



The Ties that Bind: Mutual Building and Loans and the Problem of Agency, 1880-1920

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I examine how immigrants used ethnic building and loans (B&Ls) to establish personal networks and overcome the problem of asymmetrical information flows in home finance. American B&Ls were cooperative institutions whose main purpose was to encourage home ownership by promoting thrift and mutual cooperation among its members. First appearing in 1831, B&Ls were very popular with ethnic Americans by the end of the century, in part because they worked to build confidence and trust among their members through the use of formal and informal personal networks. These networks appeared in part because ethnic B&Ls were neighborhood associations that held meetings and printed documents in the native language of the immigrant members. Similarly, as mutual organizations, the members had a direct voice in selecting and overseeing management. While these networks increased the degree of agency for thrift members, managers also used them to help evaluate credit risks; in fact, the character of a potential borrower was an important criterion in the loan approval process.

In his book *The Jungle*, Upton Sinclair chronicles the many challenges faced by the Lithuanian immigrant Jurgis Rudkus and his extended family in their effort to establish a new life in the industrial American city of Packingtown. One of these challenges involved buying a house, which Jurgis (like most Americans) felt was the only suitable environment for raising a family. Achieving this element of the “American Dream,” however, proved difficult. Problems, including a language barrier, financial naivete, and an unfamiliarity with legal documents forced Jurgis to rely on others to help guide his decisions. Only after buying the house did Jurgis find out that he was given inaccurate advice, and that the monthly payments were twice what he had been led to believe. Because the family was unable to stay current on their contract, they ultimately were evicted from the house. This experience of falling victim to the “buying a home swindle,” served to confirm Jurgis’s belief that “in matters of business all men are to be accounted liars.”¹

¹ Upton Sinclair, *The Jungle*, (New York, 1985), 60-6, 85-7, quotation at p. 62.

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Although Jurgis' story is a fictional account, the difficulty of building agency (that is, the relationship of trust between individuals and financial institutions) was a very real concern for immigrants. One way they tried to overcome this problem was by joining ethnic building and loans (B&Ls). In this paper, I examine why immigrants used these institutions to form personal networks and how these networks gave them the confidence and trust needed to enter into long-term financial transactions. I have identified three broad reasons why B&Ls were so effective in achieving this goal. The first is that immigrants were often familiar with thrift business practices, because similar procedures were used by cooperatives in their home countries. A second reason why they had confidence in B&Ls was that they were neighborhood businesses typically serving specific ethnic communities. The most important reason why ethnic B&Ls gave immigrants a high degree of agency was that thrift managers consciously worked to establish open relations with members and promote a spirit of cooperation. Not only did personal ties build trust and confidence in management, but management also used them to make business decisions. Before examining these factors in detail, however, it is necessary to briefly discuss the American thrift industry towards the end of the nineteenth century.²

Building Personal Networks in Ethnic B&Ls

Thriffs first appeared in the United States in 1830s as a way to help people of limited means become homeowners and save for the future. Modeled on the British building societies, B&Ls required depositors to become owners of the association through the purchase of shares. These shares were paid for over time in monthly installments, and when enough money accumulated, members could borrow from the B&L to buy a home. Because each person's loan amount equaled the face value of their subscribed shares, the loans were essentially advances on the unpaid portion of the shares. The member/borrower repaid the loan by continuing to make the same monthly share payment, plus interest on the advance.³

There are several reasons why saving and borrowing at a B&L appealed to working-class Americans. The first is that the shares were paid for over time, and the required monthly payments of \$1-3 per share were generally affordable. Second, because B&L profits were distributed

² For a discussion of the role of agency in business and finance see Jonathan Barron Baskin and Paul J. Miranti, Jr., *A History of Corporate Finance* (New York, 1999), 20-24 and Jonathan Barron Baskin, "The Development of Corporate Financial Markets in Britain and the United States, 1600-1914: Overcoming Asymmetric Information," *Business History Review* 62 (Summer 1988): 199-237.

³ Edmund Wrigley, *The Working-Man's Way to Wealth* (Philadelphia, 1872), 12-20; Seymour Dexter, *A Treatise on Cooperative Savings and Loan Associations* (New York, 1889), 26-42.

to members as credits to their accounts, thrifts were among the few institutions to pay compound interest on deposits. The key reason B&Ls were so attractive, however, was that the home loans they made were both longterm and fully amortizing. Unlike bank loans, which were typically repaid interest only with the full principal due in 3 to 5 years, thrift mortgage payments included both principal and interest, and had terms of 6 to 10 years.⁴

Although the first loan ever made by a thrift defaulted, the overall success of these associations in helping working-class people acquire homes led to their steady expansion across the country. By 1894, more than 5,500 B&Ls were in existence, and nearly 40 percent of these were located in and around the industrial centers of the East and Midwest. One important reason for the rapid growth of these associations was their popularity with immigrants. An estimated 10 percent of all thrifts had distinct ethnic origins and served German, Italian, Irish, Scottish, Polish, Hungarian, Serbian, Croatian, Lithuanian, Estonian, Latvian, and Russian communities. In some cities, ethnic thrifts were so numerous that B&L trade associations were formed along national lines. National thrift leaders recognized and approved of ethnic Americans' role in the thrift business, noting that thrifts were "being rapidly carried forward among the foreign element which is truly for the good of the local community."⁵

While immigrants appreciated the financial advantages of saving and borrowing from a thrift, many became members because of their high degree of confidence in how these institutions were operated. B&Ls followed many of the same procedures used by financial cooperatives in Europe. For example, England was home to a thriving network of building societies and friendly societies, while the German Housewives Societies and Friendly Societies for Building were equally popular with working-class men and women. In Poland, mutual-aid cooperatives called "People's Banks" had operated since the nineteenth century and held millions in worker savings. Like American thrifts, these societies were dedicated to helping people of limited means achieve greater financial security. Their organization and plans of operation were also very similar. More importantly, they all required members to adhere to the principle of thrift and mutual cooperation for their long-term success.⁶

⁴ Henry Rosenthal, *Cyclopedia of Building, Loan and Savings Associations*, (Cincinnati, 1923), 114-7, 143-9; Robert Reigel and Russell Doubman, *The Building-and-Loan-Association*, (New York, 1927), 6-10.

⁵ Carroll Wright, *Ninth Annual Report of the Commissioner of Labor, Building and Loan Associations*, (Washington, D.C., 1894), 291, 323; "Organization of Associations Among Foreigners," *American Building Association News* [hereafter *ABAN*] 30 (Jan., 1910), 187.

⁶ Mary Hinman Abel, "Housekeepers' Clubs in Germany," *Financial Review and American Building Association News* [hereafter *FRABAN*] 12 (June, 1893), 90; "The Housing Question in Germany," *ABAN* 24 (Dec. 1905): 235; "The

A second reason immigrants joined B&Ls was that these were neighborhood institutions dedicated to meeting financial needs of distinct ethnic communities. Organizing a B&L was relatively easy; most states required a minimum of only five members to receive a charter. Also, because thrifts were allowed to operate from almost any location, many met at local taverns, which were centers of neighborhood social activity. As a result, the average thrift in 1894 had just 300 members, and more than a third of all B&Ls had less than 100 members. Furthermore, by limiting their business activities to specific neighborhoods, hundreds of thrifts could operate profitably in a single city. For example, Chicago had more than 300 B&Ls and Philadelphia was home to 500 such associations.⁷

As neighborhood businesses, few B&Ls used outside advertising to attract members, but instead relied on word-of-mouth recommendations. Not only was this method ideally suited to the tight-knit nature of ethnic communities, but it also meant that new savers and borrowers were usually already known to the membership. This method of solicitation was not an impediment to size, as one of Chicago's largest thrifts with \$5 million in assets drew all its members from an extended neighborhood 4 miles long and one mile wide using only word-of-mouth advertising. Immigrants also felt more comfortable with B&Ls because they often held their meetings and published financial documents in their native language. Thrifts provided members with easy to understand financial tables to help them calculate the current value of their shares, and it was common for managers to restructure loans if borrowers had trouble meeting their obligations.⁸

Personal Networks and Thrift Managers

A third reason that helps explain immigrants' high degree of agency in ethnic B&Ls is that as owners, members had a direct voice in the selection and oversight of management. Thrift leaders maintained that "the

International Aspect of Home Financing Institutions," *ABAN* 53 (Aug. 1933): 359, 385-6.

⁷ Wright, *Ninth Annual Report*, 291; "Loan Associations for Store Workers," *ABAN* 31 (Sept. 1911): 391; Joseph Sundheim, *Law of Building and Loan Associations*, (Philadelphia, 1922), 33-9; "Irish-American of Buffalo," *ABAN* 29 (March 1909): 127; "Tavern Societies," *ABAN* 29 (April 1909): 149; John Novak, "The Bohemian League of Building and Loan Associations of Chicago," *Proceedings of the Twenty-Third Annual Meeting the United States League of Local Building and Loan Associations* (Cincinnati, Ohio, 1914), 278-9.

⁸ "Monthly Dues," *ABAN* 22 (Nov. 1903): 244; Albert Shaw, *Cooperation in a Western City*, American Economic Association Monograph vol. 1, no. 4 (Baltimore, Md., 1886), 278-290, quotation at p. 279; Albert Wachowski, "The Polish Nationality and Their Building and Loan Associations," *ABAN* 29 (Jan. 1909): 24-5.

depositors in any association must feel it not only as a right but a duty to watch closely the whole management of affairs, and especially the character of the men." This power was considered a key to the success of B&Ls, and unlike commercial banks where "the relationship between management and depositors [was] remote," made thrifts "perfectly democratic" businesses. According to one Polish B&L executive, "the work of a [thrift] is more on the line of a social organization. Perhaps it is the fact that the members know personally their own officers which they have chosen . . . that gives them so much confidence in the [association]."⁹

The "democratic spirit" with which B&Ls were governed was further enhanced by the fact that the public image of turn-of-the-century thrifts was very different from that of other financial institutions. Unlike commercial banks, B&Ls were portrayed as being part of a self-help movement of social uplift that worked to improve the character and morals of their members. To advance these objectives, thrift leaders insisted that managers be selected based on their personal integrity and character, not simply on title or standing in the community. Similarly, because these officers held a "sacred trust" with the members, forming personal networks was also critical to a thrift's financial success. According to one observer, because "the members have easy access to the officers and meet with them in daily life, the opportunity and temptation to do wrong is minimized. . . [as] officers are encouraged and constrained to do right by the elbow touch of the entire membership."¹⁰

Despite the importance of forming a "bond of friendship and familiarity with members," thrift managers realized that close personal relations were not always feasible. Consequently, managers were encouraged to follow other activities to instill member trust, such as conducting business openly and publically and keeping operations simple by making only home mortgage loans. Associations were audited frequently and subject to state supervision whenever possible. Managers were encouraged to minimize expenses, not only to maximize the amount

⁹ Robert Treat Paine, Jr., "Homes for the People," *Journal of Social Science* 15 (Feb. 1882): 104-120, quotation at p. 119; Charles N. Thompson, "The Building and Loan Association as an Institution for Savings of the Industrial Classes versus the Savings Bank: A Comparison of the Benefits to be Derived from Them," *FRABAN* 12 (Aug. 1893): 203; Bell, "Building Associations: How Operated, Advantages, Etc." Albert Wachowski, "Polish United Building and Loan Associations," *ABAN* 31 (Dec. 1911): 492-3, quotation at p. 423; W. A. Linn, "Building and Loan Associations," *Scribner's Magazine* 5 (June 1889): 709.

¹⁰ Robert Treat Paine, Jr., *Cooperative Savings Banks or Building Associations*, (Boston, 1880), 6-12, quotation at p. 6; W. P. Ogden, "Personality of the Secretary in Relationship to Members," *FRABAN* 17 (July 1896): 7; W. E. N. Hemperly, "Position of the Savings and Loan Association in the Community," *ABAN* 22 (Dec. 1902): 343; "California Associations," *FRABAN* 13 (Dec. 1893): 291; D. A. Tompkins, "Working People's Homes," *Cassier's Magazine* 23 (March 1903): 612-15.

of money available for home loans, but to give members confidence that they were not trying to gain financially from their positions. In fact, one interesting characteristic of thrifts at this time was that many directors and officers served for little or no pay.¹¹

The creation of personal networks through B&Ls not only had many benefits for immigrants, managers used them to make sound credit decisions. One of the many risks of lending money was a borrower providing misleading information. While property appraisals and credit reports helped to mitigate this “moral hazard,” managers needed to find a way to evaluate a borrower’s “character.” They were encouraged to be “good judges of human nature. . . [and] look not only at a borrower but their companions in life.” Their use of personal networks to assist them is evidenced by the fact that loan reports typically contained extensive interviews with friends and employers of prospective borrowers. Some lenders even considered a borrower’s personal character more important than the value of the underlying collateral, noting that “the value of a property should [only] be a safeguard . . . in case the judgement of the borrower as a credit risk should prove wrong.” This practice of “character lending” symbolized the degree of confidence and trust personal networks could engender, and was an important source of thrift business well into the twentieth century.¹²

Conclusions

Overcoming the problem of agency in financial transactions was a persistent challenge for both consumers and lenders. Consumers needed to be confident that lenders would exercise their fiduciary responsibility, while lenders need to find ways to ensure that loans were repaid promptly and in full. One way immigrants achieved a high degree of agency in home finance in the late-nineteenth century was by joining ethnic B&Ls. These were small, neighborhood associations whose members typically knew each other. Significantly, because B&Ls were portrayed as self-help institutions that encouraged mutual cooperation, thrift managers encouraged the formation of informal personal networks with members. Over time, the ability of depositors to form close ties with managers became an indelible characteristic of all thrifts, and to this day separates them from commercial banks and other financial institutions.

¹¹ J. J. Stoddard, “The Status of the Building and Loan Associations as Financial Institutions,” *ABAN* 24 (Feb. 1904): 45; “Notes” *ABAN* 23 (Nov. 1903): 253; “For Proper Auditing,” *ABAN* 23 (Dec. 1903): 344; Wright, *Ninth Annual Report*, 297-8.

¹² Henry Morton Bodfish and A. D. Theobald, *Savings and Loan Principles*, (Chicago, 1936), 197-202, 215; E. P. Beach, “The Selection of Loans,” *FRABAN* 13 (June 1894): 137; “Calls Character Security Value,” *New York Times*, 6 June 1937, sec. 9, quotation at p. 6.