to issue and sell mortgage bonds. In the following year the New York legislature provided for the organization of the land bank, a central institution with the power to issue bonds on the security of farm mortgages turned over to it by local savings and loan associations.

In 1915 laws providing for the organization of credit unions or coöperative banks were passed in Massachusetts, North Carolina, Oregon, and Utah. Massachusetts and Utah, following the example set by Wisconsin, enacted special laws for the organization of farm land banks. Similar measures were defeated in California, Indiana, Iowa, Michigan, and Nebraska. In Kansas and North Carolina the laws on building and loan associations were amended to enable those institutions to make long-term loans on agricultural lands. The California legislature authorized the governor to appoint a commission to investigate rural credit schemes at home and abroad.

In some states there has been a disposition to regard the land credit problem of such serious nature as to warrant the adoption of a policy of state aid. For a number of years Idaho, Indiana, Iowa, North Dakota, Oklahoma, Oregon, South

point of view the laws are of two fairly distinct types. One type seeks merely to reduce a portion of the waste in the present land credit system by improving the method of making loans and by giving greater mobility to funds seeking mortgage investment. The other contemplates, in addition, a material reduction in the farmer's rate of interest either through the organization of a strong central bank or through a program of minimum state aid.

The Wisconsin law<sup>56</sup> is a typical example of the former type of legislation. It provides for the voluntary formation of land-mortgage associations having a capital stock of not less than \$10,000. These institutions can make long-term loans—repayable in annual instalments of 1 per cent of the original loan—on the security of agricultural lands, forest lands, or lands occupied by dwelling houses within the state. Loans are limited to 65 per cent of the value of such real estate if improved, and to 40 per cent if unimproved. No association can lend to a single individual a larger sum than 15 per cent of its capital and surplus. On the security of the mortgages so taken and deposited with the state treasurer, each association may issue bonds, equal in amount to the total unpaid principal of loans outstanding, up to twenty times its capital and surplus. The rate of interest paid by the borrower is limited to the rate agreed upon plus an annual charge for expenses which can not exceed 1 per cent of the face of the loan. The bonds are made legal investments for trust funds and are exempt from taxation whenever the taxes upon the mortgaged real estate are payable either by the mortgagor or the mortgagee.

The laws of Missouri, Montana, New York, and Oklahoma are

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Dakota, and Utah have been investing certain permanent school funds in farm mortgages. In 1913 Wisconsin adopted a similar policy, authorizing that the state's school fund be loaned to farmers for the purpose of making permanent farm improvements. Another law of the same year provided for the issuance of bonds by counties to enable farmers to clear their lands for agricultural purposes. So far nothing has been accomplished by either law (*Wisconsin Bulletin* 247, Jan. 1915, p. 31). In the early part of 1915 the legislature of Wyoming authorized the state treasurer to invest, subject to certain conditions, the funds arising from the sale of state lands in irrigation bonds. A bill providing for the investment of the state's permanent funds in farm mortgages at not less than 6 nor more than 7 per cent failed to pass. The North Dakota legislature proposed an amendment to the state constitution which, if adopted, will enable the state to establish a loan fund and pledge its credit either to individual farmers or to rural credit associations. In Montana, authority has been given to the state treasurer to issue bonds and make long-term loans to farmers on the security of first mortgages whenever the demand for bonds is equal to the demand for farm loans. Applications and subscriptions are to be received by the county treasurers. To insure prompt payment of interest on the bonds a guarantee fund has been provided by the state. Finally, Missouri and Oklahoma have provided for the appropriation of certain state funds to be used as initial working capital for a system of long-term loans. Additional funds will be obtained through the sale of bonds secured by first mortgages or deeds of trust.

56. *The Banking Laws of Wisconsin*, Revision of 1913, pp. 55-66.

examples of the second type of legislation. If they succeed in accomplishing the definite purpose for which they were enacted, the farmer's rate of interest on long-term loans will be about 6 per cent in Montana and Oklahoma, and 5 per cent or less in Missouri and New York. These rates are well below the rate that is current in the respective states.

The Missouri law<sup>57</sup> is the most drastic of these measures. Briefly, it provides for the establishment of a Missouri land bank, annexed to the office of the state bank commissioner, under the direction and supervision of a board of governors composed of the governor of the state, the attorney general, the secretary of state, the state treasurer, and the state auditor. Loans varying from \$250 to \$10,000 are to be made to farmers up to 50 per cent of the value of their lands for terms of not less than five nor more than twenty-five years. An amortization scheme, borrowed with some inaccuracies from the *Crédit Foncier*, provides for the repayment of the principal within the term of the loan in fixed annual payments consisting of interest, one-half per cent on account of the reserve, and the remainder on account of principal. The law expressly stipulates that loans are to be made only for the ordinary productive purposes, *i. e.*, to complete the purchase price of land, to pay off existing incumbrances, and to make permanent improvements. Of the total amount loaned, 25 per cent may be used for the purchase of stock and machinery.

The initial working capital of the bank, \$1,000,000, is to be appropriated by the legislature from the funds in the state treasury. One-half of this amount will be loaned to applicants at a net interest rate of 4.3 per cent. Thereafter, capital will be provided through the sale of debenture bonds, issued in series of \$500,000, and loaned to farmers at the rate which the bank must pay on the bonds. Whenever there are deeds of trust on hand aggregating \$500,000, a new series of bonds will be issued until the total issue has reached \$40,000,000. Further issues may be made indefinitely at a ratio of \$30 of bonds to \$1 of the reserve.

An effort is made to give the bonds a high standing as invest-

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57. *Laws of Missouri*, 1915, H. B. 877, p. 196. The law can not become operative until December 1, 1916. There was some doubt at the time the measure was proposed as to whether it would be constitutional for the legislature to appropriate \$1,000,000 from the state treasury for the purpose of organizing the bank. To avoid all possible constitutional difficulties it was deemed best to postpone the organization of the bank until the law could be submitted to the voters of the state under the "initiative".

ment securities. Every series of bonds will be secured by a like amount of deeds of trust on farm lands within the state appraised at double the face value of the bonds. For the purpose of insuring careful appraisal, the state is to be divided into districts and an expert appraiser appointed for each district at a salary of \$2,000. The appraiser is to have the coöperation of local banks in securing information relative to the applicant for a loan, and the services of state and county officials in passing upon title abstracts. These services are to be rendered without fee. Furthermore, the bonds will have as security the bank's reserve fund. The board, however, has the discretionary power to refund to each borrower who has made regular payments for at least ten years, the reserve of one-half per cent collected on his payments, or that portion of it which remains after charging it with its share of expenses and loss. When the reserve fund has accumulated to an amount sufficiently large that it will no longer be needed to insure the solvency of the bank, the legislature is to provide for its repayment to the state. Finally, the bonds are exempt from taxation; and in all cases where the law requires a deposit of securities to be made with the superintendent of insurance or the state treasurer, the bonds are to be available for that purpose "as if they were the bonds of the state of Missouri".

The Montana law<sup>58</sup> provides that the state treasurer may issue 5 per cent bonds, secured by farm mortgages, whenever the county treasurers have received sufficient applications for loans and subscriptions to bonds to warrant a series of \$100,000. Smaller bond issues may be made from time to time at a rate of interest agreed upon by all the applicants for loans. Loans will be amortized by semi-annual payments equal to 4 per cent of the face value of the mortgages. One-eighth of each payment or less, in the discretion of the state treasurer, will be used to pay the expenses of administration. The inference is that the farmer's rate of interest will be 6 per cent or less when bonds are issued in series of \$100,000.

The law authorizes the appropriation of \$20,000 from the state treasury to be used as a guaranty fund. In the event of default by a mortgagor, the state treasurer will draw upon this fund to satisfy the holders of bonds, but the amount thus drawn must be restored to the fund either from the proceeds of foreclosure sale or by a

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58. *Laws of Montana*, 1915, ch. 28.

direct levy on all mortgagors benefiting under the same bond issue. The effect of this guaranty on the investment character of the bonds seems to be of doubtful value when one reflects that the mortgages rather than the bonds are to be exempt from taxation.

The proposed Land Bank of the State of New York is an adaptation of the Central Landschaft of Prussia. The law<sup>59</sup> provides that the bank may be formed by ten or more savings and loan associations with aggregate resources of \$5,000,000 when they have subscribed \$100,000 to its capital. On the security of first mortgages made by the local associations and placed in trust with the state comptroller, the land bank may issue bonds, exempt from taxation, up to 80 per cent of the face value of the mortgages so long as its total outstanding indebtedness does not exceed twenty times its capital. A portion of the profits of the bank equal to one-half per cent of the capital must be set aside each year as a guaranty fund until the fund is equal to 15 per cent of its capital.

The savings and loan associations were adopted as the local organizations in the new system because of the excellent law under which they have operated. At present they are among the soundest financial institutions in the state. They can make loans only to members. The property pledged as security for a loan must be located within a radius of fifty miles of the office of the association and loans must be limited to 75 per cent of the appraised property value. Nothing in the law has prevented these associations from lending to farmers but, since they have been dependent on local savings for their capital, their operations have been confined to urban communities.

The new law attempts to overcome these limitations. A savings and loan association having invested in the shares of the land bank, and having no debts or second mortgages, may pledge 75 per cent of its mortgages or other securities for cash or bonds of the central institution. With the funds thus obtained—which can not be in excess of twenty times the share capital it has contributed to the land bank—the local association can make farm loans to members on the amortization plan for terms of forty years. The rate of interest to be paid by the farmer will be the rate paid on the bonds plus a small charge to cover expenses.

The land bank is now fully organized. Over forty associations

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59. *Laws of New York*, ch. 369, art. X.

with total assets of approximately \$20,000,000 have met the organization requirements. The first bond issue of \$250,000, maturing in ten years and bearing an interest rate of  $4\frac{1}{2}$  per cent, has also been authorized. A successful effort is being made to sell the first issue of bonds to the large financial institutions. The funds thus derived from the sale of the bonds will be loaned by the land bank to member associations at 5 per cent. Owing to the coöperative structure of these associations the cost of placing the loans will be comparatively small and the farmer's rate of interest is expected to be well below that rate once the system has become firmly established. At present, the one concern of the organizers is to arouse the interest of farmers in the new system so that they will be induced to become members of the local associations.<sup>60</sup>

The Oklahoma law<sup>61</sup> is the outgrowth of the state's experience in making loans to farmers. Since 1907 that state has been lending its permanent school funds on the security of farm mortgages. Loans limited to one-half the value of land, exclusive of the value of improvements, have been made by the commissioners of the land office for terms of five years at an interest rate of 5 per cent. On the whole the system was well administered, but the number of loans was naturally limited. With a view to supplying the demand for state loans, the new law created another loan fund out of the lands set apart for the benefit of the higher institutions of learning. Loans are to be made for terms of twenty-three and one-half years, with provision for amortization, at an interest rate of 6 per cent. The maximum loan that can be obtained by any one individual or family is \$2,000 and then only on condition that the borrower reside upon the land given as security.

In order to provide sufficient funds for all applicants the commissioners of the land office are authorized to sell without recourse the mortgages taken in part payment for the University lands, or to issue bonds, bearing an interest rate of 5 per cent or less, up to 75 per cent of the value of the mortgages. With these funds additional loans can be made and the commissioners are empowered to issue 5 per cent bonds up to 90 per cent of the value of the mortgages taken for such loans. When the University lands are finally sold, an almost inexhaustible fund will be available for farm

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60. See *Journal of the American Bankers' Association*, Jan., 1916, p. 576.  
61. *Laws of Oklahoma*, 1915, chs. 34, 284.

loans—provided the state has no difficulty in floating the bonds. Although not guaranteed by the state, the bonds will bear the signatures of the governor, the president of the state board of agriculture, and the state auditor. They will be exempt from all taxation except the tax on incomes and will be approved security for the deposit of public funds and legal investments for trust funds. As yet, no bonds have been issued by the commissioners.

Numerous other land credit measures have been seriously considered by Congress and the state legislatures, but the measures already outlined furnish sufficient and conclusive evidence that the land credit problem is being boldly, if not blindly, attacked. With no American precedent to follow and no consensus of opinion as to the kind of land credit machinery best adapted to American conditions, a great deal of irregular legislation has been evolved. Even the members of the commissions who have studied at first hand the various systems in operation in foreign countries seem to have gained little from their investigations except a dignified enthusiasm for reform.

In general, three distinct kinds of legislation have been passed or proposed. On the one hand are the less conservative reformers who would rely upon a scheme of government aid. They would have the state or federal governments engage directly in the business of making long-term loans to farmers at a low rate of interest. In no other way, they claim, can a young farmer secure a rate of interest sufficiently low to make the ownership of a farm a practical certainty. On the other hand, those who are opposed to a government subsidy of any kind, particularly one for the benefit of farmers, insist that there is need only for legislation that will provide new machinery for the mobilization of farm credit at the hands of private initiative. Finally, there are those who, in advocating coöperative organization as a remedy for all economic ills, would transplant with little modification the German *landschafts* to this country.

The dissimilarity of these three proposals is probably due to an incomplete understanding of the land credit problem. The problem is clearly of a two-fold nature. It involves a consideration

not only of the credit needs of landowners, but also of the credit needs of tenants who would become landowners. There is a fundamental difference between the requirements of these two classes. The former require long-term credit for the purpose of equipping the farm; the latter need long-term credit in order to complete the purchase price of land. Those who advocate a program of government loans at a low rate of interest have in mind the promotion of home ownership and the welfare of the tenant classes; while those who would rely upon private initiative or coöperative efforts to reduce the rate are concerned chiefly with the needs of landowners.

In view of the two-fold nature of the land credit problem, two distinct kinds of legislation are needed. No one program of reform is capable of treating both classes of farmers alike without being prejudicial to the interests of the farm tenant. It follows, therefore, that some provision should be made whereby tenants will be encouraged to become their own masters; and, on the other hand, independent machinery should be established to enable landowners to obtain a rate of interest commensurate with the security they have to offer. These two problems of land credit legislation will now be given separate consideration.

## CHAPTER IV

### LAND CREDIT FOR LANDOWNERS

The problem of supplying landowners with capital for the improvement and development of their farms is not a difficult one. It involves merely the establishment of new and specialized machinery which will provide for a longer term of loans, repayment of the principal by amortization, and the elimination of excessive commission charges.

In accomplishing this reform, direct government aid is undesirable and unnecessary. The well established principle that the state, as the guardian of its citizens, should protect the weak against the strong is, fortunately enough, inapplicable in the case of landowners. As a class they are among the most prosperous citizens. To enhance their individual prosperity by extending to them the credit of the state or federal government would be an unwarranted infringement of democratic principles. In all justice the same assistance would needs be granted to merchants, manufacturers, and other individual borrowers. It follows, therefore, that in the establishment of a system designed to extend land credit to farmers on as favorable terms as have been accorded to the commercial and industrial classes by the national and state banking systems, chief reliance should be placed upon self-help and private initiative. Where these individual qualities offer a basis for remedial action, direct government aid would be pernicious and destructive.

Those who advocate coöperative organization among farmers as the proper remedy for a defective land credit system have a point of view which requires more serious consideration. The claim is forcefully made that, with the proper legislative authority, farmers could take the initiative, form coöperative land credit institutions and solve their own land credit problems. In support of the feasibility of such institutions and what they might accom-

plish for the farmer in this country, the advocates of the plan are wont to cite the work of the German *landschafts*.

In general, a *landschaft* is a highly organized association of landowners who are authorized to borrow on collective rather than individual mortgage security. By issuing bonds secured by mortgages on the property of all members they can offer to the investor a security far superior to that possessed by the individual mortgage. The collective guaranty and the requirement that all borrowers be members constitute the fundamental and characteristic features of these associations.

The origin of the *landschaft* was not voluntary. At the close of the Seven Years' War, agriculture was in an impoverished condition and interest rates were high. To relieve the distress of the large landowners who were more deeply involved in debt than any other class, and on whom the burden of the war had fallen heaviest, Frederick the Great forced the nobles of Silesia to form a *landschaft*. Whether the members of the association wished to borrow or not, their lands were made jointly liable for all loans granted by the association.

The Silesian *landschaft* was founded in 1770.<sup>62</sup> Similar associations were founded for Pomerania in 1781, for western Prussia in 1787, and for eastern Prussia in 1788. These were compulsory associations of all the large landowners within a province, whether borrowers or not, and their estates were compulsorily included in the guaranty of the bonds of the association of that province. The four associations thus formed have retained with few exceptions their original characteristics although the actual liability of non-borrowing guarantors has greatly diminished by reason of the fact that the associations have accumulated large reserves to cover possible losses.

At present, there are in Germany twenty-three of these coöperative land credit institutions. Seventeen are located in Prussia, two in Saxony, and one in each of the states of Bavaria, Wurttemberg, Mecklenburg, and Brunswick. With the exception of the Wurttemberg Credit Association, which issues bonds on the security of both urban and rural mortgages, their bonds are secured

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62. Unless otherwise indicated, the facts in regard to these associations have been drawn from J. R. Cahill's *Report to the Board of Agriculture and Fisheries of an Inquiry into Agricultural Credit and Agricultural Coöperation in Germany*. (Sen. Doc. 17, 63 Cong., 1 Sess.) pp. 38-54.

by mortgages on rural property only. For the most part, the associations in Prussia are confined in their operations to the provinces within which they are located. The associations outside of Prussia operate over the whole of their respective states.

The *landschafts* which were formed during the nineteenth century are of a different pattern from the older institutions. An example of their method of organization and operation—although in non-essential matters these later institutions differ from one another—is afforded by the Mortgage Credit Association for the Province of Saxony, founded in 1864.<sup>63</sup> This association is directly under the supervision of a royal commissioner and the minister of agriculture. Its members consist of borrowers who have pledged rural property as security for loans. In general assembly they elect a council of administration which, in turn, appoints a board of directors. One of the members of the board is the general director, another is an active member of the *landschaft*, and among others is a *syndic* who attends to all legal matters affecting the association. One of the most significant powers of the *landschaft* is the power to enforce payment of all debts which are due it without recourse to law.

In every district of the province is a representative of the *landschaft* through whom local business is transacted, subject of course to the approval of the board of directors. Loans are made up to two-thirds of the value of land. The principal basis for determining the value of the borrower's land is the land-tax assessment. If the borrower applies for a loan of twenty to thirty times the net income of the land, no special appraisalment is required. If, however, the applicant calls for a larger amount, two special appraisers are sent as agents of the *landschaft* who, together with the district representative, appraise the land offered as security. If properly secured, there is no limit to the size of an individual loan. On one estate the association has loaned the sum of 3,000,000 marks; on the other hand, a borrower must possess at least four acres of land before he can become a member of the organization.

When all matters pertaining to title and appraisalment have been settled by the *landschaft* and the mortgage has been made out and registered, the borrower receives the amount of his loan in bonds of

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63. The facts in regard to this particular association have been drawn from *Information and Evidence* (Sen. Doc. 214, 63 Cong., 1 Sess.) pp. 363-367.

the association. These are not secured, as were those issued by the older *landschafts*, by a mortgage upon specific property with concurrent guaranty by the association, but represent a claim upon the association for a mortgage claim of like amount. The liability of the borrower is limited to the amount he has borrowed plus 5 per cent. The rate of interest paid on the bonds varies from 3 to 3½ per cent.

In order that the borrower might find a ready market for his bonds, the association followed the example set by other *landschafts* and established, in 1898, the *Landschaft Bank*. The officers of this institution are the officers of the association. It has a working capital of 3,000,000 marks representing the profits and savings turned over to it by the association. Although it conducts a general banking business, its primary purpose is to act as intermediary between the borrower and the ultimate purchaser of his bonds, and to facilitate the amortization of loans which the *landschaft* has made. It therefore buys the borrower's bonds at the current market price for resale to the investor. The borrower pays to the bank the regular interest rate which the bonds bear, one-fourth per cent for the bank's services, and three-fourths per cent yearly for amortization. The earnings which accrue from these operations are carried to the association's surplus fund until the fund has equaled 5 per cent of all outstanding obligations. Since the association has no capital stock and pays no dividends, the excess earnings above the reserve fund are used to augment the borrower's amortization payments thereby reducing the term of his loan.

The amortization payments which are continually being made to the *Landschaft Bank* are used to redeem the *landschaft's* bonds so that there may not be more bonds outstanding than are covered by mortgage security. The bonds are subject to call at par. If the market price is above par, the bank may select by lot sufficient bonds to cancel maturing mortgages; if the price is below par, bonds will be purchased in the open market by the bank or the borrower and the amortization payments will be completed that much sooner. The various *landschafts* make it a regular practice to buy in their bonds when the market is favorable.

In 1873, when a number of associations were having difficulty in marketing their bonds, there was created a Central Mortgage Credit Association for the Prussian State for the purpose of widen-

ing the market for the bonds of the provincial associations. At present, eight of the Prussian associations are affiliated with the central organization. It is managed by a board of directors composed of the leading officials of the affiliated associations. It issues central bonds for its members who have retained, nevertheless, full authority to issue their own bonds as before. If a farmer finds that the bonds of the central landschaft are selling at a better price than are the bonds of his own association, he may request that his bonds be given in exchange for bonds of the central landschaft.

The par value of the bonds of the twenty-three provincial landschafts together with the outstanding issues of the central landschaft amounted at the end of 1910 to well over \$800,000,000. A little more than one-eighth of this amount was represented by central bonds. The volume of the outstanding bonds of the central association was exceeded by the bonds of both the Silesian Mortgage Credit Association and the East Prussian Mortgage Credit Association. It appears that the central landschaft has not been altogether successful, for its bonds have not maintained superiority over those issued by the provincial associations. This is largely due to the fact that the market for such bonds has always been mainly provincial, and furthermore to a strong distaste on the part of the associations themselves for centralized organization.

Experience has shown, however, that the methods employed by the provincial associations for financing the long-term credit requirements of landowners are thoroughly in accord with sound land credit principles. The loans which they grant are not subject to recall. They are repayable at the mortgagor's convenience and the extinction of the debt is accomplished gradually. Owing to the abundant security possessed by their bonds they can be sold on advantageous terms, and the landowner is able to borrow for long-time periods without being subject to the expensive necessity of renewal or to any uncertainty as regards his average rate of interest. In fact the landschaft bonds have, at times, an investment status superior to that possessed by government bonds—if the comparative market prices of these securities are reliable criteria. On June 13, 1913, when the 4, 3½, and 3 per cent government bonds of Germany were selling at 96, 84.80, and 74.80 respectively,

landschaft bonds bearing the same rates of interest were quoted at 100, 96, and 80.50 respectively.<sup>64</sup>

Moreover, the ease with which these institutions mobilize land credit is evidenced by the fact that the borrower's actual rate of interest corresponds very closely to the rate paid on the bonds. He pays, of course, a small entrance fee to his association and contributes moderately to the cost of administration. But these expenses are extremely low, for the principal reason that the associations are non-profit organizations. The directors themselves are landowners and borrowers holding honorary office. They are thoroughly acquainted with the individual needs of landowners and the value of landed property. The management is therefore both efficient and inexpensive. Some associations are able, on account of their large accumulation of funds, to grant loans to members with scarcely any extra charge beyond the immediate expenditure actually incurred.

If it were possible to adapt these institutions to meet the needs of American landowners, both large and small, one phase of the land credit problem would be easily solved. And, indeed, nothing should be done in any way prejudicial to the formation of such organizations. On the contrary, if it is so desired, they should be given legislative sanction under conditions which would allow government supervision and insure careful management. But in the absence of all American precedent in this field of activity it is not likely that a mere enabling act would effectively accomplish the needed results. Unless an association imposed on borrowers a heavy liability in addition to that imposed by their mortgage contracts, the bonds would be regarded with suspicion by conservative investors. Moreover, if additional liability were imposed, *good* farmers would be loath to join an association. Rather than create a lien on their property for the benefit of others, they would prefer to borrow from other sources. Thus the chances for successful organization would be extremely small.

In this connection, it should be remembered that the first associations in Germany were compulsory organizations. It was not until their success had been firmly established that other associations were voluntarily formed. For the most part these associations of borrowers were not coöperative in structure—only two were

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64. Statement of David Lubin, Sen. Doc. 196, 63 Cong., 1 Sess., p. 49.

formed with a capital stock after the manner of a true coöperative credit association. Yet all of them had in their foundation a strong coöperative spirit.

It is this that is lacking with the American farmer. The frontier stage is not far enough in the past to have allowed the development of a coöperative spirit. The farmer is still a strong individualist. Living a comparatively isolated life, he has become accustomed to looking after his own affairs without the assistance of others; and it is seldom that he will brook their interference. On account of the continual shifting of the rural population, the character of his neighbors is ever a matter of uncertainty. There is, moreover, no religious or communal bond to overcome the mutual distrust that frequently arises. These conditions militate strongly against the growth of a coöperative spirit. Furthermore, farmers are suspicious of coöperative enterprise in all its forms. Partly for this reason coöperation in buying and selling has made little headway. The number of failures has been large. It would seem unwise, therefore, to urge the establishment of farmers' coöperative land credit banks until coöperation in its milder and safer forms has secured a permanent footing.

For the present, then, it is unlikely that the *landschaft* form could be successfully adapted to American needs except by limiting rigidly the liability of borrowers and by permitting others than borrowers to become financially interested. But such an institution would differ radically from the *landschaft* form. It would be an association composed of lenders as well as of borrowers. In short, the admission of non-borrowing members seeking pecuniary gain would be a virtual acceptance of the contention that only through private enterprise can the land credit problem of landowners be properly solved. Those who believe in the efficacy of private initiative as a remedial agent for a defective land credit system would advocate the establishment of institutions patterned after the joint-stock mortgage banks of Germany or the *Crédit Foncier* of France.

Of the thirty-seven joint-stock mortgage banks in Germany, the Prussian Central Land Credit Company, organized in 1870, is by far the most important institution of its kind for making loans to landowners.<sup>65</sup> It operates over the whole of Germany and has over

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65. The facts in regard to this institution have been drawn from the *Cahill Report*, Sen. Doc. 17, 63 Cong., 1 Sess., pp. 72-74.

four hundred appointed agencies. It makes long-term loans, varying in size from 1,000 to 6,000,000 marks, up to two-thirds of the value of farm lands as appraised by its own valuation experts. On the security of the mortgages it may issue bonds up to twenty times its original capital of 36,000,000 marks. Provision is made for the extinguishment of loans in  $56\frac{1}{2}$  years by an annual amortization charge of one-half per cent, or in 44 years by an annual payment of 1 per cent. After a loan has been in force for a period of ten years it may be paid off in full if the borrower so desires.

In 1913, the rate of interest paid on the bonds varied from 4 to  $4\frac{1}{2}$  per cent. The rate paid by the farmer exceeds this rate by about one-fourth per cent. He pays, in addition, a charge of two or three per cent of his loan at the time the loan is granted—one-half per cent goes to the state, one-half per cent to the bank, and the remainder is used to cover other expenses. Owing to the greater liberality in the conditions under which loans may be granted, the bank is an active competitor of the *landschafts* in the farm mortgage business.

The capital stock and surplus of the bank is 62,400,000 marks. About one-third of this amount is used as a revolving fund to keep the outstanding bonds equal in volume to the mortgages which secure them. When it is necessary to reduce the number of outstanding bonds, they are purchased by the bank in the open market if the price is below par; otherwise they are called by lot at par. In 1912, the total volume of outstanding bonds secured by mortgages amounted to 802,877,650 marks. The value of rural and urban mortgages held as security amounted to 275,835,053 and 560,948,153 marks respectively. No other German mortgage bank has invested so large a proportion of its funds in mortgages on rural property. Compared with the *landschafts*, its volume of rural mortgage loans is exceeded only by that of the Silesian, the East Prussian, and the Posen associations.

But the bank is not confined in its operations to the granting of loans on the security of rural and urban property. It makes long-term loans to municipalities, towns, parishes, etc., and provides the necessary capital for such loans by issuing communal bonds. Unlike its mortgage bonds these may be used for the investment of trust funds. The bank does not conduct a general deposit business, but its other operations are sufficiently profitable

to enable it to pay liberal dividends to its shareholders. In 1913 the dividend rate on a capital of 44,400,000 marks was 9½ per cent. From 1870 when the bank was organized down to 1912, the average annual dividend rate was 9.13 per cent.

The business of the bank is under the immediate supervision of a special royal commissioner, subject to the authority of the ministry of agriculture. The special commissioner acts as fiduciary agent and must give his consent before any bond issue can be made. He may require a fresh valuation of any property on which a mortgage has been taken or he may refuse altogether to accept a given mortgage as security for bond issues. The president of the bank and members of the board of directors are required to have their appointments confirmed by the Crown. Since the bank enjoys certain special privileges and is under the strict supervision of the government, it holds the confidence of the investing public.

The *Crédit Foncier of France*, organized in 1852, is the largest and most successful institution of its kind in the world. It was the outgrowth of a law of the same year providing for the organization of decentralized land credit institutions. Within a short time, however, the plan came to be regarded with disfavor. Greater centralization was deemed advisable in order to insure solvency, proper governmental supervision, and public confidence. Accordingly, the Land Bank of Paris, the first company to be organized under the law, was authorized to absorb other existing companies. The new institution, officially known as *La Société du Crédit Foncier de France*, was given a subsidy of 10,000,000 francs and was granted a monopoly for twenty-five years. Although the monopoly was never renewed, the bank retained certain special privileges which have practically eliminated all possibility of competition.

The following account of the *Crédit Foncier* has been given by Myron T. Herrick:<sup>66</sup>

“The governor and two subgovernors of the *Crédit Foncier* are appointed for life by the President of the Republic. It is subject to the surveillance of the Treasury Department of the Government, and three of its directors must be high officers of the department. It may use the Government treasuries for the receipt of its

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66. *Preliminary Report on Land and Agricultural Credit in Europe*, Sen. Doc. 967, 62 Cong., 3 Sess., p. 21.

dues and the deposit of its surplus funds and enjoys a reduction in stamp and registration duties.

“Its debentures are registered or payable to bearer, and the claim of a third party to them can not be made in court except in case of theft or loss. Trust and public funds may be invested in them. Its mortgages are exempt from the decennial registration and consequent charges required of other mortgages. It has a cheap and speedy method of ‘purging’ the title of real estate in case of disputes. In the event of default the courts can not grant the debtor any delay and payments due it upon loans can not be garnisheed or attached. It is allowed summary proceedings for attaching mortgaged property in case of violation of contracts. If dues are not paid or if the property deteriorates it may attach and sell the property simply upon notice and publication. During attachment proceedings it has a right to all returns from the estate. The sale may be by auction in a civil court or at a notary public’s office, if the court permits, and no adverse claim to the proceeds of the sale can be allowed until its claims are fully satisfied.

“The regulations under which the *Crédit Foncier* transacts its business are very strict. The mortgage loans must be first liens. The property must have a clear and unencumbered title and yield a certain durable income. Loans on theaters, mines, and quarries are not accepted. The amount loaned on any property must not exceed half its value, or one-third the value for vineyards, woods, orchards, and plantations. Factory buildings are estimated without regard to their value for particular purposes. A borrower can not bind himself to pay a greater annuity than the total annual income of the property mortgaged, while on the other hand the society is not allowed to charge borrowers 0.6 per cent over the rate at which it obtains money on its debentures issued at the time of the loans. An excess of only 0.45 per cent is allowed on loans to municipalities. The outstanding loans and debentures issued must exactly correspond in amounts.

“After paying a 5 per cent dividend the *Crédit Foncier* must set aside between 5 and 20 per cent of the balance of the profits each year for the obligatory reserve, and continue to do so as long as the same does not equal one-half of the capital stock. The investment of this reserve is left to the board of directors. The capital stock of the society must be always maintained at the ratio

of one-twentieth or more of the debentures in circulation and is the primary guaranty of its obligations, especially the debentures. The capital at present is \$40,000,000 divided into 400,000 shares of \$100 each; but authority has been obtained to increase the same to \$50,000,000, represented by 500,000 shares, which will be done before the debentures in circulation pass the legal limit. One-fourth of the capital must be invested in French rentes or other treasury bonds; one-fourth in office buildings of the society, or by loans to French colonies, or in securities deposited with the Bank of France as a guaranty for advances. Shares can not be issued at a price below par. They are nonassessable. The surplus may be loaned on mortgages or to municipalities or may be used in other mortgage business allowed by the statutes; and for buying its own debentures, making advances to borrowers in arrears, or purchasing mortgaged property in foreclosure; and for acquiring commercial paper acceptable by the Bank of France or securities to be deposited with that bank.

“The governor of the *Crédit Foncier* must be the owner of at least 200 shares of stock of the society. He receives a salary of \$8,000. The subgovernors must hold 100 shares each. Their salaries are \$4,000. They perform such functions as are delegated to them by the governor, and in order of their nomination fulfill his duties during his absence on account of illness or other causes. The governor appoints and dismisses all agents of the society and superintends the organization of the service in Paris and elsewhere. He countersigns the debentures and signs the share certificates and all other papers and documents and must strive to promote the interests of the society in every way. The governor is the head of the board of directors, which is composed of himself, the two subgovernors, the auditors, and 20 to 23 directors. This body possesses the administrative powers of the society and is beholden only to the laws and the general assembly of the stockholders for the proper exercise of the same. The three auditors are the guardians of the society. Their duties are to watch, investigate, and make reports. The only power they have is to call extraordinary general meetings of the shareholders.

“The general assembly of the stockholders meets regularly once a year. It consists only of the 200 largest stockholders, of whom 40 make a quorum if they hold one-tenth of the stock of the society.

Each member has one vote for every 40 shares of stock held, but can not cast more than five votes in his own name, nor more than ten in his own name by proxy. He has, however, a right to one vote even though his shares be less than 40 in number. The general assembly receives the report of the governor, and also of the auditors, if any. It elects the directors and auditors and decides on all resolutions or proposals for the increase of capital, the amendment of the by-laws and constitution, and generally on all matters not otherwise specifically provided for.

“The only places outside of France where the *Crédit Foncier* can do business are Algiers and Tunis. Under a clause in its charter which allows it, with the sanction of the Government, to enter into projects for improving the soil, developing agriculture, and to extinguish existing debts on real estate, etc., the society has been authorized to finance drainage projects and to advance money on the paper of the *Sous-Comptoir des Entrepreneurs*, an incorporated association of builders. It may also receive deposits up to \$20,000,000, one-fourth of which must be kept in the Government treasury and the balance invested in Government paper, treasury bonds, or high-class bankable commercial notes and securities. In connection with its banking house it has large deposit vaults.

“The *Crédit Foncier* is permitted to take short-term mortgages and does a big business in that line. But the true purpose of its existence and the greatest part of its operations are the granting of long-time loans. These are made on mortgages to individuals and without mortgage to municipalities and public establishments. The periods run from 10 to 75 years. The annuities required to be paid for amortizing the loan for the average period used are so small as to appear insignificant. The success achieved by the *Crédit Foncier* in popularizing the amortization principle for real estate loans is the chief cause of its great renown. At present its interest rate for mortgage loans is 4.3 per cent per annum, for public establishments 4.1 per cent, and 3.85 per cent for municipalities. The total annuity, including both interest and amortization sum, for a 25 year mortgage loan is a little over 6.5 per cent. With this small annual payment the debt is gradually wiped out, and nothing is left to be paid at the end of the term. The longer the term the smaller the annuity, and vice versa. The loans now exceed \$870,000,000. \* \* \*

“The Cr dit Foncier is obliged to keep the interest and amortization payments in separate accounts, the latter going to create a sinking fund for the retirement of outstanding debentures. As stated above, the amounts of the loans and debentures must balance each other; consequently, as loans are paid up debentures must be paid off. Borrowers have the right to pay in advance, which they frequently exercise, so the proper adjustment of the balance is beyond the control of the society. It is for this reason that the debentures, although calculated to be redeemed synchronously with the loans they represent, have no fixed time for maturity and are callable at option. In each issue a certain number are repayable by lots, with prizes for the lucky holders. A bond last year drew a prize of \$40,000. The right to give prizes at the lottery drawings is one of the special privileges of the society. The debentures are of two kinds—those representing the mortgages are called ‘fonci res’ and those representing the loans to municipalities and public establishments are called ‘communales’. They are issued in series. The smallest denomination is \$20. They may be bought by installments and are the most popular form of investment in France, being held largely by farmers and poor people in the cities. The issue of 1912 for \$100,000,000 at 3 per cent, payable within 70 years, was oversubscribed 18 times. The total land mortgages and municipal indebtedness in France is figured at \$2,800,000,000. Nearly one-third of this is represented by the loans of the society.”

That the land credit needs of landowners can be adequately supplied by institutions conducted for profit is shown by the successful records of the Prussian Central Land Credit Company and the Cr dit Foncier. They have been efficiently managed and carefully supervised. Although differing substantially in the matter of size, both are joint-stock institutions, *i. e.*, associations of lenders rather than of borrowers. They lend on farm mortgage security in conformity with sound land credit principles and mobilize land credit through the issuance of debenture bonds. Owing to the large share capital which they possess and to the rigid supervision imposed by their respective governments, they have retained the confidence of the investing classes.

Undoubtedly some adaptation of these forms would be both

feasible and desirable in the United States. The greater efficiency growing out of private enterprise, the dangers involved in any unnecessary extension of governmental activity, and the improbable success of coöperative land credit render the adoption of any other plan of reform indefensible.

The foundation for some such system is already in existence. There are the numerous farm mortgage companies which, in spite of legislative handicaps and a badly organized system, have been instrumental in reducing the farmer's rate of interest during the last twenty-five years by developing a market for mortgage investments. These agencies would welcome any legislative action designed to promote conservative business practice.<sup>67</sup> In view of the intimacy of their contact with agricultural conditions and what they have already accomplished in the way of mobilizing land credit, it would seem that the first step in any program of reform should be the formulation of some plan for their reorganization.

Much discussion has arisen as to whether or not the new system should be highly centralized. It has been urged, not without a great deal of force, that debenture bonds could not be issued to advantage in this country unless backed by the assets and prestige of a great central institution like the *Crédit Foncier*. In fact, some doubt has been expressed as to whether debentures could be issued at all. On the other hand it is pointed out that the decentralized mortgage banks of Germany, notably the Prussian Central Land Credit Company, occupy a position scarcely inferior to the *Crédit Foncier* as bond issuing institutions; and that decentralized banks would be better adapted to deal with American conditions.

In considering this question of centralization, the United States Commission came to the conclusion that, although a central land credit bank having the sole power to issue debenture bonds would command a wider market in the sale of its securities, a system of competitive farm land banks would be more in conformity with the character of American institutions and would, therefore, be better adapted. This opinion seems to be well founded. Public sentiment in the United States is strongly opposed to centralization in banking power—an attitude that is deserving of much weight in

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67. See pamphlet entitled *Recommendations of the Farm Mortgage Bankers' Association of America with reference to H. R. 6838 and S. 2986*, Chicago, Feb. 15, 1916.

devising a feasible plan of reform. The commission, however, went too far in recommending that banks be allowed to organize with as small a capital stock as \$10,000. If European experience has anything to offer with regard to the formation of joint-stock mortgage banks, it is that they should have a large share capital and should be carefully supervised by government officials. The smaller the banks and the greater their number, the less rigid would government supervision become.

It is true that the American investor is distrustful of debenture bonds. He prefers to hold a mortgage lien on a specific and tangible piece of property regardless of the fact that the ultimate security for his loan is earning capacity rather than property. This preference is clearly shown in the attitude of American investors toward railroad debentures—although the market for these bonds has steadily improved. But collateral trust bonds more nearly resemble in character the bonds that would be issued by an established land-mortgage bank than do railroad debentures. These are frequently sold at high prices. The Northern Pacific-Great Northern collateral trust 4s, secured by the stock of the Chicago, Burlington and Quincy Railroad Company, have steadily sold close to par. Many other issues secured by stocks and bonds having a definite income yielding power are well thought of in financial circles.

There is no good reason why the bonds of well regulated farm land banks should not attain a similar standing once the public has become accustomed to the debenture securities. The chief reason for the present attitude of distrust toward these bonds is that the memory of the old farm mortgage craze and its disastrous results still lingers. After 1870 scores of investment companies were formed in the Middle West to make loans on city and rural property. The principal market for their bonds and mortgages was located in the New England and other Eastern States. Their promoters were over confident, their methods faulty, and for the most part they were grossly mismanaged. When the western boom collapsed in the early nineties, these unregulated companies, with few exceptions, failed. Farms mortgaged for more than they were worth were abandoned, interest could not be paid on debentures, and investors refused to renew their loans at maturity. Had their mortgages been drawn for longer terms and the companies them-

selves been subjected to regulatory laws, the effects of the collapse would not have been so cumulative. As it was, the failure of a few large companies involved others until the disaster became widespread. Only those who held on to their investments either because they were unable to dispose of them or because they were confident of a return of prosperity, recovered their losses with the subsequent rise in property values.

The few companies that survived this collapse of real estate and farm values are now the strongest and most prosperous institutions of their kind. One of those is the Pearsons-Taft Land Credit Company of Chicago, established in 1865. It is by far the oldest and largest concern in the United States engaged exclusively in the business of making farm loans. It now has outstanding loans to the amount of \$16,000,000 secured by farm mortgages in eighteen states. About three-fourths of these loans are held by its clients in the form of individual mortgages. The balance is held by the company or deposited with the Illinois Trust and Savings Bank under a carefully prepared deed of trust as security for debenture bonds. On April 12, 1916, the official statement of the company showed that bonds to the amount of \$3,843,262 were outstanding. The rate of interest which the debentures bear has varied from 4 to 5.3 per cent according to market conditions. They are issued for terms of twenty years and are secured not only by a like amount of farm mortgages but also by a capital stock and surplus of \$220,000. Since 1900 the company has been making long-term loans repayable by amortization, but thus far the number of such loans has been small in comparison with the total volume of business.<sup>68</sup>

Evidences of renewed confidence in land-mortgage bonds are not lacking. An example of a farm mortgage institution, more recently formed, which has been successful in issuing debenture bonds is afforded by the Woodruff Trust Company of Joliet. This company, organized under the general trust company laws of Illinois, has been issuing land-mortgage bonds for the past four years. It has a capital stock of \$500,000, a majority of which is owned by the stockholders of the First National Bank of Joliet. It makes long-term loans, repayable by amortization, on the security of farm lands at 6 per cent. A loan of \$1,000 is amortized

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68. The writer is indebted to Oren E. Taft, President of the Pearsons-Taft Land Credit Company, for the facts in regard to the business of this company.

by forty semi-annual payments of \$43.26. On the combined security of the mortgages held in trust, the company issues bonds to the public at 5 per cent and invests the proceeds in further agricultural loans. This process leaves a margin of profit sufficiently large to enable it to pay liberal dividends to its stockholders. Although the company is confined in its business operations to a very restricted territory, a statement of its financial condition on May 1, 1916, showed bonds and guaranteed mortgages outstanding to the amount of \$1,361,718, a gain of 100 per cent over the outstanding issues of the previous year. Its close affiliation with the First National Bank of Joliet reduces materially the expenses of operation.<sup>69</sup>

Many other companies are in the organization stage. In Wisconsin there has been organized a corporation known as the Wisconsin Mortgage and Security Company, with a capital stock of \$100,000. All of its stockholders are bankers intimately acquainted with agricultural conditions throughout the state. It is expected that the company will acquire first farm mortgages from local banks, place them with a trustee under an indenture of trust and issue bonds against them. This institution will merely supplement the state controlled system of rural credits adopted by Wisconsin in 1913.<sup>70</sup>

In Kansas there is being organized the Kansas Land Credit Trust Company with a capital stock of \$500,000. It is planned to have the stock widely scattered over the state; to be owned, in fact, by the stockholders in land credit banks. One of these institutions will be established in each county. The local institution will make long-term loans at 6 per cent, turn over the mortgages to the central trust company, and debenture bonds will then be issued against them. Once this system is fully organized it ought to be successful. With a widely scattered body of stockholders, the difficulties heretofore encountered by land-mortgage companies in educating the farmer to a proper understanding of long-term loans and amortization will have been largely overcome. Besides, in providing for an organization extending into every agricultural section of the state, the business of making farm loans can be carried on with a com-

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69. See *Rural Credits in Operation*, an address delivered by George Woodruff before the convention of the Southern Commercial Congress at Muskogee, Oklahoma, April 27, 1915.

70. See *Journal of the American Bankers' Association*, Nov., 1915, p. 393.

paratively small margin of expense and the volume of transactions ought to be sufficiently large to assure liberal returns to the stockholders.

Finally, it is noteworthy that two small companies formed in Wisconsin under the law of 1913 have sold approximately \$100,000 of land-mortgage bonds bearing 5 per cent,<sup>71</sup> while the Land Bank of the State of New York, organized under the law of 1914, has sold its first bond issue of \$50,000 bearing 4½ per cent interest to the Guaranty Trust Company of New York City.<sup>72</sup> Perhaps these laws are open to serious criticism—the former in that it allows bond issuing banks to be formed with too small a capital stock, and the latter for the reason that it has weakened the financial stability of the savings and loan associations.<sup>73</sup> Yet their operation thus far lends strength to the conviction that land-mortgage bonds can be successfully utilized to mobilize land credit in this country.

When provision has been made for the incorporation and regulation of land-mortgage banks, authorized to make long-term loans on the security of farm lands and to provide capital through the sale of debenture bonds, the long-term credit needs of landowners can be readily supplied. It is not to be expected that these institutions will greatly reduce the farmer's rate of interest. An improvement in the method of making loans is, under existing conditions, much more to be desired. But by giving greater mobility to private capital and eliminating the expense growing out of renewal commissions, they can at least give the farmer a rate of interest commensurate with the security he has to offer.

Whether these companies should be organized under a state or federal charter is no longer a question of vital concern. It has been strongly urged, however, that inasmuch as the existing laws governing land transfers, title registration, foreclosure, taxation, and other matters pertaining to land are state laws which differ materially from one state to another, the area of operation of a land-mortgage bank should be confined to a single state so that its bonds would be secured by mortgages of uniform quality; and therefore that legislation providing for the formation and control of such institutions logically belongs within the province of state activity.

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71. *Ibid.*, p. 392.

72. *Journal of the American Bankers' Association*, Jan., 1916, p. 576.

73. Cf. *Journal of the American Bankers' Association*, Feb., 1916, p. 675.

Much could be said in favor of state as opposed to federal legislation in this field. But now that the federal government has enacted a rural credit law primarily for the benefit of landowners, there is scarcely any need for the states to concern themselves further with legislation of this kind once they have revised obnoxious laws pertaining to land. The new federal law will undoubtedly hasten this reform in state law. While serious criticism may be directed against its purpose and proposed methods, it will be instrumental, nevertheless, in providing a mobile system of land credit for landowners. It will not, as some have thought, have any far-reaching effect on the welfare of the tenant classes. It does not strike at the cause of the tenancy problem. The credit problem of tenants calls for more radical treatment if land-tenure reform is the goal.

## CHAPTER V

### TENANCY AND LAND TENURE REFORM

In the sense that its citizens were free to become their own masters, the United States was, during the first century of its existence, truly a "free country". The large supply of unoccupied land and the adoption of a liberal policy for its settlement gave to every agriculturist a ready means of independent livelihood. There was, therefore, an approximate equality in opportunity. So long as these conditions existed, a democracy of equality and economic independence was natural and inevitable; and ownership rather than tenancy remained the characteristic form of land tenure.

But in recent years a change in the form of land tenure has gradually been making its appearance. The percentage of farms operated by their owners is, for the United States as a whole, declining.<sup>74</sup> Although this change became apparent long ago in some of the older states, it is only within the last twenty-five years that tenancy seems to have made great headway. In some sections of the country the decline in the percentage of farms operated by their owners has been nothing short of precipitous. According to the *Thirteenth Census of the United States*,<sup>75</sup> 0.7 per cent of the farms in Oklahoma in 1890 were operated by tenants; by 1910 the percentage had risen to 54.8. In Kansas the percentage of farm tenancy increased from 16.3 in 1880 to 36.8 in 1910. A similar increase is recorded for Nebraska during the same period. These are comparatively new states, where one would expect to find a high percentage of ownership, but the increase in the number of

74. The general increase in the percentage of farm tenancy, as reported by the *Thirteenth Census of the United States*, Vol. V, p. 102, is shown in the following table:

Year	Percentage of farms operated by tenants
1880	25.6
1890	28.4
1900	35.3
1910	37.

75. Vol. V, pp. 125-126.

owned farms in the less fertile portions of the western counties has not been sufficient to counterbalance the rapid increase in tenancy in the older sections. In states like Iowa and Illinois, well developed and long settled, the transition from ownership to tenancy has steadily advanced until at the present time there are several counties in which more than one-half the number of farms under cultivation are operated by tenants. Finally, in Alabama, Arkansas, Georgia, Louisiana, Mississippi, South Carolina, and Texas, less than one-half the number of cultivable farms are operated by their owners.

With regard to the number and status of tenants in the Southwestern States, the Manly Report of the Commission on Industrial Relations says:<sup>76</sup>

“Tenancy in the Southwestern States is already the prevailing method of cultivation and is increasing at a very rapid rate. In 1880, Texas had 65,468 tenant families, comprising 37.6 per cent of all farms in the state. In 1910, tenant farmers had increased to 219,571, and operated 53 per cent of all farms in the state. Reckoning on the same ratio of increase that was maintained between 1900 and 1910, there should be in Texas in the present year (1915) at least 236,000 tenant farmers. A more intensive study of the field, however, shows that in eighty-two counties of the State where tenancy is highest, the average percentage of tenants will approximate sixty.

“For Oklahoma we have not adequate census figures so far back, but at the present time the percentage of farm tenancy in the State is 54.8 and for the 47 counties where the tenancy is highest the percentage of tenancy is 68.13.

“Tenancy, while inferior in every way to farm ownership from a social standpoint, is not necessarily an evil if conducted under a system which protects the tenants and assures cultivation of the soil under proper and economical methods, but where tenancy exists under such conditions as are prevalent in the Southwest, its increase can be regarded only as a menace to the Nation.

“The prevailing system of tenancy in the Southwest is share-tenancy, under which the tenant furnishes his own seed, tools, and teams, and pays to the landlord one-third of the grain and one-fourth of the cotton. There is, however, a constant tendency to

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76. *Final Report of the Commission on Industrial Relations*, pp. 127-131.

increase the landlord's share, through the payment either of cash bonuses or of a higher percentage of the product. Under this system tenants as a class earn only a bare living through the work of themselves and their entire families. Few of the tenants ever succeed in laying by a surplus. On the contrary, their experiences are so discouraging that they move from one farm to the next in the constant hope of being able to better their condition. Without the labor of the entire family the tenant farmer is helpless. As a result, not only is his wife prematurely broken down, but the children remain uneducated and without the hope of any condition better than that of their parents. The tenants having no interest in the results beyond the crops of a single year, the soil is being rapidly exhausted, and the conditions therefore tend to become steadily worse. Even at present a very large proportion of the tenants' families are insufficiently clothed, badly housed, and underfed. Practically all of the white tenants are native born. As a result of these conditions, however, they are deteriorating rapidly, each generation being less efficient and more hopeless than the one preceding.

"A very large proportion of the tenants are hopelessly in debt and are charged exorbitant rates of interest. Over ninety-five per cent of the tenants borrow from some source, and about seventy-five per cent borrow regularly year after year. The average interest rate on all farm loans is 10 per cent, while small tenants in Texas pay 15 per cent or more. In Oklahoma the conditions are even worse, in spite of the enactment of laws against usury. Furthermore, over eighty per cent of the tenants are regularly in debt to the stores from which they secure their supplies, and pay exorbitantly for this credit. The average rate of interest on store credit is conservatively put at 20 per cent and in many cases ranges as high as 60 per cent.

"The leases are largely in the form of oral contracts which run for only one year and which make no provision for compensation to the tenant for any improvements which may be made upon the property. As a result, tenants are restrained from making improvements and in many cases do not properly provide for the upkeep of the property.

"Furthermore, the tenants are in some instances the victims of oppression on the part of landlords. This oppression takes the

form of dictation of character and amount of crops, eviction without due notice, and discrimination because of personal and political convictions. The existing law provides no recourse against such abuses.

“As a result both of the evils inherent in the tenant system and of the occasional oppression by landlords, a state of acute unrest is developing among the tenants and there are clear indications of the beginning of organized resistance which may result in civil disturbances of a serious character.

“The situation is being accentuated by the increasing tendency of the landlords to move to the towns and cities, relieving themselves not only from all productive labor but from direct responsibility for the conditions which develop. Furthermore, as a result of the increasing expenses incident to urban life, there is a marked tendency to demand from the tenant a greater share of the products of his labor.

“The responsibility for the existing conditions rests not upon the landlords, but upon the system itself. The principal causes are to be found in the system of short leases, the system of private credit at exorbitant rates, the lack of a proper system of marketing, the absence of educational facilities, and last, but not least, the prevalence of land speculation.

“A new factor is being introduced into the agricultural situation through the development of huge estates, owned by corporations and operated by salaried managers upon a purely industrial system. The labor conditions on such estates are subject to grave criticism. The wages are extremely low, 80 cents per day being the prevailing rate on one large estate which was thoroughly investigated; arbitrary deductions from wages are made for various purposes; and a considerable part of the wages themselves are paid in the form of coupons, which are, in all essential particulars, the same as the ‘script’ which has been the source of such great abuse. Furthermore, the communities existing on these large estates are subject to the complete control of the land-owning corporation which may regulate the lives of citizens to almost any extent. There is an apparent tendency toward the increase of these large estates and the greatest abuses may be expected if they are allowed to develop unchecked”.

There are a number of factors that have contributed to the growth of farm tenancy. In a particular community tenancy may be due to backward educational facilities, to pure inertia on the part of the rural classes, or to a preponderance of foreign-born farmers in the rural population. Or it may be due to the fact that the prevailing type of agriculture lends itself readily to a system of tenant farming. The tenant is seldom equipped for cultivating a large farm intensively. He can cultivate a large farm extensively or a small farm intensively. In the grain-growing sections of the Middle West, for instance, where the size of the farm unit is large and where extensive methods of cultivation are still possible, tenancy has increased rapidly. In the South, tenancy grew out of the agricultural disorganization following the emancipation of the slaves and the breaking up of the large estates shortly after the Civil War.

But the primary cause of the general increase in farm tenancy lies in the fact that land values have risen. The young man who aspires to land ownership can no longer depend upon the generosity of the federal government. On the contrary, if he has only his hands to work with, he is obliged to spend a number of years in apprenticeship, either as a farm tenant or laborer, in order to acquire sufficient capital from his earnings to become his own master. In spite of natural handicaps many succeed eventually in acquiring farms, but owing to the continued rise in land values the possibility of acquiring land from its earnings in the course of a natural life time is gradually becoming more remote.

The close correspondence between land values and the percentage of tenancy in the North Central States, as reported by the *Thirteenth Census of the United States*,<sup>77</sup> is shown in the table on the following page.

The ratio between the value of land and the percentage of farm tenancy is not comparable in all of these states for the reason that they are not uniform in character. Yet in certain contiguous states such as Kansas and Nebraska, Iowa and Illinois, where agricultural conditions are very similar, or in contiguous counties within a state, the ratio of land values to tenancy is fairly constant. In the Southern States, where land values are much lower and the percentage of tenancy much higher, the ratio, while not comparable

77. Vol. V, table 22, p. 122 and table 30, p. 80.

State	Percentage of tenancy	Average value of land per acre
Kansas.....	36.8	\$35.50
Nebraska.....	38.2	41.84
South Dakota.....	24.6	34.70
North Dakota.....	14.3	25.70
Minnesota.....	21.0	37.00
Iowa.....	37.8	83.00
Missouri.....	29.9	41.76
Illinois.....	41.4	94.90
Wisconsin.....	13.9	43.30
Michigan.....	16.0	32.00
Indiana.....	30.0	62.00
Ohio.....	28.4	53.30

to that obtaining in the Northern States, is nevertheless sufficiently uniform from county to county to justify the conclusion that rising land values have been largely responsible for the general increase in tenancy.

If the rise in the value of land had been proportionate to the increase in its productive capacity, it is not likely that tenancy would have increased so rapidly. But at the present time the value of land is speculative. Owing to the exhaustion of the supply of free land and the rapid rise in the prices of farm products during the last fifteen years, there has been a growing confidence in the minds of farmers that the ownership of land is equivalent to the certainty of an unearned increment. All classes indeed have contributed to the speculative spirit. The prosperous landowner, on realizing a surplus from his farming operations, has found it more profitable to invest his funds in additional land than to attempt to increase the productivity of the land he already possessed. Likewise, merchants, bankers, and private investors, equally aware of the possibilities attached to land ownership, have discovered in land acquisition a pleasant and profitable avocation. Much of the land so acquired has naturally been turned over to tenants (many of whom are wholly incompetent) for a cash rental insufficient in some cases to meet the annual tax levy.

The result of this speculative activity has been to raise the value of land far above any investment valuation that could be made on the basis of present productive capacity. Land which yields a cash rent of \$3 per acre may sell for considerably more than \$100.

When the cost of borrowing on farm mortgage security is from 6 to 7 per cent, the natural return from the land is less than one-half the expenses that would be incurred by the prospective purchaser.

That it is more profitable for the man with small capital to rent a farm than to buy one has been clearly demonstrated by investigations of the federal Department of Agriculture.<sup>78</sup> In the summer of 1911, the Department made a farm-management survey of certain districts in Indiana, Illinois, and Iowa. On two hundred and seventy-three farms operated by their owners, it was found that after deducting 5 per cent interest on the capital invested the operators received an average labor income of \$408. On two hundred and forty-seven rented farms, tenants received an average labor income of \$870, and landlords an average interest rate of  $3\frac{1}{2}$  per cent on their invested capital. Where the owners who cultivated their own farms were allowed  $3\frac{1}{2}$  per cent interest on their investment instead of 5 per cent, they received approximately the same labor income as tenants. "One farmer out of every three paid for the privilege of working his farm",<sup>79</sup> expecting to recover his current loss from the natural rise in the value of land.

Thus land speculation, even though the land be cultivated, has given rise to a ratio between farm earnings and expenses extremely unfavorable to ownership by the actual cultivator. So long as this ratio continues, tenancy may be expected to go on increasing. The period of apprenticeship which the man of small means must serve as a tenant must continue steadily to grow longer. This is a situation not to be viewed with complacency. Face to face with the prospect of life-long tenancy, the young farmer of ambition and enterprise is likely to abandon the occupation of farming for the higher money wages and more attractive social life of the city. The gradual decline in the population of many rural communities bears witness to the strength of this tendency. The most vigorous blood has been irreparably lost. Those who have remained on the soil without the vision of economic independence have fallen victims to an enervating environment. Already, there has developed a type of American tenant not far removed in intelligence and mode of living from the level of European peasantry.

Moreover, as a system, farm tenancy is wasteful. The tenant

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78. See *Bulletin No. 41*, United States Department of Agriculture, 1914, pp. 9-12.  
79. *Ibid.*, p. 10.

depletes the soil, neglects the maintenance of farm buildings, and manifests little interest in the application of scientific principles to agriculture. Having no permanent ties to the community in which he lives, he is unconcerned with the betterment of roads, the improvement of educational facilities, or the development of a wholesome community life. These landmarks of tenancy are not easily destroyed.

Finally, experience has shown that a system of tenant farming gives rise to endless friction between the tenant and landowning classes. Sooner or later absentee landlordism becomes the rule. The relation between owner and tenant becomes what Carlyle would have called a "cash nexus", necessitating continual and unfriendly adjustment. These conditions militate strongly against the spirit of American institutions. Concurrently with the growth of absentee landlordism, rural population is divided into classes, landlords and landless, and there arises an inequality in opportunity directly opposed to a democracy of equality and independence.

In a democracy, then, the ideal form of land tenure is ownership. Opportunity to acquire and the right to possess hold for the young man a certain magic which makes for initiative, independence, and citizenship. Unlike the farm tenant, the cultivator who owns his own farm is interested in the welfare of his community and the maintenance of property rights. The contrast is tersely expressed in the well-known sentiment, "Any man would die for a home, but who would die for a boarding house?" Even socialists, strong in their advocacy of collective ownership of all the instruments of production, find difficulty in arguing out of existence the social advantages to be derived from a system of limited holdings. Indeed, in some of the writings of modern socialists there is a tendency to withdraw from the old extreme position and to grant the desirability of small land proprietors. Only through some such concession in doctrine can the socialist appeal arouse any interest among the millions of small farm owners.

Private ownership of agricultural land, where the land is held as the property of the cultivator, does not give rise to great inequality. On the contrary, it fosters that spirit of equality and independence so essential to the welfare and content of the rural classes. In short, landowners who cultivate their own farms are the best type of agricultural workers. Like Jefferson's "cultiva-

tors of the earth", they "are the most valuable citizens. They are the most vigorous, the most independent, the most virtuous, and they are tied to their country and wedded to its liberty and interests by the most lasting bonds".<sup>80</sup>

There are various ways of attacking the tenancy problem in a democracy. One of the simplest devices for this purpose is the tax weapon. If a special tax, say one per cent, were imposed on land not operated by the owner, it would check the growth of absentee landlordism. If, in addition, a progressive tax were imposed on all holdings above a certain minimum value, it would tend to discourage land speculation—one of the primary causes of farm tenancy. There seems to be a strong need for such taxes. For although absentee landlordism has not yet become a positive menace to the democracy of rural life, the speculative character of land values is indicative evidence that the problem will soon emerge. So long as the value of land continues to rise, the owners of large estates will be extremely loath to part with their holdings. And if, perchance, they find the acquisition of additional land to be a burdensome investment in their own generation, they are wont to derive abundant consolation from the assurance that their children will have the benefit of an unearned increment and sufficient soil to support a healthy family tree! Large farms so bequeathed are not likely to be cultivated by the beneficiaries.

Concentration in land ownership has already assumed large proportions. In 1905, the Public Lands Commission reported that "nearly everywhere the large landowner has succeeded in monopolizing the best tracts, whether of timber or agricultural land".<sup>81</sup> In 1915 the Commission on Industrial Relations reported that "the farms of 1,000 acres and over, \* \* \* valued at two and one-third billion dollars, comprise 19 per cent of all the farm lands of the country and are held by less than one per cent of the farm owners".<sup>82</sup> Another investigator has declared that "the drift toward concentration of landownership is alarming; already 5 per cent of the total area of the United States is owned by less than

80. *The Writings of Thomas Jefferson*, (Ford ed.) Vol. IV, p. 88.

81. Sen. Doc. 154, 58 Cong., 3 Sess., p. 14.

82. *Final Report of the Commission on Industrial Relations*, p. 35.

2,000 persons. The holding of lands for speculative purposes has become an evil of menacing proportions".<sup>83</sup>

A progressive land tax together with a special tax on absentees would, if properly administered, have a remedial effect on the tenancy problem. By discouraging concentration in holdings and by reducing the speculative value of farm lands, it would tend to readjust the ratio between farm earnings and expenses so that the ownership of land would not be beyond the reach of the actual cultivator. But it is highly improbable that any such measures could be effectively carried out in this country. The use of the tax weapon for the purpose of social or economic reform has always been attended with difficulties well-nigh insuperable. If it is imposed expressly for the purpose of breaking up large estates, it may easily be evaded. Moreover, it could be imposed in the United States only by the state governments, which, in the past, have shown themselves utterly incompetent to cope with the problems involved in the administration of simple property taxes. Under these conditions it would be futile to hope for a general application of the tax remedy or, if it were applied, to expect the states to accomplish any practical or desirable results.

One of the most drastic proposals that has been made for dealing with tenancy and related problems is that the state, as the guardian of its citizens, should enter extensively into the business of acquiring land and, as the sole landowner, should reduce all farmers to the status of tenants. The advocates of this plan claim, among other things, that it would overcome the vexatious relations that are likely to arise between the farm tenant and the private landowner. Others who have not completely lost faith in the institution of private property would offer a variant and less radical proposal; in effect, that the state should lease the land so acquired in small holdings to cultivators on terms that would render ultimate ownership possible.

The latter method was adopted in a small way in Great Britain in 1908 with the passage of the Small Holdings and Allotments Act.<sup>84</sup> In that country the value of land has come to be excessive on account of the social position which ownership affords, and

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83. Charles W. Holman: *Marketing and Farm Credits*, p. 321. A collection of papers read at the third annual session of The National Conference on Marketing and Farm Credits.

84. For a fuller discussion of the provisions of this act and the effects of its operation, see Herrick and Ingalls, *Rural Credits*, pp. 148-151.

tenancy has long been the characteristic form of land tenure. According to the terms of the Act, designed partly to mitigate the tenancy evil, the government is authorized to acquire, under certain conditions, that portion of any farm in England or Wales in excess of fifty acres and to sell or lease it to a farmer or laborer who desires land for the purpose of cultivation. If the owner and the government can not agree as to what constitutes a fair price for the land, the government may acquire control of it compulsorily.

The effect of this drastic measure has been to make the ownership of large estates less attractive by actually destroying a certain portion of their capital value. Several members of the peerage have been intimidated into converting their ancestral estates into cash lest the government should adopt even more stringent measures looking toward complete land nationalization. Incidentally, the outlook of the British tenant has been substantially improved. From year to year there has been a steady increase in the number of small holdings. Up to 1913, 154,977 acres had been acquired either by purchase or lease for the benefit of the small cultivator.

This piece of legislation was not the first of its kind to be passed by the British government. It was merely an adaptation of the drastic principles that had been successfully employed for a number of years in landlord-ridden Ireland, a country whose history is essentially one of a land struggle. For many generations the Irish peasantry were steeped in misery and poverty due to the prevailing system of large estates and absenteeism. The greater the thrift and industry of the tenant classes the more burdensome their rental obligations became. In years of agricultural prosperity it was the practice of landlords to raise the occupiers' rent, while in adverse years the rental payments fell into arrears. In the years of irregular crop production following the potato famine, the estrangement in the relations between landlords and tenants became acute. Discontent grew into open revolt, the property of landlords was wantonly destroyed, while the rent collectors and eviction bailiffs met with organized resistance from the peasantry.

It was out of these distressing conditions that the Irish land policy arose.<sup>85</sup> In 1870, Gladstone's first land act was passed. It was the earliest definite attempt to deal with the grievances of the

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85. Unless otherwise indicated the facts in regard to the Irish land-purchase legislation have been drawn from C. F. Bastable's article, *The Irish Land Purchase Act of 1903*, *Quarterly Journal of Economics*, Nov., 1903, pp. 1-21.

Irish tenant. It sought not only to provide for an amicable adjustment of the relations between landlord and tenant but also to facilitate the sale of land to tenants. Owing, however, to continued agricultural depression the act failed to accomplish the purpose for which it was intended and further remedial legislation was demanded. This demand was partly met by the act of 1881. It provided especially for "fixity of tenure", a "fair rent", the right of "free sale" of the tenants' interest in rented land, and created a special commission to determine the "fair rent" of the tenants' holdings. It was essentially a rent-fixing act the immediate effect of which was to cause a reduction of more than 20 per cent in the average rentals. But its purchase clauses were unsuccessful and numerous amendments were subsequently made in order to facilitate the transfer of land from landlords to tenants.

The operation of these laws greatly improved the status of the Irish tenants. By 1903 a large portion of the land in Ireland was either owned by the actual cultivators or was held by them at fixed rents. But there was still much dissatisfaction. Landlords, knowing that their proprietorship had been rendered insecure, were desirous of selling their estates, and they were confronted with the obvious difficulty that the only possible purchasers were tenants of limited means. The tenants, moreover, were discontented because they were not always able to acquire complete control of their holdings.

Accordingly, the interests of these two classes were joined by the Irish Land Purchase Act of 1903. This legislation marked the climax in the evolution of the Irish land-tenure reform policy. It was essentially a land-purchase rather than a rent-fixing act. It reconstructed the Land Commission which had been created in 1881 and gave it authority to purchase land with government funds, for resale to tenants, when the owners voluntarily agreed to sell at an estimated price. But the most important method of effecting a transfer of land was by direct agreement between landlord and tenants for the sale of a whole estate. Here the parties concerned were to agree on a price to be paid the landlord; that is, they were to agree to a reduction of the tenants' rent on which the price of land is based. Rents fixed before 1896 were to be reduced at least 20 and not more than 40 per cent before transfer could be sanctioned; rents fixed after that date were to be reduced between

10 and 30 per cent. The Estates Commission—an administrative branch of the Land Commission—was required to accept any agreement between landlord and tenants which satisfied these conditions as to reduction. It could, if adequate reason were shown, sanction sales outside the limits of these maxima and minima reductions. Furthermore, it could acquire lands compulsorily if its offers to purchase were refused.

This legislation and its amendments necessarily involved the credit of the British government. Landowners were to receive payment for their lands in cash, the amount being determined by the annuity which the purchaser agreed to pay. In addition, those who sold their entire estates were to receive a cash bonus of 12 per cent of the purchase price. Funds for these purposes were to be obtained for the most part by the issue of British government stock bearing  $2\frac{3}{4}$  per cent interest. In short, the government virtually forced the landowners to sell their estates and advanced 100 per cent of the purchase price (repayable in instalments) to tenant purchasers. In 1909 the purchaser's annuity was fixed at  $3\frac{1}{2}$  per cent and the period for the extinction of a loan at  $68\frac{1}{2}$  years.<sup>86</sup>

Naturally, the Irish land-purchase policy has been severely criticized. Its critics have condemned it as paternalistic. They have contended that it would tend to destroy individualism and personal initiative. But in view of the results already accomplished such criticism is unjust and unwarranted. The magic of property has given the Irish peasant a new incentive. His industry has increased, the appearance of homes and farm buildings has greatly improved, and the disorder which formerly existed on account of landlord and tenant relations has practically disappeared. In 1915 over 450,000 farmers owned their homes representing two-thirds of all the land in Ireland, whereas in 1876 over half of the land was owned by about 700 men.<sup>87</sup> This transformation has been effected only because an opportunity for self-help and economic independence was offered.

Nearly every European government lends its credit in some form or other for the purpose of helping the poorer classes to help themselves. In Norway, a most interesting and suggestive ex-

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86. Herrick and Ingalls: *Rural Credits*, p. 157.

87. Charles W. Holman: *Marketing and Farm Credits*, p. 317.

periment in state aid to land purchasers has been on trial since 1903. In that year the Norwegian Parliament established the Norwegian Bank for Laborers' Holdings and Dwellings to provide needy laborers or farmers with capital for the purchase of land or the erection of buildings.<sup>88</sup> The main purpose underlying the adoption of this program was to retard the continuous movement of the rural population to the cities. Furthermore, two-thirds of the cultivated farms in Norway were of a size which required the employment of paid laborers. It was thought that by encouraging agricultural laborers to become the owners of their own homesteads a larger supply of labor would be available for the country districts.

The capital of the bank is supplied out of government funds. In 1912 it amounted to \$2,680,000. Its directors are the directors of the Norwegian Mortgage Bank at Christiania and its management is under the supervision of the minister of finance. Loans may be granted for two purposes—either for the purchase of small farms or for the erection or purchase of laborers' dwellings. A small farm is one of not less than 1.24 acres nor more than 4.94 acres of cultivated land, the value of which does not exceed \$804. Loans for the purchase of such holdings are made by the bank to applicants who are Norwegian citizens, who have not previously owned rural real estate, who are capable of cultivating the land, and who do not own property valued at more than \$402. The maximum loan is limited to nine-tenths of the appraised value of the property to be purchased. It may be made directly to an individual with the guaranty of his commune, or the bank may advance the money to a commune for the purchase and subdivision of land into allotments for laborers' dwellings. The maximum rate of interest on these loans is 3½ per cent. They run for terms of forty-two years and the repayment of the principal need not begin until the sixth year.

Loans for the erection or purchase of laborers' dwellings are granted under the same general conditions either to individuals of "moderate means" or to building societies and communes. In all cases they are secured by the tax power of the commune. The land on which the laborer's house is to be located must not exceed

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88. For fuller details in regard to the operation of this system see *Bulletin of the United States Bureau of Labor Statistics*, No. 158, pp. 389-401.

1.24 acres nor must the combined value of house and land exceed \$1,340 in towns or \$804 in the country. Loans of this type bear 4 per cent interest. They are drawn for terms of twenty-eight years and repayment of the principal begins after the second year. All loans whether for the purchase of small holdings or the erection of dwellings may be repaid at any time by the borrower.

The bank may increase its loanable funds, if insufficient, by issuing bonds so long as the outstanding issues do not exceed six times its capital. The bonds bear an interest rate determined by the bank directors. They run for periods varying from thirty to eighty years and are withdrawn gradually by lot. The bonds as well as the loans authorized by the bank are guaranteed by the state. Up to June 30, 1913, the bank had placed 22,600 guaranteed loans, of which 13,140 were for the purchase of land holdings and 9,460 for the erection of dwellings. The total outstanding loans amounted to about \$8,576,000. From the time of the bank's organization, 174 foreclosure sales had been made but with scarcely any loss to the state.

Other notable experiments in state aid to agricultural and, directly or indirectly, to industrial workers are in operation in Denmark and the Australian States. With regard to the Danish system, the federal Department of Labor has given the following account:<sup>89</sup>

“The special advantages which have existed in Denmark for the small peasant proprietors since 1899 are of great interest and importance in the agricultural development of Denmark. A series of laws beginning with that of March 24, 1899, furnished to rural and urban laborers of small means State funds with which to purchase small holdings. Each law was passed for a term of only five years, but so beneficial were the results that no law failed of reenactment. The most recent law now in force is that of June, 1914, which is to continue in force for three years.

“According to this law workmen and other persons of small means between 25 and 50 years of age who are citizens of Denmark may secure a State loan to aid in the purchase of a small holding (2.7 to 10.9 acres) not to exceed 5,000 crowns (\$1,340) in value; the total amount loanable, however, is only nine-tenths of above, the borrower being compelled to supply one-tenth of the purchase

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89. *Bulletin of the United States Bureau of Labor Statistics*, No. 158, pp. 123-124.

price. The borrower pays interest at 3 per cent plus a payment on the principal to make a total payment of 4 per cent a year of the total sum loaned.

“The amounts appropriated under each act in each of the five-year periods to which the act applied are as follows: Act of 1899, \$3,685,000; act of 1904, \$4,020,000; act of 1909, \$5,360,000; act of 1914 (3 years), \$4,020,000.

“These laws have had very beneficial results. The total number of peasant proprietors who, by the assistance of the State fund, became owners of their properties from 1900 to March 31, 1914, was 7,117. The State has loaned in all approximately 33,634,000 crowns (\$9,013,912). That the state has been successful in encouraging the younger farmers to establish themselves as owners is shown by the fact that 3,895 (71.6 per cent) of the 5,441 borrowers concerning whom information is available, up to 1911, were between the ages of 25 and 40, and 1,274 (23.4 per cent) were from 40 to 50 years of age. Over four-fifths (82.2 per cent) of the purchasers of properties were married. Day laborers made up 72.7 per cent, agricultural laborers and domestic servants 9.7 per cent, and other occupations not specified 17.6 per cent.

“The average size of holding purchased was 3.16 hectares (7.81 acres) under the law of 1899, but since 1904 there has been a gradual increase in the size of the farm purchased. Thus under the act of 1909 the average size was 4.22 hectares (10.42 acres).

“The total losses have amounted to only 10,000 crowns (\$2,680).”

In the United States, the problem of tenancy is not so different from the problem in other countries as to warrant a weak or *laissez-faire* policy. Fundamentally, it is a rural problem. While there has also been a steady increase in tenancy among urban workers, the increase has been partly due to the persistent movement of the rural population toward industrial centers—that is, tenancy in the city is deemed preferable to tenancy and isolation in the country. The problem of checking this rural movement is, first of all, a problem of land credit. An effective land-purchase act would not only brighten the prospects of the agricultural laborer and the farm tenant, but, in so far as it succeeded in pro-

moting home ownership among the rural classes, would also lessen the pressure of population in industrial centers and strengthen the bargaining power of industrial workers.

Unfortunately, too little has been accomplished in this country toward making the conditions of rural life more attractive to the younger generation of farmers. It was with this end in view that the rural credit movement originated. But most of the land credit legislation enacted during the past three years for the benefit of the landless farmer is of an exceedingly doubtful character. It is based for the most part on a popular belief that the general increase in farm tenancy is to be attributed to a defective land credit system and that a material reduction in the rate of interest to *all* farmers would enable farm tenants to become their own masters.

The probable effect of such legislation on the tenancy problem seems entirely to have been overlooked. While it is undoubtedly true that the adoption of a land credit system providing for a low rate of interest and a longer term of loans repayable by amortization would enable a man of small means eventually to become a landowner, (true amortization as a method of repaying the principal literally compels the borrower to save) it does not follow that farms thus acquired would be farms of profitable size or that the percentage of farm tenancy would decline. After all, there is an intimate relation between the value of land and the current rate of interest. However strained that relation may become, the value of land is certain to rise in response to a reduction in the farmer's rate of interest. Indeed, there is abundant evidence that a lower rate would only add to the present speculative element in farm land investments. Recently, there have come to the attention of the writer a great many cases where prosperous farmers are incurring heavy mortgage indebtedness at fairly high interest rates and acquiring new land, in the belief that direct governmental aid will enable them ultimately to convert their interest charges to lower rates and to realize a speculative profit on the land thus acquired in advance. Manifestly, legislation which *promotes* the spirit of land speculation by promising higher land values tends not only to make it more difficult for a tenant to acquire in the course of his productive years a farm of the most profitable size, but also to encourage concentration in ownership, absentee landlordism,

and its concomitant, farm tenancy. In short, the effect of legislation which seeks to improve the prospects of tenants by reducing the rate of interest to all farmers may be to accentuate rather than to mitigate the problem.

If any reform measure is to succeed in reducing the percentage of farm tenancy in the United States merely by reducing the borrower's rate of interest, the lower rate must be accompanied by specific limitations on the borrowing power of present landowners. About the only way in which this could be accomplished without resorting to "class legislation" would be through the adoption of a program following out the fundamental principles embodied in the liberal land policy of the federal government. First of all, there should be, in any such scheme of reform, a careful limitation on the amount of long-term credit that could be extended to any one individual. Some attempts of this kind have already been made in current legislative measures. The Missouri law provides that individual loans shall not be in excess of \$10,000, and that applications for loans under \$5,000 shall be given administrative preference. The new Oklahoma law fixes the maximum loan at \$2,000. But even this restriction seems liberal. Certainly, any larger grant would only encourage land purchasers to indulge in the same kind of speculative ventures that have characterized farm land investments for a number of years. Furthermore, an effective policy would provide that loans be made only for the purpose of *acquiring* land and on condition that the land acquired be cultivated by the owner as resident for a definite period of years or until the loan is repaid. These restrictions would virtually, but not technically, prohibit a utilization of the scheme by present landowners and private speculators. A reasonable relation might be maintained between the value of land and its productive capacity; and, with a lower rate of interest, the farm tenant of worthiness and ambition would have better prospects of becoming a landowner.

Whether the government should adopt the foregoing plan and make loans directly to landless farmers solely for the purpose of acquiring land, or should itself purchase large tracts of land—as is the practice of the British government in Ireland—for resale to tenants on easy terms of repayment, is a question that can be decided only in terms of the success of the various experiments as

they are now being conducted. It is probable that the former plan would be more feasible at the present time although perhaps not so effective as the latter. But until machinery has been devised that will make the landless classes the sole beneficiaries of government aid, such aid should be definitely withheld.

Thus far the only piece of American legislation really designed to promote ownership is the Oklahoma law of 1915. If no difficulty is experienced in floating the bonds, an almost inexhaustible fund will be available for Oklahoma tenants at a rate of interest well below the rate that is current in the state. Much permanent gain would result from the successful administration of the law. But, in the opinion of the writer, the problem of land-tenure reform is one of such magnitude as to be beyond the scope of state legislation. After all, state legislation on current problems is notoriously irregular and ineffective. Already the states have shown a disposition blindly to attack the land credit problem. In view of the complex nature of this problem and its intimate relation to the tenancy problem, a strong national policy seems desirable.

The federal government is in a much stronger position than any one state to carry through an effective program. It could market its bonds to better advantage, grant a lower rate of interest to the landless man, and apply a uniform remedy to a common problem. Furthermore, the federal government should have precedence in this field of legislation by virtue of a function it has assumed in the past. For many years it was a liberal donor of the public lands. Its policy made for ownership and democracy. Now that the supply of free land has been exhausted, a program involving special aid to the landless man would be a logical continuation of that policy.

Those who are opposed to this kind of government intervention need carefully to revise their understanding of the land-tenure problem. Eventually democracy will have its way and it would be better to attack the tenancy problem in its infancy than to adopt retributive measures later on. Approximate equality in opportunity rather than in possessions is the goal. Whether this means socialism or a compromise regime is immaterial. This much, however, is certain: to object to a well designed system of government aid to land purchase on the ground that it is unnecessary is to discredit the desirability of democracy; to condemn it as "socialistic" is equivalent to paying one's compliments to socialism.

## CHAPTER VI

### THE FEDERAL FARM LOAN ACT

The passage of a land credit measure by the federal government has at last been accomplished. On July 17, 1916, President Wilson approved the Federal Farm Loan bill,<sup>90</sup> thereby settling for a time a question that has given rise to no small amount of legislative interest. During the past four years repeated attempts have been made to discover a practical formula for constructive land credit legislation. The merits of various programs have been carefully estimated and discussed. Now that the mystery surrounding one of the problems of agricultural finance has been definitely cleared, and a program of reform finally adopted, it is expected that the long-term credit facilities of farmers will be improved in no less degree than the Federal Reserve Act improved the machinery for granting loans to the commercial classes. Incidentally, the new law marks the fulfilment of a party platform pledge, a pledge that was accepted and ardently supported by the President during his candidacy.

It would be beyond the scope of the present discussion to deal with any but the fundamental provisions of the new law. As a piece of legislation it is exceedingly complicated, and far more experimental than the Federal Reserve Act from which its inspiration was originally drawn. That measure was intended to reform a commercial banking system already in existence, while the Federal Farm Loan Act contemplates the establishment of an indefinite number of new institutions to supplement, if not to supplant, the numerous agencies now engaged in the business of making farm loans. Moreover, in recognition of the experimental nature of any one plan of reform, and in view of the conflicting notions as to which plan should be followed, provision is made for the employment of three distinct programs so that by one means if not by

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90. For a chronological history of the bill see Sen. Doc. 500, 64 Cong., 1 Sess., p. 29.

another the law may succeed in accomplishing the definite purpose for which it was enacted.

In the first place, it provides for the creation of a Federal Farm Loan Bureau in the Department of the Treasury under the immediate supervision of a Federal Farm Loan Board consisting of the Secretary of the Treasury and four other members to be appointed by the President. As soon as practicable after the members of the Board have been appointed, they are authorized to divide the country into twelve districts, no one of which may contain a fractional part of any state, and to establish in each district a federal land bank having a capital stock of not less than \$750,000. Shares will be issued in convenient denominations of \$5, and may be purchased by individuals, firms, corporations, and the state or federal governments. In case any part of the required capital remains unsubscribed thirty days after the opening of the subscription books, the Secretary of the Treasury is authorized to subscribe for the balance. Provision is made, however, for the gradual retirement of the stock held by the United States as soon as subscriptions from other sources are found to be adequate.

Beneath this superstructure, the law contemplates the formation of national farm loan associations. These may be formed in any federal land bank district, subject to the approval of the Federal Farm Loan Board and the land bank directors, by ten or more natural persons who are the owners or are about to become the owners of land qualified as security for mortgage loans, and who desire loans in the aggregate of not less than \$20,000. An association thus formed must invest 5 per cent of the amount of each loan in the stock of the federal land bank within its district. Its management will be in the hands of a board of five directors who together with all officers except the secretary-treasurer will serve without compensation unless the payment of salaries is approved by the Federal Farm Loan Board. Only borrowers can become members and while no limit is placed on the number of shares that one might own in an association, no more than twenty votes may be cast by a single shareholder.

After an association has received its charter from the Federal Farm Loan Board, it can make long-term loans within its district up to 50 per cent of the value of farm lands and 20 per cent of the value of improvements at a rate of interest, including commissions,

not to exceed 6 per cent. Such loans may be made only for the following purposes; (1) to provide for the purchase of land for agricultural purposes; (2) to provide "equipment" and "improvements" as defined by the Federal Farm Loan Board; and (3) to liquidate mortgage indebtedness existing at the time when the first national farm loan association is organized in or for the county containing the mortgaged land. The borrower is required to subscribe for stock in his association<sup>91</sup> up to 5 per cent of the amount of his loan, to cultivate the land offered as security, and to repay the principal in annual or semi-annual instalments. After a loan has been in force for a period of five years, additional payments of \$25 or any multiple may be made toward the extinguishment of the principal on regular instalment dates. The longest term for which a loan may run is forty years and the size of individual loans may vary from \$100 to \$10,000.

On the security of the mortgages purchased from and indorsed by the national farm loan associations of its district, each land bank is empowered to issue an equal amount of farm loan bonds, bearing an interest rate not to exceed 5 per cent, up to twenty times its capital and surplus. These may be delivered to the association of which the borrower is a member or, at his option, they may be sold by the land bank for his benefit. In any case he pays the rate of interest borne by the bonds plus an administrative charge which can not exceed 1 per cent of the unpaid principal of his loan. In addition he will pay, as at present, the cost of appraising the land and perfecting the title, together with the legal fees imposed by his state for recording the mortgage, etc.

It is on the formation of national farm loan associations that the internal organization of the land banks is dependent. Until the stock subscriptions of the associations in a federal land bank district have amounted to \$100,000, the officers and directors of the district land bank are to be appointed by the Federal Farm Loan Board. Thereafter, the board of directors will consist of nine members, six of whom, known as local directors, will be chosen by and be representative of national farm loan associations. The remaining three, known as district directors, will be appointed by the Federal Farm Loan Board to represent the public interest. No

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<sup>91</sup>. Stock held by borrowers, as well as the federal land bank stock purchased by national farm loan associations, will be retired upon full payment of loans.

director in a federal land bank may have any official connection with any other institution engaged in the business of banking or in the negotiation of land-mortgage loans.

Some doubt was evidently in the minds of the framers of the law as to whether national farm loan associations would be immediately formed or, if formed, whether they would be sufficiently numerous to reach the great mass of borrowers. Since the land bank system is designed for and largely dependent on the formation of national farm loan associations, the failure on the part of borrowers to form the local organizations might defeat the purpose for which the land banks were established. In anticipation of this contingency the law provides that if within one year after its passage associations have not been formed in a given locality and are not likely to be formed, the Federal Farm Loan Board may in its discretion appoint banks, trust companies, mortgage companies, or savings institutions incorporated under state laws as agents through which federal land banks can make farm loans subject to the same conditions as if they were made through national farm loan associations. Such agents are empowered to negotiate mortgage loans so long as the aggregate of the unpaid principal of their outstanding loans does not exceed ten times their capital and surplus, or until the district in which they are authorized to operate is adequately served by national farm loan associations. In the meantime they will be held liable for the payment of the mortgages they have negotiated and will receive a small commission for their services.

In order to give further protection to the farm mortgage companies already in existence and to make room for private enterprise in the new system, a third possible source of land credit is contemplated. It is provided that any ten or more natural persons may form a joint-stock land bank, under a federal charter, with power to make land-mortgage loans and to issue farm loan bonds. Such banks must have a capital stock of at least \$250,000. They can make mortgage loans and issue farm loan bonds under the same conditions and restrictions as imposed on federal land banks with the following exceptions: (1) the territory within which they may operate is limited to the state where the principal office is located and to some one contiguous state; (2) loans may be made on the security of farm land for any purpose and without restriction as to the amount to be loaned to a single borrower; (3) the

borrower is not required to purchase stock or to cultivate the mortgaged land; (4) the rate of interest received on loans or paid on bonds is not subject to alteration or review by the Federal Farm Loan Board; (5) the bonds of joint-stock land banks can be issued only up to fifteen times their capital and surplus; (6) the bonds must be readily distinguishable from the bonds of federal land banks.

The powers conferred upon the Federal Farm Loan Board in the administration of this intricate system are almost unlimited. In addition to those already indicated, the Board has the following important powers: (1) to exercise general supervisory authority over federal land banks, national farm loan associations, and joint-stock land banks; (2) to grant or refuse any specific issue of farm loan bonds; (3) to regulate the charges imposed on borrowers for appraisal, determination of title and recording; (4) to alter the rate of interest charged on loans by federal land banks so as to secure as much uniformity in rates as possible; (5) to require federal land banks to cooperate with one another in the payment of interest coupons on federal farm loan bonds; (6) to appoint land bank examiners, land bank appraisers, and a farm loan registrar for each federal land bank district and to fix their compensation; (7) to declare the mortgages on farm lands within a state to be ineligible as a basis for bond issues if after investigation it finds that the laws of that state afford insufficient protection to the holders of first mortgages.

An effort is made to give farm loan bonds a high standing as investment securities. Every series of bonds will be secured by a like amount of first mortgages<sup>92</sup> on farm lands. In the appraisal of land there is little opportunity for collusion. Before any mortgage loan is made by a joint-stock or federal land bank it must first have the approval of local appraisers and the special appraisers of the federal land bank district. Likewise, when a land bank applies for the privilege of issuing bonds, the application must be approved by the proper farm loan registrar with whom collateral security has been placed in trust. If, after investigation, the Federal Farm Loan Board finds the collateral unsatisfactory, it may reject the application or demand additional security.

In the case of bonds issued by federal land banks special security

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92. United States bonds may be substituted.

is offered. The bonds of any one of these banks will be secured by the capital, reserves, and earnings of all the federal land banks and by mortgages previously indorsed by agents or by national farm loan associations within its district. Every mortgage so pledged will be further secured by the double liability assumed by borrowers on their stock.<sup>93</sup> And in the event that federal land banks are unable for a time to meet all claims arising on account of the payment of interest coupons and the redemption of bonds, they may rely upon federal assistance. That is, the Secretary of the Treasury is authorized, in his discretion, to deposit government funds with federal land banks and to charge a rate of interest not exceeding the rate current on other government deposits. The aggregate of all sums so deposited may not exceed \$6,000,000 at any one time.

In other respects, the bonds of joint-stock and federal land banks will have similar security<sup>94</sup> and will enjoy similar privileges. All first mortgages executed to land banks and all farm loan bonds are to be regarded as "instrumentalities of the Government of the United States" and as such will be exempt from all federal, state, municipal, and local taxation. The same exemption applies to the capital, reserve, and surplus of federal land banks and national farm loan associations. Farm loan bonds will be lawful investments for all fiduciary and trust funds and may be accepted as security for all public deposits. They may also be purchased by member banks of the federal reserve system.

Finally, the law provides that the Secretary of the Treasury may designate any land bank, federal or joint-stock, as a depository of public money, except receipts from customs, and as a financial agent of the government. This feature of the law is not, like that already referred to, intended to afford relief to land banks when temporarily embarrassed, for the deposits permitted under this section may not be invested in mortgage loans or farm loan bonds. It is merely a skillful manoeuver to aid in establishing the constitutionality of the law.

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93. The law is not clear as to whether those who borrow from agents of federal land banks will be held doubly liable on their stock. See sections 9 and 15.

94. One possible exception to this statement should be noted. While the law imposes double liability on all stock holders in joint-stock land banks, it makes no attempt to fix the same liability on shares of federal land bank stock purchased by the government or the public, presumably for the reason that these shares will be retired when the subscriptions of national farm loan associations have become sufficient to give the land banks their required capital.

In the evolution of this intricate program the knowledge of European practice has been a confusing element. From the very beginning the merits of coöperation as exemplified in the land-schaft system received unanimous recognition. But in view of the individualistic nature of the American farmer the successful adaptation of the coöperative form appeared to be impossible. For this reason the United States Commission favored a system of joint-stock banks, patterned somewhat after the joint-stock mortgage banks of Germany, with the provision that they be organized along coöperative lines if desirable; while others, with a less dignified enthusiasm for reform, favored the more expeditious program of direct government loans.

The present law is obviously designed to reconcile these conflicting proposals. It is founded on the strong conviction that coöperation offers not only the most desirable remedy for the problem of agricultural finance but also one that is entirely feasible if supported by federal assistance. Accordingly, liberal aid is provided and the establishment of the federal land bank system is assured. Lest this preliminary organization fail to inspire the development of a coöperative spirit and the formation of national farm loan associations, federal land banks may still be utilized to make loans through existing institutions. Finally, the law endeavors to provide new machinery for the mobilization of land credit at the hands of private initiative. This portion of the law was not contained in the Hollis-Bulkley bill which formed the basis of the present measure. It was incorporated into the final draft of the Hollis bill as reported by the Joint Committee on Rural Credits only at the instance of those committee members who had served on the United States Commission.

Thus the Federal Farm Loan Act represents a drastic attempt to solve once and for all the farmer's land credit problem. Its specific purpose is of a three-fold nature; *i. e.*, to improve current methods of granting loans, to reduce the waste growing out of excessive administrative and commission charges, and, so far as possible, to equalize interest rates on land-mortgage loans. This is by no means a small program nor can the full effects of its operation be anticipated. Nevertheless, some of the possibilities inherent in the measure are worthy of careful inspection.

In the first place, the law rightly provides for a longer term of

loans and the repayment of the principal by amortization. This provision is in conformity with sound land credit principles. It will obviate a great deal of uncertainty as regards the farmer's rate of interest and will literally compel the borrower to save. The privilege accorded to borrowers of repaying the principal of their loans in annual as well as semi-annual instalments is also well taken for the reason that annual payments will be more convenient for those engaged in specialized farming. There is, however, one feature of the amortization plan that does not take account of the peculiarities of the American farmer, namely, the provision that no extra payment can be made toward the extinguishment of the principal until the loan has been in force for a period of five years. While there is some justification on administrative grounds for this restriction, it will undoubtedly deter a great many borrowers from liquidating present loans or from borrowing under long-term contracts. As a class, farmers are especially optimistic. They are accustomed to loans having a maturity of five years and not infrequently they expect to extinguish the whole of their principal before the expiration of that term. Rather than forego the liberal privileges of repayment now accorded by farm mortgage and life insurance companies, some borrowers will prefer to pay a slightly higher rate of interest.

Another feature of the proposed reform which is not likely to make a strong appeal to the average farmer is the requirement that before loans are granted by federal land banks, the borrower must subscribe for stock in a national farm loan association or, if he borrows through an appointed agent, in the federal land bank itself. Although he may arrange with the federal land bank to advance, as a part of his loan, the price of the stock subscription, the actual cost of appraisal and the determination of title, together with the legal fees and recording fees imposed by the state in which his land is located, his power to borrow on the security of land alone is limited in any case to  $47\frac{1}{2}$  per cent of its value, while his total liability on account of the ownership of stock may become  $52\frac{1}{2}$  per cent. If the experience of one of the so-called coöperative land credit companies now attempting to make loans in this manner in the Middle West may be taken as a reliable criterion, it will require no little effort to induce intelligent farmers to purchase stock, least of all to assume double liability on their shares.

Nor is the additional provision—that the commissions paid by federal land banks to agents or national farm loan associations be deducted from dividends on land bank stock—any material improvement over the present system so far as the actual method of granting loans is concerned. It is meant of course to prevent the payment of commissions in advance. But there are numerous sources from which borrowers can obtain loans up to 50 per cent of the value of cultivable land, and if the size or term of the loan is such as to call for the payment of a large commission, the agent will accept a second mortgage on the land in lieu of cash.

In the second place, no objection can be urged against the well meant purpose of the law in so far as it is designed to reduce the cost of borrowing by reducing administrative charges and by giving greater mobility to funds seeking farm mortgage-investment. The present system of land credit is highly immobile. Owing to obnoxious state legislation, backward methods of farming, and the memory of the real estate collapse of the nineties, capital is still somewhat distrustful of land-mortgage security. Middlemen are everywhere required to direct a flow of capital to agricultural channels, and the machinery which they utilize to bring borrowers and lenders into contact with one another is altogether uneconomical and obsolete. This is especially true in the Southern and Western States where farmers are dependent on foreign capital. In North Dakota and Oklahoma, for instance, the average rate of interest received by one hundred and twenty-six American life insurance companies in 1914 amounted to 5.88 and 5.91 respectively.<sup>95</sup> According to a recent estimate by the federal Department of Agriculture, the average annual commission paid by borrowers in those states amounts to 1.8 per cent.<sup>96</sup> Such charges add materially to the borrower's rate of interest. In the Eastern States, the commission charge is a less important element in the cost of borrowing because of the large supply of local capital.

The device to be employed in mobilizing land credit to better advantage is the farm loan bond. In principle, bonds issued on the collective security of farm mortgages are well adapted to this purpose. They ought, as in European countries, to be the means of drawing capital from centers where it is now redundant to those

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95. *Supra*, p. 31.

96. *Supra*, p. 33.

agricultural sections where the supply of local capital is inadequate. Moreover, within a given community they should make a large quantity of capital ordinarily diverted to other channels available for agricultural purposes. The only reason why such machinery has not been utilized more extensively in recent years by farm mortgage companies is because of the popular distrust manifested toward unregulated land-mortgage bond issues. Only a few of the strong companies whose reputation for integrity and conservatism is of the highest standing have been able to sell debenture bonds. Owing to the strict federal supervision that will be given to the land bank system, the difficulties that would otherwise be encountered in marketing land-mortgage bonds should be largely overcome.

The specific mechanism intended to reduce the administrative charge will vary in its effects according to the source of credit. In all cases the yearly charge for commission, which is included in the borrower's rate of interest, is limited to 1 per cent of the unpaid principal, and other charges made to borrowers on account of appraisal and the perfection of titles will be regulated by the Federal Farm Loan Board. When loans are granted by national farm loan associations or appointed agents of federal land banks, a commission charge of not more than one-half per cent may be retained by the institution making the loan. The remainder will contribute to the profits of the federal land bank and may be partly recovered by borrowers in the form of dividends on stock. The significance of this arrangement is that those who borrow through national farm loan associations will pay the lowest possible administrative cost. They will share not only in the profits of a federal land bank, in common with those who borrow from appointed agents, but also in the profits of the association to which they belong. Borrowers from joint-stock land banks will recover no portion of the administrative charge, unless of course they happen to be stockholders.

Manifestly the framers of the law cherished the hope that national farm loan associations would be immediately formed; and there is good reason to believe that many such associations will be organized in those communities where religious or communal bonds already exist. Others will undoubtedly follow as soon as the success of the initial organizations has been established. But too much should not be expected of these associations. Farmers as a class are not possessed of a coöperative spirit. They have not

yet reached the stage where they will care to have their personal affairs a matter of common knowledge. Nor has their time become so valueless that they can afford to devote it gratuitously to the organization and management of associations from which others will receive an equal benefit. Under these conditions it is not likely that the greater economies offered by the national farm loan association will be sufficiently attractive to *good* farmers to induce a majority of them to organize. Certainly, those who live in the newer sections of the country will prefer to borrow from agents of federal land banks or from institutions conducted solely for profit.

The position that joint-stock land banks will occupy in the new system is also a matter of some uncertainty. If formed, they should prove to be attractive sources of credit to those who prefer to deal with private institutions. Borrowers would not be obliged to purchase stock, to cultivate their mortgaged land, or to expend their loans for specific purposes. Nor would there be any restriction on the amount that might be loaned to a single individual. But in other respects the law imposes such onerous restrictions on the powers of these banks as to discourage their formation. Why, for instance, should they not be allowed to operate in more than two states if they can do so with profit? It is a basic principle with those institutions that are noted for their conservatism in making farm loans to operate over an extended territory. The Pearsons-Taft Land Credit Company of Chicago has loans outstanding in eighteen states.<sup>97</sup> The Union Central Life Insurance Company of Cincinnati has gradually extended its farm loan territory until it now operates in thirty-four states.<sup>98</sup> Considerations of safety demand widespread investments. Similar considerations would demand that an institution having the power to issue farm loan bonds be allowed to make land-mortgage loans in several states. It is obvious, therefore, that the rigid limitation on the investment field of joint-stock land banks will not only detract from the security of their bonds but it may also prevent the large farm mortgage companies now operating over a wide territory from reorganizing under a federal charter.

Another discomfoting feature that will be prejudicial to the reorganization of farm mortgage companies is the requirement that

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97. According to a personal letter from Oren E. Taft, president of the company.

98. *Annual Report*, Dec. 31, 1915, p. 5.

loans made by joint-stock land banks must be approved by the Federal Farm Loan Board before they can be pledged as security for farm loan bonds. In practice this restriction could have but one effect, namely, that as a matter of prudence joint-stock banks would not make loans until they had first been approved by the federal authorities. And in the meantime borrowers might seek the prompt service accorded by other agencies.

It is extremely unfortunate, if private enterprise is to play a prominent role in the new system, that more leniency was not shown toward the joint-stock land banks. In other countries they have been found to be well adapted to the mobilization of land credit, and, although their earnings are not excessive, capable of operating profitably in competition with coöperative and state aided ventures. These facts seem to have been appreciated only in part by the members of the Joint Committee on Rural Credits. For with a view to *equalizing* the profits that might be made by federal and joint-stock land banks they limited the bond issuing power of joint-stock banks to fifteen times their capital and surplus.<sup>99</sup> This action was in virtual recognition of the superior efficiency of private enterprise when given an equal opportunity. It is inconceivable why the opportunity should have been withheld.

A third purpose of the law is to mobilize land credit so effectually that interest rates on mortgage loans will be equalized. The equalization of these rates, varying from 5.3 per cent in New Hampshire to 9 and 10 per cent in the Southern and Western States<sup>100</sup> is expected to be a simple matter. Farm loan bonds will be well secured. Those issued by federal land banks will offer a number of attractive features not possessed by European land-mortgage bonds. To make certain that approximate uniformity in interest rates will be realized, the law fixes the maximum rate to be paid on bonds at 5 per cent and the highest rate, including commissions, to be paid by farmers at 6 per cent. As a precautionary provision, however, the limitation on interest rates is worse than useless. Either the high rates paid by farmers in the South and West will be reduced to conform to the legal maximum or investors will be unwilling to purchase the bonds of land banks operating in these

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99. See *Report of the Joint Committee on Rural Credits*, House Doc. 494, 64 Cong., 1 Sess., p. 14.

100. *Supra*, p. 33.

sections. In view of the abundant security offered by the bonds of federal land banks the latter possibility seems doubtful.

The successful operation of the law, then, will result in the equalization of farm mortgage rates. Farmers in the South and West with inferior security<sup>101</sup> will be able to borrow on as favorable terms as the farmers who live in the older agricultural sections. The demand for a material reduction in the current rate of interest will have been fully met. But in responding to this ubiquitous demand, there appears to have been no justification for drastic action. While it is true that the farmer's rate of interest is higher than the rate paid by *some* industrial and commercial corporations, the vendors of such comparisons forget that farming as a business is highly individualistic and is likely to remain so. If the farmer's rate of interest is excessive it is not because it is higher than the rate paid by corporate enterprises or by European farmers but because it is so much higher than the rate received by the ultimate lender. The difference represents the cost of mobilizing land credit under a wasteful and badly organized system. A more economical organization rather than an approximate equalization of rates should have been the goal of remedial legislation.

Serious consequences may follow if the set purpose of the law is fully realized. A material reduction in the current rate of interest, unaccompanied by careful restrictions on borrowing power, is opposed to the welfare of the tenant farmer who aspires to land ownership. The potential effect of lower rates is to promote the spirit of land speculation, raise the value of land, and only further the movement toward concentration in ownership. These conditions, in turn, invariably breed farm tenancy and absentee landlordism. It is unfortunate that the present law takes so little account of such contingencies. It contains no definite restriction that will effectively prevent land speculation. Although the borrowers who depend upon the federal land bank system are required to engage in the cultivation of their mortgaged land and to expend their loans only for the most specific purposes, residence on the

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101. Some would insist that their security is not inferior, on the ground that the land is actually better in many cases than land in Iowa, Illinois, and Southern Wisconsin. But this point of view fails to take any account of the purpose for which land is used. Crops are the sustaining element in farm loans. Where one-crop systems are in vogue land is highly speculative in value even though it is regularly cultivated. Until a more diversified culture has become prevalent in the South and West, farm lands in those sections will be inferior as security for mortgage loans no matter what system of land credit is adopted.

land is not made a condition of borrowing. Moreover, the maximum loan that can be granted to a single borrower seems much too large. It should at least have been limited to the amount necessary for the acquisition of a farm of profitable size—a farm that could be cultivated in a profitable manner by one operator. Finally, it should be remembered that not one of these restrictions is imposed on those who borrow from joint-stock land banks.

Perhaps a great deal will depend upon the course that is followed by the Federal Farm Loan Board in the interpretation of its powers as to whether or not the land bank system will prove positively harmful. The law is ambiguous and indefinite on a number of points. It is not clear, for instance, whether the Board has power to regulate the rate of interest paid on farm loan bonds.<sup>102</sup> But it does have power to refuse to authorize any specific issue and it might exercise that power tacitly on the ground that the rate borne by the bonds was too high or that the underlying mortgages represented loans made for speculative purposes. If, therefore, the Board places a liberal construction on its powers and, in coöperation with the land bank directors, rejects a large percentage of the applications for loans—as is the practice in New Zealand and Australia where systems of state loans are in force—the spirit of land speculation might be kept within present bounds. But the small borrower is the one who would suffer most from this policy because he is not usually possessed of unquestionable security. In either case the system would play into the hands of those land-owners who are already prosperous.

On the whole the law is a badly disguised attempt to establish a system of government loans, under the cloak of coöperation, where government loans are not needed. It is essentially a land

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102. Section 16 provides that "joint stock land banks shall not be subject to the provisions of subsection (b) of section seventeen of this Act as to interest rates on mortgage loans or farm loan bonds". The subsection referred to gives the Federal Farm Loan Board power "to review and alter at its discretion the rate of interest to be charged by Federal land banks for loans made by [italics are the author's] them under the provisions of this Act, said rates to be uniform so far as practicable". Nothing is contained in this subsection relative to the interest rate on bonds of federal land banks. But subsection (f) of the same section gives the Board power "to prescribe the form and terms of farm loan bonds"; and section 20, dealing with the form of farm loan bonds, says "they shall have interest coupons attached, payable semi-annually, and shall be issued in series of not less than \$50,000, the amount and terms to be fixed by the Federal Farm Loan Board". If by "terms" is meant the rate of interest, the law is contradictory. Such an interpretation would give the Federal Farm Loan Board power to regulate the rate of interest on bonds of joint-stock land banks, and section 16 would flatly deny that power. If the word "terms" is not meant to include the rate of interest, then a portion of section 16 is meaningless as it attempts to exempt joint-stock land banks from restrictions that are not imposed.

owner's measure and one that will prove to be cumbersome and needlessly expensive in its operation. Federal land bank stock owned by the government will not share in dividend distributions; members of the Federal Farm Loan Board will receive an annual salary of \$10,000 together with all necessary traveling expenses; the salaries of the twelve farm loan registrars, the numerous land bank examiners, the attorneys, experts, assistants, clerks, laborers, and other employees required to conduct the business of the Board will likewise be paid by the tax payers. For the sake of simplicity and economy the problem of supplying landowners with adequate land credit facilities should have been left entirely to private initiative, subject in some measure to the same administrative authority that now supervises the national banking system. Or if a system of government loans was regarded as the only *desirable* solution of the land credit problem, the so-called McCumber amendment which passed the Senate in February, 1915, might well have received more serious consideration. Although defective both in principle and purpose, it at least offered a plan having the combined merits of simplicity, economy, and certainty. It would have utilized to better advantage the institutions already in existence and, if found to be ill-adapted or grossly defective, could easily have been abandoned.

After all, there was no necessity for any kind of federal legislation affecting the land credit problem of landowners. That problem is of a comparatively simple nature and rightly belonged within the province of state legislation. There is, however, the more pressing problem of land credit with which the federal government should have been deeply concerned, namely, the problem of making the conditions of country life more attractive to the *younger* generation of farmers. In accomplishing this end some form of land-purchase legislation is needed. In the long run no other course of action seems capable of checking the growth of tenancy and the depopulation of rural communities. Doubtless the framers of the present law were sincere in the belief that by applying one remedy to a two-fold problem these tendencies would be stayed. But in reality they seem only to have given a subsidy to present landowners, a subsidy that may aggravate rather than mitigate the problem of tenancy. It will now remain for the states to attack

this important problem, as they have attacked others, by applying unlike remedies to a common ill when uniform treatment should be administered.