# ARTICLE

# RISK, DISCRETION, AND BANK SUPERVISION

Peter Conti-Brown & Sean Vanatta*

*This Article argues that an old but overlooked form of governmental oversight—bank supervision—sits at the center of two foundational tensions in the governance of the American economy. The first is the extent to which the financial system is controlled by public actors (i.e., the government) versus private actors (e.g., the banks). The second is the extent to which the contest for that control is regulated by bright-line rules versus by the exercise of regulatory discretion. On the first tension, this Article argues that supervision is the public and private participation in financial risk management, such that public actors cannot relinquish control of residual risk while private actors do not relinquish control of frontline risk management. In this sense, risk management is shared, but not shared equally: bank supervisors represent a government that has essentially guaranteed the resilience of the financial system through formal and informal commitments. Supervision is the part of the government that is created and evolves— however imperfectly—to manage those relationships, guarantees, and commitments. The second tension, between*

* Peter Conti-Brown is the Class of 1965 Associate Professor of Financial Regulation, The Wharton School of the University of Pennsylvania; Nonresident Fellow in Economics Studies, The Brookings Institution. Sean Vanatta is Senior Lecturer in Financial History and Policy, University of Glasgow. For important and thorough comments, we thank Dan Awrey, Brian Feinstein, Howell Jackson, Kate Judge, Jeremy Kress, Saule Omarova, Rory Van Loo, David Wishnick, David Zaring, and participants in the Wharton FinReg workshop. We thank too James Blume, Sophia Rosser, and Caroline Hackley for research assistance. This article draws from and expands on our forthcoming book, PRIVATE FINANCE, PUBLIC POWER: A HISTORY OF BANK SUPERVISION IN AMERICA (2025).

*rules and discretion in managing those commitments, represents the defining ethos of bank supervision. The process of supervision is not simply the verification of compliance with laws promulgated by Congress; rather, it is a flexible use of discretion within a system whose boundaries are defined by rules that are intentionally broad and vague. This last point is of profound importance in the post-Chevron era: as regulations receive less deference in courts, supervisory assessments will likely expand in importance even further.*

*Using the rich history of supervision in the United States from the antebellum period to the present, this Article presents a theoretical conception of supervision as the space where bankers and the government engage each other in sometimes cooperative, sometimes contentious disputes with substantial influence on the direction of financial and economic policy. This conception of bank supervision makes important contributions to our understanding of issues of importance to banking, such as climate change finance and deposit insurance, but also has important implications for administrative law, constitutional law, and the evolution of state capacity in the United States in the long 20th century.*

## INTRODUCTION: BANK SUPERVISION AND THE STRUCTURE OF AMERICAN FINANCE

This Article argues that two of the most important debates about American state capacity in general, and banking and finance in particular, are better understood as part of the same conversation. First, scholars and policymakers argue whether the financial system is, or should be, public or private.[1] This debate raises the question whether scholars and policymakers should treat private initiative as the defining ethos in the provision of financial services, or whether these services are sufficiently essential to justify their

[1] *See, e.g.*, Saule Omarova, *The People's Ledger: How to Democratize Money and Finance the Economy*, 74 VAND. L. REV 1231 (2021); Lawrence H. White, *The Dynamics of Competitive Coinage: Evidence from Private Mints in the American Gold Rushes* (GMU Working Paper in Economics No. 19-41, 2020), https://ssrn.com/abstract=3499386 [https://perma.cc/6MLK-M7UL].

reconceptualization as a "public good" subject to associated regulations.[2]

Second, scholars and policymakers debate whether the exercise of public power over the financial system should be based in rules, to ensure compliance with the principles of due process and the rule of law, or subject to supervisory discretion, to ensure adaptability and flexibility.[3] On the one hand, some have argued that because a substantial majority of the interactions between the government and the financial system are not rooted in these rule-of-law traditions, discretionary supervision itself "sits uncomfortably with the responsibilities of government in a democracy."[4] On the other hand, enforcing a rigid rules-based approach to supervision may constitute what legal scholar Jeremy Kress regards as part of an overall "war on supervision" that the banking agencies allegedly waged during the Trump Administration.[5]

This Article presents a view of banking and bank supervision that unites these debates into a single intellectual framework.[6] Supervision is an unusual form of government

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[2] *See, e.g.*, Morgan Ricks, *Money as Infrastructure*, 2018 COLUM. BUS. L. REV. 757 (2018).

[3] *See, e.g.*, Randal K. Quarles, Spontaneity and Order: Transparency, Accountability, and Fairness in Bank Supervision (speech before the Am. Bar Ass'n Banking L. Comm. Meeting, Wash. D.C., Jan. 17, 2020), https://www.federalreserve.gov/newsevents/speech/quarles20200117a.htm [https://perma.cc/NSG2-F89J]; Jeremy Kress, *The War on Bank Supervision*, YALE J. ON REG. NOTICE & COMMENT, Dec. 18 2020, https://www.yalejreg.com/nc/the-war-on-bank-supervision-by-jeremy-kress/ [https://perma.cc/3PLA-VKUR]; Daniel K. Tarullo, *Bank Supervision and Administrative Law*, 2022 COLUM. BUS. L. REV. 279 (2022).

[4] Quarles, *supra* note 3, at 3.

[5] Kress, *supra* note 3.

[6] The study of bank supervision is growing substantially. In Dec. 2020, the Federal Reserve, Harvard Law School, and The Wharton School hosted a rare joint conference on the subject and produced four literature reviews of bank supervision from the perspectives of law, economics, history, and international practice, that summarize the challenges and opportunities that scholars and policymakers confront in defining the field. *See* Julie Andersen Hill, *Bank Supervision: A Legal Scholarship Review* (Univ. of Ala. Legal Stud. Rsch. Paper No. 2627472, 2021),

power that evolved fitfully during the nineteenth century before becoming more concrete after the banking panics of the Great Depression. We argue that bank supervision is the set of institutional practices that bind private and public actors in a constant dialogue not only about compliance with law but also about the line between public and private responsibility for the residual risk of the financial system. Importantly, the negotiation of that line constantly abuts the methodological question of how such negotiation should occur: through a highly structured system of *ex ante* rules with *ex post* enforcement and independent review or through a more discretionary system based on the exercise of public power over private actors, a system that lurks outside the usual legal frameworks of public law.

The consequence of this framework for bank supervision is that debates about the private versus public responsibility for finance and whether government power should be formal and rules-based or informal and discretion-based are, in fact, the same debate. Bringing these two conversations together yields two important insights. First, the financial system is not a public utility managed by private interests, but by privately owned and managed by both public and private interests. Nor is the line between co-management starkly drawn, tilting fitfully toward one or another extreme at different points in history but never a fully private nor a fully public system. Second, bank supervision is always about the exercise of powerful discretion within a broad system of vague rules. The

https://ssrn.com/abstract=3777580 [https://perma.cc/GG47-ZEFU]; Beverly Hirtle & Anna Kovner, Banking Supervision (Fed. Rsrv. Bank of N.Y. Staff Report No. 952, Rev. Dec. 2021), https://www.newyorkfed.org/research/staff_reports/sr952 [https://perma.cc/7LB5-PS5H]; Sean Vanatta, Histories of Bank Supervision (2021), https://ssrn.com/abstract=3749116 [https://perma.cc/QCE2-F9EC], Jonathan Fiechter & Aditya Narain, Enhancing Supervisory Effectiveness - Findings from IMF Assessments (Bank Supervision Conf., 2020), https://custom.cvent.com/20310C03166C4C11B1AA63B0D6300264/files/event/67aec69c628d459d8366466979e3f8af/5bc86be980124876a00cbc409377a771.pdf.

balance between these poles is, once again, historically constituted, contingent, and evolutionary.

There are important implications to these debates about the nature of the American state and economy. To shear the controversies of nuance, those on the political left tend to favor a financial system where money is sovereign, finance is public, and supervisory discretion mostly untrammeled, whereas those on the political right tend to favor a private system where money is intermediated, finance is private, and regulation is rules-based with minimal discretionary liberties. Our theoretical framework reveals that these ideological contests are overwrought and underspecified. This Article's theory of banking insists that each of these ideas is fluid, vulnerable, and subject to constant redefinition. Bank supervision, in turn, is the institutional setup for the ongoing negotiation of these contested ideologies and the implementation of their temporary settlements. It is not a fixed resolution to the problems of managing financial risk across institutions and across the system, but a monitoring mechanism that evolves as exigencies shift with time. There can be no permanent "settlement" of these issues.[7] Each generation settles the questions again and again, building institutional layer upon institutional layer.[8]

The framework presented in this Article differs importantly from three other streams of thought on banking and bank supervision. The first is easiest to dismiss: the term "bank supervision" is often erroneously conflated as a synonym with the much more tractable term, "regulation." This is a ubiquitous error, albeit one that recedes as scholars focus increasingly on supervision as a unique phenomenon.

[7] *See* Lev Menand, *Why Supervise Banks? The Foundations of the American Monetary Settlement*, 74 VAND. L. REV 951 (2021); Lev Menand, *The Logic and Limits of the Federal Reserve Act*, 40 YALE J. ON REG. 197 (2022).

[8] *See* Kathleen Thelen, *Historical Institutionalism in Comparative Politics*, 2 ANNU. REV. POLITICAL SCI. 369 (1999); *see generally* KATHLEEN THELEN, HOW INSTITUTIONS EVOLVE: THE POLITICAL ECONOMY OF SKILLS IN GERMANY, BRITAIN, THE UNITED STATES, AND JAPAN (2004).

Supervision is as different from regulation as regulation is from legislation—they touch common ideas but are different methodologies, epistemologies, and institutions.

A second erroneous conception of supervision is the one embraced by the U.S. Federal Reserve, which characterizes "regulation" as the rules, and "supervision" as the process of "ensur[ing] that an institution complies with those rules and regulations."[9] This conception is more common and harder to dismiss. We will devote space in Part I to assess alternatives to this reductionist "principal-agent" model of supervision and explain both why this model is wrong and why its error is intellectually important. In brief, the entire debate about the discretion that supervisors must exercise over the financial system is a recognition, whether implicit or explicit, that there is more to the supervisory apparatus than simple verification of legal obedience.

We depart from a third suite of characterizations of supervision not as conceptual errors, *per se*, but as alternative accounts of what bank supervisors are meant to do. For example, legal scholars have variously characterized supervision as a kind of grand settlement of contentious monetary questions introduced in the Civil War and durable until the end of the twentieth century[10]or as a "monitoring" system similar to what occurs in other domains such as food, workplace, or environmental contexts.[11]

These characterizations, and others like them, capture parts of the basis of bank supervision, but only parts, rendering them misleading in their limitations. Supervision is not simply about ensuring duly enacted rules are followed, nor is it meant to accomplish a single task, whether in monitoring or money creation. Supervision is instead a process through which important policy decisions are made, again and again, that exists apart from other mechanisms of legal obedience,

[9] *See* BD. OF GOVERNORS OF THE FED. RSRV. SYS., THE FEDERAL RESERVE SYSTEM PURPOSES AND FUNCTIONS 72 (10th ed. 2016).

[10] *See* Menand, *Why Supervise Banks*, *supra* note 7.

[11] *See, e.g.*, Rory Van Loo, *Regulatory Monitors: Policing Firms in the Compliance Era*, 119 COLUM. L. REV. 369 (2019).

such as corporate governance, compliance, litigation, enforcement, and especially regulation. In this sense, supervision relocates the situs of policy conflict but does not necessarily or frequently resolve those conflicts in any permanent way.

These are the accounts our framework argues against. That high-level description of this Article, however, requires more explanation: if supervision is fundamentally and epistemologically distinct from other mechanisms of legal obedience, what is its purpose?

We argue that bank supervision is the uneasy and incomplete truce between two rival systems of managing financial risk: (1) a completely rules-based approach to ensure compliance with legal rules created elsewhere and (2) the untrammeled, discretionary exercise of governmental power. Supervision is the sometimes more, sometimes less structured middle ground that permits government power to be flexibly deployed to prevent crises and mitigate their effects without undermining principles of due process and rule of law that permit society to form and build on expectations of how government power will be exercised.

Again, this framework reveals something important about the nature of financial risk and who owns it. Bank supervision sits at the intersection of private and public power: it reflects neither the delegation of public power to private actors, nor is it an unlawful intrusion of public oversight over private prerogatives. It is, fundamentally, a kind of corporatist bargain of shared public and private power that allocates financial risk among private actors and public officials. Present debates about the boundaries of these lines fall, consciously or not, within that corporatist framework.[12]

[12] In this way, bank supervision functions within debates about corporatism that its critics and defenders have elaborated for decades. *See* GABRIEL KOLKO, THE TRIUMPH OF CONSERVATISM: A REINTERPRETATION OF AMERICAN HISTORY, 1900–1916 (1977); Oscar Molina & Martin Rhodes, *Corporatism: The Past, Present, and Future of a Concept*, 5 ANNU. REV. POLITICAL SCI. 305 (2002).

This new framework yields important lessons and insights to ongoing discussions, both in the historiography of the nineteenth and twentieth centuries and on several issues of relevance to twenty-first century public policy. Historically, the evolutionary process of institution-building in and around bank supervision informs several key debates about state capacity in the postbellum nineteenth century, the Progressive Era, the New Deal Era, the postwar era, the civil rights revolution, and late twentieth century neoliberalism. For instance, one area on which it sheds more light is the growth of the American state—an area of focus and influence by scholars such as Lowi, Novak, Skowronek, and Mashaw.[13] Importantly, federal bank supervision predates the Interstate Commerce Commission—the conventional starting point for bureaucratic development in the United States—by more than two decades, and it existed for several decades before that at the state level. This Article contributes to the understanding of the development of state capacity from the Progressive Era, when bank supervision unsuccessfully strove to manage residual risk that should have belonged most concretely to private banks, through to the New Deal, when the advent of deposit insurance made the commitment to managing residual risk definitive. Unlike conventional narratives about the development of Progressive-Era government oversight of commerce—whether the corporatist vision of Kolko,[14] the technocratic arguments of Wiebe,[15] or the interest-group vision of Sanders[16]—we argue that supervision in the Progressive Era was an experimental

[13] *See generally* THEODORE J. LOWI, THE END OF LIBERALISM: IDEOLOGY, POLICY, AND THE CRISIS OF PUBLIC AUTHORITY (1969); WILLIAM NOVAK, THE PEOPLE'S WELFARE: LAW AND REGULATION IN NINETEENTH CENTURY AMERICA (1996); STEPHEN SKOWRONEK, BUILDING A NEW AMERICAN STATE: THE EXPANSION OF NATIONAL ADMINISTRATIVE CAPACITIES, 1877–1920 (1982); JERRY L. MASHAW, CREATING THE ADMINISTRATIVE CONSTITUTION: THE LOST ONE HUNDRED YEARS OF AMERICAN ADMINISTRATIVE LAW (2012).

[14] KOLKO, *supra* note 12.

[15] *See* ROBERT H. WIEBE, THE SEARCH FOR ORDER 1877–1920 (1967).

[16] *See* ELIZABETH SANDERS, ROOTS OF REFORM FARMERS, WORKERS, AND THE AMERICAN STATE, 1877–1917 (1999).

period wherein interest groups fought for primacy but government power failed to coalesce successfully around a single vision of what state capacity should be used to do.

The New Deal Era—and the response to the Bank Holiday of 1933 in particular— marks the true ascension of bank supervision into the practice largely understood today.[17] During the holiday, Roosevelt tied his own political legitimacy to the technocratic work of bank examiners, and thus to bank supervision at large. Congress adopted that model of technocratic executive oversight by expanding the supervisory role of the Comptroller and Federal Reserve while also creating a new model of supervision based in deposit insurance. The move was not merely institutional, however; the practice of positioning supervision as the space where public and private actors vie for control through rules and the exercise of power became the dominant model of risk management. While there was some minor institutional innovation after the New Deal—the creation of thrift supervision, housing finance supervision, and supervisory coordination in the 1970s and 1980s—the basic institutional framework did not evolve much thereafter, arguably until 2008 (after which there was substantial institutional evolution). Following the New Deal, supervision became the adjudicative space between the private-sector financial system and the public-sector risk managers within government.

Besides the clarity that this account of supervision offers for our understanding of history, it also informs a variety of contemporary debates. This Article discusses three specifically: (1) the debates about whether and how federal

[17] We develop that narrative historical account in Peter Conti-Brown & Sean Vanatta, *The Logic and Legitimacy of Bank Supervision: The Case of the Bank Holiday of 1933,* 95 BUS. HIST. REV. 87 (2021). We are responding to the primary narratives of the holiday discussed in Ben S. Bernanke, *Nonmonetary Effects of the Financial Crisis in the Propagation of the Great Depression,* 73 AM. ECON. REV. 257 (1983) and BARRY EICHENGREEN, HALL OF MIRRORS: THE GREAT DEPRESSION, THE GREAT RECESSION, AND THE USES-AND-MISUSES OF HISTORY 296 (2015).

supervisors should evaluate climate-related risks, (2) the appropriate scope and content of federal bank merger policy, and (3) the appropriateness of expanding deposit insurance coverage. A view of supervision as compliance or serving a monetary function cannot provide much insight into these questions; supervision as the adjudication between public and private risk management, between rules and discretion, can.

This conception of state capacity and bank supervision also informs how we should think about government power in a world after the judicial elimination of *Chevron* deference.[18] Importantly, that deference was a canon of statutory interpretation to restrain courts from evaluating administrative interpretations of congressional intent[19] Bank supervision, particularly in the ways we describe here, is about the use of discretionary judgment the exercise of which Congress has given to supervisors, mostly in secret, with few restrictions for over 160 years.

In presenting these arguments, we join an increasingly sophisticated theoretical and historical conversation on the meaning of bank supervision, a very old intellectual effort that has received new life following the 2008 financial crisis.[18] Where we build on this literature is to present bank supervision as a separate field for resolving policy disputes, not as systematic resolution in its own right. This conceptual shift allows us to cast additional light on the policy maneuvers that would otherwise remain firmly out of sight.

[18] *See* Loper Bright Enters. v. Raimando, 603 U.S. 369 (2024).

[19] *See, e.g.*, G. L. Bach, *Bank Supervision, Monetary Policy, and Governmental Reorganization*, 4 J. FINANCE 269 (1949); G. L. Bach, *A Further Note on Bank Supervision and Monetary Policy*, 5 J. FINANCE 421(1950); Julie Dickson, *Too Focused on the Rules: The Importance of Supervisory Oversight in Financial Regulation*, 18 CARDOZO J. INT'L & COMP. L. 623 (2010); Lev Menand, *Too Big to Supervise: The Rise of Financial Conglomerates and the Decline of Discretionary Oversight in Banking*, 103 CORNELL L. REV. 1527 (2019); Menand, *Why Supervise Banks, supra* note 7; Van Loo, *supra* note 11. This literature is usefully summarized in Hill, *supra* note 6; Hirtle & Kovner, *supra* note 6; and Vanatta, *supra* note 6.

The remainder of this Article proceeds as follows: Part I outlines the framework of public-private supervision more thoroughly, including where that theory departs from other conceptions about regulation, discretion, and the rule of law. Part II explains the history of federal supervision from its antecedents in the antebellum era, to its tenuous founding in the National Banking Acts of 1863 and 1864, and through the New Deal, when the institutional framework for risk management became more concrete. Part III discusses the evolutionary process whereby supervision became a much more expansive, and much more disputed, mechanism of government power, with the addition of consumer financial protection, antidiscrimination, and community reinvestment. Part IV explains the implications of these ideas for contemporary debates about climate change, anti-trust policy, and deposit insurance, and explains the relevance for agencies' risk management strategies in the post-Chevron era.

## I. WHAT SUPERVISION MEANS

### *A. A Conceptual Overview*

In the United States, supervision is nearly as old as banking. State governments developed oversight regimes in the decades before the Civil War, and the federal government has played a permanent supervisory role since that conflict. In these early frameworks for bank supervision, the United States is unique. Except for Sweden (in 1909) and Japan (in 1916), most developed nations formalized bank supervision only after the 1930s banking crises, sometimes well after.[20]

Despite its long history in the United States and despite the earlier efforts cited above, supervision has not long been a

[20] *See* RICHARD S. GROSSMAN, UNSETTLED ACCOUNT: THE EVOLUTION OF BANKING IN THE

INDUSTRIALIZED WORLD SINCE 1800, at 162–67, 221–22 (2010); Eiji Hotori & Mikael Wendschlag, The Formalization Of Banking Supervision topic for sustained scholarly engagement, partly because supervision and supervisors are chameleon-like. Supervision resembles several well-studied governance mechanisms—such as regulation, civil and criminal litigation, self-regulation, ethics, and norms. Indeed, it is sometimes confused with them. Supervision is also in the shadows, a part of a hidden, robust regulatory state that Brian Balogh called "government out of sight."[21] But supervisory invisibility is no curious relic of the nineteenth century. By law in the present day, much of what supervisors do is wrapped in a thick cloak of secrecy under the banner of "confidential supervisory information," the publication of which can land leakers in jail.[22]

These scholarly lacunae leave open two foundational questions: What is supervision? And what makes it distinct from other modes of governance? As noted in the Introduction, supervision is often mistaken for regulation, which is easy enough to define. To take the Federal Reserve's 2016 definition, its regulatory function "entails establishing the rules within which financial institutions must operate—in other words, issuing specific regulations and guidelines governing the formation, operations, activities, and acquisitions of financial institutions."[23] Supervision, the Fed

In Japan And Sweden, 22 SOC. SCI. JAPAN J. 211 (2019); EIJI HOTORI, MIKAEL WENDSCHLAG & THIBAUD GIDDEY, FORMALIZATION OF BANKING SUPERVISION: 19TH–20TH CENTURIES (2021); Patrice Baubeau, Eric Monnet, Angelo Riva & Stefano Ungaro, *Flight-to-Safety and the Credit Crunch: A New History of the Banking Crises in France During the Great Depression*, 74 ECON. HIST. REV. 223 (2021).

[21] BRIAN BALOGH, A GOVERNMENT OUT OF SIGHT: THE MYSTERY OF NATIONAL AUTHORITY IN NINETEENTH-CENTURY AMERICA (2009).

[22] *See* Margaret E. Tahyar, *Are Bank Regulators Special?,* 5 BANKING PERSPECTIVES 23 (2018), https://www.davispolk.com/sites/default/files/tch_banking_perspectives_-_are_banking_regulators_special.pdf [https://perma.cc/734F-5Z6D]; Peter Conti-Brown, *The Curse of Confidential Supervisory Information*, BROOKINGS INST. (2019), https://www.brookings.edu/research/the-curse-of-confidential-supervisory-information/ [https://perma.cc/9NHS-PX96].

[23] BD. OF GOVERNORS, *supra* note 9, at 74.

continues, "involves monitoring, inspecting, and examining financial institutions" and "seeks to ensure that an institution complies with those rules and regulations, and that it operates in a safe and sound manner."[24] On this view, if regulation involves rules, supervision entails the tools government officials use to ensure financial firms comply with the rules.

The Federal Reserve's 2016 definition of supervision is at once expansive and limited. It is expansive in that each of the actions ascribed to supervision—monitoring, inspecting, and examining—contain in them a host of subsidiary practices, which supervisors use to shape behavior: to guide, to suggest, to demand, and to compel. The definition is limited in its implicit claim that supervision is merely the implementation of law and the compliance with rules.

The narrowness of the Fed's 2016 definition becomes visible when it is placed against an earlier—and much longer—version, published by the Fed in 1954:

> As a government activity, bank supervision encompasses a wide variety of technical functions relating to the operation of banks. These concern: (1) the issuance and enforcement of supervisory and other regulations; (2) the organization and chartering of banks; (3) the periodic examination of banks and the requiring of steps by bank management to correct unsatisfactory or unsound conditions found through such examination; (4) the review and analysis of periodic reports of conditions and earnings and expenses; (5) the rendering of counsel and advice on bank operating problems when requested, particularly in the case of smaller banks; (6) the approval of proposed changes in the scope of corporate functions exercised by individual banks and of proposed changes in their capital structures; (7) the authorization of establishment of branches and of the exercise of trust powers; (8) the approval of bank mergers and consolidations; (9) the organization and

[24] *Id.*

> regulation of bank holding companies; (10) the regulation of bank service corporations; and (11) the liquidation of banks (Board of Governors 1954, 166-67).[25]

The Fed in 1954 had a better sense of the functions and epistemologies of supervision than the Fed in 2016. Instead of monitoring, inspecting, and examining, which are largely instances of passive oversight, the Fed's 1954 definition described active supervisory governance. This definition is not just one of examining, but requiring correction; not just reviewing, but analyzing; not just implementing the law, but rendering counsel and advice. Here, the supervisory purview was much wider than mere compliance. Supervisors assertively deployed official judgement and discretion, often to mold behavior according to preferences and objectives that were distinct from any formal rules.

While the ubiquitous conflation of supervision with regulation is erroneous, the active versus passive sense of supervision is not so much an error as an arc. The transformation evident in these definitions—from an active, self-confident government in 1954, to a chastened, restrained government in 2016—maps onto consensus narratives of the American state, as it is activist in the wake of the New Deal, but retrenched following the Reagan Revolution.[26] Although the competing definitions suggest the diminution of supervisory authority over this period, just the opposite occurred. Supervisors in the twenty-first century must tackle even more responsibilities—from cyber security to civil rights—than in 1954. The conceptual question, then, of what supervision is at its foundation in the face of these many responsibilities, still requires an answer.

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[25] BD. OF GOVERNORS OF THE FED. RSRV. SYS., THE FEDERAL RESERVE SYSTEM PURPOSES & FUNCTIONS 166–67 (3rd ed. 1954).

[26] *See, e.g.*, MARTHA DERTHICK & PAUL J. QUIRK, THE POLITICS OF DEREGULATION (1985); RICHARD A. HARRIS & SIDNEY M. MILKIS, THE POLITICS OF REGULATORY CHANGE: A TALE OF TWO AGENCIES (1989). For a general overview, see DAVID HARVEY, A BRIEF HISTORY OF NEOLIBERALISM (2005).

Legal scholars, historians, and economists have recently begun to pursue this conceptual work, typically to build historical foundations for normative claims about how supervision should function in the present. Economic historian Eugene White, for example, views federal supervision as a constant tug between regimes that embrace strictly rules- based, market discipline—his preference—and those that rely more heavily on supervisory discretion.[27] Economic historians Charles Calomiris and Mark Carlson see the role of examiner in the late nineteenth century in a similar way, focusing primarily on their roles in risk management and information disclosures.[28]

Legal scholars, meanwhile, have proposed supervision as more durable legal structures in a more systematic, consistent way. For example, Lev Menand offers a variety of taxonomic categories, including "Supervisors as Rule Enforcers," "Discipline Facilitators," and "Gap Fillers," among others.[29] But the historical record often resists such stability, and the role Menand envisions for supervision—as part of a long-settled institutional framework created by far-seeing legislators—is incompatible with history. Menand's effort, consistent with a growing scholarly tradition at the intersection of law, economics, and history sometimes called "the money view," would systematize supervision under a different, normative framework: supervisors are

[27] *See* Eugene White, Lessons from the History of Bank Examination and Supervision in the United States, 1863-2008 (Fin. Mkt. Regul. in the Wake of Fin. Crises: The Hist. Experience Conf., at 15, (2009)), available at https://ssrn.com/abstract=2101709 [https://perma.cc/SE6G-9W7Y].

[28] *See* Charles W. Calomiris & Mark A. Carlson, *Bank Examiners' Information and Expertise and Their Role in Monitoring and Disciplining Banks Before and During the Panic of 1893* (Nat'l Bureau of Econ. Rsch., Working Paper No. 24460, 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3154244 [https://perma.cc/R52A-AEXK].

[29] Menand, *Why Supervise Banks*, *supra* note 7.

"franchisors," guardians of the monetary franchise outsourced by the government to banks.[30]

Menand views supervision, then, as vital to what he calls the American Monetary Settlement created during the Civil War that, in his view, reflects the most normatively desirable structure of finance into the twenty-first century. What this theory is missing is an account of what supervision has been in the 160 years since the Lincoln Administration.

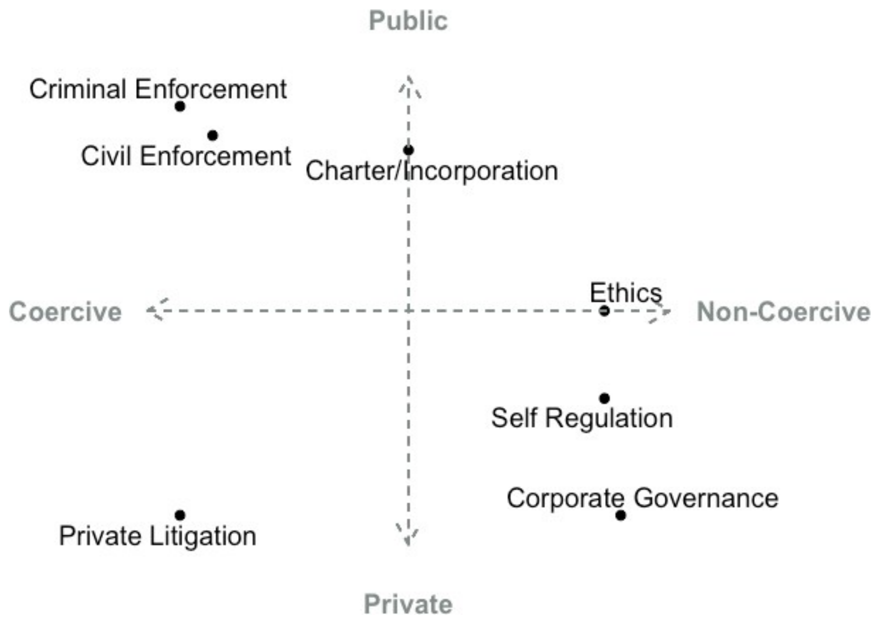
### *B. Epistemologies of Supervision*

To understand how bank supervision operates as a system, we begin with a typology that shows how it sits alongside its alternatives. The typology has two parts. First, supervision functions as a distinct mechanism of legal obedience—a means by which government or private actors seek to alter behavior. These mechanisms can be displayed on two axes: the first being a choice between public and private mechanisms, the second being the exercise of coercive or non-coercive power. In this sense, supervision represents a choice for policymakers—principally, but not exclusively, Congress—distinct from other alternatives. It is a choice, as Figure 1 indicates, which authorizes government officials to exercise substantial discretion about how to alter behavior. To return to the Fed's 1954 definition, supervision can involve "the rendering of counsel and advice" (private, non-coercive), "requiring of steps by bank management to correct unsatisfactory or unsound conditions found through such

[30] For key works in the Money View tradition, see Hyman Minsky, *The Financial Instability Hypothesis* (Levy Econ. Inst. of Bard Coll. Working Paper No. 74, 1992), https://www.levyinstitute.org/pubs/wp74.pdf [https://perma.cc/69FF-Z2NY]; PERRY MEHRLING, THE NEW LOMBARD STREET: HOW THE FED BECAME THE DEALER OF LAST RESORT (2010); CHRISTINE DESAN, MAKING MONEY: COIN, CURRENCY, AND THE COMING OF CAPITALISM (2015); MORGAN RICKS, THE MONEY PROBLEM: RETHINKING FINANCIAL REGULATION (2016).

examination" (private, coercive), or "the liquidation of banks" (public, coercive).[31]

Figure 1 – Paradigms of Supervision: External

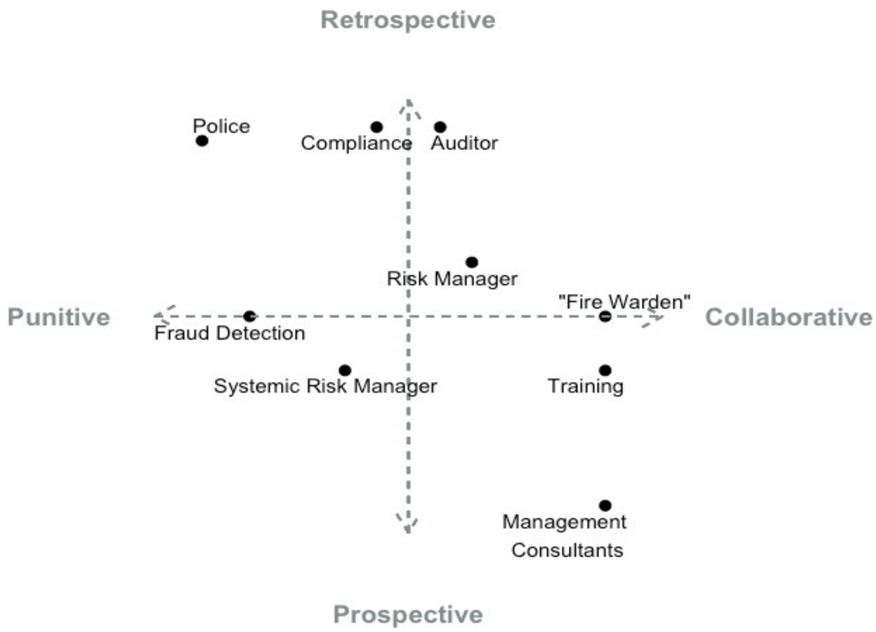



Relatedly, the definition of supervision hinges on what supervisors think they are trying to accomplish, self-conceptions that divide not only according to an external logic of coercion versus non-coercion and public versus private, but also an internal one. These self-conceptions operate within a framework with axes spanning punitive to collaborative and from retrospective to prospective, as summarized in Figure 2. The alternatives presented here are evident in the 1954 definition and become even more visible when comparing it with its 2016 counterpart. In 1954, to take one example, the Fed emphasized "the rendering of counsel and advice on bank operating problems when requested, particularly in the case of smaller banks," a statement that embraces the training and

[31] BD. OF GOVERNORS, *supra* note 25, at 167.

management consulting roles on the collaborative-prospective corner of the chart.[32] Although the Fed may have been engaged in similar activities in 2016, it no longer held them as a defining feature of compliance-focused supervision.

Figure 2 – Paradigms of Supervision: Internal




This conception of supervision captures some of the descriptive and normative accounts of scholars cited above, without rooting that conception too much in a single point of time and imposing that moment on the rest of the tumultuous history that followed. As a policy matter, the costs and benefits of the Fed's expansive view of supervision in 1954 and more circumscribed view in 2016 are open to debate, and supervision, itself, provides the context in which that debate unfolds.

[32] *Id.*

### C. Rules versus Discretion in Bank Supervision

At its core, supervision is about options, which are exercised differently at different times and yield varying consequences. These options also highlight the central difference between supervision and other forms of government power because such options leave supervisors with the discretion to decide just what supervision should be. This discretion defines the logic of bank supervision. It also expands the kinds of categories that fit into the broad definition of supervision, cited above, as the way in which individual governmental actors influence the behavior of individual financial institutions. The competing objectives of law enforcement, crisis response, monetary policy, consumer protection, antidiscrimination, and more, are each available to supervisors as they encounter the banks under their watch. Congress sets these objectives within constraints shaped by historical contexts that have shifted over time.

Placing discretion at the center of supervision means that the practice of supervision will line at which the Government shall interfere and the point at which Government discipline shall commence is a matter of some delicacy to determine."[33] Or, as Randal Quarles, the former Vice Chair for Supervision of the Federal Reserve, put more colorfully in 2020, identifying the line between regulation and supervision only becomes clear to banking regulators and supervisors after "fasting and much prayer."[34]

Viewing bank supervision through the lens of discretion—whether historically or theoretically—allows us to see where supervisors draw their lines and how those lines evolve over time.[35] The exercise of supervisory discretion is, definitionally, a moving target, animated by different and conflicting

[33] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 50 (1884).

[34] Randal Quarles, Dean's Lecture (Lecture, Yale L. Sch., New Haven, CT, Feb. 26, 2020) (transcript used with permission and on file with the Columbia Business Law Review).

[35] *See* JERRY MASHAW, BUREAUCRATIC JUSTICE: MANAGING SOCIAL SECURITY DISABILITY CLAIMS (1983).

paradigms, experienced in different ways within different supervisory organizations.[36] This framework also permits us to avoid imposing demands for paradigmatic consistency that the historical record cannot support; there is no enduring financial settlement in U.S. history, for example, that survives the tumult of the last 160 years.

Supervision as discretion also explains how supervision became the dominant mechanism compelling legal obedience in the financial system, even beyond its more studied counterpart, regulation. Discretion permits supervisors to make bespoke policy through a variety of mechanisms, within a broad rules-based system to which it is not fully restricted. The options available to supervisors depicted in Figure 2 permit them to change their roles from, say, fraud detection and police power, used to catch money launderers within financial institutions, to the development of new risk management techniques, used to provide training to banks and bankers about appropriate accounting or other standards.

Discretion gives supervisors substantial freedom, so there is no wonder that they prefer it. Quarles lodged a sustained critique of supervisory discretion: "We have a public interest in a confidential, tailored, rapid-acting and closely informed system of bank supervision. And we have a public interest in all governmental processes being fair, predictable, efficient, and accountable."[37] To "square the circle," Quarles argues that we must recognize that "supervision sits uncomfortably with the responsibilities of government in a democracy."[38] The exercise of power in the United States should be defined by "generality, predictability, publicity, and consultation."[39]

[36] *See* MICHAEL LIPSKY, STREET-LEVEL BUREAUCRACY: DILEMMAS OF THE INDIVIDUAL IN PUBLIC SERVICE (1980); *see also* Daniel E. Ho & Sam Sherman, *Managing Street-Level Arbitrariness: The Evidence Base for Public Sector Quality Improvement*, 13 ANN. REV. L. & SOC. SCI. 251 (2017).

[37] Randal Quarles, Spontaneity and Order: Transparency, Accountability, and Fairness in Bank Supervision (Am. Bar Ass'n Banking L. Comm. Meeting, Washington, D.C., 2020).

[38] *Id.*

[39] *Id.*

Supervision looks very little like this and should, in Quarles's view, conform much closer to it.

Quarles's focus on the rule-of-law concerns associated with supervision is not unique. Many commentators in the financial industry itself have expressed similar views, including the view that significant components of modern supervisory practice are illegal because they are insufficiently rooted in rulemaking, and thus in violation of the Administrative Procedure Act (the APA).[40]

Daniel Tarullo, Quarles's predecessor at the Fed with oversight of bank supervision, has offered his own scholarly answer to this conundrum.[41] Tarullo argues that although general principles of administrative law do suggest much of supervisory action is open to rule-of-law challenges with uncertain results, bank supervision's statutory bona fides are strong, reflecting as they do "the heterogenous nature of financial intermediation" and the fact that supervision is an "ongoing relationship between a bank and agency officials."[42] Each of these factors suggests that traditional principles of administrative law and political power—the rule-of-law concerns that animates the supervisory critique above—are less applicable to bank supervision than they might appear.

In other words, there is an existential debate afoot on what supervision should be. Supervision-as-discretion takes a clear view that does not fit neatly into this debate as it has been introduced. Our argument is not about the APA, but about the nature of bank supervision as it has evolved and adapted to

[40] *See* Greg Baer & Jeremy Newell, *How Bank Supervision Lost Its Way*, BANK POL'Y INST., May 25, 2017, https://bpi.com/how-bank-supervision-lost-its-way/ [https://perma.cc/JNN7-YB62]; Hal Scott, *Stress Tests: Restore Compliance with the APA*, BANKING PERSPECTIVES, Sept. 3, 2017, https://www.bankingperspectives.com/stress-tests-restore-compliance-with-the-apa/; *Bank Capital and Liquidity Regulation: Hearing Before the S. Comm. on Banking, Housing, and Urban Affairs*, June 7, 2016, https://capmktsreg.org/wp-content/uploads/2023/03/HSS_Written_Testimony-SBC-6-7-16.pdf [https://perma.cc/42A9-FZTH] (written testimony of Hal S. Scott).

[41] *See generally* Tarullo, *supra* note 3.

[42] *Id.* at 284.

its status within the financial system. That evolution has produced a set of disparate practices that place discretion at the center. Efforts, then, to reduce or remove discretion within supervision run the risk of eliminating what is distinct about supervision at all.

### *D. Supervision as Residual Risk Management*

Our theoretical account of supervision, then, builds on four sequential insights. Supervision is (1) about the relationship between individual actors in government and individual financial institutions—where the rubber hits the road of government and market power. It is further defined by (2) evolutionary processes and resistance to efforts to impose a single defining ethos, leaving instead supervisors—and Congress—to use (3) supervisory discretion to choose among competing conceptions of what that individual relationship should be. However, the most important payoff of this account is the fourth insight: that this system has (4) proved so resilient to change, and so amenable to expansion, because supervisory discretion functions as a risk absorber for the entire financial system. Bank supervision is the promise that the government will participate with the private sector to manage and take responsibility for the residual risk stemming from design choices inherent to the American financial system. Contrary to other categories of risk—national security after September 11, 2001, for example—financial crises have become viewed, to some degree, as the cost of the American system. Supervision, then, is not just about punishing wrongdoers or responding to financial panics; rather, it is about managing a large and ever-growing system of political and financial risk that we, as a society, have decided we want to take, using a variety of tools and strategies that at times converge and at times conflict.

Supervision is, in this way, about managing the moral hazard in the financial system. The concept of "moral hazard" comes from nineteenth century insurance theory and denotes the concern that people or firms that take out insurance to protect themselves against specific kinds of risk will be less dutiful about avoiding those risks.[43] Eliminating moral hazard is often cited as the defining problem of institutional design in the financial system.[44] We argue, instead, that moral hazard is irretrievably baked into our system: banking, by its very nature, will always be a contest and collaboration between public and private actors. Therefore, that moral hazard is not a policy problem to solve for bank supervisors. Managing moral hazard is the job description.[45]

To state the point differently, Congress uses regulation to eliminate moral hazard; it uses supervision to manage moral hazard.

Recasting bank supervision as a category of political and financial systemic risk management allows us to answer some important questions about finance and the administrative state. First, what are the political incentives for expanding supervisory discretion into private markets given the ostensible partisan hostility to such government intrusions? And more fundamentally, why is public supervision used to manage private risk at all, rather than forcing private actors to manage that system themselves or rendering the system fully public, as some would prefer? The answer to the first question is that Congress sees bank supervision as an out-of-sight solution to the vexing costs of publicly acknowledging that the financial system is not a fully private affair. That emphasis on Congress is deliberate: unlike other areas of the administrative state, Congress has almost uniformly focused on expanding supervisory prerogatives, even in the face of presidential pushback. Indeed, in important periods—especially from 1977–2008 and again in 2017– 2021—the President and his appointees have sought to narrow the range of supervisory options in a process we call "de-supervision." Instead, Congress, at almost every turn, has sought to expand

[43] *See, e.g.*, David Rowell & Luke Connelly, *A History of the Term "Moral Hazard"*, 79 J. RISK & INS. 1051, 1069–72 (2012).

[44] *See generally* Arthur E. Wilmarth, *Reforming Financial Regulation to Address the Too-Big-To-Fail Problem*, 35 BROOK. J. INT'L L. 707 (2010).

[45] We thank Scott Shapiro for this pithy sentence.

supervisory discretion by providing more categories of power for supervisors to adopt. This is true even when supervisory scandals and financial crises cause members of Congress to insist that supervisors were "asleep at the switch." One of the constant realities of the history of bank supervision in America is that Congress regularly "blames" supervisors with failing to exercise their discretion in ways that would prevent error even while they substantially expand that discretion.[46]

Then, the second question: Why do we have this one-way ratchet, even in the face of failure? Supervision as discretion and risk management offers two answers. First, since the creation of the federal bank supervisory system in 1864, Congress has continued to use bank supervision as a kind of equity cushion to absorb risks that our system encourages. These risks include, of course, financial risks, such as bank failures and the risk of systemic failure of the financial system. They also include, importantly, political risks, such as the risk that banks will fail in scandal, that banks will violate the law through racial discrimination, or that banks will find themselves at the center of a drug cartel-funded international money laundering ring. These are political risks because Congress has passed laws that do not (and perhaps cannot) fix these problems once and for all. As such, Congress has delegated discretion to supervisors who are better suited to absorb the uncertainties of hard problems—be they concerns over financial inclusion, anti-money laundering, or other institutional priorities.

While the shape of our supervisory system, and its location as a form of risk absorption, owes more to the idiosyncrasies

[46] Supervision's role as residual risk bearer also explains another curiosity about the history of bank supervision. In his work on the Food & Drug Administration (FDA), Daniel Carpenter offers a theory of discretion and autonomy that is rooted in the FDA's reputation and its ability to perform functions with outcome legitimacy amongst various audiences. These successes in turn fed the accretion of power: better performance, better reputation, more congressionally supported autonomy within which the FDA can exercise more discretion. *See* Daniel Carpenter, Asleep at the Switch (from Sen. Chris Dodd, S. Banking Comm. Hearing on America's Credit Crisis, Mar. 4, 2008).

of historical development than to grand design, supervision's role as Congress's risk absorber reflects an overarching ideology of risk central to financial markets in the United States. Legal rules can be over- or under- inclusive. The U.S. financial system is under-inclusive in that some impermissible activity will inevitably occur because the system rewards the risk-taking that private actors (and Congress itself) do not wish to absorb. Banking law seeks to allow some of the bad to permit all the good; it does not seek to prohibit all of the bad and thus some of the good. Given the inevitability that such a system will have for scandal and failure, bank supervisors represent the category of public power meant to manage that risk ahead of time and then absorb it when failure (of whatever variety) is realized.

This is not to say that the system we have is the only one we can imagine. Scholars have suggested reforms large and small that would change the way we divide that line, from proposing the Federal Reserve as a retail bank,[47] to increasing the role of the postal service in providing financial services,[48] to attempting to describe the U.S. financial system in explicitly public terms.[49] But our account of supervision suggests some historical modesty to these efforts. The only consistency across two centuries of bank supervision is that bank supervisors are given increasing amounts of responsibility to use their discretion to manage private risk at public expense. This practice serves as the bedrock of our political economy and financial system, for good or ill.

The model of supervision just described—supervision as a fitfully evolved (and still evolving) set of practices and functions that permits government actors to use discretion to manage residual systemic risk through individual banking relationships— does a better job than alternatives in

[47] *See* John Crawford, Lev Menand & Morgan Ricks, *FedAccounts: Digital Dollars*, 89 GEO. WASH. L. REV. 113 (2020).

[48] *See* Mehrsa Baradaran, *It's Time for Postal Banking*, 127 HARV. L. REV. F. 165 (2014).

[49] *See* Omarova, *supra* note 1.

explaining some of the enduring features of the U.S. financial system. Alternative models of supervision—supervision as passive compliance verification, supervision as ongoing monitoring, supervision as part of a grand nineteenth century monetary bargain, supervision as bureaucratic power run amok, to name those with which we engage most directly—fail to integrate the financial system as it was and as it is into the wider experience of government, practice, and political economy.

## II. SUPERVISION'S SLOW AND SUDDEN INSTITUTIONAL BEGINNINGS: 1789–1933

The history of bank supervision is the story of how the residual-risk-and-discretion model of bank supervision came to be. Part II narrates a period of unusual supervisory tumult and experimentation, through the Bank Holiday of 1933. This story shows why both skeptics of supervisory discretion and champions of supervisory power anchored in one epistemological framework alike misunderstand the institutional evolution of American finance. This history begins in the early days of the American Republic when central banking institutions began early experiments with supervision before leaving those issues unevenly to the states. It then explores a major but unstable monetary intervention during the Civil War: the creation of the Office of the Comptroller of the Currency (the OCC), an office that identified examination and supervision as a priority without defining what those practices entail. After the creation of the OCC and the clarification of its supervisory power in 1864, the postbellum and Gilded Age supervisory system grappled—unevenly and with substantial failure—with the perception that the government owned the residual risk that its officials managed through the exercise of supervisory discretion. Supervision had not yet adopted the risk-and-discretion framework transparently, in large part because supervision lacked any plausible financial mechanism of owning that residual risk.

This lacuna was filled conceptually with the creation of the Federal Reserve System in 1913 but did not reach its apotheosis until arguably the most important episode in supervisory history: the Bank Holiday of 1933, when the Roosevelt Administration gambled much of its credibility and legitimacy by placing substantial authority in the discretionary hands of supervisors to save the financial system. In the process, the Administration, the supervisors, and especially Congress institutionalized this model of bank supervision that has dominated the political economy ever since.

### *A. Origins: 1789–1870*

Supervision arises from three distinct historical trends: one legal, one fiscal, and one monetary. Legally, supervision is a version of corporate "visitorial" authority that attached to sovereign power over chartered institutions. The visitorial authority evolved as a Blackstonian English common law concept that gave the king, as "founder of all corporations, in the strictest and original sense," the authority to inspect or "visit[]" any civil corporation to ensure it charter provisions were being obeyed.[50] The fiscal authority emerged from the union, in early chartered banks, of private ownership and public functions—namely, collecting taxes, holding government deposits, and making payments on the government's behalf. The monetary function arose, in turn, to assure government officials and the wider public that bank notes (credit instruments) that circulated as currency were convertible into gold and silver coin (specie money).

These trends converged in the creation and management of the First and Second Banks of the United States. In the 1791

[50] *See* 1 BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND *455, *468–69; Sara Sager, *Preemption Rights of National Bank Operating Subsidiaries: The Fight for Visitorial Power*, 30 J. CORP. L. 183 (2004).

charter of the First Bank, Congress preserved for itself the power to "inspect such general accounts in the books of the bank," largely to retain fiscal oversight.[51] The First Bank's visitorial authority, as previously with the Bank of England, was implied. The Second Bank of the United States, chartered in spring 1816, contained an identical inspection provision but also made the visitorial paradigm explicit: "a committee of either house of Congress" could at any time "inspect the books" and "examine into the proceedings of the corporation" for the purpose of reporting "whether the provisions of this charter have been . . . violated."[52] Although neither charter explicitly linked the monetary function to inspection, the fundamental purpose of both banks was to provide a stable, uniform circulating medium. When a Congressional committee used its visitorial power to inspect the Second Bank in 1818, they reported on two aspects: "those which related to the general management of the bank," that is, its monetary functions, "and those which were connected with the question of a violation of its charter."[53]

Congress's 1818 inquiry, and indeed much of the political controversy surrounding the First and Second Banks, focused on the quasi-public banks' private counterparty supervision. Although the Constitution prohibited the States from

[51] MATTHEW ST. CLAIR CLARKE, LEGISLATIVE AND DOCUMENTARY HISTORY OF THE BANK OF THE UNITED STATES: INCLUDING THE ORIGINAL BANK OF NORTH AMERICA 33, 518 (1832).

[52] *Id.* at 593, 811. We have found evidence, however, for significant state legislative inspection of banks, especially as part of the chartering process. As one legislator observed in 1831, when bank chartering required a specific legislative act, "it is the duty of the Legislature to ascertain by competent testimony, whether the amount of business and capital in the place where the bank is to be established, are such, as to require the accommodation; and above all, whether those who ask the privilege, are men of unsuspected character." HOWARD BODENHORN, STATE BANKING IN EARLY AMERICA: A NEW ECONOMIC HISTORY 13 (2003) (quoting Anonymous, A Defence of Country Banks; Being a Reply to a Pamphlet Entitled 'An Examination of the Banking System of Massachusetts' 21–22 (1831).

[53] *Id.* at 715.

participating in the issuance of paper currency,[54] by 1820 there were 300 banks issuing currency with minimal standardization. In theory, these notes were freely redeemable in the specie coinage of the United States, a promise that facilitated their use as a medium of exchange. The biggest supervisory question in antebellum America, then, was between essentially private institutions; the Banks of the United States sought to ensure that the state-chartered banks they did business with could do that business well. Counterparty risk management thus became an important factor in the development of early American supervision, and this process essentially took place in the market. As any noteholder could present notes for redemption, bankers were encouraged to issue notes with care. The Banks of the United States, as the largest financial institutions, could collect, consolidate, and compel repayment at scale, turning the possibility of redemption into a promise that kept state bankers in line.[55]

This was a decisive—and to some, monstrous—power, made even more powerful because the core risk management buffer undergirding the banking system was the private, personal liability of bank shareholders. Personal liability encouraged bankers to practice sound banking, for if they did not, they would be ruined.[56]

The capacity of the Banks of the United States to issue sound notes, overseen by the federal government, and the Banks' capacity to enforce soundness among state-bank counterparties, reflect the essence of the view that supervision existed to ensure the soundness of money that

[54] U.S. CONST. art. 1, § 8, cl. 5.

[55] *See* BRAY HAMMOND, BANKS AND POLITICS IN AMERICA FROM REVOLUTION TO THE CIVIL WAR (1957); JAMES WILLARD HURST, A LEGAL HISTORY OF MONEY IN THE UNITED STATES 1774–1970, at 151–72 (1973); JANE KNODELL, THE SECOND BANK OF THE UNITED STATES: CENTRAL BANKER IN AN ERA OF NATION-BUILDING, 1816–1836 (2017).

[56] *See* Kris Mitchener & Matthew Jaremski, *The Evolution of Bank Supervisory Institutions: Evidence from American States*, 75 J. ECON. HIST. 819, 828 (2015).

we call the "currency view" of bank supervision. The currency view has important antecedents in nineteenth-century currency debates, such as in the 1820s–1840s United Kingdom,[57] and continues to resonate today.[58] Under this view, bank examination and supervision is not about exercising the sovereign's right as the chartering authority. While visitorial power is certainly core to the legal justification for government oversight, supervision serves another critical function: ensuring the soundness of currency, which, for contemporaries meant assuring that bank notes could be converted into specie.[59]

Andrew Jackson's veto of the Second Bank's recharter in July 1832 eliminated a centralized institution of currency quality control, but the currency view endured, albeit through metamorphosis.[60] Almost immediately, the states—already active in creating banking institutions of various types—stepped into the breach. The so-called free-banking era descended upon the United States: legislative enactments no longer initiated a bank charter; rather, states adopted more permissive chartering standards.[61] The free-banking era did not introduce an era free of supervision, however, but the more self-conscious combination of visitorial and currency approaches to supervision.[62] The institution of the "bank

[57] *See* Anna Schwartz, *Banking School, Currency School, Free Banking School*, *in* MONEY 41 (J. Eatwell et. al. eds. 1989); Charles Goodhart & Meinhard Jensen, *Currency School Versus Banking School: An Ongoing Confrontation*, 4 ECON. THOUGHT 20 (2015).

[58] *See* Menand, *Why Supervise Banks*, *supra* note 7; Menand, *Logic and Limits*, *supra* note 7.

[59] Arthur J. Rolnick, Bruce D. Smith & Warren E. Weber, *Establishing a Monetary Union in the United States, in* EVOLUTION AND PROCEDURES IN CENTRAL BANKING 237–48 (David E. Altig & Bruce D. Smith eds., 2003).

[60] The subsequent Independent Treasury Act of 1840 also eliminated the fiscal justification for bank oversight by preventing the Treasury from depositing federal money in banks. When these provisions were eased under the National Banking Acts, fiscal supervision remained with the treasury, distinct from the work of the comptroller and successor institutions.

[61] *See* HAMMOND, *supra* note 55, at 572–604.

[62] *See* Mitchener & Jaremski, *supra* note 56, at 826.

examiner"—an individual employed by the chartering authority to investigate banker behavior—arose roughly during this period. So too did other important parts of the supervisory footprint, including the authority by examiners to exercise discretion in deeming a bank safe and sound, changes in capital structure to expose shareholders to increased liability, and other such innovations.[63] States also sought alternatives to the private risk buffer of personal liability. Some developed insurance schemes with either public backing or mutual, private risk pooling. Others required circulating notes to be backed by sound assets, layering state oversight on top of market redemption.[64]

The free-banking era must be one of the most caricatured periods in U.S. monetary history—known derisively for its "Wildcat banks."[65] One challenge of the era arose in stark relief during the Civil War, when the stress on an exclusively state-based monetary system, with the varieties that such federalist experiments invite, met the federal government's capacity for war financing. This produced a monetary crisis. The Union's financial system barely lasted six months before buckling under fiscal and monetary pressures occasioned by coordination failures.[66] The Lincoln Administration, after experimenting with attempts to pull gold from state bank

[63] *Id.*

[64] CARTER H. GOLEMBE & CLARK WARBURTON, INSURANCE OF BANK OBLIGATIONS IN SIX STATES, DURING THE PERIOD 1829–1866, FED. DEPOSIT INS. CORP., at 12 (1958).

[65] For a comprehensive treatment of the period, see HOWARD BODENHORN, STATE BANKING IN EARLY AMERICA: A NEW ECONOMIC HISTORY (2003). For more apologetic treatment, see George Selgin, *Free Banking and Monetary Control*, 104 ECON. J. 1449, 1449–59 (1994) and LAWRENCE WHITE, FREE BANKING IN BRITAIN (1996). And for a nuanced examination of the boundaries between legitimate and illegitimate banking, see STEPHEN MIHM, A NATION OF COUNTERFEITERS: CAPITALISTS, CON MEN, AND THE MAKING OF THE UNITED STATES (2009).

[66] *See* BRAY HAMMOND, SOVEREIGNTY AND AN EMPTY PURSE (1970); ROGER LOWENSTEIN, WAYS AND MEANS: LINCOLN AND HIS CABINET AND THE FINANCING OF THE CIVIL WAR (2022); Lev Menand & Morgan Ricks, *Federal Corporate Law and the Business of Banking,* 88 U. CHI. L. REV. 1361, 1384–85 (2021).

vaults and then issuing United States Notes unbacked by any redemption commitment (the [in]famous "greenbacks") eventually responded with the creation, through two statutes, of the National Banking System.[67]

The National Banking Acts of 1863 (referred to at the time as the National Currency Act) and 1864 (the more significant piece of legislation) were designed to correct a specific problem. Namely, the greenback, created by Congress in 1862, was too public in its design. Together, the laws largely entrusted the new national banking system to the self-interest of bank stockholders and market surveillance by bank counterparties (1863), mediated by a new system of mandated reporting administered by the Comptroller (1864). They embodied, in short, the currency view.[68]

Note redemption was initially at the center of Congress's supervisory design. The law detailed precisely how and where notes were to be redeemed and what steps the Comptroller could take when "such association has refused to pay its circulating notes as aforesaid and is in default."[69] At the same time, because the law required national bank notes to be backed by U.S. bonds held by the Treasury, Congress made it functionally impossible for banks to fail to redeem their notes.[70] Like the state systems, the National Bank Acts used private liability as the core risk absorber, imposing double liability on bank stockholders. In the case of capital

[67] HAMMOND, *supra* note 66, at 60–62, 94–105, 168–69; MARGARET G. MYERS, A FINANCIAL HISTORY OF THE UNITED STATES 149–53 (1970); ROBERT P. SHARKEY, MONEY, CLASS, AND PARTY: AN ECONOMIC STUDY OF CIVIL WAR & RECONSTRUCTION 22–28, 255–69 (1959); Patrick Newman, The *Origins of the National Banking System*, 22 INDEP. REV. 383 (2018); John A. James & David F. Weiman, *The National Banking Acts and the Transformation of New York City Banking During the Civil War Era*, 71 J. ECON. HIST. 338 (2011).

[68] National Bank Act, ch. 58 §§ 12, 24, 50, 12 Stat. 665, 668, 671, 679 (1863); National Banking Act, ch. 106, §§ 12, 34, 53, 13 Stat. 99, 102–03, 109–10, 116 (1864).

[69] National Bank Act, ch. 58 §§ 25–29, 12 Stat. 665, 672–73 (1863); National Banking Act, ch. 106, §§ 26, 47, 13 Stat. 99, 107, 114 (1864).

[70] *See* HAMMOND, *supra* note 55.

impairment or outright failure, their personal resources could be called on to meet the liabilities of the bank, creating strong incentives for bank principals to carefully monitor their agent bank officers.[71]

The National Bank Acts represented the first major institutionalization of federal bank supervision in the United States, going much further than the Second Bank's more informal oversight mechanisms. To enforce sound bank behavior, the National Bank Acts mandated that national banks submit detailed quarterly statements of condition, which were then published in Washington D.C. and the bank's hometown paper.[72] It also created a corps of federal bank examiners, whose recruitment and professionalization were major priorities for the first Comptroller of the Currency, Hugh McCulloch. Congress and McCulloch, through legislation and its implementation, gave these examiners the power to inspect bank behavior and note issuance to ensure safety and soundness of the money and the banking institutions.[73] This inspection power enabled examiners to ensure banks complied, in McCulloch's phrase, "with the spirit and intention of the law."[74] To this end, the legislative and regulatory processes sought to maintain the negative power of note redemption as the ultimate check on unsound banking while adding some general ability to promote banking innovation generally.

While bank supervision evolved substantially from this point of origin, three artifacts of the Civil War period remain important to modern bank supervisory systems. First, McCulloch's role in shaping bank examination is essential

[71] *Id.*

[72] National Bank Act, ch. 58 §§ 24, 12 Stat. 665, 671 (1863); National Banking Act, ch. 106, §§ 34, 13 Stat. 99, 109–10 (1864).

[73] National Bank Act, ch. 58 §§ 51, 12 Stat. 665, 679–80 (1863); National Banking Act, ch. 106, §§ 54, 13 Stat. 99, 116 (1864); *see also* ROSS M. ROBERTSON, THE COMPTROLLER AND BANK SUPERVISION (Off. of the Comptroller of the Currency, 1968), 71–72.

[74] INSTRUCTIONS TO EXAM'RS OF NAT'L BANKS, S. EXEC. DOC. NO. 31, at 12–13 (1st Sess. 1881).

because the law gave little clear guidance on what federal examiners' responsibilities should be. Congress provided for examination regimes in the past, particularly for steamship boilers and imported medicines,[75] but these earlier regimes were designed to be ad hoc interventions rather than a permanent bureaucracy. Congress continued that approach in the National Banking Acts. Examiners would be appointed "as often as shall be deemed necessary and proper" by the Comptroller.[76] The innovation of giving supervisors discretion starts with that legislative delegation, with the very determination of when government oversight would be performed.

The second development was the almost immediate expansion of supervisory authority beyond the focus on the soundness of currency. "It is a common saying among bankers, when speaking of governmental supervision, 'Take care of the currency; make that as secure as possible, but do not interfere with the *business* of the banks,'" Comptroller Hiland R. Hulburd observed in 1869. "As far as practicable," he continued, "business *should be* left free and untrammeled; but in this country, the business of issuing circulating notes is so involved with the lending of money; the ability to redeem on demand is so dependent on the amount of reserve kept on hand, and the character of the loan, that it is impossible to apply safeguards to the currency, without applying prudence and reasonable restrictions to the business of lending."[77] Put differently, although the National Bank Acts made bank notes secure by backing them with U.S. bonds, the banking system

[75] The steam inspection regime of 1838 looked much like the bank examination regime of 1864, but in the meantime, the steam examination regime had made major advances that were not incorporated into bank examination. JERRY L. MASHAW, CREATING THE ADMINISTRATIVE CONSTITUTION: THE LOST ONE HUNDRED YEARS OF AMERICAN ADMINISTRATIVE LAW 187–208 (2012); Act of July 7, 1838, ch. 191, 5 Stat. 304.

[76] National Banking Act, ch. 106, § 54, 13 Stat. 99 (1864).

[77] ANNUAL REPORT OF THE OFF. OF THE COMPTROLLER OF THE CURRENCY XIII–XIV (1869).

was still replete with risks that could sweep away the banks. Supervisors needed to monitor and control those risks.

To provide prudence and occasional restrictions, McCulloch, Hulburd, and their successors took the ambiguities of legislation and interpreted them in favor of permanent, wide-ranging bank oversight. These early Comptrollers sought a thriving experiment in national banking, and that necessitated a partnership, intermediated by bank examiners, between the Comptroller and bankers. The key to this intermediation experiment was the development of discretionary supervisory tools, including chartering, examination, and receivership, and the backing provided to them by the new OCC and the emerging federal administrative bureaucracy.[78]

In the process of institutionalizing bank supervision, federal examiners were often compelled to interpret their broad congressional authority as attaching to more and more banking practices. Viewed positively, this involved guiding bankers toward "a straightforward, upright, legitimate banking business," as McCulloch phrased it, and away from "splendid financiering."[79] Bankers pushed back, sometimes aggressively: "There is no authority in law" to do what the Comptroller had done, the New York magazine *Financier* objected in January 1872; "[n]o such office as bank examiner was ever created." But by the time bankers started making this complaint, it was too late; the bank examiners would never depart the scene again.[80]

[78] For important works on the development of the American administrative state, see RICHARD BENSEL, YANKEE LEVIATHAN: THE ORIGINS OF CENTRAL STATE AUTHORITY IN AMERICA, 1859–77 (1990); BRIAN BALOGH, GOVERNMENT OUT OF SIGHT: THE MYSTERY OF NATIONAL AUTHORITY IN NINETEENTH- CENTURY AMERICA (2009); Jerry L. Mashaw, *Federal Administration and Administrative Law in the Gilded Age*, 119 YALE L.J. 1365 (2010).

[79] HUGH MCCULLOCH, INSTRUCTIONS AND SUGGESTIONS OF THE COMPTROLLER OF THE CURRENCY IN REGARD TO THE ORGANIZATION AND MANAGEMENT OF NATIONAL BANKS 35 (1864).

[80] *The Examination of Banks*, FINANCIER, Jan. 20, 1871, at 39.

The third major, enduring supervisory development that arose during this era was the discovery that purely public money—the greenbacks—and purely private money—the free banks—could not meet the political and financial needs of all parties. This recognition led to one of the central, durable themes of bank supervision: the adjudication between public and private actors for the responsibility of residual risk management. The business of banking would be left to the bankers, as Hulburd explained, subject to the prudence and restrictions imposed by the government through ongoing dialogue. The National Banking System thus created a framework for periodic oversight; however, it did not create a clear identification of which aspect of the system, public or private, would be left in control in the event of failure. That clarity would require many more decades of trials and errors.

Congress gradually liberated what had been a more rigid chartering process for national banks to a more permissive one in the 1870s. After that liberation, the motivating ethos of bank supervision began shifting from the currency approach that focused on verifying the soundness of currency issued by national banks to one that emphasized the business of banking more generally. The examination reports themselves marked this subtle transition. In essence, the reports were designed to enable examiners to perform the visitorial function of ensuring that banks abided by their charters, with specific sections set off to encourage scrutiny of whether banks maintained an adequate reserve or made loans in greater proportion to their capital than allowed by law. Reports not only included a recitation of the by-then standard call report, which recorded dividends to shareholders and other insider dealings, but also long sections of expansive commentary by examiners on all matters affecting the banks.[81] Examiners used the space, creating a running bureaucratic narrative about the life (and sometimes sickness and death) of each national bank.

[81] *See* Grace *Ballor*, Gabriela Recio & Sean H. Vanatta, *Surveillance Archive: Using Reports in Business History*, 18 MGMT. & ORG. HIST. 43, 46 (2023).

Most of these reports focused not on note issuance per se, but on the duty of examiners to evaluate—and sometimes correct or affirm—banker behavior. Examiners evaluated bank officers ("President:…of good means & the best financial standing;" "Cashier:…entirely competent for the position"). They looked at record keeping ("Records: in good shape;" "Other Books: well kept"). They evaluated bank assets ("Loans in good condition & closely looked after"). Examiners even considered the bank offices ("two story brick, good location") and the quality of the safe ("the best kind of burglar proof doors"). What examiners lacked was the authority to compel changes in behavior. Short of closing a bank, they could only guide, nudge, and cajole.[82]

By the 1870s, few of the examination reports look specifically at note issuance.[83] Instead, the rise of a new class of bank customers—the rising class of depositors—fundamentally changed the understanding of the business of banking and, with it, the nature of its federal supervision. The currency view of bank supervision was the dominant lens at the legislative beginning of federal bank supervision, but it receded in importance in the face of these changes almost immediately.

### B. *Scandals, Crises, and Bank Supervision, 1870–1907*

If the currency view of bank supervision was essentially stillborn, its successor regime was still not fully established. A major definitional problem remained. If bank examiners working for the Comptroller were a form of public risk managers for the private institutions, rather than simply monetary policymakers *avant la lettre*, who owned the

[82] Butler Ward, *Examiners Report (First Nat'l Bank, Le Roy, N.Y., Charter No. 937)* (Oct. 16, 1866) (on file with Nat'l Archives, Records of the Off. of the Comptroller of the Currency, Records of the Examining Division (Division of Reports) 1863–1927, Record Group 101.4, box 124).

[83] *See generally* Nat'l Archives, Records of the Off. of the Comptroller of the Currency, Records of the Examining Division (Division of Reports) 1863–1927, Record Group 101.4.

problem when private institutions failed? The Gilded Age would provide limited and unsatisfying answers to this question.

Scholars have focused at great length on the banking panics of the Gilded Age.[84] Less attention has been paid to the banking scandals of the Gilded Age. Each scandal played a major role in shaping the institutions of supervision toward the idea that private financial failure was not merely the domain of private financiers.

The first major scandal for bank supervision was the Callender affair, which unfolded dramatically in the early 1870s. The protagonist, Charles Callender, had been a clerk in the Currency Bureau and then a National Bank Examiner, covering Philadelphia and later New York City. Callender developed a reputation for forbearance, pursuing what the press called a "'nursing' policy" of keeping "moribund institutions alive if possible," even when their condition warranted closure.[85] After three of these banks failed spectacularly in 1871, the public learned that supervisory forbearance was the least of Callender's crimes. He was actively extorting the banks under his supervision. Congress and the press exploded in indignation. The corrupt examiner became a byword for the corruption of the age.[86] Callender's case profoundly shaped the Comptroller's posture toward

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[84] *See* OLIVER MITCHELL WENTWORTH SPRAGUE, HISTORY OF CRISES UNDER THE NATIONAL BANKING SYSTEM, S. DOC. NO. 61-538, at 89–90 (1910); ELMUS WICKER, THE BANKING PANICS OF THE GREAT DEPRESSION (2000); RICHARD WHITE, THE REPUBLIC FOR WHICH IT STANDS: THE UNITED STATES DURING RECONSTRUCTION AND THE GILDED AGE, 1865–1896 (2017).

[85] *Stability of the Monetary Situation*, COM. AND FIN. CHRON., Dec. 16, 1871, at 794, https://fraser.stlouisfed.org/title/commercial-financial-chronicle-1339/december-16-1871-528120 [https://perma.cc/24KL-GLJC].

[86] *The Bank Examination Fraud*, CHI. TRIB., Dec. 24, 1871, at 4; *Callender Held to Bail*, N.Y. TIMES, Dec. 21, 1871, at 2; *The Case of Callender—Examination of the President of the Ocean Bank*, N.Y. TIMES, Dec. 28, 1871, at 2; *Trial of Ex-Bank Examiner Callender*, N.Y. TIMES, May 31, 1874, at 2.

supervision in anticipation of the even more devastating 1873 Panic.[87]

Callender's misdeeds inspired hot outrage. "A graver charge was never laid at a man's door," the *Chicago Tribune* declared. "Not alone because he was bleeding weak banks by blackmail, not alone because he was using his official position to illegally increase his income, but because he was aiming a direct blow at the commerce of the country by bolstering rotten banks." Bolstering rotten banks allowed the rot to spread—building up risk in a system where private, personal responsibility was the only risk absorber. As such, Callender's misdeeds fundamentally undermined the legitimacy of the nascent national banking system and its supervisory regime. It also led to a frank acknowledgment that supervision was, at least in part, a partnership between public and private institutions. "The best thing to do with the position," the *Financier* wrote in 1872, "is to leave it unfilled altogether and let Mr. Callender's odium remain as its memorial." Instead, the Comptroller allowed the New York Clearinghouse, a private institution, to nominate Callender's replacement, Charles A. Meigs (Clearinghouse bankers, appointed as ad hoc examiners, had rooted out Callender's misdeeds in the first place). Private sector control over federal appointments—not influence, but absolute control—remained an informal tradition that continued well into the twentieth century.[88]

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[87] *Charles Callender's Loans*, N.Y. TIMES, Mar. 31, 1874, at 4; *Failures of National Banks*: *Hearing Before the H. Comm. on Banking and Currency*, 42nd Cong., H. Misc. Doc. 42-153 (1872) at 5. The scandal also implicated or exposed Boss Tweed (a director of one of the corrupt banks) and Comptroller Hurlburd (under a cloud of suspicion after he accepted a carriage from a national banker who accused him of importuning a bribe.) *See* Jeffrey D. Broxmeyer, *Political Capitalism in the Gilded Age: The Tammany Bank Run of 1871*, **16 J. GILDED AGE & PROG. ERA 44 (2017)**; *The Case of Callender*, N.Y. TIMES, Dec. 28, 1871, at 2; *Financial Troubles*, N.Y. TRIB., Dec. 13, 1871, at 1; *Failures of National Banks*, *supra*, at 15, 39.

[88] *The Examination of Banks*, FINANCIER, Jan. 20, 1872; John A. James & David F. Weinman, *The National Banking Acts and the Transformation of New York City Banking During the Civil War Era*, 71 J. ECON. HIST. 338

The Panic of 1873 accelerated this trend toward private risk management. In September 1873, the merchant bank Jay Cooke & Company failed, sparking a major financial panic.[89] As country banks called in their reserves and cash drained from New York, the Comptroller was powerless. The Comptroller's tools—chartering, examination, forbearance, and liquidation—were not sufficient to manage financial panic because the Comptroller did not have the one thing that a panic needed: money. Writing the same year as the panic, the British economist Walter Bagehot famously wrote that panics are "a species of neuralgia, and according to the rules of science you must not starve it. The holders of the cash reserve must be ready not only to keep it for their own liabilities, but to advance it most freely for the liabilities of others."[90] This is the famous "lender of last resort" function, but the Comptroller could not perform it. There was no financial mechanism for a process that had been located unevenly through banks chartered at both the state and federal level.[91]

In the absence of that public balance sheet, leadership fell instead to the private Clearinghouse. In response to the crisis, the New York Clearinghouse worked backwards from the Comptroller. It started with the provision of liquidity via its balance sheet (or at least, its bespoke payment system and the

(2011); Patrick Newman, *Origins of the National Banking System*, 22 INDEP. REV. 383 (2018).

[89] The Panic of 1873 exercised a major impact on the political and economic landscape of the U.S., perhaps hastening the end of Reconstruction. *See* WHITE, *supra* note 84, at 264–73; IRWIN UNGER, THE GREENBACK ERA: A SOCIAL AND POLITICAL HISTORY OF AMERICAN FINANCE, 1865–1879, at 164-65, 190-94, 213-15 (1964); Nicolas Barreyre, *The Politics of Economic Crises: The Panic of 1873, the End of Reconstruction, and the Realignment of American Politics*, 10 J. GILDED AGE & PROG. ERA 403 (2011).

[90] WALTER BAGEHOT, LOMBARD STREET A DESCRIPTION OF THE MONEY MARKET 51 (3d ed. 1873).

[91] In moments of panic, the Treasury secretary would often inject cash into the New York money market, either by pre-paying treasury bonds or increasing federal deposits in New York City banks. *See* MARGARET MYERS, A FINANCIAL HISTORY OF THE UNITED STATES 189 (1970); *see* SPRAGUE, *supra* note 84, at 89–90.

balance sheets of its member organizations) and moved toward supervision only as it followed from that liquidity support. If the Panic of 1873 revealed how much supervision had become a public-private partnership, it also revealed a singular defect in the then-junior public partner. In 1873, the Clearinghouse served the lender of last resort function. As the crises of the Gilded Age continued, it would become clear that the Clearinghouse could not or would not continue it.

This combination of scandal and crisis marked the Gilded Age and profoundly shaped the institutions of bank supervision. Just as examiners lacked the tools to combat panic, they also struggled to root out another persistent source of bank failure: fraud. Fraud detection as a supervisory calling was likewise rooted in the visitorial power. Examiners could and did detect fraud. Examiner Andrew Mygatt, *The New York Times* observed, "ha[d] brought many cashiers to the state prison."[92] Yet the fundamental information asymmetry between (dishonest) bankers and federal examiners who showed up annually to inspect their books was profound. The consequences of fraud were also asymmetric. When examiners failed to detect fraud, and especially when defalcations resulted in losses to bank depositors, such supervisory failures undercut the legitimacy of federal oversight. After a major fraud scandal in the early 1880s, observers began to recycle the objections to examination raised by the New York legislature in the 1840s; when bankers were honest, examiners weren't needed, and when bankers were dishonest, examiners were hopelessly out of their depth. "He is a stranger," the *Century Magazine* observed in March 1882, who "can know little, except by hearsay, of the character and habits of the bank's officers, or of the security of its loans."[93]

In response to these twin failures—in crisis prevention and fraud prevention—Comptroller John Jay Knox and his successors began to articulate a revised vision of federal bank examiners' behind-the-scenes work. Knox pushed

[92] *Bank Examiner Mygatt*, N.Y. TIMES, Mar. 7, 1886, at 7.

[93] *Broken Banks and Lax Directors,* CENTURY ILLUSTRATED MAG., Mar. 26, 1882, at 770.

examination away from the image of courageous fraud detection, acknowledging in his statements to Congress that examiners were unlikely to catch the long cons that dominated the headlines. Instead, in acknowledgement of the asymmetries that undercut supervision, Knox sought to make private shareholders and their appointed directors the primary risk monitors and absorbers in the banking system. "The examiner can have but a limited knowledge of the habits and character of those employed in the bank," Knox explained to Congress in 1881. He further elaborated:

> If the teller is making false entries, and daily abstracting the funds of the bank; if the bookkeeper is keeping false accounts and rendering untrue statements; if the cashier is placing forged paper among the bills receivable and upon the register book, and transmitting such paper to distant places where it is purported to be payable, it is not possible for an examiner, in a day or two, to unravel this evil work, which may have continued for months, and obtain a correct balance sheet.[94]

If the examiner's duty, then, was not to be a perfect fraud detective, it was instead "to inform himself of the condition of the bank, and to require that its business shall be conducted in conformity with law."[95] Knox wanted the banks' directors to be the sole owners of residual risk, financial or otherwise, because "[t]he men employed by them in the banks are under their supervision."[96] "The directory must continuously look after its own servants. The examiner looks after the acts of the directors."[97] To accomplish this, examiners would highlight the "restrictions . . . intended to protect these institutions, by imposing upon them general rules, which experience has shown may be properly done by the government *without its thereby becoming the guardian of the bank, or of the moneys of*

[94] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY XXXVI (1881).
[95] *Id.* at XXXVI.
[96] *Id.* at XXXV.
[97] *Id.* at XXXVII.

*its depositors or stockholders, or being in any way responsible for the management of its funds*."[98] The mood Knox offers—which reflected a sympathetic banking press—was a choice for bank supervision in this period of institutional design.[99]

It seemed, then, that the ideal of governmental actors standing behind private institutions and their own internal risk management would be the norm. It was not to be. The three remaining major crises of the Gilded Age—in 1884, 1893, and 1907—and a slew of further financial scandals created even more distance between the demands made to the private bank supervisory system and what that system could deliver politically. Initially, the supervisors tried to insist that theirs was not a residual risk-bearing responsibility. Comptroller Edward S. Lacy remarked in 1891, "The duties of the Comptroller, and in some sense the examiners, are largely negative . . . . The Comptroller is therefore mainly charged with the responsibility of indicating to bank managers what they shall not do."[100]

But the Clearinghouse could not assume the positive role it had adopted in 1873, either. Then, the Clearinghouse banks pooled their reserves to meet the cash demands of country bankers, who sought to recall their reserves from New York to meet nervous depositors at home.[101] Demands fell heaviest on banks with large out-of-town balances, while responsibility for propping up the system fell on strong banks focused on the New York market. Resentment provided fertile soil for self-interest. In future panics, the Clearinghouse rejected reserve pooling, while the leading banks, in economic historian O. M.

[98] *Id.* at XXXV.

[99] *Id.* at XXXV (1881); *Bank Examinations and Bank Directors*, 36 BANKERS' MAG. & STAT. REG. 414 (Dec. 1881); *Bank Examinations*, 36 BANKERS' MAG. & STAT. REG. 542 (Jan. 1882); *Bank Examinations*, INDEPENDENT, Jan. 12, 1882; *Broken Banks, supra* note 93, at 771–72; *Bank Examinations and Bank Directors*, 39 BANKERS' MAG. & STAT. REG. 241 (Oct. 1884); *Bank Examinations*, 39 BANKERS' MAG. & STAT. REG. 483 (Jan. 1885); *Bank Examinations Once More*, 39 BANKERS' MAG. & STAT. REG. 651 (Mar. 1885).

[100] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 27 (1891).

[101] *See* SPRAGUE, *supra* note 84.

W. Sprague's measured view, did "not seem to have been rendering anything like that assistance which their resources would have permitted," despite the federal government placing large cash deposits in these same banks.[102] In the severe crises of 1893 and 1907, this allowed the panic to metastasize and spread across the country.

Another key development of the period was the fundamental change in the banking business model away from the reliance on note issuance and toward maturity transformation and the holding of deposits. This development also undermined the currency and monetary vision of the original national banking system, but for a very different reason. More bluntly, by the early 1880s it was no longer profitable for national banks to issue bank notes, which formed the foundation of the nation's circulating currency.[103] The transition to deposit banking is arguably one of the most important economic and financial transitions in U.S. financial history. Instead of handing notes across the counter, banks made loans by crediting a depositor's checking account. The borrower could then write checks against money *within* the bank, as deposits, rather than spending cash that circulated outside of it.[104] In 1867, there were roughly $1.70 in deposits for every dollar of circulating currency (specie, greenbacks, bank notes). By 1890, the ratio was five to one, at which point the Comptroller determined that "the deposits of a national bank are now its principal source of profit."[105] By 1914, there were more than ten dollars in deposits for every dollar in currency.[106] Even as debates about the form of American

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[102] *Id.* at 268.

[103] *See* Charles Calomiris & Joseph Mason, *Resolving the Puzzle of the Underissuance of National Bank Notes*, 45 EXPL. ECON. HIST. 327 (2008); Matthew Jaremski & Peter Rousseau, *The Dawn of an 'Age of Deposits' in the United States*, 87 J. BANKING & FIN. 264 (2018).

[104] *See* H. G. Moulton, *Commercial Banking and Capital Formation: I*, 26 J. POL. ECON. 498 (1918).

[105] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 10 (1890).

[106] *See* JOHN JAMES, MONEY AND CAPITAL MARKETS IN POSTBELLUM AMERICA 22 (1978).

physical currency raged—first between greenbacks and gold, and then between gold and silver—deposits quietly became the primary form of American money.[107]

This new reality created some tensions in the relationship between bank lending, bank failure, and supervisory oversight. Within the note-issue paradigm, comptrollers had largely conceptualized bank failure as note fraud, a matter of particular concern for the Comptroller, whose office had the task of defending that currency—i.e., the notes issued by national banks. By the 1880s, it was clear that honest but incompetent lending decisions could just as easily jeopardize a bank. The Comptroller could not protect the currency simply by enforcing the rules. But federal examiners were not equipped to monitor or evaluate the loans of the nation's banks using pure discretion either. Even if they did so, bankers could now look to the states for a lighter supervisory touch. This meant that banks that had little interest in note issuance but deep interest in deposit taking were now just as much a part of the nation's currency system, but well outside the Comptroller's reach. "The exact line at which the Government shall interfere and the point at which Government discipline shall commence," Comptroller Henry Cannon wrote in 1884, "is a matter of some delicacy to determine."[108]

The rise of deposit banking also exposed the core inadequacy of the Comptroller's effort to shift risk management onto private bank shareholders. With double liability, bank shareholders bore much of the risk of failure, but not all of it. As deposits became a larger share of bank liabilities, depositors in turn became, as a group, a larger holder of the residual risk. Note holders were secure but depositors were not. This imbalance created more momentum for bank runs because unsecured depositors sought to quickly

[107] *See* Bruce G. Carruthers & Sarah Babb, *The Color of Money and the Nature of Value: Greenbacks and Gold in Postbellum America*, 101 AM. J. SOCIO. 1556 (1996); *Comptroller Knox on the Currency*, WASH. POST, Aug. 15, 1881, at 2.

[108] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY, at L (1884).

convert their deposits into secure notes at any sign of trouble. Political calls for new risk management philosophies, rooted not, or not only, in private liability, but rather in central banking or deposit insurance, grew louder over time.

Several comptrollers endorsed these calls. As they waited for congressional action, these comptrollers also developed new discretionary tools to manage risk where they could. First, the comptroller sought to increase loan quality and bank liquidity through loan criticism. Over the nineteenth and into the twentieth century, examiners developed metrics for evaluating bank assets that ranged from slow (illiquid) to loss.[109] Loan criticism enabled examiners to guide banker behavior, especially toward standards of liquidity in line with commercial banking theory (i.e., the real bills doctrine). In moments of panic, the comptroller also adopted forbearance. Instead of necessarily liquidating a bank that closed its doors to halt frantic depositor withdrawals, the comptroller could instead allow the bank to resume business (for example, after the arrival of a transcontinental shipment of currency).[110] While significant, these powers proved insufficient to overcome the moments of severe neuralgia. The punishing crises of 1893 and 1907, which the comptroller was virtually powerless to forestall without the means of converting deposits into notes, created momentum for reform.

At the end of the Gilded Age, bank supervision was well established as a mechanism for ensuring private and public

[109] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY, 26–27 (1891); Letter from Leo T. Crowley to Marriner S. Eccles (Feb. 9, 1938), 120 DIARIES OF HENRY MORGENTHAU JR. 289, on file with FRASER, https://fraser.stlouisfed.org/archival-collection/diaries-henry-morgenthau-jr-6880/volume-120-634692?page=296 [https://perma.cc/NCD3-F425]; 225 Bank Suspensions: Case Histories from Examiners' Reports (1933), FEDERAL RESERVE, COM. ON BRANCH, CHAIN, & GROUP BANKING 15, on file with FRASER, https://fraser.stlouisfed.org/title/225-bank-suspensions-797 [https://perma.cc/7NZ9-YB85]. The Federal Reserve lists this report as circa 1932, but the final version was completed in 1933.

[110] Charles W. Calomiris & Mark Carlson, *Bank Examiners' Information and Expertise and their Role in Monitoring and Disciplining Banks Before and During the Panic of 1893,* 54 J. MONEY, CREDIT & BANKING 381 (2022).

collaboration with financial management. The ability for bank supervisors to do more than nudge and cudgel bankers to protect themselves, however, was not yet a part of the institutional landscape. That would come, awkwardly and in starts, during the Progressive Era.

### *C. Institutional Layering and the Risk Management Model of Bank Supervision, 1907–1925*

Among the many reasons the U.S. Federal Reserve System eventually entered the institutional landscape of American finance, providing the missing authority behind risk management and supervision backed by a plausible balance sheet was chief among them. "The depositing bank," the Comptroller of the Currency proposed shortly after the Panic of 1907, "could be sure that at any time, as long as it was solvent, it could go to the central bank and get any amount of cash needed on the notes of its customers, or other good security."[111]

The need to unite the two functions of supervisory risk management and governmental balance sheet support was well apparent after the nineteenth century's crippling rhythm of financial panics. The institutional posture of shared risk management via the Comptroller of the Currency was already reasonably well-entrenched by the early twentieth century, despite the objections from some bankers early on. But the idea of the balance sheet necessary to make good on those supervisory commitments was still politically toxic in many corners of the American polity. That anathematic quality of a central bank made the path from the Panic of 1907 to the passage of the Federal Reserve Act of 1913 a circuitous one at best.[112] It also meant that the final result was not, as some scholars have argued, a great rethink of pre-existing monetary

[111] ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 71 (1907).

[112] *See* ROGER LOWENSTEIN, AMERICA'S BANK: THE EPIC STRUGGLE TO CREATE THE FEDERAL RESERVE (2016); PETER CONTI-BROWN, THE POWER AND INDEPENDENCE OF THE FEDERAL RESERVE (2016).

frameworks so much as it was an instance of important, politically inflected institutional layering.[113] What emerged from this pivotal period in the institutional development of bank supervision was two-fold: bank supervision would flow into the new creature of the U.S. Federal Reserve System, but it would do so according to a logic that would look quite different from what had come before.

The explanations for the strange legislative path are manifold, reflecting the diverse coalitional interests behind "currency reform" that ultimately led to the System's creation. The institutional interests of the Comptroller of the Currency are a good place to start. The obvious debilities in the national banking system did not lead to the Comptroller's advocacy for the elimination of the national banks, but to the layering of more federal institutional complexity. Shortly after the Panic of 1907, Theodore Roosevelt appointed Lawrence O. Murray as Comptroller, with a charge to reform the system. "When I became comptroller it seemed to me that we needed three things," Murray explained to Congress in 1908, "a more efficient law for the comptroller to work under, whereby he would be taken out of the category of a common scold and given the power to do something; better examinations of the banks by bank examiners; and more cooperation or direction by the directors."[114] Murray recognized that, although private shareholders backstopped the banking system through their personal liability, the financial and political consequences of failure exceed the capacity of the private risk buffer. The

[113] For the view that the Federal Reserve Act followed a specific intellectual design and logic independent of political processes, see Menand, *Logic and Limits*, *supra* note 7. Although the concept has enjoyed a long and circuitous metahistory, see Jeroen van der Heijden, *Institutional Layering: A Review of the Use of the Concept*, 31 POLITICS 9 (2011), institutional layering refers to the idea that "new rules are attached to existing ones, thereby changing the ways in which original rules structure behavior." *See* JAMES MAHONEY & KATHLEEN THELEN, *A Theory of Gradual Institutional Change*, *in* EXPLAINING INSTITUTIONAL CHANGE: AMBIGUITY, AGENCY, AND POWER 16 (2010).

[114] *Hearings Before the Nat'l Monetary Comm'n*, 60th Cong. 78 (1908) (statement of Lawrence O. Murray, Comptroller of the Currency).

residual rested with the public. Murray sought more power to manage that risk.

The time between the Panic of 1907 and the passage of the Federal Reserve Act coincided with a significant expansion of the supervisory function under Murray's leadership, including the implementation of more rigorous professionalization standards for bank supervisors, the expansion of counterparty supervision of nonbank (and non-national banks), and the substantial reorganization of the entire examination force.[115] In the final Federal Reserve Act, Murray and others succeeded in preserving the Comptroller and the national banking system, and with them a discretionary supervision rooted in the visitorial power. They also further professionalized the examination corps by placing them on salaries rather than the fee-for-examination model that had existed for the previous fifty years.[116] Both these achievements entrenched bank supervision in a risk management posture, placing a professional corps of bank examiners ever-present in the halls of private financial institutions rather than permitting the quasi-public central bank to function in the currency view of counterparty supervision that existed elsewhere.

While the Federal Reserve System that emerged from the legislative process was modeled in some ways on central banks elsewhere in the world, the unique institutional layering on top of the American system introduced opportunities for institutional fragmentation and institutional innovation alike.[117] The fragmentation occurred through the addition of more supervisory engagement by the Federal Reserve. Congress granted the Fed the authority to

[115] *Controller Warns Bank Examiners*, N.Y. TIMES, Sept. 22, 1908; *Nat. Bank Examiner at Large*, WALL ST. J., Jan. 11, 1909; *To Inform Bank Examiners,* WALL ST. J., May 18, 1910; *Comptroller's Credit Bureau*, WALL ST. J., Sept. 28, 1910; *Shakeup of Bank Examiners*, CHI. DAILY TRIB., Sept. 8, 1910.

[116] *See* NICHOLAS R. PARRILLO, AGAINST THE PROFIT MOTIVE: THE SALARY REVOLUTION IN AMERICAN GOVERNMENT, 1780–1940 (2013).

[117] J. LAWRENCE BROZ, THE INTERNATIONAL ORIGINS OF THE FEDERAL RESERVE (1997).

examine banks through the Comptroller itself, through state examiners and through examiners appointed by the Fed.[118] Yet, while the Fed could in theory examine through these existing institutions, its supervisory objectives ran in different directions from the very beginning, as dictated by its core risk management tool—namely, its balance sheet (or, more precisely, the balance sheets of the individual federal reserve banks). In 1918, the Board laid out a simple examination philosophy: "The primary object of Federal Reserve examinations will be to obtain more detailed information as to credits."[119] This was not, then, visitorial power derived from the sovereign chartering authority; rather, it was a form of private risk management, aimed at protecting the balance sheets of the reserve banks from credit risk, rather than policing bank compliance with chartering provisions. Nevertheless, Congress empowered the Fed not only to examine bank assets when presented for rediscount, but also to use the visitorial power of examination to proactively monitor bank behavior long before the Fed pulled private risk onto its quasi-public balance sheet.

Thus, after the founding of the Federal Reserve System, the state of bank supervision consisted as follows. The Comptroller of the Currency's corps of bank examiners, now mostly independent of the Clearinghouses, was professional, salaried, and managing themselves in the space between the public and private financial system. States throughout the country had largely adopted the Comptroller's model of open chartering and bank examination.[120] This was a coordinated

[118] Federal Reserve Act of 1913, 12 U.S.C. § 481.

[119] Letter from Warren P. G. Harding, Fed. Reserve Governor, to Carter Glass, Fed. Reserve Chairman, regarding the Department of Examination, No. X-1327, 9 *Mimeograph Letters and Statements of the Board 143* (Dec. 23, 1918), on file with FRASER, https://fraser.stlouisfed.org/archival-collection/mimeograph-letters-statements-board- 4957/letter-governor-re-department-examination-federal-reserve-banks-512234 [https://perma.cc/AQ6L-CMCS].

[120] *See* George Barnett, Nat'l Monetary Comm'n, State Banks and Trust Companies Since the Passage of the National-Bank Act, 61st Cong., S. Doc. No. 61-659 (1911).

effort: in 1902, the states founded the National Association of Supervisors of State Banks, an organization designed to coordinate state bank supervisory efforts against the threat of national bank dominance.[121] With the advent of the Federal Reserve System, these two communities of examiners, state and federal, were joined by a third wedged between them.[122] The Fed's examiners, at this early stage, relied on the examination efforts of both state and national bank examiners and introduced their own corps as well.

Things did not go smoothly with that division of labor. One node of conflict centered on when and how the Federal Reserve Board and the Federal Reserve Banks should have access to the detailed information about individual banks' businesses collected through the Comptroller's examination reports. Most of the directors of the Federal Reserve Banks were themselves bankers, or close associates of bankers. Indeed, Congress designed these curious institutions to allow member banks to fill two-thirds of the board seats. Even the other third, filled by the Federal Reserve Board, had to include two of three members with "tested banking experience."[123] The Federal Reserve System was built by politicians, largely for the benefit and with the close participation of bankers.[124] This proximity created a problem for bank supervision, given the sensitive

[121] Nat'l Ass'n of Supervisors of State Banks, Proceedings of the Fourth Annual Convention of the National Association of Supervisors of State Banks, at iv (Madison, Wis.: Democrat Printing Co. 1905). This organization is now the Conference of State Bank Supervisors.

[122] Before the founding of the Federal Reserve, city clearinghouses also undertook supervision of member banks. Like formal government oversight, these practices evolved from an ad hoc system performed by bankers to a formal system enacted by salaried, independent examiners. The Chicago Clearinghouse was the first to hire a dedicated examiner in 1907, and it was soon followed by others. *See* JAMES G. CANNON, NAT'L MONETARY COMM'N, CLEARING-HOUSES 137, 61st Cong., S. DOC. NO. 61-491 (1910).

[123] The original provisions were in Section 4 of the Federal Reserve Act. This provision is among the most amended of the Federal Reserve Act, but the bankers still retain much of their influence.

[124] *See* LAURENCE BROZ, THE INTERNATIONAL ORIGINS OF THE FEDERAL RESERVE SYSTEM (2009); KOLKO, *supra* note 12.

information contained in examination reports that would be provided to Fed directors and written about these directors' competitors. Members of the Federal Reserve Board, tasked ambiguously with supervision over supervision, were immediately keyed into this dynamic. "[U]nder no circumstances should any information contained in the Bank Examiner's reports be open for the inspection of the directors of any Federal Reserve Bank," an early member of the Federal Reserve Board wrote to the Comptroller of the Currency in December 1914.[125] The Comptroller went one step further, suggesting that the Federal Reserve Act allowed but did not require the Comptroller to share reports with the Board.[126]

In a broader sense, the goal of the tripartite structure was to promote coordination and cooperation across three risk management systems (state, comptroller, and federal). In practice, however, institutional competition encouraged risk avoidance and risk shifting. Already in the dual chartering system, the comptroller and state supervisors worked to entice strong banks into their oversight regimes while

[125] Letter from Warren P. G. Harding, Fed. Reserve Governor, to the Chairmen of all Fed. Reserve Banks, on the Right of Directors of Federal Reserve Banks and Branches to Examine Reports of Examination of Member Banks (Feb. 2, 1922), No. X-3318, 16 MIMEOGRAPHED LETTERS AND STATEMENTS OF THE BOARD 119 (quoting a letter from Preston Delano to the Comptroller of the Currency (Dec. 22, 1914)), on file with FRASER, https://fraser.stlouisfed.org/archival-collection/mimeograph-letters-statements-board-4957/letter-governor-re-right-directors-federal-reserve-banks-branches-examine-reports-examination-member-banks-511603/ [https://perma.cc/8B7W-RZWF].

[126] Meeting Minutes (Oct. 15, 1915), 2 MINUTES OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM 862, 865–66, https://fraser.stlouisfed.org/title/minutes-board-governors-federal-reserve-system-821/meeting-minutes-october-15-1915-28714 [https://perma.cc/6DJW-N53M]; Charles S. Hamlin, Diary Entry Regarding His Report on Fed. Reserve Authority over the Comptroller (Oct. 21, 1915) (on file with Libr. of Cong., Charles S. Hamlin Papers, Correspondence, 1869–1955, Box 356, Vol. 3 (Jan. 17, 1915–Aug. 30, 1916), at 122), https://www.loc.gov/resource/mss24661b.35617/?sp=40&st=image [https://perma.cc/UFX4-U352].

expelling weak banks into rival systems.[127] The Fed added a new outlet for risk shifting.

The Fed examiners also developed their own modes of risk management, focused on "modernizing" the lending practices of member banks. Because the Reserve Banks' risk management operated through their balance sheets, Reserve Banks (and the board, as their supervisor), took a keen interest in the quality of loans that they would rediscount. Under the rubric of "acceptability"—that is, mandating to member banks what assets would be acceptable for rediscount—Reserve Banks required increasingly thorough documentation from member banks, including credit files and balance sheets for borrowers.[128] The Reserve Banks even developed industry-specific forms to account for idiosyncratic land tenure and credit practices. In one case, the San Francisco and Atlanta banks developed forms for citrus growers, which pressed cost accounting into the Florida swamp by imposing new supervision requirements on member banks.[129] To protect its balance sheets—or the collective balance sheets of the Reserve Banks—the Fed sought to compel more robust risk management within the private banks.

U.S. finance thrived throughout the 1910s and 1920s. At the time, some attributed this to the genius of the Federal Reserve System, a refrain that grew in enthusiasm as the 1920s advanced, including when Congress debated whether to

[127] *See* HAMMOND, SOVEREIGNTY AND AN EMPTY PURSE, *supra* note 66, at 349–50.

[128] *See e.g.*, Letter from Walter Eddy to C. C. Henking Noting the Impracticability of Uniform Financial Statements (Dec. 12, 1923) (on file with Nat'l Archives, Records of the Fed. Rsrv. Sys., Rec. Grp. 82, Box 1348, Folder 3), https://fraser.stlouisfed.org/archival/1344/item/540583 [https://perma.cc/PU6U-R7LC].

[129] V. K. Bowman, Assistant Cashier, Fed. Rsrv. Bank of Atlanta, Citrus & Truck Industry in 6th Fed. Rsrv. District: Memorandum to Oscar Newton (July 18, 1927) (on file with Nat'l Archives, Records of the Fed. Rsrv. Sys., Rec. Grp. 82, Box 1348, Folder 4), https://fraser.stlouisfed.org/archival-collection/records-federal-reserve-system-1344/eligibility-paper-financial-statements-1927-1941-540584 [https://perma.cc/NC8Z-UJ7W].

extend the Federal Reserve's congressional charter in perpetuity in 1927.[130] There was a hollowness to this enthusiasm and to its causal attributions. The Great War had devastated rival international financial centers, leaving the United States as the victor by default. A rising availability of opportunities, at home and abroad, for banks meant that examiners' willingness and even ability to identify with confidence risk factors that might end in crisis were checked by market enthusiasm and inexperience.

At the end of this burst of legislative creation, then, stood the U.S. Federal Reserve System, with a supervisory corps that looked much like its alternatives housed in the Comptroller and state bank regulators, but with an ethos that was fundamentally different. The Fed's balance sheet put public and private money on the hook for managing residual risk. But the purpose was to protect that balance sheet, not to defend itself in an evermore heated competition for bank charters. The legacy of this ethos and this chartering competition within the tripartite bank supervisory landscape would find its nadir in the devastating banking panics of the 1930s.

### *D. Institutional Innovation, Institutional Fragmentation: 1925 – 1945*

Crisis, of course, came as it always does—slowly, then suddenly. Initially, banks failed primarily in the rural agricultural regions of the Midwest and Southeast. Suspensions came constantly, in waves. In 1925, banks failed at a rate of 52 a month, a number that reached 55 a month by 1929. Most of these failures were small institutions; sixty percent had a capital stock of $25,000 or less; four-fifths were in towns of fewer than 2,500 inhabitants. The vast majority of

[130] *See e.g.*, Frank A. Vanderlip, *Should the Federal Reserve Banks be Rechartered Now*, BANKERS' MAG., May 1926, at 677; Andrew Mellon, *Why the Reserve Bank Charters Should be Renewed Now*, BANKERS' MAG., Jun. 1926, at 805.

these were neither national banks nor members of the Federal Reserve System.[131] By 1930, the pace of failure quickened, revealing profound inadequacies within the supervisory toolkit and prevailing modes of risk management.[132] In the decades prior, states and the federal government had ceased using chartering as a site of supervisory discretion. Moreover, the continued upsurge in bank deposits meant that depositors bore an ever-larger quotient of financial risk in relation to bank shareholders, whose liability was capped. This imbalance likely encouraged entrepreneurs to found far more banks than necessary.

Despite the creation of a federal balance sheet to promote financial stability, the deployment of that balance sheet for residual risk management was not yet the modus operandi. Supervision remained rooted in a postbellum ethos of mostly toothless discretion; supervisors could scold bankers for their decisions but had little else they could do besides send them into receivership—something that bankers, politicians, and even supervisors themselves were often loathe to do. With so many banks already in existence, the primary reform options centered on different ways of diversifying bank assets (that is to say, encouraging private risk management), either through branch banking (diversifying exposure to rural and urban loans) and asset liberalization (enabling banks to buy bonds, engage in long term lending, and more). The McFadden Act

[131] EUGENE N. WHITE, THE REGULATION AND REFORM OF THE AMERICAN BANKING SYSTEM, 1900–1929, at 126–87, esp. 132 (1983); WICKER, *supra* note 84, at 5–6; Gary Richardson, *Categories and Causes of Bank Distress During the Great Depression, 1929–1933: The Illiquidity Versus Insolvency Debate Revisited*, 44 EXPL. IN ECON. HIST. 588 (2007).

[132] OFF. OF THE COMPTROLLER OF THE CURRENCY, DOC. NO. 3032, ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 2–3 (1930); OFF. OF THE COMPTROLLER OF THE CURRENCY, DOC. NO. 3046, ANNUAL REPORT OF THE COMPTROLLER OF THE CURRENCY 2 (1931); Eugene N. White, *'To Establish a More Effective Supervision of Banking': How the Birth of the Fed Altered Bank Supervision,* in A RETURN TO JEKYLL ISLAND: THE ORIGINS, HISTORY, AND FUTURE OF THE FEDERAL RESERVE 46 (Michael D. Bordo & William Roberds eds., 2013).

took steps toward branching and asset liberalization, with mixed results.[133]

In essence, as the crisis deepened after the stock market crash in 1929, supervisors were in a bind. They took the view that bankers still owned the risk in the financial system, but they also understood that those risks were asymmetric, falling narrowly on bank depositors and more broadly on the communities served by small banks. As such, although supervisors understood the dire condition of the banks, they would not take responsibility for closing them. The political consequences were too dire. Throughout the banking crises of the 1930s, supervisors practiced forbearance, trying to instill public confidence by keeping the banks open. When the need for assertive rescue action became unavoidable, Hoover looked to private risk management, organizing the National Credit Corporation to take on risk that the Federal Reserve Banks would not. As the pace of failure accelerated in 1931-1932, so too did the deterioration of Herbert Hoover's political prospects. After Franklin Roosevelt's landslide in 1932, things got worse, starting in the Upper Midwest and soon spreading to the rest of the country. Within hours of Roosevelt's inauguration in 1933, the entire national financial system was shut down in a government-ordered "holiday."[134]

This episode is simultaneously one of the most important in U.S. political history and one of the most misunderstood.[135]

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[133] *See* H. H. Preston, *The McFadden Banking Act*, 17 AM. ECON. REV 201 (1927).

[134] We develop the arguments below at more length in Conti-Brown & Vanatta, *supra* note 17.

[135] Franklin D. Roosevelt, Fireside Chat on Banking (Mar. 12, 1933), https://www.presidency.ucsb.edu/documents/fireside-chat-banking [https://perma.cc/8ED3-GGQS]. This is one of the most well-documented periods in the history of the New Deal, including with important recollections. *See* Frances Awalt, *Recollections of the Banking Crisis in 1933,* 43 BUS. HIST. REV. 368 (1969); RAYMOND MOLEY, AFTER SEVEN YEARS (1939); Charles A. Beard & George E. Smith, *The Old Deal and the New*, 51 ECON. J. 484 (1941); ARTHUR SCHLESINGER, THE AGE OF ROOSEVELT: THE COMING OF THE NEW DEAL 6 (1959); William Silber, *Why Did FDR's Bank Holiday Succeed?,* 15 ECON. POL'Y REV., 19-30 (2009); Bernanke, *supra* note 17.

The essence of what made the holiday successful was Roosevelt's forceful shift of financial risk management from private bankers onto the public. He did so first by staking his administration on the reopening. This required the coordination of previously competing supervisory regimes, especially the Comptroller and the Federal Reserve. Together, in frantic day and night meetings, these agencies pooled their collective information to determine which banks could plausibly reopen, and which needed to be kept shut. Ultimately, Roosevelt and the supervisory agencies secured credibility by closing weak banks, effectively guaranteeing the health of banks that reopened.[136]

The bank holiday proved a turning point for the institutionalization of bank supervision. As a technical matter, the work of identifying which banks the government, through the examiners, would permit to remain open, would be required to fail, and would have to navigate risk management as an intermediate step before one of those alternatives, placed bank supervision as the residual bearer of financial risk within the financial system. It also enshrined the inevitability of supervisory discretion in reaching those determinations of life, death, and reform for individual banks. The currency view of supervision—on life support since the 1870s—was now dead. The rise of bank supervision as the co-owner, alongside the banks, of the residual risks that banking activities created, was the new order of the day.

Bank supervision contributed to and benefited from an important kind of political legitimacy that it lacked prior to the holiday. Before Roosevelt's inauguration, supervision by itself could not forestall bank runs. After his inauguration, FDR—however wide his mandate—also lacked the ability to will

[136] Francis G. Awalt, Personal Account of F. G. Awalt, Mar. 1933 (on file with Herbert Hoover Presidential Library, Francis G. Awalt Papers box 1, folder 11); Emanuel Goldenweiser, contemporaneous notes (Mar. 3, 1933) (on file with Herbert Hoover Presidential Library, Francis G. Awalt Papers, box 1, folder 11); Ogden Mills to William Wooden (Mar. 4, 1933) (on file with Herbert Hoover Presidential Library, Francis G. Awalt Papers, box 1, folder 7).

away the crisis. Instead, bank supervision became legitimate in the holiday and, in the process, legitimated a new president, creating a mutually constitutive process of law, society, and bank examination.[137] Even the bankers recognized it as such. "Only by prompt and favorable [intervention by bank supervisors] can the depositors of Paige Trust Company and the people in the communities served by this bank realize the full benefits of the 'New Deal,'" a group of shuttered North Carolina banks urged the Comptroller of the Currency in September 1933.[138] Associating the work of bank examination with the political moment was intentional, for whatever hostilities bankers felt toward their examiners or Roosevelt's political revolution before the crisis, they knew how pivotal examination and FDR's New Deal were, together, to their recovery.

The bank holiday gave new wind to FDR's mandate and with it the rest of the New Deal. In subsequent legislation, Congress solidified the shift of residual risk from the private sector to the government in several profound ways. First, in the Emergency Banking Act of 1933, Congress gave the Reconstruction Finance Corporation the authority to buy preferred stock in banks.[139] Through this program, which enabled the government to recapitalize thousands of weak banks, the government literally owned the residual risk of bank failure. Later, with the passage of the Banking Act of 1933, congress created a more enduring commitment. First, it created the Federal Deposit Insurance Corporation (the FDIC) to shift (some) depositor risk onto the government.[140]

[137] The idea that "law" and "society" are mutually constitutive is one of the bedrock contributions of both the law and society movement and the critical legal history subset of it. *See* Robert Gordon, *Critical Legal Histories,* 36 STAN. L. REV. 57 (1983).

[138] KCR to Comptroller of the Currency (Sept. 7, 1933) (on file with Nat'l Archives, Records of the Off. of the Comptroller of the Currency, Rec. Grp. 101, Records Relating to the Banking Holiday, Box 1, folder DC-AA-1933).

[139] Emergency Banking Act of 1933, Pub. L. 73-1, 48 Stat. 1, Title II.

[140] Banking Act of 1933, Pub. L. 73-66 § 8 (amendments to the Federal Reserve Act § 12B(bd)) (1933); ANNUAL REPORT OF THE FEDERAL DEPOSIT INSURANCE CORPORATION (1934), 8.

Second, it eliminated double liability for national bank shareholders, finally rejecting shareholder liability as a functional risk management framework.[141] Collectively, these moves signaled that the government, not private shareholders, stood as the final backstop of the banking system.

Though visible in hindsight, this transformation took time to develop. Many in Congress and most in the administration did not support deposit insurance, while the original design also mandated that insured banks eventually join the Federal Reserve system. Instead, the result of the New Deal banking reforms was a three-layered supervisory structure, with each layer operating according to a different risk management logic. The chartering authorities—the comptroller and the states—remained committed to visitorial oversight. The Federal Reserve, in turn, managed risk through its balance sheet, powers that became more centralized and coordinated after the 1935 Banking Act. Finally, the FDIC linked the state and federal systems, supervising in defense of its insurance fund.[142]

The creation of the Federal Reserve System gave hints of the public-private partnership at the center of bank supervision, a growing realization from the Gilded Age that, for political reasons, neither politicians nor bankers could transparently embrace. The creation of the FDIC constituted this very embrace. Bank supervision would never be the same.

During the New Deal and almost perpetually thereafter, reformers have sought to consolidate these overlapping institutions. Their resistance to consolidation can cynically be chalked up to institutional competition, which certainly has played a role. It is also significant that these institutions are each rooted in a different risk management framework, such that their supervisory role is an outgrowth of their approach to managing residual risk. In the Progressive Era, these

[141] *See* Jonathan R. Macey & Geoffrey P. Miller, *Double Liability of Bank Shareholders: History and Implications*, 27 WAKE FOREST L. REV. 31, 32 (1992).

[142] Banking Act of 1933 § 8(y).

frameworks emerged as substitutes: central banking *or* deposit insurance. Yet after the New Deal, they were reconceptualized—again, gradually—as compliments: central banking *and* deposit insurance.

In the New Deal era, the FDIC was first among equals, which led to significant changes in how supervision occurred. Federal supervisors reconfigured how they evaluated bank assets, discarding frameworks developed under the real bills doctrine, while retaining the role of examiners in criticizing bank assets. Supervisors also discarded liquidity and market prices as meaningful metrics of bank wellbeing. With the FDIC ready to assume the assets and liabilities of a failed bank, the core criterion for determining bank solvency was the "intrinsic value" of bank assets, a measure entirely in the realm of supervisory discretion.[143] As they reformulated their approach to evaluating bank balance sheets, supervisors also placed increasing emphasis on systematically evaluating bank management. Competent bankers could be trusted to manage more risk; incompetent bankers would require more government oversight. Finally, although deposit insurance provided only limited protection ($2,500), the FDIC developed tools that would enable it to shield all depositors. Through purchase and assumption transactions, the FDIC would

[143] Leo T. Crowley, Memorandum on the Classification of Loans (c. Sept. 1934) (on file with Nat'l Archives, Rec. Grp. 34, Records of the Fed. Deposit Ins. Corp., Off. of the Chairman of the Bd. of Directors, Letters and Memorandums of Leo T. Crowley); Leo T. Crowley, Report of the Meeting (Sept. 10, 1934) (on file with Nat'l Archives, Rec. Grp. 34, Records of the Fed. Deposit Ins. Corp., Off. of the Chairman of the Bd. of Directors, Letters and Memorandums of Leo T. Crowley, box 2, folder Examining Division: Hopkins, R. L.); R. L. Hopkins Memorandum to Leo T. Crowley, Necessity for Continued Examination of Banks in the Manner Now Adopted (Apr. 27, 1935) (on file with Nat'l Archives, Rec. Grp. 34, Records of the Fed. Deposit Ins. Corp., Off. of the Chairman of the Bd. of Directors, Letters and Memorandums of Leo T. Crowley, box 2, folder Examining Division: Hopkins, R. L.).

merge a failed bank with a healthy bank, while pulling the toxic assets onto itself.[144]

These internal changes were paired with significant external changes. Most importantly, during the New Deal, the federal government not only assumed responsibility for the banking system, but for the economy as a whole. Although Roosevelt wanted more engaged supervision, strict oversight was anathema to his purposes because it limited bank lending. In a broader sense, the ideology of commercial banking, rooted in the currency school and the real bills doctrine, was out of step with the industrial economy. Firms needed long term capital, not short-term loans. To revive economic growth, the Roosevelt administration created new categories of safe assets for bankers to invest in, including Federal Housing Administration insured mortgages. Some officials, like Marriner Eccles, wanted to go further, reconceptualizing supervision as a tool for countercyclical policy. Yet such an aggressive use of public power to shape bank balance sheets pushed beyond what most officials were willing to do. All recognized that the balance between public and private had shifted significantly during the New Deal, but the ideology of free enterprise and individual risk-taking, while restrained, remained deeply entrenched.

* * *

The first seventy years of federal bank supervision were tumultuous and uncertain, with the supervisory framework developing alongside the scandals and crises of the Gilded Age, the advent of the Federal Reserve System, and the institutionalization of federal deposit insurance. Through this process, the major questions of what supervision should be had all been posed and some had been answered. Supervision was no longer strictly a mechanism for enforcing the nation's monetary system—those days passed almost immediately

[144] Michael B. Burgee, *Purchase and Assumption Transactions under the Federal Deposit Insurance Act,* 14 FORUM 1146 (1979).

after the Civil War.[145] It became instead about managing the boundary between the private and public aspects of the American financial system. The scandals and crises of the Gilded Age pushed the comptroller into the position of guaranteeing sound banking, a position it sometimes sought and sometimes resented. But the alternatives—that the banks would manage their own risk without placing outsized burdens on the public system, or that coalitions of banks through clearinghouses would do the same—proved incapable of providing the stability that the economic and especially political systems required.

The creation of the Federal Reserve System was meant to answer this problem by providing quasi-governmental support to the financial system that the national banking system could not quite do. The mechanism was, again, primarily monetary—the furnishing of an elastic currency using banking methods to accomplish that task. But it was also in large part supervisory. The Federal Reserve Banks, supervised by the Federal Reserve Board, would conduct their banking affairs consistent with these statutory mandates, and the Reserve Banks in turn would use their banking business to supervise the member banks that participated in that system. This, though, was a particular kind of supervision, aimed at shielding the Reserve Banks from excessive credit risk, on the one hand, and at convincing member banks to improve their risk management strategies, on the other.

The Federal Reserve System was heralded in its first fifteen years for supervisory successes that it largely did not

[145] This is not at all to say that supervisors were not always deeply concerned with money creation and the functioning of the payments system. The real bills doctrine, which undergirded supervisory evaluation of bank assets, provided an intellectual framework for squaring the currency view with the fact that banks could create deposit liabilities (i.e., those liabilities should only pair against short-term, self-liquidating loans, ensuring the deposits thus created would disappear in due course). *See* Judge Glock, *The "Riefler-Keynes" Doctrine and Federal Reserve Policy in the Great Depression*, 51 H. POL. ECON. 297 (2019). Likewise, supervisory forbearance provided a tool for maintaining payments availability in times of acute—but likely temporary—crisis.

deserve. The Great War had fundamentally altered the allocation of financial power in the world such that the United States emerged as the financial center by default. The banking crises of the early 1930s, culminating in the Bank Holiday of 1933, exposed profound fissures in the system. The recognition that bank supervisors held responsibility for the residual risk of the system, in the public mind at least, was not sufficient to protect the system from cataclysmic failure. Roosevelt's use of bank examiners as the central technocratic force in making good on the promises of the holiday, followed by the institutionalization of deposit insurance and the multiplication of bank supervisory structures, answered the question once and for all: banks would be supervised to ensure proper risk management, but in the event of failure, a mélange of bank supervisory structures would guarantee that the worst of the banking panics of the 1930s would not be repeated.

## III. THE RISE AND REACH OF SUPERVISORY DISCRETION: 1945–1980

What remained for the second half of bank supervision's history? Disputes about the boundary between public and private remained constant and sometimes quite hot, especially during the postwar period of financial tranquility in the United States. But the major trends in the second half of the history of supervision are three-fold. First, government actors, often pushed by private actors through a political economic process, fought over intragovernmental ownership of residual systemic risk. Sometimes, this resulted in turf warfare to ensure continued participation in managing systemic risk; other times, it was a game of hot potato as one set of supervisory actors sought to push ownership to others.

Second, the period from the New Deal through the 1980s consisted of a virtually one-way congressional ratchet whereby Congress gave more and more authority to bank supervisors, spread throughout the federal government. This included an increased role in existing areas of law that had previously skipped banking supervisors—namely, antitrust enforcement and merger review—and it included new areas of federal law entirely— namely, antidiscrimination and consumer financial protection. In response to crises, scandals, or nothing obvious at all, Congress also pushed forward with expanding the reach of supervision. This expansion of tasks and responsibilities meant that supervisors retained even more discretion, not only in reaching conclusions about core supervisory decisions—solvency, for example, or capital adequacy—but about prioritization. Supervisors can and did put some activities higher on the list of priorities than others, exercising a kind of prosecutorial discretion that left some policy areas underenforced and others over-enforced.

Third, despite the clear institutionalization of the government's support for, and even ownership of, residual risk in the system, the line between public and private ownership shifted constantly, and sometimes bitterly, as ideological trends through the end of the twentieth century pushed bank supervisors to a conception of banking as a fully private affair, with supervision as the belt to the private-sector suspenders of risk management. The promise of deposit insurance had been that it would not need to be used, nor would the other institutionalized forms of residual risk management (such as the Fed's lender of last resort functions). In their place, private actors would be allowed to allocate risk throughout the system to parties most willing and able to bear it.

This theory of bank supervision eventually failed. In fact, it never succeeded. Throughout the heyday of its dominance—the 1990s and 2000s—the world was not free from financial instability, and, although this was a period of profound de-supervision, bank supervisors still owned the ultimate responsibility for a system that breaks down.

The financial crisis of 2008 changed this presumption. Afterwards, Congress institutionalized further the role of supervisors as the manager of residual risk through the Dodd-Frank Act's twin mechanisms of (1) substantially expanding the concept of systemic risk management and (2) creating an orderly liquidation authority to sidestep the traditional legal systems of restructuring insolvent institutions (such as bankruptcy or FDIC liquidation). This embrace of the long-assumed and long-practiced residual risk management was controversial: a "big wet kiss to Wall Street," in then presidential candidate Mitt Romney's evocative description. But despite that clarity, after the election of Donald Trump in 2016, the United States entered into another period of de-supervision wherein supervision was pushed to a more regularized, regulation-like system. The pandemic of 2020 brought with it another extraordinary intervention into financial markets of all types and sizes, placing the supervisory commitment and the monetary commitment of the U.S. government in the same position: to guarantee stability through management of residual systemic risk.

This Section tells the history of the push and pull of these unique responsibilities and political pressures.

### *A. 1945-1960: Supervising Financial Concentration, Antitrust, and Bank Holding Companies*

The nineteenth century conception of bank supervision depended for the most part on a limited model of banking: a single bank as a single unit, controlled by a single executive team and a board of directors. But by the early twentieth century, this conception— although protected by numerous state and federal laws—was a decreasingly accurate description of the state of the U.S. financial system. The rise of branch banking and what would become the bank holding company—also called chain and group banking, although there are important differences between and among these categories—put pressure on the old model.[146] It also put pressure on what it meant to "supervise" these new institutions within the framework solidified in the post New Deal era.

Although U.S. policymakers embraced three risk management buffers—personal liability, central banking, and

[146] *See* Eugene White, *The Political Economy of Banking Regulation, 1864–1933*, 42 J. ECON. HIST. 33–40 (1982).

deposit insurance—after the decline of the Second Bank of the United States in the 1830s, they rejected a fourth: size. Beginning in the nineteenth century and building momentum into the twentieth, some bank reformers argued that enabling banks to grow via branching or other structures would allow for greater asset diversification and safety for depositors.[147] They pointed to examples abroad, including Canada and the British clearing banks, as clear examples where branching and stability seemed to go hand in hand. In the twentieth century, some states began to authorize branching, creating yet another vector of competition between state and federal systems. In the McFadden and 1933 Banking Acts, Congress gradually liberalized branching rules so that national banks could build branches in line with state-chartered banks.[148]

Supervising branched banks was difficult. Should examiners treat each branch as a unit bank or rely on the central management systems of the head office to shape their work? Supervising holding companies was more difficult still, in part because only some parts of the company were subject to examination, e.g., subsidiary national banks.[149] Yet, holding companies could incorporate state banks, trust companies, and non-financial businesses, all of which remained outside the oversight of federal supervisors. In the run up to the Great Depression, holding companies often hid risks and fueled speculation. Size could diversify and defuse risk, but it could also concentrate it.[150]

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[147] *See, e.g.*, *Comptroller Pole, Group Banking*, 129 COM. AND FIN. CHRON. 70 (Dec. 21, 1929).

[148] McFadden Act, Pub. L. 639, 69th Cong. H.R. 2; Banking Act of 1933, Pub. L. 66, 73rd Congress., H.R. 5661.

[149] G. T. Cartinhour, *Federal Regulation of Group Banking*, 4 J. BUS. U. CHI. 127 (1931).

[150] Two prominent examples are Caldwell & Co. and the Michigan holding companies the Detroit Bankers Company and the Guardian Group, all of which failed spectacularly during the Great Depression. *See* Awalt, *supra* note 135; DARWYN H. LUMLEY, BREAKING THE BANKS IN MOTOR CITY: THE AUTO INDUSTRY, THE 1933 DETROIT BANKING CRISIS AND THE START OF THE NEW DEAL (2009); JOHN BERRY MCFERRIN, CALDWELL & COMPANY (1939);

Congress and bank supervisors knew this and attempted to create a system that would protect smaller banks from competition and the threat of larger bank collections. These laws, from 1913 to 1933, were focused mostly on how the governance of these holding companies must operate, and with what kinds of transparency. There was precious little clarity on what the supervision of the holding company—and not just the chartered bank within the holding company—should be.

The bank holding company—briefly, a *company* that *controls* a *bank*, although these three terms were and are somewhat difficult to define—exists today as a relic of some of these restrictions, mostly abolished in 1994. The bank holding company is also mostly an American phenomenon, a response to legal constraints closely wedded to U.S. history, politics, and law.[151] The serious supervisory challenges arose in tandem; given the legal fiction of the corporation, how does a supervisor get a good sense of the ways that corporate families function in and around banking? How do supervisors ensure that risks—idiosyncratic and systemic alike—are appropriate? How does one understand the interconnections within a bank holding company and beyond, to the broader system? Do holding companies facilitate financial concentration in ways that contravene the spirit and letter of antitrust law? And especially relevant to the twentieth century until 1994, how do supervisors verify that holding companies are honoring legal limits on interstate banking, both state and federal?

In 1935, Marriner Eccles, the Utah banker whose calls for substantial fiscal intervention catapulted him to national attention during the transition between the Hoover and Roosevelt administrations, was nominated to the newly created position of Chairman of the Federal Reserve System.

*see also Stock Exchange Practices: Hearings Before the S. Comm. on Banking and Currency*, 73d Cong. pt. 10, 12 (1934).

[151] *See* Margaret Tahyar & Saule Omarova, *That Which We Call a Bank: Revisiting the History of Bank Holding Company Regulations in the United States*, 31 R. BANKING & FIN. L. 114–16 (2012).

Eccles quickly zeroed in on the supervisory threat of holding companies, a world he knew very well. Eccles's banking empire in the Mountain West, First Security Corporation, was one of the first multi-bank holding companies in the United States.[152] One of the first, perhaps, but not the largest by the late 1930s. That honor belonged to A.P. Giannini's Transamerica, a holding company that controlled the California-based Bank of America (formerly the Bank of Italy), as well as banks in New York, Washington, Oregon, Nevada, and Arizona. Transamerica aspired, in Giannini's words, to become a financial services "department store," an institution that could meet any customer's financial needs, no matter the customer or need. To meet this goal, Giannini acquired a variety of disparate financial actors, ranging from mortgage originators, insurance companies, and investment brokerages. For good measure, Transamerica also owned a salmon cannery, an oil and gas prospecting company, and a metal forging business. "This company," James Bonbright and Gardiner Means wrote in their 1932 treatise on holding companies, "has an intercorporate structure so ramified as almost to pass beyond the bounds of comprehension."[153]

By the late 1940s, Transamerica presented, according to the Fed, what today we would call a systemic risk to the financial system. Eccles had initially been sympathetic to the Giannini banking interests.[154] But their relationship soured

[152] *See* MARRINER S. ECCLES, BECKONING FRONTIERS: PUBLIC AND PERSONAL RECOLLECTIONS 41–50 (1951).

[153] *See* JAMES C. BONBRIGHT & GARDINER C. MEANS, THE HOLDING COMPANY: ITS PUBLIC

SIGNIFICANCE AND ITS REGULATION 333 (1932); *see also Branch, Chain, and Group Banking: Hearings Before the H. Comm. on Banking and Currency,* 71st Cong. 1545 (1930) (statement of A. P. Giannini); *Transamerica--The Bankholding Company Problem*, 1 STAN. L. REV. 658 (1949); *Bank Holding Bill: Hearings Before a Subcommittee of the S. Comm. on Banking and Currency*, 81st Cong. 193-094 (1950) (statement of W. L. Andrews, Vice President and Treasurer, TransAmerica Corp.).

[154] Eccles was no friend to small banks. Writing to Roosevelt in November 1936, he railed against their continued existence: "It is still possible for persons who have no

due in part to the problem of supervising the Giannini empire.[155] By 1942, Transamerica threatened to monopolize,

competence in banking to open so-called banks," the Fed Chairman complained, which "are in reality nothing more than pawn shops." These "mushroom miscalled banks" he continued, accounted for "the greatest holocaust of bank failures" causing "the greatest losses and misery among their depositors and" bringing "a large share of discredit down upon the heads of bankers generally." Worse, "through their various associations groups of these so-called independent bankers have been the most implacable foes of this Administration." Nevertheless, Eccles came to recognize that monopoly power on the other side of the market could also fundamentally undermine the national banking structure. Memorandum from Marriner Eccles to Franklin Roosevelt (Nov. 12, 1936) (on file with Univ. of Utah, Marriner S. Eccles Papers, box 5, folder 6), https://fraser.stlouisfed.org/archival-collection/marriner-s-eccles-papers-1343/memorandum-president-468480 [https://perma.cc/VSY8-H9M5].

[155] The conflicts between Giannini and the supervisory authorities at the state and federal level ran over decades. For the roots of this specific conflict, see Leo Crowley, Notes Concerning the Bank of America National Trust and Savings Association (Oct. 22, 1937), 354 MORGENTHAU DIARIES, https://fraser.stlouisfed.org/archival-collection/diaries-henry-morgenthau-jr-6880/volume-354-634932 [https://perma.cc/XVT5-VBS9]; Statement of the Reserve Board Relating to Certain Views Expressed at the Conference in the Office of the Secretary of the Treasury on Jan. 21, 1941 (Mar. 14, 1941) (on file with Univ. of Utah, Marriner S. Eccles Papers, box 17, folder 5), https://fraser.stlouisfed.org/archival-collection/marriner-s-eccles-papers-1343/statement-reserve-board-relating-certain-views-expressed-conference-office-secretary-treasury-january-21-1941-466321 [https://perma.cc/AL5K-SYBG]; Letter from A.P. Giannini to Marriner Ecceles (Aug. 17, 1942) (on file with Univ. of Utah, Marriner S. Eccles Papers, box 19, folder 5), https://fraser.stlouisfed.org/archival-collection/marriner-s-eccles-papers-1343/group-1-transamerica-correspondence-459761 [https://perma.cc/UY84-C482]. For supervisory conflict in general, see MARQUIS JAMES & BESSIE R. JAMES, BIOGRAPHY OF A BANK: THE STORY OF BANK OF AMERICA (1954).

as Eccles recalled, "a good part of the banking business of the Western seaboard."[156] Other banking supervisors agreed (and, given the sheer variety of financial institutions within the Transamerica family, each supervisor's sign-off was necessary). The Fed, the Comptroller, and the FDIC thus ordered Transamerica to stop its acquisition spree.[157]

Giannini ignored them and for good legal reason. The novelty of his enterprise was such that there was no clear legal authority to supervise holding companies at all. While the institutionalization of residual risk management was well established by 1947, the primary legal tools of supervision remained chartering, examination, and liquidation—of individual banks. The Fed sought something very different in this order. The Banking Act of 1935, which Giannini supported, authorized the Fed to enforce the Clayton Act's provisions where they applied to banks. The Fed argued that Transamerica's position in western banking markets in five states constituted a monopoly in violation of the antitrust laws. In 1953, the U.S. Court of Appeals for the Third Circuit overturned the Fed's legal theory, essentially on purely antitrust grounds. In essence, the Fed was defeated in its effort to limit the concentration of financial power nationally by the then widespread belief that the proper geographic scope of banking was the community.[158]

The *Transamerica* decision, although mostly forgotten today, played a key role in spurring a series of laws that would make the Fed's action in that case legally airtight, including the Bank Holding Company Act of 1956 (and its substantial

[156] *See* ECCLES, *supra* note 152, at 443.

[157] Letter from Chester Morrill to Transamerica Corporation (Feb. 12, 1942) (on file with Univ. of Utah, Marriner S. Eccles Papers, box 19, folder 4), https://fraser.stlouisfed.org/archival-collection/marriner-s-eccles-papers-1343/letter-transamerica-corporation-459762 [https://perma.cc/T6L9-VC2F].

[158] Law Dep't, Fed. Rsrv. Sys., *Clayton Act Proceeding: Transamerica Corporation,* FED. RSRV. BULL. 368 (Apr. 1952); Transamerica Corp. v. Bd. of Governors of Fed. Rsrv. Sys., 206 F.2d 163, 169 (3d Cir. 1953).

amendments in 1970) and the Bank Merger Act of 1960 (and its substantial amendments in 1966). The Acts approached the same problem (financial concentration) from two different directions. The Bank Holding Company Act and its amendments were designed to subject bank holding companies to similar supervisory requirements as banks, despite the lack of a bank charter at the level of the holding company. The twin aims of holding company legislation were to prevent the expansion of holding companies such as Transamerica within gaps of the supervisory system and to force these holding companies to divest from nonbanking assets. The point was to shore up the New Deal commitment to separating traditional commercial banking activities from other areas of commerce—no more salmon fisheries for Transamerica.[159]

The Bank Merger Act came a few years later, in part as a recognition of what the Bank Holding Company Act failed to accomplish, but also (and more importantly) as a recognition that growing concentration in financial services presented a different kind of problem than other areas of antitrust law. The banking panics of the 1930s had made the banking-antitrust nexus clear, but in the opposite direction of the antimonopoly Progressive Era impulses. Rather than fearing

[159] Benjamin J. Klebaner, *The Bank Holding Company Act of 1956,* 24 S. ECON. J. 314 (1958). The 1956 Bank Holding Company Act targeted Transamerica specifically and multi-bank holding companies generally. It carved out a loophole for "one-bank" holding companies later exploited by the First National City Bank and other firms in the late 1960s. Congress then enacted the Bank Holding Company Act of 1970 to close this loophole, giving the Federal Reserve supervisory authority over these firms as well. Michigan Law Review, *Implementation of the Bank Holding Company Act Amendments of 1970: The Scope of Banking Activities*, 71 MICH. L. REV. 1170 (1973); TREAS. DEP'T, SUMMARY OF THE BACKGROUND OF DEVELOPMENT OF THE ONE-BANK HOLDING COMPANY PROBLEM AND A GENERAL OUTLINE OF THE PRINCIPLE POINTS TO BE INCLUDED IN A LEGISLATIVE RESOLUTION OF THIS PROBLEM (1969); Memorandum for the President discussing the establishment of the Presidential Comm'n on Fin. Structure and Regul. (Jan 19. 1970) (on file with Richard M. Nixon Presidential Library, President's Commission on Financial Structure and Regulation, FG 267, Box 1), https://catalog.archives.gov/id/255220770 [https://perma.cc/225S-HF6S].

financial concentration, the New Deal bank supervisors wanted to use the strong to absorb the weak to avoid the costliness of a disorderly resolution. Eccles, in a letter to Franklin Roosevelt, defended this anti-antitrust view as getting rid of the "mushrooms miscalled banks" that seemed to flourish in dank corners of the mismanaged financial ecosystem.[160]

The 1940s brought global cataclysm to nearly every aspect of life throughout the world, in some form or another. An exception was the American banking system. Through the end of the war and into the 1950s, bank failures faded in memory, leading legislators and supervisors to assume that the institutionalization of residual risk management had solved most of the problems that the long nineteenth century had posed. Yet the pre-New Deal regulatory structure, which favored small banking, layered over by New Deal limits on price and product line competition, significantly constrained the profitability of commercial banking in the 1940s and 1950s. Declining profitability—the "profits squeeze"—led to a quest for scale among the nation's largest banks, one encouraged by the continued growth and expanding financial demands of the nation's large corporations.[161] The 1955 merger of Chase National Bank and the Manhattan Company headlined a merger boom in the mid-1950s.[162]

At the time of the merger, bank-related antitrust law was confused, at best. The New Deal bank merger ethos—that bigger banks were better in the face of financial instability—

[160] Memorandum from Marriner Eccles, *supra* note 154.

[161] *See* AM. BANKERS ASS'N, THE COMMERCIAL BANKING INDUSTRY: A MONOGRAPH PREPARED FOR THE COMMISSION ON MONEY AND CREDIT, 76–81 (1962); DAVID ROCKEFELLER, MEMOIRS 197 (2003). To understand how the profits squeeze prefigured the later problem of disintermediation, see GERALD F. DAVIS, MANAGED BY THE MARKETS: HOW FINANCE RESHAPED, 112–15 (2009).

[162] *See* JOHN DONALD WILSON, THE CHASE: THE CHASE MANHATTAN BANK, N.A., 1945–1985, at 43–

73 (1986); Paul Heffernan, *Merger Confirms New Banking Era*, N.Y. TIMES, Jan. 16, 1955, at F1; *Celler Plans Inquiry,* N.Y. TIMES, Jan. 15, 1955, at 21.

had yielded to the pre-New Deal Brandeisian impulses to protect small business enterprise. This created an incoherence to what, if anything, bank antitrust policy should be. Federal law had mostly ceded ground to the states, and the states did not have a good theory of what should motivate merger evaluations for banks. Figure 3 illustrates the confusion.

*Figure 3. Policy Preferences Motivating Merger Evaluations*

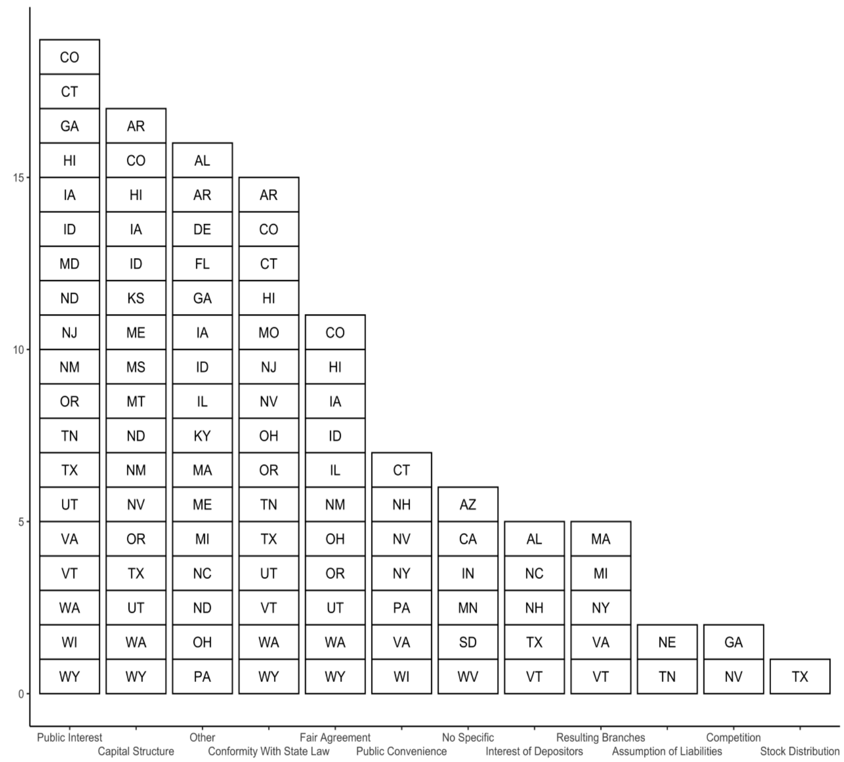


Figure 3 canvasses state laws to determine what factors bank (or competition) authorities would take into consideration when determining whether a bank merger should go forward. Competition, the primary motivating factor in antitrust, was an afterthought as the major concern for only Georgia and Nevada. The most important factors were essentially the public interest (especially when combined with the public necessity).[163]

The mélange of state-law concerns motivated Congress to act with respect to all banks that touched the federal banking apparatus—which, by 1960, was all banks everywhere. The resulting Bank Merger Act of 1960 contained several major provisions that extended discretionary bank supervision via antitrust. First, the law rationalized the merger approval process through the three federal banking regulators: the comptroller if the merged bank continued with a national charter, the Fed if the resulting bank were a state member bank, and the FDIC if the resulting bank were a state nonmember bank. Second, there would be no public hearing for banks to challenge the supervisory determination on mergers, nor for merger opponents to air their views. A notice of the intention to merge, published in the newspaper, with supervisory approval was the outcome instead.[164] Third, building on the existing complexity of state merger policy, the BMA determined the relevant factors that banking agencies would consider. These not only included the "effect of the transaction on competition," but also "the financial history and condition of each of the banks involved, . . . the general character of its management, the convenience and needs of the community to be served," among several other factors. Congress offered no hint as to how such factors would play off each other. Bank supervisors were granted substantial discretion in reaching their decisions, guided by these broad, and sometimes contradictory, factors.

Finally, Congress expected, "in the interest of uniform standards," the agencies to work together and with the Department of Justice (the DOJ) by requiring each agency and the DOJ to comment on every merger before any one of the

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[163] *Hearings on S. 1062, Regulation of Bank Mergers Before the S. Comm. on Banking and Currency,* 86th Cong. 183 (1959). Our thanks to Andrew Baker for his help recreating this chart.

[164] Bank Merger Act of 1960, Pub. L. No. 86-463, May 13, 1960. For the debate that led to the defeat of public hearings, see 105 CONG. REC. 8125, 8143–44 (1959) (statement of J. William Fulbright).

other agencies (absent a showing of emergency). These opinions were advisory; only the relevant banking agency could approve or prohibit a given merger, depending on its charter and membership in the Federal Reserve System. But each agency was to inform the others of their respective views.

Almost as soon as it began, the 1960 Act invited the various parties to struggle for dominance. The biggest fight was between the comptroller of the currency, which sought to approve mergers that would increase its own regulatory footprint, against the DOJ that sought a more aggressive role in passing on the legality of proposed mergers. In four instances, the DOJ disagreed with the comptroller on the mergers, prompting the comptroller to approve the mergers formally and the Attorney General to sue in federal court. The courts sided with the DOJ, leading to two major determinations by the Supreme Court that the DOJ would reign supreme in bank antitrust policy.[165]

After these major reversals in Court, Congress took notice and launched a legislative process that contemporaries would regard "as bizarre as that of any statute ever passed."[166] It began when the lead author of the Bank Merger Act of 1960, Willis Robertson (Democratic Senator of Virginia) declared the Supreme Court's interpretations of the statutory text "erroneous" and in need of clarification so that the Court would recognize bank mergers as belonging to a different tradition than antitrust. Through twists and turns, intraparty fights and betrayals, Congress enacted the Bank Merger Act Amendments of 1966 to clarify the predominance of bank supervision in antitrust review. The new framework, which has lasted mostly unchanged in the half century since its passage, gives supervisors the first cut on evaluating bank mergers against a variety of factors, with the DOJ having one

[165] The two principal cases were *United States v. First Nat'l Bank & Tr. Co. of Lexington*, 376 U.S. 665, 679 (1964) and *United States v. Phila. Nat'l Bank*, 374 U.S. 321, 350 (1963).

[166] David T. Searls & Harry M. Reasoner, *The Bank Merger Act of 1966: Its Strange and Fruitless Odyssey,* 25 BUS. L. 133, 139 (1969).

month to review approved deals for any potential antitrust violation.

The Court's jurisprudential shift away from antitrust enforcement in the 1980s was the last major change that left bank mergers almost exclusively in the hands of bank regulators. This shift tracks the rest of the approach to the problem of bigness and concentration that Congress took in banking. The conclusion: leave this to supervisors to understand, manage, and navigate. There are very few hard legal standards that the supervisors must abide. The fate of financial concentration for banking was not for courts and lawyers and not even for legislators and regulators. It was primarily the domain of bank supervisors.

### *B. Supervising Consumer Financial Protection*

Although a major component of New Deal legislation and regulation was attention to the "consumer," the story of consumer financial legislation as part of the supervisory apparatus of banking does not begin in earnest until 1968 with the passage of the Truth-in- Lending Act (TILA).[167] The law owed its genesis and ultimate enactment to the entrepreneurial energy of Illinois Senator and former University of Chicago economist Paul H. Douglas.[168] Prior to TILA, consumer credit regulation was primarily a state, not

[167] *See* ELLIS WAYNE HAWLEY, THE NEW DEAL AND THE PROBLEM OF MONOPOLY: STUDYING ECONOMIC AMBIVALENCE (1995); MEG JACOBS, POCKETBOOK POLITICS: ECONOMIC CITIZENSHIP IN TWENTIETH-CENTURY AMERICA (2005).

[168] *See* Edward Rubin, *Legislative Methodology: Some Lessons from the Truth-in-Lending Act*, 80 GEO. L.J. 233, 234 (1991) (arguing that the act demonstrates Congress's inability to craft regulatory legislation); *see also* Anne Fleming, *The Long History of 'Truth in Lending*, 30 J. POL'Y HIST. 236, 236–37 (2018); Christopher Peterson, *Truth, Understanding, and High-Cost Consumer Credit: The Historical Context of the Truth in Lending Act,* 22 FLA. L. REV. 808, 877 (2003); SEAN VANATTA, PLASTIC CAPITALISM: BANKS, CREDIT CARDS, AND THE END OF FINANCIAL CONTROL 108–32 (2024).

federal, concern.[169] Douglas initially framed the debate around macroeconomic stability, but gradually emphasized protecting consumers from harmful and deceptive lending practices.[170] He did so against constant opposition from congressional proponents of states' rights, who in the midst of the Civil Rights movement sought to defend state prerogatives against all federal encroachment.[171] Elections and presidential leadership provided the electoral pressure that ultimately resulted in the passage of the bill.[172]

The Truth-in-Lending Act tasked the Federal Reserve with regulating credit disclosure—with writing the rules that creditors would have to obey—and tasked the remaining bank supervisory agencies with ensuring "compliance" with these rules.[173] Subsequent consumer legislation, including the Fair Credit Reporting Act (1970)[174] and the Equal Credit Opportunity Act (1974),[175] would likewise adopt this language, placing consumer enforcement with the different federal banking and consumer protection agencies, and explicitly tying that enforcement to the keyword compliance.[176]

In one sense, mandated price disclosure and post-hoc compliance oversight mirrored the reporting and public

[169] BARBARA A. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION (1965).

[170] Paul H. Douglas, Speech before the National League of Insured Savings Associations (May 10, 1960) (on file with Chicago Historical Society, Paul H. Douglas Papers, Douglas Statements 1960, box 1297).

[171] Letter from A. Willis Robertson to Paul H. Douglas (Dec. 12, 1961) (on file with Chicago Historical Society, Paul H. Douglas Papers, Douglas correspondence 1961, box 1299).

[172] See Rubin, *supra* note 168, at 251–52.

[173] Truth in Lending Act § 108, 15 U.S.C. §1607.

[174] Fair Credit Reporting Act § 621, 15 U.S.C. §1681s.

[175] Equal Credit Opportunity Act § 704, 15 U.S.C. §1691c.

[176] For discussion of FDIC compliance work under this act, see *Federal Government's Role in the Achievement of Equal Opportunity in Housing: Hearings Before the C.R. Oversight Subcomm. of the H. Comm. on the Judiciary*, 92nd Cong. 849–850 (1971) (letter from Frank Wille to Theodore S. Hesburgh (Oct. 19, 1971)).

surveillance regime of the nineteenth century. Like the system of public call reporting instituted by the 1860s Banking Acts, price disclosure made market participants—here, consumers—monitors of financial institutions' behavior. Transparent prices enabled consumers to make informed decisions, encouraging banks to improve performance and lower prices. Yet, unlike the nineteenth-century disclosure regime, which left supervisors to manage non-compliance through direct and private supervisory engagement with bankers, TILA and subsequent consumer protection legislation enabled consumers to file class-action lawsuits against firms that failed to comply.[177] As Proxmire observed, "the law should be largely . . . self-enforcing."[178]

Placing enforcement power in the hands of activist consumers accorded with the consumer movement's goals of consumer empowerment, but it also created a difficult tension for bank supervisory officials. At first, supervisors tried to incorporate consumer oversight into their existing examination practices, evaluating bankers' knowledge of the rules and advising them on how to achieve compliance.[179] But

[177] *See* JOHN C. COFFEE, ENTREPRENEURIAL LITIGATION: ITS RISE, FALL, AND FUTURE (2015).

[178] *Truth in Lending—1967: Hearings Before the S. Subcomm. on Fin. Inst. of the S. Comm. on Banking and Currency*, 90th Cong. 682 (1967) (statement of J. L Robertson, Vice Chairman, Bd. of Governors, Fed. Rsrv. Sys.).

[179] For example, in June 1969, the FDIC issued examiners a 7-page Truth-in-Lending compliance checklist, though which examiners evaluated bank managers' relative knowledge about the new regulations and randomly sampled consumer credit files to see that banks were following the rules. Memorandum from Edward H. DeHority to Supervising Examiners (June 23, 1969) (on file with Nat'l Archives, Records of the Fed. Deposit Ins. Corp., Record Group 34, Memorandums to Supervising Examiners, 1934–1969, box 21). The Federal Reserve Banks and the comptroller also used a checklist. Memorandum from James H. Booth to John T. McClintock (June 4, 1973) (on file with Fed. Rsrv. Bank of N.Y. Archives, Truth in Lending, Commercial Paper, Loans, 403.1A); *Oversight on Consumer Protection Activities of Federal Banking Agencies: Hearings Before the S. Comm. on Banking, Housing and Urban Affairs*, 94th Cong. 57–58 (1976) (statement of James A. McCaffrey).

federal supervisors also recognized compliance policing might rub against their safety and soundness mission.[180] TILA's civil penalties, combined with new consumer class action lawsuits that the act encouraged, "could conceivably threaten the solvency of a bank," a 1971 FDIC memo warned.[181] Therefore, the FDIC required its examiners to separate compliance paperwork from other examination forms, even filing work papers in separate envelopes. "All reference to" truth-in-lending, examiners were instructed, "should be omitted from Reports of Examination." Thus, the FDIC very quickly hived off truth-in-lending and later consumer compliance functions from its core safety and soundness functions.

Consumer oversight threatened to disrupt ingrained norms of supervisory practice. By the postwar era, supervision relied on a confidential enforcement regime, worked out between supervisors and bank management in bank offices. "We . . . have concluded," the comptroller explained in 1976, "that it was the intention and expectation of Congress that the banking agencies would use the same private approach to consumer law enforcement as they do in regard to other banking laws."[182] Facing the threat of class action lawsuits, bankers looked to their examiners for advice on how to manage new consumer-regulatory risks. The "private approach," however, was at odds with the premise of publicity woven through the consumer protections legislation, as well as the orientation, through civil penalties, toward rectifying

[180] Memorandum from Edward J. Roddy to Regional Directors (Sept. 24, 1971) (on file with Nat'l Archives, Records of the Fed. Deposit Ins. Corp., Record Group 34, Memorandums to Regional Directors, 1967–1975, box 1).

[181] Memorandum from Edward J. Roddy to Examiners and Assistant Examiners (June 30, 1971) (on file with Nat'l Archives, Records of the Fed. Deposit Ins. Corp., Record Group 34, Memorandums to Regional Directors, 1967–1975, box 1). By 1976, at least 160 class action cases had been brought against financial and other credit-granting institutions. CONG. RSCH. SERV., CLASS ACTIONS BROUGHT IN FEDERAL COURTS UNDER SECTION 130 OF THE TRUTH IN LENDING ACT (1976).

[182] *Oversight on Consumer Protection Activities of Federal Banking Agencies: Hearings Before the S. Comm. on Banking, Housing and Urban Aff.*, 94th Cong. 461 (1976) (response of the Comptroller of the Currency).

past wrongs. Congress wanted bank supervisors to work on behalf of consumers to make amends for past mistakes, not—as supervisors had imagined their role—to work with bankers to prevent errors in the future.

The new consumer emphasis created increasing problems in the context of the ongoing agencies' risk-management responsibilities. In the mid-1970s, the agencies responded by creating distinct consumer offices and experimenting with separate compliance examinations. By creating consumer departments and compliance teams, the supervisory agencies strengthened the compliance ethic, giving compliance an institutional identity by divorcing it from future-oriented safety and soundness supervision.[183] This professionalization of supervisory compliance staff led, in turn, to the similar professionalization of compliance staff in banks. Beginning in 1977, the *Magazine of Bank Administration* ran a seven-part series on "Implementing a Program for Consumer Regulation Compliance," a topic also taken up in other industry publications.[184] The "compliance officer" was officially born. Hiring in compliance was part of a larger explosion of compliance costs, a subject of perennial bank complaint.

[183] *Oversight on Consumer Protection Activities: Hearings Before the S. Comm. on Banking Housing and Urban Aff.,* 94th Cong. 447, 453, 457 (1976); *Home Mortgage Disclosure and Equal Credit Opportunity: Hearings Before the S. Comm. on Banking, Hous., and Urban Aff.*, 94th Cong. 3–4 (statement of Philip Jackson, Member, Bd. of Governors, Fed. Rsrv. Sys.) (1976); *Banking Regulatory Agencies' Enforcement of the Equal Credit Opportunity Act and the Fair Housing Act: Hearings Before a H. Subcomm. on Gov't. Operations*, 95th Cong. 305 (1978) (statement of Carmen J. Sullivan, Acting Director, Off. of Consumer Affs. and C.R., Fed. Deposit Ins. Corp.).

[184] Joyce M. Saxon, *Implementing a Program for Consumer Regulation Compliance*, 53 MAG. BANK ADMIN. 18 (1977); William L. Hearn, *Why Have a Compliance Officer*?, 60 J. OF COM. BANK LENDING 29 (1978); Karen A. Oswald, *Developing and Maintaining an Ongoing Consumer Compliance Program*, 1 J. RETAIL BANKING 33 (1979); Neil B. Murphy, *Economies of Scale in the Cost of Compliance with Consumer Credit Protection Laws: The Case of the Implementation of the Equal Credit Opportunity Act of* 1974, 10 J. BANK RSCH. 248 (1980).

Ultimately, like antitrust, consumer protection legislation created a bank policy constituency outside the nexus of shared risk management. Federal bank supervisors faced a fundamental dilemma: help bankers proactively manage the risks of consumer enforcement or help consumers retroactively police banker behavior. Through discretion and institutional mitosis, they sought to split the difference, unintentionally seeding a risk- management arms race.

### *C. The Expanding Portfolio: Bank Supervision and Antidiscrimination*

The third major component of the expanding portfolio of bank supervision was antidiscrimination. The long legacies of redlining and racial exclusion left African- Americans without access to the low-cost financing, which enabled white households to build substantial housing wealth.[185] The initial wave of federal Civil Rights legislation did little to address this problem.[186] As activists increasingly demanded economic equality as the necessary complement to civil equality, Congress sought to address financial inclusion through the

[185] *See* Mehrsa Baradaran, *Jim Crow Credit*, 9 U.C. IRVINE L. REV. 887 (2019).

[186] *See* Douglas Massey, *The Legacy of the 1968 Fair Housing Act*, 30 SOCIO. F. 574 (2015).

1968 Fair Housing Act,[187] which outlawed discrimination in housing, including discrimination in housing finance.[188]

The law's ambitions were grand: "[i]t is the policy of the United States to provide, within constitutional limitations, for fair housing throughout the United States."[189] The enforcement mechanisms, however, had been weakened through political compromise. The Department of Housing and Urban Development (HUD) had no tools to compel compliance with the Housing Act's provisions. The DOJ, meanwhile, could only bring suit if there was "a pattern or practice" of discrimination. HUD tasked supervisory agencies with ensuring compliance. As with consumer regulation, examiners initially did so through the regular course of examination.[190]

Although the forceful class action provisions of the Truth-in-Lending led examiners to take the threat of consumer

[187] There was a parallel effort to use supervision to combat discrimination in bank employment. On September 24, 1965, Lyndon Johnson issued executive order 11246, required federal contractors to develop and implement affirmative action policies. All banks with 50 or more employees were required to file equal opportunity reports. Examiners determines if banks filed their reports and if banks had written affirmative action plans and reported non-compliance to the Treasury's Equal Employment Opportunity Department. Letter from Charles E. Walker to Frank Wille (Feb. 25, 1971) (on file with Nat'l Archives, Records of the Fed. Deposit Ins. Corp., Record Group 34, Memorandums to Regional Directors, 1967–1975, box 1); Memorandum from Edward J. Roddy to Regional Directors (Mar. 31, 1971) (on file with Nat'l Archives, Records of the Fed. Deposit Ins. Corp., Record Group 34, Memorandums to Regional Directors, 1967–1975, box 1).

[188] Fair Housing Act, Pub. L. No. 90-284, 82 Stat. 83 (1968).

[189] *Id.* at 81.

[190] Letter from P.E. Coldwell, President of the Fed. Reserve Bank of Dall., to President of Each State Member Bank in the Eleventh Federal Reserve District (May 2, 1969), Circular No. 69-113, District Notices, https://fraser.stlouisfed.org/title/5569/item/544107 [https://perma.cc/PV6D-N3X3]; Letter from Alfred Hayes, President of the Fed. Reserve Bank of N.Y., to the President of Each State Member Bank in the Second Federal Reserve District (May 2, 1969), Fed. Rsrv. Bank of N.Y. Circulars, https://fraser.stlouisfed.org/title/466/item/14043 [https://perma.cc/V6BS-VMGX].

litigation seriously, there is little evidence that bank examiners took assertive action on fair housing. Instead, supervisory officials relied on the 1968 Act's weak enforcement mechanisms, which authorized HUD to act only on the basis of consumer complaints, to shield themselves from responsibility. Supervision by complaint was further weakened by the DOJ's insistence that it was "not interested in individual cases, but rather in a pattern of discrimination."[191] Establishing such patterns required evidence, which federal supervisors assertively failed to seek. Federal supervisors could not conceive of "any system of bank recordkeeping which would produce reliable or useful data in this area," Comptroller William B. Camp told Congress in 1971.[192] Meanwhile, the Federal Reserve board summarized its campaign of willful ignorance: "[t]he Board does not know of any specific cases of discrimination, nor does it know of any specific institutions whose practices indicate discriminatory loan practices."[193]

Within the supervisory agencies, consumer protection took priority because consumer enforcement penalties posed a much more significant risk to banks than the weak enforcement provisions of 1968 Fair Housing Act.[194] As they carved out separate consumer compliance departments, the federal banking agencies rolled civil rights oversight into the consumer protection remit, effectively subsuming racial equity under the goals of consumer protection.

The supervisory approach to antidiscrimination changed in the mid-1970s, in part because of Congress's increasing

[191] *Bias on Mortgages Claimed at Hearing*, WASH. POST, Oct. 7, 1971.

[192] *Federal Government's Role in the Achievement of Equal Opportunity in Housing: Hearings Before the C.R. Oversight Subcomm. of the H. Comm. on the Judiciary*, 92nd Cong. 852 (1971) (statement of William B. Camp, Comptroller of the Currency).

[193] *Id.* at 841–42 (statement of Robert C. Holland, Sec'y of the Fed. Open Market Comm.).

[194] *Oversight on Consumer Protection Activities of Federal Banking Agencies: Hearings Before the S. Comm. on Banking, Hous., and Urb. Affairs*, 94th Cong. 241–45 (1976) (statement of Arthur F. Burnes, Chairman of the Fed. Rsrv. Sys.).

dissatisfaction with the record of the supervisory agencies and in part because anti-discrimination transformed into a consumer protection issue.

This pattern continued following the enactment of the Equal Credit Opportunity Act of 1974 (as expanded in 1976) (ECOA). ECOA—originally passed to prevent discrimination "on the basis of sex or marital status" in "any aspect of a credit transaction," but eventually to prohibit discrimination on a host of other protected categories, including race—gave the DOJ and HUD the primary control over its implementation.[195] Still, bank supervisors remained the frontline of antidiscrimination compliance. As with the HUD Act, supervisors outsourced oversight to the public, relying on complaints of discrimination to launch an investigation. Further, supervisors incorporated their civil rights compliance programs into their emerging consumer compliance teams. The FDIC created the Office of Consumer Affairs and Civil Rights (the OCACR).[196]

Violation of ECOA meant prosecution, although often the bank supervisors are the first to learn that there is a problem afoot. In 1996, the DOJ issued guidance to the banking regulators to outline when referral for prosecution is appropriate.[197]

Most antidiscrimination statutes in bank supervision, then, take on a very highly discretionary flavor, since the question is triggered by discretion at two levels: whether to investigate the presence of discrimination on the basis of protected categories and whether, after investigation, to refer alleged violations for prosecution. According to the Federal

[195] 15 U.S.C. § 1691(a).

[196] *Banking Regulatory Agencies' Enforcement of the Equal Credit Opportunity Act and the Fair Housing Act: Hearings Before a Subcomm. of the H. Comm. on Gov't Operations*, 95th Cong. 1014 (1978) (statement of Carmen J. Sullivan, Acting Dir. of Off. of Consumer Affs. and C.R.).

[197] Memorandum from the Dep't of Just. on Identifying Lender Practices that May Form the Basis of a Pattern or Practice Referred to the Dep't of Just. (1996), https://www.justice.gov/sites/default/files/crt/legacy/2014/03/05/regguide.pdf [https://perma.cc/4U56-RW36].

Reserve's 1977 Equal Credit Opportunity Act report to Congress, the comptroller found that "97 percent of all national banks were in violation of the act to some extent."[198] Thus, even when federal supervisors were willing to look for discrimination, their preference remained to seek voluntary corrective action, rather than to pursue forceful—and potentially politically or financially risky—remedial measures.

The Community Reinvestment Act of 1977 (the CRA) is a different animal altogether. William Proxmire, Paul Douglas's intellectual successor in the Senate on banking disclosure and consumer protection, sponsored the bill to address redlining, the historical discriminatory practice of "deliberately avoiding making loans in black communities[.]"[199]

The supervisory ethos of the CRA was more similar to TILA (centered on disclosure) than ECOA (which relied on enforcement).[200] The CRA simply required banks to disclose the level of lending in low-income communities (often neighborhoods where most residents were racial minorities) that bank supervisors would then use to rate banks as "Outstanding" or in "Substantial Noncompliance" or, more often, somewhere in between.[201]

[198] *Banking Regulatory Agencies' Enforcement Hearing, supra* note 196, at 472.

[199] *See* Baradaran, *supra* note 185, at 935.

[200] 12 U.S.C. § 2901(a)(1).

[201] 12 U.S.C. §§ 2903(a); 2906(b)(2). There is a vibrant historical debate about the origins of redlining. For a review of sources see Peter Conti-Brown & Brian Feinstein, *Banking on a Curve: How to Restore the Community Reinvestment Act*, 13 HARV. BUS. L. REV. 335 (2023). Briefly, governmental maps that literally used red lines to denote poor neighborhoods that should not receive federal support were an early source of the frustration. *See* KENNETH JACKSON, CRABGRASS FRONTIER: THE SUBURBANIZATION OF THE UNITED STATES (1987). Hillier argues that these governmental maps were irrelevant for future redlining, which came from other sources. *See* Amy Hillier, *Redlining and the Home Owners' Loan Corporation*, 29 J. URB. HIST. 394, 394 (2003). Glock suggests that, despite the FHA's earlier discriminatory practices, their own lending patterns lent more aggressively in majority-minority neighborhoods. *See* Judge Glock,

The CRA thus became squarely the subject of supervision: the CRA exam itself was a separate enterprise from other exams but was conducted under the same supervisory teams for those primary supervisors at the Fed, FDIC, and Comptroller. The strategic decision that Congress chose for supervisors in the face of these ratings also put into conversation various other strands of supervisory discretion. Supervisors were to use the results of these exams to either reward compliant banks or punish non-compliant banks when they sought permission to expand their businesses, principally through new mergers and applications for new business lines. Since part of the CRA exam included inputs from those in the community where reinvestment was supposed to take place, banks had a powerful incentive not only to do well on these exams but also to recruit community groups to support their bids for expanded business.[202]

* * *

The examples outlined above—antitrust and merger evaluation, consumer protection, and the enforcement of civil rights—show an important turn in the postwar institutional shift for bank supervision. The basic institutionalization accomplished from 1863 to 1933 remained in place; bank supervisors were co-owners of risk management with the banks themselves but held strong to the residual systemic risks of financial collapse. These risks were divided among the different agencies: macroeconomic stability risk belonged to the Fed, the robustness of the national banking system to the comptroller, and protection of depositors and the Deposit Insurance Fund to the FDIC. As a partial consequence of the successes of the residual risk management of these systemic risks, Congress continued to expand the portfolios to include these other important policy priorities. What Congress did not do is tell supervisors how to optimize these sometimes-

*How the Federal Housing Administration Tried to Save America's Cities,* 28 J. POL'Y HIST. 290, 308 (2016).

[202] *See* REBECCA K. MARCHIEL, AFTER REDLINING: THE URBAN REINVESTMENT MOVEMENT IN THE ERA OF FINANCIAL DEREGULATION (2020).

conflicting priorities. That optimization was left to the supervisors themselves, a process that only expanded their discretionary authority over the entire system. Even when supervisors failed to achieve Congress's priorities, as in anti-discrimination policy, the (ironic) outcome was the creation of new supervisory tools and the expansion of official discretion.

## IV. MODERN APPLICATIONS OF RISK, DISCRETION, AND BANK SUPERVISION: CLIMATE CHANGE, MERGER POLICY, AND DEPOSIT INSURANCE

The positive theory of bank supervision that we have articulated through this extensive history contains, as noted, four components: supervision exists (1) at the intersection between public and private that has (2) evolved into a large apparatus touching on various policy goals whereby (3) Congress has given supervisors discretion to prioritize and implement these sometimes conflicting, sometimes complementary goals. These factors have created a system that is (4) resilient to permanent reform because it is a risk absorber for the entire financial system.

In this final section, we outline the ways that this framework can help us make sense of three of the most important and pressing policy issues currently facing banks: (1) how to evaluate the risks imposed by global climate change, (2) how to manage bank concentration and bank merger policy, especially in times of crisis, and (3) how to understand the relationship between hard-to-price deposit insurance and bank supervision.

### *A. Global Climate Change and Bank Supervision*

The question of how central banks and bank supervisors will manage climate- related risks has become one of the most contentious in current debates about our financial system. Sarah Bloom Raskin, Joe Biden's nominee for Vice Chair for Supervision and a former central banker and Deputy

Treasury Secretary under the Obama administration, faced defeat in the U.S. Senate due to her views that "financial regulators have yet to show that they are thinking creatively about potential solutions" and that they must "ask themselves how their existing instruments can be used to incentivize a rapid, orderly, and just transition away from high-emission and biodiversity-destroying investments."[203] Her fate was sealed when Senator Joe Manchin, Democrat of West Virginia, indicated that Raskin "failed to satisfactorily address [his] concerns about the critical importance of financing an all-of-the-above energy policy to meet [the] nation's critical energy needs."[204] The Federal Reserve has been most vocal in trying to walk a line on the appropriate interventions for a central bank in this space, not always speaking with one voice. "Our view is that is an issue that was given to other agencies to deal with," the Fed's General Counsel, Mark Van Der Weide said in 2020.[205] Fed Chair Jay Powell made similar kinds of commitments, claiming climate change is "an important issue but not principally for the Fed."[206] On the other hand, former Fed Vice Chair Lael Brainard contended that while "there is substantial uncertainty surrounding how or when" the economic and

[203] *See* Sarah Bloom Raskin, *Changing the Climate of Financial Regulation*, PROJECT SYNDICATE (Sept. 10, 2021), https://www.project-syndicate.org/magazine/us-financial-regulators-climate-change-by-sarah-bloom-raskin-2021-09 [https://perma.cc/9DB9-PE5U].

[204] *See* Jane Mayer, *Sarah Bloom Raskin Withdraws Her Nomination to the Federal Reserve Board*, NEW YORKER (Mar. 15, 2022), https://www.newyorker.com/news/news-desk/sarah-bloom-raskin-withdraws-her-nomination-to-the-federal-reserve-board [https://perma.cc/86KP-Y4VV].

[205] Am. Bankers Ass'n, *Fed Official: No Near-Term Plans for Climate Risk Weights, Stress Tests,* BANKERS J. (Jan. 17, 2020), https://bankingjournal.aba.com/2020/01/fed-official-no-near-term-plans-for-climate-risk-weights-stress-tests/ [https://perma.cc/LRL6-YVRV].

[206] *See* Katia Dmitrieva, *Federal Reserve Leaves Action on Climate Change to Politicians*, BLOOMBERG (Nov. 13, 2019), https://www.bloomberg.com/news/articles/2019-11-13/federal-reserve-leaves-action-on-climate-change-to-politicians.

financial consequences of climate change will materialize, "we can begin to identify the factors that could propagate losses from natural disasters, energy disruptions, and sudden shifts in the value of climate-exposed properties."[207] All of these examples suggested a much more aggressive approach to climate change be part of the Fed's bailiwick.

Scholars have been similarly divided. Some advocate for wholesale engagement of banking regulators and central banks in combating climate change.[208] Others view such moves as a kind of "central bank activism."[209] Still others call for "technocratic pragmatism" for the Fed to "develop the expertise necessary to address complex, emergent problems that affect the Fed's broad statutory missions," including climate change.[210]

The risk-and-discretion model of bank supervision makes clear that whether bank *regulators* do anything, bank *supervisors* already own this residual risk. This fact is true whether Congress formally assigns the risk to them, in an important sense, since Congress has already given supervisors the responsibility for ensuring both systemic financial stability and idiosyncratic risk for individual financial institutions—so-called macroprudential and micro-prudential risk, respectively.

To be clear, the risk-and-discretion framework does not resolve what non-bank supervisors should do. Central bankers may or may not have political cover or legal ability to

[207] Lael Brainard, Governor, Fed. Rsrv. Sys. Bd. of Governors, Address at The Economics of Climate Change Research Conference sponsored by the Federal Reserve Bank of San Francisco: Why Climate Change Matters for Monetary Policy and Financial Stability (Nov. 8, 2019), https://www.federalreserve.gov/newsevents/speech/brainard20191108a.htm [https://perma.cc/H2KU-BEGJ].

[208] *See* Graham Steele, *Confronting the 'Climate Lehman Moment': The Case for Macroprudential Climate Regulation*, 30 CORNELL J. L. & PUB. POL'Y 109 (2020).

[209] *See* Christina Skinner, *Central Bank Activism*, 71 DUKE L.J. 247–328 (2021).

[210] *See* Peter Conti-Brown & David Wishnick, *Technocratic Pragmatism, Bureaucratic Expertise, and the Federal Reserve*, 130 YALE L.J. 639 (2021).

use tools of monetary policy, conventional or unconventional, to engage in climate change remediation or prevention. What the framework provides is the recognition that supervisors share residual risk management with the private sector. If private banks are paying attention to climate risk–and they are, increasingly, and to an overwhelming extent– then bank supervisors must follow.[211]

While the politics of climate change are far from resolved, recognizing bank supervisors as the government's agents in the financial system authorized to use their discretion to manage all residual risk suggests that those who have opposed bank supervisory maneuvers fight against a system that is already well entrenched. In this sense, whether Congress specifically legislates to encourage supervision to expand further into climate change prevention and remediation is almost immaterial. A well-motivated bank supervisor can already begin this work; all bank supervisors, no matter their motivation, will bear the responsibility for crises that follow for mismanaged risk. At the same time, the historical experience of bank supervision also suggests that certain approaches that seek to harness the bank supervisory system to advance climate goals may be less effective than advocates suppose. Legislation which seeks to use supervisors in a regime that addresses climate risk by punishing banks that do not comply with congressional policy goals may create a conflict of supervisory prerogatives. Like consumer protection and anti- discrimination, examiners may prioritize safety and soundness over all else, giving them an opportunity to "ignore" one congressional edict in the name of honoring another.

[211] *See* Daniel Beltran et al., What Are Large Global Banks Doing About Climate Change? (Int'l Fin. Discussion Papers, Paper No. 1368, 2023), https://www.federalreserve.gov/econres/ifdp/what-are-large-global-banks-doing-about-climate-change.htm [https://perma.cc/TUL9-6L2J].

### B. Bank Merger Policy in the Twenty-First Century

A growing chorus of scholars and policymakers–and in some cases, scholars- turned-policymakers–have invited a reexamination of antitrust policy in the twenty-first century.[212] The basic insight is that historical programs of antitrust enforcement arising in the 1960s that focused on consumer welfare as the only meaningful category of consequence were wrong. More important, these scholars argue, is to understand that "a company's power and the potential anticompetitive nature of that power cannot be fully understood without looking to the structure of a business and the structural role it plays in markets."[213] In banking, this antitrust ethos has entered scholarly discourse, too.[214]

In banking and finance, there has been bipartisan enthusiasm for this approach. For example, the day after the 2020 presidential election, the Trump Administration's DOJ sued Visa to block the acquisition of tech startup Plaid.[215] Furthermore, in July 2021, President Joe Biden issued an executive order stating the policy of the Administration to "to enforce the antitrust laws to combat the excessive concentration of industry, the abuses of market power, and the harmful effects of monopoly and monopsony."[216] In the same order, he instructed the DOJ, Federal Reserve, FDIC,

[212] *See* TIM WU, THE CURSE OF BIGNESS: ANTITRUST IN THE NEW GILDED AGE (2018); Lina M. Khan, *Amazon's Antitrust Paradox*, 126 YALE L.J. 710 (2016).

[213] Khan, *supra* note 212, at 717.

[214] *See* Jeremy Kress, *Modernizing Bank Merger Review*, 37 YALE L.J. 435 (2020). Tim Wu, Lina Khan, and Jeremy Kress have all joined the Biden Administration in various capacities (Wu as Deputy Director of the White House's National Economic Council, Khan as Chair of the Federal Trade Commission, and Kress as Special Advisor to the Assistant Attorney General for Antitrust at the Department of Justice).

[215] Press Release, U.S. Dep't of Just., Justice Department Sues To Block Visa's Proposed Acquisition of Plaid (Nov. 5, 2020), https://www.justice.gov/archives/opa/pr/justice-department-sues-block-visas-proposed-acquisition-plaid [https://perma.cc/X3SJ-B38Z].

[216] Exec. Order No. 14,036, 86 Fed. Reg. 36,987 (July 14, 2021).

and OCC to "review current practices and adopt a plan . . . for the revitalization of [bank] merger oversight."[217]

Banking antitrust has, as noted above, has long been a confused and confusing subfield given the different supervisory priorities that different governmental actors might place upon it. This complexity remains unchanged. The banking crisis of 2023 highlights this tension further. As Silicon Valley Bank barreled toward its government-assisted crash—the second-largest bank failure in U.S. history— the government scrambled to find a suitable partner to acquire the bank, imposing conditions on the very banks that were qualified to take over. Meanwhile in international contexts, Credit Suisse, the second-largest bank in Switzerland, was acquired following its March 2023 failure by the largest bank in Switzerland, UBS; both Swiss banks were considered global systemically important banks.

Risk-and-discretion bank supervision provides precisely this kind of flexibility to choose or invoke problems or solutions with bank concentration, as the circumstances permit When bank lobbyists advance the argument that economies of scale from bank concentration justify a consumer welfare approach—permitting nearly every proposed banking merger—they ignore decades of evidence indicating that bank merger policy operates differently. The same tendency to overlook historical evidence applies when neo-Brandeisian critics advocate for blocking mergers solely based on concentration, regardless of potential benefits.

The reality for bank merger policy is that supervision facilitates any vision for merger policy. The law is too broad and supervisory discretion too capacious to limit it. This breadth illustrates here, as elsewhere, why the personnel selected to lead supervisory functions are so enormously important. A chief supervisor of a federal banking agency can accomplish a wide array of conflicting goals across administrations, depending entirely on their own balance of competing priorities.

[217] *Id.*

### *C. Deposit Insurance and Bank Supervision*

Before the 2008 financial crisis, scholars in the United States long thought that the problems of bank runs had been solved by the advent of deposit insurance.[218] Other countries came to a similar conclusion. For example, Canada established deposit insurance in 1967 after successfully weathering the Great Depression. Similarly, the United Kingdom shifted from partial to full deposit insurance in 2009. Similarly, the United Kingdom, which had a regime of partial deposit insurance, instituted full insurance in 2009.

The United States has had a long history of gradual then sudden expansions of deposit insurance, sometimes in the face of crisis and often in response to lobbying from banks.[219] But it has always been limited. The original terms of the Glass-Steagall Act of 1933 were to extend such insurance only to $2,500 per account. Two years later, Congress expanded that to $5,000. In 2008, after a run of uninsured depositors on several institutions, Congress more than doubled the $100,000 level prevailing since 1980 to $250,000.

In the aftermath of the banking crisis of 2023, debates rage anew about whether to expand that insurance limit or even to eliminate it entirely.[220] Sometimes these calls come to enhance supervision to mitigate underpriced insurance,

[218] *See* Michael D. Bordo, *The Lender of Last Resort: Some Historical Insights* (Nat'l Bureau of Econ. Rsch. Working Paper No. 3011, 1989), https://www.nber.org/system/files/working_papers/w3011/w3011.pdf [https://perma.cc/9PKS-AZQP].

[219] *See* Eugene N. White, *Deposit Insurance* (World Bank Pol'y Rsch. Working Paper No. 1541, 1995), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=569205 [https://perma.cc/7JDD-LVNQ].

[220] Morgan Ricks & Lev Menand, *Scrap the Bank Deposit Insurance Limit*, WASH. POST (Mar. 15, 2023), https://www.washingtonpost.com/opinions/2023/03/15/silicon-valley-bank-deposit-bailout/.

sometimes they come with no connection to bank supervision at all.[221]

The risk-and-discretion framework has much to offer this debate. The FDIC was created alongside deposit insurance as the mechanism to supervise its use. This created a supervisory ethos keen to protect the value of the Deposit Insurance Fund, the financial mechanism that provides insurance payments to depositors in the event of bank failure. The primary mechanism in the deposit insurance system, however, is not consistently supervisory, but the fact that insurance is priced to compensate the fund in case of bank failures.

Our framework suggests that efforts to massively expand insurance will not be effective, given a basic asymmetry in the system of supervision and public insurance pricing. Never in U.S. history has deposit insurance been lowered. Supervision as discretion moves cyclically. What is more, the pricing of deposit insurance is subject to relentless pressure to deregulate through pricing strategies. The residual ownership of risk that bank supervisors will carry suggest that they will be responsible for failed bank entities, regardless of whether they have the funds to do so or, potentially, whether bank or bank-like entities are formally covered by deposit insurance. Expanding deposit insurance in the hopes that there will be commensurate expansions in supervision is therefore unlikely to occur.

## CONCLUSION

This Article presents a new framework for conceptualizing bank supervision, a unique and vital part of both state capacity and financial markets. We argue that the fundamental responsibility of supervisors is to negotiate: to negotiate the joint responsibility of residual risk management

[221] David Wessel, *A Debate: Should the US Raise the $250,000 Ceiling on Deposit Insurance?*, BROOKINGS INST. (May 2, 2023), https://www.brookings.edu/articles/a-debate-should-u-s-raise-the-250000-ceiling-on-deposit-insurance/ [https://perma.cc/XEC3-TJCL].

with the banks they supervise and to negotiate between and among the boundaries of different approaches to bank supervision that history has accreted over time.

This history and framework have implications beyond banking and bank supervision. As courts increase their presence in the evaluation of agency actions, some have argued in favor of more judicial presence in the field of bank supervision, characterizing the field as "the most oppressive component of the federal regulatory state."[222] That evolution is extremely unlikely to occur. For 160 years, bank supervision has existed in the shadows as an alternative mechanism for negotiating the co-ownership of financial risk. Even identifying the legally cognizable action that courts could invalidate in bank supervision is nontrivial. Instead, supervisory ownership of residual risk and co-management of frontline risk will continue to thrive and even expand in the retreat of other risk management strategies, such as regulations that require increased specificity to survive judicial challenge.

Bank supervision, in other words, is not only likely to persist in the post-*Chevron* era. It is likely to expand. This Article provides a roadmap for the options that expansion can take.

[222] *Are Bank Examiners Next on Industry Lawsuit List?,* CAPITOL ACCT. (July 10, 2024), https://www.capitolaccountdc.com/p/are-bank-examiners-next-on-industry [https://perma.cc/4U6Y-YV5R].