Banking on Trust:
Historical Perspectives on Changes and Continuities in the Strategies of Rebuilding Corporate Legitimacy in British Joint-Stock Banks, c. 1830s-60s

This thesis is submitted for the degree of PhD Leadership and Management.

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Table of Contents

Abstract vi

List of Tables vii

List of Figures viii

Acknowledgements ix

Author's Declaration xi

Chapter 1 Banking, Trust, and Historical Development 1

1.1 The Thesis: An Introductory Remark 1

1.2 Joint-Stock Banking: Conception, Constraints, and Challenges (c. 1820s-60s) . 3

1.3 Lancashire: Banking, Profits, and the Industrial Powerhouse 6

1.4 The Thesis: Structures, Subjects, and Synthesis 11

Chapter 2 The History of Joint-Stock Banks: A Literature Survey 13

2.1 Creating, Sustaining and Stabilising Trust 13

2.1.1 Trust, Networks, and Social Controls 14

2.1.2 Risk-Taking, Trust Conceptualisation, and Social Cooperation 17

2.1.3 Trust Failures: The Tact of Relationship Management 19

2.2 Moral Persuasion, Professional Induction, and Official Regulation 22

2.2.1 Banking, Reputation, and Moral Probity 23

2.2.2 The Rise of Banking Professionalism 26

2.2.3 The State of Indulgence? 29

2.3 The Little Republics: Democratic Rhetoric, Common Good and Corporate Autocracy 32

2.3.1 Republican Virtues, Trust, and the Common Good 33

2.3.2 Joint-Stock Banks, Democratic Deficit, and Corporate Autocracy 36

2.3.3 Corporate Power: Authority, Accountability, and Assurance 38

2.4 Banking Liability: Regimes, Responsibility, and Credibility 40

2.4.1 Firm as a Rock? The Test of Unlimited Liability *41*

2.4.2 Shareholder Constituency, Wealth, and Public Confidence *44*

2.4.3 Shareholder Primacy, Plight, and Protection *46*

2.5 Conclusion: The Essence of Trust 47

Chapter 3 Banking Conduct, Changes, and Continuities: A Methodological Comment 49

3.1 A Cultural Analysis 49

3.2 Hayek: Freedom, Individuals, and the Spontaneous Order 52

3.3 Organisational Trust Repair Model: An Analytical Framework 55

3.4 Cases, Sources and Uses 61

3.5 A Concluding Statement 66

Chapter 4 Early Experimentations: The Early 1830s 68

A Comparative Study of Two Manchester Banks 68

4.1 Background 68

4.2 The Coming Headwind 70

4.3 Two Dissimilar, Similar Accounts 73

4.4 Integrity: The Evidence of Guilt 75

4.5 Competence: The Trouble with the Novice 79

4.6 Governance, Transparency, and Accountability: The Limits of the Law 82

4.7 Trust: By Means of Learning or Legislation? 86

4.8 Conclusion 90

Chapter 5 From Trials to Troubles: The 1840s 92

The Bank of Manchester and the Royal Bank of Liverpool 92

5.1 Background 92

5.2 The 1844 Reform 93

5.3 The Drama Unveiled 96

5.4 Positive Discrimination 100

5.5 Untrained, Unqualified, and Unprincipled 106

5.6 Leadership Shakeup and Restitution... 111

5.7 Second Chance?... 118

5.8 Redrawing the Boundary of Power.. 122

5.9 Conclusion 125

Chapter 6 Lessons (Un)learned: The 1850s... 128

The Liverpool Borough Bank and the Same Old Mistakes 128

6.1 Background... 128

6.2 Legislative Failure, Governance Breakdown, and Moral Panic 131

6.3 Lies, Losses, and Lawsuits 133

6.4 Agency Failure.. 135

6.5 Profits or Puffery? The Failure of Financial Accountability 139

6.6 The Unlawfulness of Half-Truth.. 143

6.7 Distrust, Secrecy, and Legal Constraints 146

6.8 Conclusion 150

Chapter 7 Safe as Houses? The 1860s:.. 153

The Consolidated Bank vis-à-vis the Preston Banking Company.......................... 153

7.1 Background... 153

7.2 No Turning Back: The Progress of Joint-Stock Banks 157

7.3 A Tale of Two Banks.. 158

7.4 Rules, Role Autonomy, and Discretionary Power 161

7.5 Investigation: The Appeals of Professionalism 166

7.6 Interactions: Sticking Together... 171

7.7 Intervention: Putting the House in Order... 175

7.8 Conclusion 178

Chapter 8 Construction, Destruction, and Reconstruction: 182

An Analytical View of Trust Repair in Victorian Joint-Stock Banks..................... 182

8.1 Introduction... 182

8.2 Trust Repair Model and Banking Peculiarities: Some Adaptations................ 183

8.3 Respectability: Competence, Integrity, and Reputation.................................. 188

8.4 Accountability: Corporate Power, Control, and Accountability 193

8.5 Transparency: Shareholder Inspection, Information, and Publicity 198

8.6 Equity: Conflicts, Prioritisation, and Reconciliation...................................... 202

8.7 Legality: Prevention, Punishment, and Protection.. 207

8.8 Concluding Comments: Forward to the Past? 212

References... 217

Abstract

This thesis uses the organisational trust repair model developed by Gillespie and Dietz to examine how effectively selected joint-stock banks from Northwest England rebuilt corporate legitimacy amidst periodic commercial crises in the nineteenth century. Given organisational complexity and exposure to shifting market sentiments, this thesis focuses on how bank directors simultaneously managed trust and distrust in a hostile environment, in which different parties were prone to distrust just as much as they were to trust. By exploring various approaches to repairing organisational trust across different banking institutions, this thesis argues that successful trust repair requires one to understand how trust was damaged in the first place, because different violations require distinct reparative responses as conditioned by varying circumstances.

Following the belief that organisational legitimacy is a generalised perception among stakeholders that corporate actions are aligned with social norms and values, the research applies a cultural narrative approach to demonstrate how the interplay of socio-cultural factors drove the dynamics of trust repair. For this purpose, it uses different cultural sources, official papers, and archival materials to reconstruct the nineteenth-century contexts in which banking companies sought to repair trust. This thesis also argues that the dynamics of trust repair were essentially compounded by four key features of banking, namely: (1) information and power asymmetry between management and stakeholders; (2) competing expectations from different stakeholder groups; (3) the delicate balance between returns and risks from financial investment, and (4) the interconnectedness of banking institutions and the real economy. Through the combination of a contemporary theoretical framework with the historical contexts, the thesis aims to present the case for (1) understanding the past through the perspectives of management scholars in the twenty-first century, and (2) assessing the applicability of modern trust repair strategies in relation to historical patterns and practices.

List of Tables

Table 1.1 Joint-Stock Bank Branches and the Shareholder, 1844-99

Table 1.2 Joint-Stock Banks in Britain, 1826-99

Table 3.1 Organisational Components and Trustworthiness: A Banking Context

Table 6.1 Liverpool Borough Bank: Board of Directors, 1856-7

Table 7.1 Consolidated Bank, Limited: Board of Directors, Oct. 1863

List of Figures

Figure 5.1 Composition of Shareholders by Region: The Royal Bank of Liverpool, Oct. 1847

Figure 8.1 Organisational System Components and Impacts of Banking Characteristics on Public Perception of Organisational Trustworthiness

Figure 8.2 Constraints of Banking Characteristics on Trust Repair Efforts

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Author’s Declaration

I declare that this thesis is my own work and has not been submitted in substantially the same form for the award of a higher degree elsewhere. Certain sections of this thesis have been published as a journal article titled ‘Crisis, criticisms, and damaged credibility’ in *Business History*. The article carries the analytical framework (as covered in chapter 3.3 of this thesis) and shows how it is adapted to the banking context (chapter 8.2). It also contains the case analysis about the Royal Bank of Liverpool, which forms a substantial part of chapter 5.

Chapter 1
Banking, Trust, and Historical Development

1.1 The Thesis: An Introductory Remark

Banks – both in the nineteenth century and now – rely on trust. Failure of trust in banks can result in not only the failure of the bank, but that of the wider economy too. For this reason, trust in banks interests not only their customers and creditors but governments. On 27 May 1855, Lord Palmerston made it clear in his address to the House of Commons that as financial intermediaries, the functions of a bank "were altogether different" and fundamentally "partook of the nature of trust" (*Commons Hansard*, vol. 139, 27 Jul. 1855, c. 1446). Indeed, banking is inherently a risky business because of the "contradictory role expectations" entrenched in its intermediary function between lenders (i.e. depositors) and borrowers (Koslowski, 2009, p. 26). Bankers are custodians of depositors' money on one hand, and provide credit to the borrowers with the money they do not own on the other (Turner, 2014). Without trust from either party this intermediary function could not be fulfilled: depositors must trust the bankers that some good returns would be made on their money, and bankers in turn must trust the borrowing customers to repay in due time. Following this contradiction – as Turner (2014) rightly echoes – banking is distinct from other enterprises because its functioning is fundamentally anchored upon risk-taking and trust. Therefore, trust is of considerable importance for ensuring that the banking system could reliably fulfil its "Schumpeterian role" in driving commercial expansion and entrepreneurial ventures (Turner, 2014, p. 16).

Banking and financial crises lead to a general breakdown of trust (Gillespie et al, 2012; Koslowski, 2009). In Britain, the Secondary Banking Crisis (1973-5) and the Great Financial Crisis (2007-8), for instance, exposed the underlying rots and weaknesses of some banking institutions plagued by toxic lending portfolios and specious financial strategies. Nonetheless, unlike modern banking crises mentioned above during which a collapse in public confidence was (largely) staved off by bailouts funded by taxpayers "unprecedented in their scale and scope" (Turner, 2014, p. 2), nineteenth-century Britain witnessed the successful resuscitation of a few troubled banking entities – a process

during which restored trust was key to renewed cooperative relationships between management and stakeholders. Among these were the North and South Wales Bank (1847), the Royal Bank of Liverpool (1847), the City of Glasgow Bank (1857), the Consolidated Bank (1866), the Preston Banking Company (1866), and the Metropolitan Bank (1866). Insofar as scandals weaken corporate legitimacy and undermine public confidence, unlike contemporary banking in which rapid commoditisation and a sales-driven culture have weakened long-term trust sustained by personal integrity and frequent interactions (Jaffer et al., 2014d), the above notable examples in Victorian Britain show that the survival of troubled banking institutions was highly contingent upon the robustness of their relationship with different clusters of stakeholders.

Knowing how to repair trust and mitigate distrust is therefore a key demonstration of critical management competency (Lewicki & Bunker, 1996). This key argument is underscored by a few studies (see, for example, Gillespie & Dietz, 2009; Kim et al., 2009; Pfarrer et al., 2009), each of which identifies the sources of failures and recommends different strategies for restoring trust at different stages of organisational crises. Using contemporary management theories, this thesis aims to develop a historical understanding of how far – and how successfully – nineteenth-century joint-stock banks repaired organisational trustworthiness in the event of financial distresses or scandals. In connection with this central objective the main questions to address in this thesis are listed as follows:

(1) In the event of trust failures, how did banking organisations authenticate their corporate legitimacy in relation to the ideals of virtuous banking embodied in the Victorian capitalist order?
(2) How did the mechanism of corporate governance adapt to restore trust and rearticulate the issues of accountability and ethicality to arrive at an "ideal" business response amidst competing expectations?
(3) How effectively might different trust repair strategies work, as constrained by competing expectations and the broader regulatory, economic, and cultural environment?
(4) How did the bureaucratic machinery adjust its moral perception of the capitalist order and revise its approach to promoting stable and responsible banking accordingly?

Importantly, this study presents a case for using economic and business history as a valuable context to develop different perspectives of corporate trust repair in the twenty-first century. In so doing, it regards trust and trustworthiness of banking companies as depending on the institutional context – "an aspect of reality that changes through historical time" (Dow & Dow, 2014, p. 1342). Turner (2014, p. 4) similarly asserts that historical crises are useful inputs for "understanding the dynamics and commonalities, as well as the basic anatomy, of banking crises". This approach brings together different disciplines to explain the nature of trust and distrust in banking, in acknowledgement of the relevance of human actions and social process which drive the construction, destruction, and reconstruction of trust.

1.2 Joint-Stock Banking: Conception, Constraints, and Challenges (c. 1820s-60s)

Originally founded in 1694 as the banker and debt manager for the English government, the Bank of England was the first joint-stock bank in Britain. The key purpose was to bolster Britain's public finances in the face of a long-drawn war with France. The Bank's monopoly power was further entrenched when its charter was renewed in 1708, which included a new clause that prohibited the formation of any other bank with more than six partners, in the name of "checking the operations of some fraudulent or speculative mining companies that had then begun to issue notes" (Gilbart, 1859, p. 229). As England's wealth and commerce expanded, the demand for banking facilities rose significantly, and private banks with no more than six members began to spread across the country. The number of such partnerships exceeded three hundred by 1800, before rising further to 761 in England about thirteen years later (Pressnel, 1956). Importantly, the new market power conceded to the Bank had virtually no impact upon the banking system in Scotland, which was then a sovereign nation in its own right (Gilbart, 1859). The freedom from such statutory constraint meant that Scottish banks – as permitted by their own company law – could be liberally formed on the joint-stock basis. As time pressed on, the disparity (in terms of size and capital) between the English and Scottish banks widened, and their respective resilience and robustness in times of crisis would soon be put to test (see Table 1.1).

The national financial crisis in 1825 – which was by far the most severe witnessed since the economic turbulence occasioned by the South Sea Bubble in 1720 – saw the collapse of many (English) private banks (Turner, 2014). Many commentators blamed the

crisis upon the chartering privileges granted to the Bank of England, which excluded the entry of all potential competing institutions and ultimately condemned them to a narrow base of partnership and small capital (Turner, 2014, p. 36). By contrast, on the whole the Scottish banks had weathered the storm comparatively well. Under the premiership of Lord Liverpool (1812-27), the Tory government seized upon the opportunity to remodel England's banking system after that of Scotland. The Banking Co-partnership Act was passed in 1826 to allow English banks to form with more than six partners. The legislation effectively challenged the monopoly status once enjoyed by the Bank of England as a note-issuing joint-stock institution in the country. While business organisations were permitted to form freely on the joint-stock principle, they were subject to unlimited liability, under which partners were liable to "the last penny" for their debt (Turner, 2014, p. 10). In 1833, more obstacles were cleared with the passage of the Bank of England Privileges Act, to allow the formation of non-issuing joint-stock banks within sixty-five miles radius of London (see chapter 4).

Table 1.1

Joint-Stock Bank Branches and Shareholders, 1844-99

		1844	1859	1879	1899
England and Wales					
Branches:	*Mean*	5.0	5.6	12.3	56.9
	Maximum	92	105	155	283
Shareholders:	*Mean*	234.7	249.8	611.9	1,878.5
	Maximum	1,000	1,114	4,960	13,390
Scotland					
Branches:	*Mean*	18.2	43.4	88.2	96.4
	Maximum	52	99	129	143
Shareholders:	*Mean*	834.3	780.6	1,474.4	2,159.0
	Maximum	1,695	1,393	2,061	3,325
Ireland					
Branches:	*Mean*	14.7	21.6	55.0	73.4
	Maximum	38	49	116	132
Shareholders:	*Mean*	424.6	556.8	1,949.4	2,996.8
	Maximum	913	1,000	4,500	6,000

Source: Turner, 2014, p. 40.

Following the relaxation in the incorporation law, joint-stock banks began to spring up across all three countries – among which England and Wales witnessed the most spectacular growth (see Table 1.2). Industrial expansion and flourishing overseas trade also fuelled banking development. This growth was nonetheless intermittently checked by bouts of economic crises that thrusted internal defects and decays of a considerable number of joint-stock banks into limelight. Bank directors were caught issuing false statements, misallocating the company's funds, or making "fraudulent advances" to their cronies or themselves (Gilbart, 1859, p. 329). To improve banking stability, in 1844 Tory Prime Minister Sir Robert Peel (1841-6) moved for the enactment of the Bank Charter Act and the Joint-Stock Bank Act, effectively limiting the growth of banking companies in the following decade (see Table 1.2 and chapter 5). The 1850s banking mania, however, proved the legislation's failure to deliver the intended outcomes. Led by the premiership of Lord Palmerston (1855-8), the Liberal government passed the Joint-Stock Companies Act of 1856 to replace its 1844 predecessor, which the *Bankers' Magazine* (Mar. 1856, p. 162) criticised as laden with "cumbrous machinery for provisional registration, complete registration, regulations for internal government, and the other clumsy contrivances". In 1858, under the new Act limited liability was finally conceded to joint-stock banks.

Table 1.2

Joint-Stock Banks in Britain, 1826-99

	1826	**1830**	**1839**	**1849**	**1869**	**1889**	**1899**
England and Wales							
State-chartered bank	1	1	1	1	1	1	1
Unlimited-liability joint-stock banks	3	14	117	113	73	2	0
Limited-liability joint-stock banks	–	–	–	–	41	102	81
Scotland							
State-chartered bank	3	3	3	3	3	3	3
Unlimited-liability joint-stock banks	5	5	13	16	9	0	0
Limited-liability joint-stock banks	–	–	–	–	0	7	8
Ireland							
State-chartered bank	1	1	1	1	1	1	1
Unlimited-liability joint-stock banks	3	3	8	8	7	0	0
Limited-liability joint-stock banks	–	–	–	–	1	8	8

Source: Turner, 2014, p. 39.

Over the century, the new-found liberty did not guarantee a smooth sailing for joint-stock banks from the start. Constantly beset with inexperience and mismanagement from time to time, they "struggle to establish a footing", having to choose between "making advances with caution", resulting in limited business – or "launching out liberally", taking heightened risks that prudent banking norms would not tolerate (Grindon, 1877, p. 235). However, aided by a favourable climate in the political economy, joint-stock banks were firmly on the course of supplanting private banks as the main economic monuments in Britain. The character of (joint-stock) banks was a subject of "more scrutiny and discussion" in newspapers, trade journals, quarterlies, and publication of other sorts (Gilbart, 1859, p. 326). The growing dominance and expanding networks of joint-stock banks implied that private banks were slowly fading into the background and "ceased to be sole masters of the ground" (Grindon, 1877, p. 235). Gilbart (1859, p. 327) foresaw and summarised the trend as follows:

> The joint-stock banks are the bankers of the rising generation. The private bankers are the bankers of the generation that is passing away. As time passes on, the joint-stock banks will arrive at the maturity of their strength, and the private banks will sink into imbecility.

Despite all their perceived drawbacks and defects, joint-stock banks had virtually become a "positive necessity" in the nation – and their continuity was nothing less than the embodiment and expression of the vitality and vigour of the British economy (Grindon, 1877, p. 236).

1.3 Lancashire: Banking, Profits, and the Industrial Powerhouse

The thesis focuses on Lancashire because of its cotton industry and the subsequent rise in the demand for banking facilities. The focus on a specific region allows detailed discussion of case studies. It begins with the 1830s during which joint-stock banks were in a stage of novelty, brought about by the passing of the Banking Co-partnership Act in 1826. It concludes with the 1860s – just about a decade after limited liability was finally conceded to banking companies. The choice of these dates is not without a reason. In the 1830s, both hopes and fears emerged that Britain was going through exciting and revolutionary times. A new banking system, the optimists argued, was precisely what

Britain needed to accommodate its industrial transformation, rapid urbanisation, technological innovation, railway expansion, and the rest of it. The pessimists, however, were fearful that the untried system would plunge the whole nation far too deep into unchartered waters, with scarring consequences on the financial stability and moral fabric of the Victorian society. In the late 1850s, the extension of limited liability appeared to signify the will of lawmakers to set banking institutions free, effectively granting them the leave and license to consolidate further as the century rolled on. Across these years, rules of the game were constantly adapted and adjusted, to account for the unprecedented social and economic changes witnessed in the nineteenth century.

The final quarter of the eighteenth century witnessed some important inventions that were set to transform the socioeconomic landscape of Lancashire. The water frame (1764) invented by Richard Arkwright, the spinning jenny (1770) by Hargreaves, the spinning mule (1779) and the power loom (1787) by Cartwright, for instance, laid the foundation for the emergence of the county as one of the most notable heartlands of the cotton industry (Belusi & Caldari, 2011). Relying on "the swift-running streams of the Pennines as a source of power for spinning mills placed high up in the valleys", the industry eventually formed the backbone of the county's economy (Crick & Wadsworth, 1936, p. 140). Following the economic prosperity that thrived upon the new manufacture, the stock of population began to multiply. As early as 1801, Lancashire was already "the second most densely populated" county; thirty years later it became "the second-least agricultural", only after Middlesex (Balderston, 2010, p. 575). By 1821, there were thirteen towns in the county with more than 20,000 inhabitants each, while Liverpool and Manchester combined accounted for more than 328,000 (Crick & Wadsworth, 1936). A burgeoning population – coupled with coal exploitations and rising use of steam-powered machinery – provided the necessary resources for the industry's further expansion in the subsequent decades. By 1851, cotton manufacturing "leapt into the front rank" among all British industries, absorbing well over half-a-million of workers (Crick & Wadsworth, 1936, p. 142). It was by far the largest employer in the nation's economy, surpassed only by agriculture and domestic service.

The growing cotton industry, which by the early nineteenth century had already overtaken the local linen industries in Lancashire, also led to the rise of some "important ancillary trades" (Crick & Wadsworth, 1936, p. 142). Coal and iron mining – alongside the making of textile and other machinery – were among the beneficiaries. The production of cotton cloth also led to a higher demand for dyeing and bleaching, for which the

chemical ingredients were copiously available in the south of Lancashire – in Cheshire and Derbyshire, for instance, where a chemical industry prospered as a result, "fostering a further localisation of the cotton industry in Lancashire" (Belusi & Caldari, 2011, p. 136). More significantly, the expanding cotton industry was catalyst to the forging of trade between Britain and the rest of the world, given its dependence on foreign plantations – especially those in the West Indies and North America – for raw cotton, and also its voluminous export of cotton products to other parts of the British Empire. By 1840, the industry represented 48 per cent of the total value of Britain's manufactured exports (Rodgers, 1962). This process likewise drove the emergence of shipping companies and mercantile services based in Lancashire.

As mechanisation gathered speed, the centre of textile manufacture in Manchester shifted from the home to factories. The town gradually became "a great marketing and manufacturing centre" for cotton products, during which it became the largest and most productive cotton spinning centre in the world (Crick & Wadsworth, 1936, p. 142). Cotton mills also opened in the surrounding towns, sprawling from Bolton, Oldham, and Rochdale – to Blackburn, Darwen, and Burnley (Gurr & Hunt, 1998). Manchester's position as a strategic transport hub was further consolidated by the Bridgewater Canal, which allowed raw cotton imported from the West Indies and North America to be transported through the port of Liverpool to the terminus at Castlefield. Opened in September 1830, the Liverpool and Manchester Railway also provided faster transport of raw materials, finished products, and passengers between the port of Liverpool and the cotton mills at Manchester. As the industry grew, warehouses, banking facilities, and mercantile services for the 280 cotton towns and villages began to spring up within a twelve-mile radius of the Royal Exchange (Williams & Farnie, 1992). By the 1870s, Manchester already earned itself the nickname "Cottonopolis" and accounted for 32 per cent of global cotton production (Partridge & Beale, 1992, p. 258; Williams & Farnie, 1992).

Compared to other parts of Lancashire, the economic history of Liverpool was somewhat unique because of its "far wider range of interest" (Crick & Wadsworth, 1936, p. 154). As an important port "ranking only after London", the city was a pronounced shipping and mercantile centre, forming a critical trading link across the Atlantic between Britain and the American continent, of which cotton trade was a prominent feature (p. 154). Infamously, vast profits derived from slave trade and privateering – which began at the close of the seventeenth century until the practice was completely stamped out in 1862

– transformed Liverpool into one of Britain's most prominent international trading and financial centres. To accommodate a growing trade volume that encompassed a vast range of commodities, more than 140 acres of new docks, with 10 miles of quay space, were constructed with great speed between 1824 and 1858 (Belchem, 2006). Liverpool's economic relationship with Manchester was of strategic necessity a complementary one, bolstered by steadily improving land and water transportation over time. Beginning 1721, both towns were already linked by canal, before their connection was further buttressed in 1830 through the Liverpool and Manchester Railway. Furthermore, with the dismantling of the monopoly status enjoyed by the East India Company in 1813, cotton trade gathered extra momentum from which the Manchester factories and mills also profited handsomely, propelled by the rapidly expanding export market in India and the Far East.

Burgeoning international trade and the cotton industry meant a vast amount of money was changing hands, giving rise to the proliferation of private banks (Crick & Wadsworth, 1936). One of the Manchester pioneers was Benjamin Heywood, the brother of Arthur Heywood, who founded a Liverpool private bank in 1773 under the title Arthur Heywood, Sons & Co. The attempts of the brothers to open a branch in Manchester failed, after which in 1788 Benjamin and his two sons, Benjamin Arthur and Nathaniel Heywood, proceeded to form a new Manchester bank, named Benjamin Heywood, Sons & Co. The firm's venture began in Exchange Street before relocating to St. Ann Street in 1795 (Orbell, 2001). Upon the father's death in the same year, the bank was renamed Heywood Brothers & Co. Meanwhile, Liverpool was served primarily by two private banks. The first of these was Leyland & Bullin, which commenced business in January 1807 at the premises in York Street. The bank was formed under a partnership between Thomas Leyland – who was "a wealthy merchant and shipowner" in possession of "a well-earned reputation for shrewdness and mercantile sagacity", and his nephew Richard Bullin (Crick & Wadsworth, 1936, pp. 143-4). The second one – named Moss, Dales & Rogers – was founded in late 1807 by John Moss, also a Liverpool merchant and shipowner. The private bank first opened its door in Exchange Buildings, before relocating to new premises in Dale Street four years later to accommodate its growing business. Both banks were intimately connected with the commerce of Liverpool, especially with shipping and other related activities, supported and sustained by a fast-growing population and volume of trade at the port (Crick & Wadsworth, 1936).

Interestingly, it was after the construction of the Liverpool and Manchester Railway – actively pioneered by Moss who was at the same time the chairman of the Liverpool and Birmingham Railway – that joint-stock banks began to make inroads into Lancashire. Joseph Macardy, a renowned Manchester stockbroker of Irish origin, alone superintended the establishment of at least three Manchester-based joint-stock banks: the Bank of Manchester (est. 1828), the Manchester and Liverpool District Bank (est. 1829), and the Northern and Central Bank of England (est. 1834) – all of which had a mixed record of performance (see chapters 4 and 5). The Union Bank of Manchester (est. 1836) stood out as one of the most well-managed companies amidst recurring bank failures in the town. A prominent and influential player in Liverpool was the Bank of Liverpool (est. 1831), established under the encouragement of an English merchant and banker named Sir William Brown of the Liberal Party, who also founded the banking house of Brown, Shipley & Co. in 1810. A smaller but somewhat stable institution was the Liverpool Commercial Banking Co. (est. 1832), promoted by Christopher Rawson, who was connected to the prominent Halifax banking family that drove the establishment of the Halifax & Huddersfield Union Banking Co. (est. 1836). A little further away from Manchester and Liverpool, the Lancaster Banking Co. (est. 1826) was one of the earliest joint-stock banks formed in the county under the guidance of Thomas Joplin, an English banker and ardent promoter of joint-stock banking. Known for its prudence, the bank successfully navigated through the twists and trials of the nineteenth century (Crick & Wadsworth, 1936; Orbell, 2001). As joint-stock banks grew more popular in the region, there were many similar institutions – great or small alike – that it was virtually impossible to name them one by one.

Preston was another Lancashire town notable for its remarkable development because of its economic ties with the cotton industry since the late eighteenth century. To quote Crick and Wadsworth (1936, p. 146), the manufacture of cotton "rapidly brought Preston to the position of third town" in the county. Between 1810 and 1830, the town's transport networks progressively improved, and its recorded population doubled from 36,000 to 72,000. Preston had no joint-stock banks of its own, and was served by a branch opened by the Manchester and Liverpool District Bank – alongside a stable private bank named Lawe, Roskell, Arrowsmith & Co. (est. 1835), which also had branches at Omskirk and Southport (Crick & Wadsworth, 1936). In 1837, having incurred a heavy loss the District Bank cut back on its branch operations, causing Preston to suffer disruptions in credit facilities. Joint-stock banks were slow to catch on at first, until the Preston Banking Co.

was formed in April 1844 to accommodate the growing trade and industry in the neighbourhood (see chapter 7). In May 1857, the vulnerability inherent in private banking became ostensibly manifest when Robert Lawe, the sole proprietor of Lawe & Co. died unexpectedly, leaving no legal arrangements to carry on the bank. Four months later, the Preston Bank filled the gap and opened branches in Omskirk and Southport in the premises formerly occupied by Lawe & Co. – following which the idea of having a local joint-stock bank bode increasingly well for the community (Crick & Wadsworth, 1936).

1.4 The Thesis: Structures, Subjects, and Synthesis

The thesis is organised into eight distinct chapters. The next chapter draws together four streams of literature, composing of a blend of historical and contemporary management scholarship, and provides a critical review of their relevance to the study: (1) the conceptualisation of trust and trustworthiness as moulded and motivated by social controls and cooperation; (2) the ethical and professional underpinnings of banking companies in connection to extra-legal and legal controls; (3) corporate governance, accountability, and power relations as embodied in the joint-stock economy, and (4) shareholder rights and liabilities as enshrined in the wider culture of shareholding and industrial capitalism. This chapter also presents a case for using these strands of literature to reconstruct a holistic social and cultural context, in which the dynamics of human actions and social processes involved in organisational failures and trust repair efforts could be mapped out and analysed.

Chapter 3 presents the methodology, theoretical and conceptual framework applied in the thesis. It shows the value of combining the cultural narrative approach and comparative case study method to produce an in-depth narrative account of different bank failures or suspensions, and the trust repair process which followed. The chapter also evaluates the consistency between this approach with Hayek's (1960) perspective of individuals as characteristically interdependent because of the constraints posed by limited knowledge, thus providing the necessary motivation for social cooperation sustained by the willingness to trust and the desire to behave trustworthily. The chapter then evaluates the usefulness of the organisational trust repair model developed by Gillespie and Dietz (2009), in conjunction with the richness of information afforded by different historical sources to this study.

Chapters 4 – 7 provide detailed case studies, covering seven joint-stock banks from nineteenth-century Lancashire which experienced difficulties between the 1830s and 1860s – namely, the Northern and Central Bank of England (est. 1834); the Manchester and Liverpool District Bank (est. 1829); the Bank of Manchester (est. 1828); the Royal Bank of Liverpool (est. 1836); the Liverpool Borough Bank (est. 1836); the Consolidated Bank (est. 1863), and the Preston Banking Company (est. 1844). These chapters delve into different trust repair strategies by which some banking companies successfully repaired trust and regained public confidence – and why some failed to do so and were forced to close for good. By covering an extended period of the century, the chapter seeks to identify possible continuities behind the pattern of bank failures and trust repair strategies as dictated by evolving circumstances and constraints.

Chapter 8 develops the connection between contemporary management theories and historical sources, providing an overarching view of how effectively Victorian joint-stock banks restored trust by reforming organisational systems or components from which the signals of trustworthiness emanated. By bridging both disciplines, this chapter evaluates (1) the usefulness and appropriateness of modern theories in explaining the intricacies behind trust failures and repairs in nineteenth-century banking, and (2) the (new) lessons and perspectives which history has to offer to modern bankers and financiers in approaching the relationship with different stakeholders as business models and regulatory environment evolve. In so doing, the thesis presents the differences – especially in terms of scope and scale of operation – between the Victorian age and twenty-first century. It also shows some striking similarities in both eras, in which banking is fundamentally anchored upon trust, risks, and social cooperation because of some unique characteristics which underpin the industry.

Chapter 2
The History of Joint-Stock Banks: A Literature Survey

2.1 Creating, Sustaining and Stabilising Trust

The approach to the study of banking performance and growth undertaken by contemporary economists has been predominantly guided by neo-classical economic assumptions centred upon the criteria of efficiency, profitability, and competition. This thesis follows a different path by looking into the historical context in which nineteenth-century British banks were socialised by interpersonal connections and communal expectation into becoming profitable and reputable business entities. In their formative years, joint-stock banks faced the challenge of vindicating their trustworthiness and reputability before they could successfully expand their ventures. Even with the passage of the Banking Co-partnership Act of 1826 paving the way for the formation of joint-stock banks, members of public remained sceptical if the new form of banking would in any wise be more stable than the old (Barnes & Newton, 2016). Propelled by radical economic transformation, banking organisations moved away from traditional and primitive structures toward larger networks composing of different parties with diverse agenda and interests (Lewicki & Bunker, 1996). Against the rising tide of public distrust and scepticism, new banks were compelled to respond quickly to changes in the marketplace, harnessing communication and problem-solving across functional responsibilities and organisational boundaries, which were critical for the maintenance and stability of business networks (Lewicki & Bunker, 1996).

There are several perspectives for viewing how trust is developed, maintained, and restored across business networks. First, in relatively simple and primitive societies in which social networks are bounded by family ties, kinship relations or religions, the shared morals, values and identities provide the necessary internal controls to govern members' behaviour. Relationships are reinforced via the "iterative development of trust, reciprocity and mutuality", promoting "a relational closeness similar to the idea of an

extended family" (Fincham & Burton, 2021; see Cookson, 1997). This thesis nonetheless maintains that as "more complex and socially diverse environments of large organisations" emerge (Kramer et al., 1996, p. 358), informal and interpersonal systems that once nurtured trust and cooperation in relatively confined and homogenous society gradually cease to be relevant. Second, a successful network critically relies on the willingness of members to engage in cooperative behaviour for the realisation of collective aims (Organ, 1988). Trust plays a prominent role here, in which case individuals would only cooperate when they believe that their trust would be reciprocally honoured by other members (Kramer, 1991; Messick et al., 1983). As explored by numerous past studies, against a backdrop of "low trust dynamics" early joint-stock banks deployed different strategies to initiate and maintain long-term cooperation with the community, transforming business relationships and economic institutions at the local or regional level. Third, this thesis looks at the challenges associated with relationship management in times of crisis. Given the exposure of Victorian banking establishments to runs and rumours, public trust and confidence were vulnerable to external disruptions, and as such have to be actively managed, and the approaches to doing so were essentially conditioned by changing contexts and circumstances.

2.1.1 Trust, Networks, and Social Controls

Long before legal benchmarks and incorporation were commonly available to guide business conduct in eighteenth-century Britain, informal social networks were crucial to ensuring commercial success "by reducing transaction costs, providing access to capital, and offering opportunities to gain intelligence and information" (Fincham & Burton, 2021). The legitimacy of one's business conduct was often assessed in terms of informal and subjective references, such as personal virtues, reputation, respectability, and wealth. Casson's (1995) study that sees entrepreneurship as a product of the cultural context in which it is positioned, is particularly useful for analysing the role of a generalised moral system and social conventions in mitigating opportunism, free-riding, and fraud. In a different study, Casson (2006) maintains that forming networks with members within closer circles of family, kinship, or friendship helps construct the common moral denominator and bolster business connections – all of which are necessary for reinforcing personal loyalties before further business expansions could materialise. A few studies (for example, Prior & Kirby, 1993; Walvin, 1997) on the success of Quakers' business

ventures largely support Casson's fundamental propositions that business interests were primarily secured through interpersonal relationship with members who shared a somewhat homogenous body of belief and spiritual values. Using social network analysis, Fincham and Burton (2021) demonstrated how the "multiplexity and density" of interpersonal connections, cemented by strict compliance (i.e. discipline) with the shared theology and moral expectations among the Quakers, functioned as "a proxy for trust and integrity" that reduced the need for repeated iterative engagements to nurture trust.

Nevertheless, the above studies underplay the importance of external changes in altering the character and perimeter by which the network of a particular community is defined. Changes in the composition of stakeholders, the blurring distinction between lawful risk-taking and reckless speculation, the relative decline in Christianity as a central moral denominator, and the rise of professionalism towards the latter part of the nineteenth century, for instance, had significant – and some irreversible – consequences on the way in which members of public assessed the legitimacy of business organisations. Another limitation of Casson's finding – as revealed in its rather narrow focus on the importance of kinship, friendship, or religious affinity in fostering trust – is remedied by the study of Pearson and Richardson (2001, p. 659), which sees business networks as possibly composing of individuals "from a number of partnerships, partially interlocked in a variety of ways, but all coming together in a single collective enterprise". Relatedly, Balliet and Van Lange (2013, p. 1090) assert that trust "permeates the range of possible social relationships", serving to stabilise and harness social networks through the inculcation of norms that harness cooperation and facilitates the recruitment of new members (see also Fukuyama, 1995; Putnam, 1995). As this thesis sees it, with the growth of the joint-stock economy eclipsing home-based or small-scale enterprises, social interdependence became a considerable issue as business networks grew in breadth and depth.

The insight offered by Pearson and Richardson (2001) is instrumental for analysing the key strategies employed by early British joint-stock banks to appeal to the trust and support of local communities. Newton's (2010) study shows that bank directors, managers, shareholders, and customers were mostly recruited from identical or neighbouring districts, after careful screening for their social respectability and financial standing. Importantly, given the asymmetry in organisational relationships as conditioned by imperfect information, identifying a good partner could mitigate the abuse and exploitation of trust (Dekker, 2004). A restricted range of selection was logical for a few

pragmatic reasons – some of which have been rightly theorised by Casson (2006). First, the relative ease to obtain local information meant banking organisations could reduce costs associated with appraising investment decisions and market competition. Second, the fact that market participants were selected and screened based on the local criteria also helps reduce transaction costs incurred by the need for enforcing contracts, monitoring moral hazards, and mitigating opportunism. Third, admitting only respectable candidates also improved the chances of establishing local reputation successfully (Barnes & Newton, 2016).

One of the main focuses of this thesis is to explore how far Victorian banking was governed by relational trust, in which cooperation can be characterised as "stable, long-standing and buttressed, very often, by social relationships" (Mayer, 1976, p. 248). Barbalet (2009, p. 371) usefully observes that relational trust is built upon "a sense of personal reliance and security" between individuals. Popp et al. (2006, cited in Fincham & Burton, 2021) rightly conceives networks as a "relational structure that sits between organisations and industries", serving to contain transaction costs, disseminate market information, and provide access to social contacts and capital. While the structure of networks could be established upon high-trust between individuals bound by kinship and friendship, this thesis extends the network analysis advanced by Fincham and Burton (2021) to provide deeper insight into different business relationships between divergent entities with diverse interests, and how they grow "across time and space". Moreover, social networks built on close relationships and trust act as a form of relational governance, deterring opportunistic behaviour and improving coordination among market participants (Popp et al., 2006; Toms & Filatotchev, 2004). The relational property and social interdependence which characterise social networks also function as a basis for "communicative rationality", facilitating the learning processes that further cement and consolidate social relationships (Boyce, 2003).

The discussion thus far clearly shows that human agents are conditioned by their respective experiences, expectations, and encounter of social norms and values (Yeager, 2011). As an integral part of the wider networks, the behaviour and development of business entities are exposed to the cultural and socio-institutional influences at various levels (Schumpeter, 1950). Marshall (1890) recognises the role of public opinions – as informed by social beliefs and conventions – in shaping and checking business behaviour and practices. These fundamental tenets are broadly consistent with the study of Barnes and Newton (2016) that without a rigorous legislative framework for banking, business

decisions were primarily informed by local norms and conventions, under which violations were likely to result in punitive exclusion from the community. Implicit codes of conduct and expected behaviour were subtly woven into (written) organisational rules. A recent study by Hollow (2022, p. 1348) also applies a "more institutionally-oriented perspective", recognising the potential influence posed by of institutional conventions and controls over individual beliefs and behaviour. According to Johnson (2010), looking at business organisations in connection to the wider institutional context in this way could lead to a reappraisal of the role played by politics, legislation, society, and culture in creating a framework that governs economic exchanges. In so doing, this research follows the perspective that the characters and practices of business organisations are inculcated and nurtured through learning and observation of the values and attributes of the community in which they are positioned (MacIntyre, 1984). The main challenge of this thesis lies in the interpretation of social conventions and compilation of evidence, which are by nature time- and context-specific (Barnes & Newton, 2016). This requires mapping out the changes in banking behaviour and practices – both within a broader institutional context and over a sufficiently extended period of time.

2.1.2 Risk-Taking, Trust Conceptualisation, and Social Cooperation

Market transactions inevitably involve the risks of opportunistic behaviour and sub-optimal performance (Das & Teng, 2001), which in turn call for risk management and appropriate controls (MacCrimmon & Wehrung, 1990). Trust, given its importance as a lubrication that makes it possible for organisations to function, deals with the underlying control problems and risk management in organisational relationships (Simmel, 1990; Tomkins, 2001). Nonetheless, the fact that trust could be abused or misplaced also makes it a risky engagement (Luhmann, 1979) – and yet it is a necessary and unavoidable risk if a cooperative relationship is to be established. In relation to this statement, Haggerty (2012, p. 236) argues that trust, reputation, and risk-taking are mutually reinforcing:

> It was not possible to take risks without some level of trust; some aspects of trust were reliant on a good reputation, which was in turn dependent on fulfilling obligations. All these elements were both dependent on, and played out in, the networks of which these men were all a part.

By holding an expectation that the other party "will behave in a mutually acceptable manner" and that "neither party will explore the other's vulnerability" (Sako, 2006, p. 268), adverse outcomes arising from opportunistic behaviour could be contained. Trust, once initiated, could be cemented through iterative business transactions, thus laying the foundation for virtuous and long-term cooperation.

The origin of trust has been a widely debated subject. Axelrod's (1984) is somewhat optimistic that trust could be conscientiously created – provided that all parties perceptively recognise the benefits of long-term cooperation. Granovetter (1985), meanwhile, views the formation of trust as critically depending on the sharing of common cultural traits or social values by the transacting parties. In fact, both positions are impregnated with defeatism in different ways, and are viewed by Sako (2006, p. 268) as of little value for "thinking about how to create trust when there is none". The former rules out the possibilities of trust, if both parties were not farsighted enough, or if antagonism is sufficiently strong to exclude cooperation. The latter, meanwhile, implies that in low-trust communities trust-building is condemned to failure from the start. According to Schilke et al. (2021, p. 244), the precondition for trust is that the trustor must have reasons to believe that the trustee would be "motivated not to behave opportunistically and to instead honour that trust", and the trustee must in turn be incentivised to preserve the relationship by behaving acceptably. Building on this notion, this thesis recognises the inevitability of social cooperation, given that individuals which make up the network of social interactions and market exchanges are mutually interdependent. One who desires to achieve his means by entering into cooperative relationships with others must be willing to trust, and to become trustworthy.

The key challenge is how to establish social cooperation in a context of "low-trust dynamics", when the performance of many of the new joint-stock banks proved disappointing. To quote Pressnell (1956, p. 509), these institutions seemed to demonstrate that "a bank with a larger capital simply did more widespread damage than a badly run bank of the old type". Barnes and Newton (2016) offer an interesting insight that under a "low-trust" condition, it made good strategic sense for early joint-stock banks to project a strong local identity and serve the community's economic interests. For smaller local banks, in particular, the expansion of business networks beyond the existing boundary was mostly preceded by successful local establishments (Newton, 2010). Schilke's (2021, p. 245) work offers three sources of information from which trustors form their judgement as to the partner's trustworthiness. First, *past interactions* signal the trustee's likely

behaviour in the given situation (Blau, 1964; Larson, 1992). Second, *future interactions* provide a "forward-thinking assessment" of how much the trustee is likely to value and maintain the relationship, and thus the tendency to behave trustworthily. Third, the *broader network* in which all transacting parties are situated are particularly useful when past and future interactions are lacking to make informed inferences about the partner's trustworthiness. "From a network perspective", as Schilke et al. (2021, p. 245) reasons, "trust can be the result of reputational concerns and can flow through indirect connections linking actors to one another" (see also Coleman, 1990; McEvily et al., 2020).

Given that a bilateral relationship is embedded in particular sets of socio-economic denominators and legal-political attributes (Sako, 2006), this thesis looks into the dynamics of trust and distrust in the event of organisational failures, and how social cooperation was restored between banking companies and stakeholders. For instance, how was trust conceptualised, articulated, and comprehended differently at the interpersonal, organisational, and institutional levels? How did the challenges and processes of trust repair vary across different contexts? In what ways, and to what extent, was the choice of strategies for creating and sustaining trust conditioned by different circumstances? How did banking firms reconcile competing expectations from different stakeholder groups? In connection to these questions, the following studies – which associate trust with one's success in inspiring confidence and projecting reliability – are useful for forming the trajectory of trust repair efforts. Morgan and Hunt (1994), for example, underline the importance of creating and maintaining trust as part of effective crisis communication. The corporate social performance theory goes further by suggesting that an organisation is morally obliged to exercise integrity and equity when dealing with stakeholders' interests (Phillips, 1997). Given that these merits are vital for enhancing long-term cooperation, this thesis does not merely focus on the immediate importance of trust in alleviating organisational crises, but also its potential in transforming "trade-based relationships" into new modes of "multilateral commercial arrangements" through the promotion of local and regional economic development (Pearson & Richardson, 2001, p. 659).

2.1.3 Trust Failures: The Tact of Relationship Management

In relation to the importance of trust in dealing with strained organisational relationships, Schilke et al. (2021, p. 246) aptly remarks that trust is "most relevant in situations when

uncertainty is high" – and yet "it is in exactly those situations that trust is most difficult to produce". Networks, trust, and reputation are susceptible to external changes (Haggerty, 2012). Economic crises, scandals or rumours, for instance, are among the most destructive forces that could shatter a firm's reputation for probity and competence. Negative expectations are typically associated with distrust, rooted in uncertainties about how and whether counterparts would honour their commitments in the future (Rad, 2017; see Lindernberg, 2000; Möllering, 2005). The legitimacy of negative expectations is confirmed when third parties, who function outside the immediate circles of the involved parties, recognise instances of distrust (Rad, 2017; Lindenberg, 2000). In consideration of various destabilising forces, Downs (2017, p. 513) outlines several important implications on the analysis of business behaviour in a volatile economic climate. First, effective networks are conditional upon tactful management of interactions and relationships, "rather than an individual managing the network as an entity in itself". Second, the power of information could drastically alter trust dynamics in a network, clearly showing "the complex and continually adapting nature of business and social interactions". Accordingly, effective relationship management is vital for promoting one's reputation, extending market search, mitigating risk, and using insider information to develop new opportunities.

According to Bülbül (2012, p. 237), in banking relationship management is particularly delicate because of the interlinkages between banks and the wider network of divergent stakeholders, in which case destabilisation could leave profound implications upon the rest of the socio-economy. First, banking transactions typically involve huge amounts of money – which is not necessarily "material money" but that which carries with it "elements of credit", and is therefore a critical matter of trust (see Simmel, 1990). Second, defaults by any counterparty could disrupt the chain of transactions, triggering more losses to other parties and institutions through higher funding costs and liquidity shocks (Craig et al., 2015; King, 2008). Given the sharpening of competing claims over limited resources during crisis, the importance of collaboration to identify alternatives that equitably address the needs of all conflicting parties cannot be overemphasised (Thomas, 1979). In the light of this remark, this thesis explores how the stability and resilience of business relationships determine how well a Victorian bank could survive and recover from a crisis (see Stevenson et al., 2014; Zafari et al., 2020). More specifically, it analyses how banks cooperated with different stakeholders to identify and reduce threats, minimising business disruptions through continual flows of resources which were

critical for organisational survival (Zafari et al., 2020). Using the work of Håkansson et al. (2009), this thesis also shows that the degree of interdependency, trust, commitment, and communication on one hand, and the extent of the use of control, coercive power, and distance on the other, conditioned the success of relationship management (see also Zafari et al. 2020).

Thus far it is clear that a critical aspect of relationship management unique to the banking industry is that a crisis could be notoriously contagious, implying that a healthy institution is not exclusively immune from the catastrophes suffered by its counterparts. More than often market hearsays amplify the scale of distrust and panics – so much so "rumour about such bank runs trigger additional runs elsewhere" (Greve & Kim, 2014, p. 204). Interestingly, Coast and Fox (2015, p. 226) see the interpretation of rumours as useful for addressing questions about "human behaviour and interaction, power, agency, community formation, government stability, mentalities and emotions … in particular historical contexts and environments". Why did some banks collapse and others survive? Did rumours originate from the ordinary people or another competing establishment? How far did rumours reflect the collective concern of the community, or were they mere malicious, unverified information circulated by ill-intentioned parties? In the light of these rhetorical questions, it is apparent that to restore trust, effective management of negative publicity and communication are salient leadership qualities (Kirkpatrick & Locke, 1991). According to Mishra (1996, p. 278), effective crisis management depends on "open communication channels among hierarchical levels and across divisional units", paving the way for "honest and complete information" to defuse damages caused by rumours and speed up the deployment of resources to deal with the problem.

Rad (2017, pp. 6-7) distinguishes between the respective usefulness of institutional trust and relational trust in stabilising organisational relationships during a crisis. As opposed to institutional trust (e.g. rules, regulations, and legislation) embedded with a pre-contractual role and structures which enhance predictability and order based on "procedural fairness", relational trust is based on "a sense of mutual reliance and security between people". This distinction, in turn, implies that relationship management can be demonstrated either through the display of interpersonal commitment and accountability, or formal corporate policies and procedures. As Sitkin and Roth (2006, p. 303) observe, bureaucratised and legalistic techniques are effective in "ameliorating context-specific reliability problems" but less so in dealing with "generalised value incongruence" beyond the immediate situation. Relatedly, Hollow (2014, p. 176) also points out that internal

checks and state regulations could only deal with fraud opportunities but not the associated motivations and rationalisations, which have more to do with "the complex and potentially uncomfortable personal and ideological factors". Moreover, because legalistic remedies are formal and faceless, they tend to aggravate distrust by "increasing perceived interpersonal distance" (Sitkin & Roth, 2006, p. 303). This thesis assesses the rationale of different approaches to restoring trust, comparing the relative effectiveness of legalistic measures and interpersonal appeals as Victorian bankers sought to regain confidence. In addition, this thesis contends that relational trust had seemingly a larger role in the context of crisis because of the underlying shortfalls of institutional structures which were supposed to facilitate the joint-stock economy. Relational trust, in this context, was vital for encouraging interdependent individuals and groups to overcome their fear and recognise the need for mutual collaboration in the face of conflicts (Gibb & Gibb, 1969; Mishra, 1996).

2.2 Moral Persuasion, Professional Induction, and Official Regulation

Unsurprisingly, to this day banking has been heavily criticised for its misconduct and moral failings. In relation to nineteenth-century bank failures, *The Economist* (1857) commented that "in nine cases out of ten the directors have abused their trust, and have made the money of the shareholders and depositors subservient only to their own uses". On the Victorian stage "the banker was the stereotypical villain of melodrama – the foreclosure of mortgages, the despoiler of widows and orphans" (Robb, 1992, p. 57). Despite Bagehot's (1873, pp. 124-5) sanguine outlook that there were no shortages of "grave, careful, and experienced men" qualified to conduct "a great bank in London", scandals were rampant enough in the mid-century that they could scarcely be treated as sporadic events but "a failing system which needed to be fixed" (Taylor, 2013a, p. 109). Legal controls were lax and inadequate, giving rise to stern public criticisms that unbridled capitalism had begotten a banking and financial system cankered with greed, indifference, and consequently a heightened sense of distrust and hostility that disrupted the market order. Well into the twenty-first century, the complaint remains that banking behaviour has not improved in spite of hefty financial penalties – to the point that Shafik (2016, p. 2) labels the underlying problem as an "ethical drift", in which misconduct was "not a case of a few bad apples, but something was rotten in the entire barrel".

This section reviews a collection of past studies which presents how different regulatory apparatuses held Victorian banking institutions in check. To argue that banking was poorly regulated simply because lawmakers wilfully clung to the belief of classical economics that users and investors should be and were capable of looking after their own interests – is to ignore or oversimplify the density of trust dynamics emerging from different regulatory regimes. Carney (2021, p. 205), for example, sees the necessity for combining "public regulation with private standards" to arrive at a "more comprehensive, lasting solution". As shown in the Victorian studies, the moral constitution and reputational sanctions embodied in the society worked alongside professionalisation and state-led enforcement, out of which a spontaneous and organic system of banking regulations gradually emerged. This all-inclusive and pluralistic approach recognises the co-existence of different forms of formal and informal controls, "coalescing in concert" to produce more comprehensive and effective regulations (McGrath & Walker, 2023, p. 792; see Braithwaite, 2017). A trajectory toward moralising and professionalising the banking sector also shifted the regulatory focus away from the state (see Black, 2001), who undertook core regulatory functions, prescribing rules and punishing misconduct using criminal and civil sanctions when necessary (see Black, 2015). With banking organisations improving and implementing internal controls without having to resort to explicit rules and guidance from the government (Grabosky, 2017; Scott, 2004), one of the key arguments of this thesis is that throughout the process both the state and a host of different private participants – perhaps unknowingly – entered into a constant discursive process to negotiate and redefine the border between acceptable and illicit banking practices.

2.2.1 Banking, Reputation, and Moral Probity

In the early Victorian age during which the company law was somewhat embryonic to govern the joint-stock economy, as guided by the principles of liberal individualism, market participants provided the checks and balances necessary for the preservation of public morality in the banking industry (see Alborn, 1995, p. 205). Directorial integrity and competence were in fact "the most direct safeguard" available to stakeholders (Johnson, 2010, p. 205). Given their subjectivity, Robb (1992) argues that these attributes were problematic to measure and track over time, leading to vague articulation of ethical boundaries and codes of conduct. Johnson (2010, p. 227) similarly argues that it appeared

increasingly difficult "to distinguish between honest and disreputable behaviour, and to hold those responsible for dishonesty to account". Even so, in the nineteenth century moral and reputational sanctions were powerful tools in checking bankers' behaviour. It was not uncommon that even the once respected figures could "fall from grace" and be ousted from the respectable circles because of their misconduct (Wilson, 2006, p. 1088). This sub-section first reviews different sources of extra-legal mechanisms in guiding bankers' behaviour and restoring market discipline. It then goes on to consider how the affiliation between financial journalism and novelistic accounts constituted the basis and dynamics of reputational sanctions within the joint-stock economy (see Poovey, 2002 and Taylor, 2013b). More importantly, this sub-section focuses on the "regulatory power" rooted in the press, given its vital contribution in exposing the internal working of the joint-stock corporations to public gaze (Taylor, 2013b, p. 682; see also Taylor, 2012).

According to Garnett (1998, p. 123), "a self-conscious cultivation of a collective ethos – a culture within which common values could be assumed as well as a common moral commitment to engage actively with the problems presented by modern economic life", was critical for recovering the moral order in the Victorian business world. A collation of past studies suggests that there are at least three categories of extra-legal forces that shaped banking conduct in the early nineteenth century. The first originated from the influence of Christian worldview over British thought and culture. Hilton (1991), for instance, highlights the significance of evangelical ethos in framing business ethics and morality in those years. Garnett (1998, p. 122) observes that the Victorian system of commerce was fundamentally sustained by "certain basic ethic assumptions and conventions of trust which were themselves in large part religious in origin". Second, Victorian novelists such as Charles Dickens and William Thackeray also played a part in propagating the ethical principles in the life of commerce and industry. By sending bankers "a message of domestic reconciliation" (Alborn, 1995, p. 211), they sought to temper "capitalist excesses" with the moral rectitude of domestic values. To the Victorian middle-class, capitalism was acceptable only if certain aspects of human life were insulated from the excesses of materialism (Searle, 1998, p. 166). Lastly, as the century advanced, the press was more than a defender of capitalism as "a law-governed, natural, and – pre-eminently – safe sector of modern society" (Poovey, 2002, pp. 22-3), increasingly took on a more assertive role in policing the workings of financial institutions. Taylor (2013b, p. 682) builds on this premise and argues that by warning

readers of financial scams and exposing corporate scandals, financial journalists were "a key reputation intermediary" in the industry.

Taylor's (2013b) analysis of the power of nineteenth-century newspapers in influencing corporate reputation is particularly useful for understanding how closely the banking scandals had become intertwined with the moral order of the joint-stock economy. Smail's (2005) work shows that a reputation for moral probity was crucial for commercial success, as credit networks grew increasingly intricate in the eighteenth century. Using the scandal of the Royal British Bank, Taylor (2013b, p. 234) shows the intense moral feelings among members of public when the plight and suffering of the victims were "sympathetically conveyed by the press". Fictional accounts, which Johnson (2010, pp. 212-3) sees as depicting "something of the inner workings of financial institutions", also served to "demystify that which was remote and arcane, and largely exonerated these institutions of any fundamental flaw by focusing on the personal traits and moral failings of the key characters". Similarly, according to Taylor (2005, p. 239), the parallel drawn between facts and fictions shows "part of the mental furniture of the Victorian imagination", as public sought to understand the notoriety of real-life fraudsters "through the prism of the novels and plays". Once the banker's behaviour was alluded to the "fictional rogues", the perpetrator's reputation was beyond recovery (p. 240). Such sense-making process underlined the guiding ethical principles to which bankers were expected to conform. Thinking about the "generic affiliation" between financial journalism and fictional writings is helpful for establishing the "formal dimension of a relationship" that illustrates the moral order and reputational sanctions that governed joint-stock banking (see Poovey, 2002, p. 19).

Another somewhat different way for approaching the regulatory power of newspapers is looking at how they forced publicity on reluctant companies, fostering an atmosphere in which attempts by boards to enforce secrecy "could legitimately be portrayed as sinister and indefensible" (Taylor, 2013b, p. 684). This approach usefully illustrates the "constitutive relationship between disclosure and secrecy" that characterised Victorian banking, which will strongly feature in this study (see Poovey, 2002, p. 19). From the perspective of modern scholars, the study by Armour et al. (2017) indicates that reputational losses are frequently tied to the harms posed upon customers or investors, and prove more castigatory than financial penalties. This finding is supported by the claim of Karpoff (et al. 2014, p. 3) that negative publicity – from the instance at which a scandal is exposed, to the moment when investigation is completed and the verdict pronounced,

coupled with speculations, stigmatisations, and interim statements received from the ongoing inquiry – "can stretch over several years". As informed by the "stakes in conformity" literature, criticisms and disapproval from the community meant deviation from the norms could attract reputational damage and destroy attachments developed from interpersonal connections (Briar & Piliavin, 1965; Toby, 1957). This will be explored in greater details in the latter part of this chapter.

The distinction drawn by Alberto (2015) between a bank's corporate culture and organisational culture might prove useful for showing how early Victorian banks responded to public criticisms and reputational concerns by negotiating a fine line between publicity and secrecy. Corporate culture represents how the bank should *ideally* serve stakeholders' interests; organisational culture depicts how this is demonstrated *in practice*. This distinction, when discussed in the light of the supposed "virtues of publicity" and "vices of secrecy", unlocks several questions for further study. For example, how did the role of newspapers as a reputation intermediary condition the bank's corporate and organisational culture? How did bank leadership respond to the pressure for publicity and demonstrate commitment to stakeholders when organisational reputation had suffered? To what extent could reputational concerns and the inspiration of the press media "to educate and encourage rationale debate" improve bank leadership and internal governance (see Taylor, 2013b, p. 699)? Given its role in "disseminating opinion and information on the companies that competed for the public's capital" (Taylor, 2013b, p. 701; see also Taylor, 2012), this thesis argues that the press media could (partly) compensate for inadequacies in the company law. It also shows that while some banks survived the scandals of their own making, promptly moving forward and "away from reputational harms", for some others the process was prolonged and arduous, impeded by "additional reputational and financial complications" because of the prevailing "corporate specifics as well as economic timing" (see Welch, 2023, p. 249).

2.2.2 The Rise of Banking Professionalism

As joint-stock banking began to take off in the 1830s, "banking profession" was "little more than a loose collection of managers and journalists", who struggled to identify and establish the ethical and administrative criteria among "a decidedly mixed crowd of financiers" (Alborn, 1995, p. 200). Even specialised publications – such as *the Bankers' Magazine* – found it difficult to strike a balance between "enforcing uniform practice"

and “cajoling hesitant merchants and manufacturers” to take up bank shares and interest-bearing accounts. “For those who joined deputations, attended professional meetings, or wrote for trade journals”, as Alborn (1998, p. 200) observes, “banking was a collective enterprise, and they consequently needed to take seriously the problem of members who ignored the still-informal rules of the group”. Among others, the scandal of the Royal British Bank in 1856 offered a classic example from which many economists tried to deduce “a suitably scientific lesson” while dismissing such failures as “exceptional occurrences” (p. 210). With the rise of professionalism in the 1870s, bankers began to distance themselves from the moral premises subsumed in classical economics that stressed on individual responsibility. This sub-section first uses contemporary literature to review how far quasi-laws and codes of behaviour prescribed by professional bodies could satisfactorily allay public distrust. It then presents a case for contextualising the emergence of banking professionalism, and how it altered the industry’s informational structure for the mitigation of unpredictability and risks arising from members’ behaviour.

In the view of Swift (2001), the recourse to legalistic or external controls may emerge from the supposition that organisational leadership cannot be relied upon to provide adequate information. Jennings (1991) likewise maintains that professional ethics require decision-makers both to discharge their duties competently, and to have the motivation to do so. With the City of Glasgow Bank failure topping the list of financial scandals in 1878, banking leaders recognised the need for providing an established “internal regulations and standards governing a given occupation” to improve business management and performance (Robb, 1992, p. 177). The Institute of Bankers, for instance, was formed to streamline the codes of conduct, thus providing members of public with a general benchmark to make informed judgement about the legitimacy of bankers’ behaviour. Certification by the Institute was therefore instrumental for banking firms to improve their image as professional and trustworthy establishments. Alborn (1995, p. 201) notes that the entrenched economic power of banks had combined with professional maturation to produce “new discursive resources that had previously been unavailable to their efforts to contain the disruptive public echoes of bank failures”. Contemporary scholars, such as Cook et al. (2021, p. 59), are optimistic that professionalisation could cultivate industry-wide norms that “shape individual choice and action, within an organisation, in an endless feedback loop that includes both ‘tone from the top’ as well as ‘echo from the bottom’”. According to Ellemers (2012), professionalisation provides individuals a gallery to

identify misconduct and assimilate positive behaviours on the job by discerning and interacting with their peers.

However, how far a "technically competent community" can reduce banking problems remains disputable (see Alborn, 1995, p. 204), with a few studies questioning the effectiveness of professionalism in nurturing healthy and responsible banking culture. To begin with, to the extent that the banking world was "alien and inscrutable to the general public", bankers could hijack professionalism for their own advantage and play up rule ambiguities to disguise unorthodox forms of frauds (Robb, 1992, p. 180). The proliferation of paper assets and new credit instruments unknown to ordinary users also bred new opportunities for market abuses. Next, given the sheer scale and complexity of banking, professional requirements may be embraced by companies but "not by groups of professional individuals and certainly not across the sector" (Smith et al., 2017, p. 436). In pursuits of risky propriety trading, perverse incentives rooted in the remuneration structure blunt the effectiveness of "governance through professionalism", making it difficult to purge the banking industry of unacceptable practices as a whole (p. 450). Third, as professional identities are increasingly framed around "logics of efficiency and commerce", the conventional "logics of ethics and public service" gradually fade into the background (Muzio et al., 2013, p. 700). The result is the steady loss of "ethical leadership and professionalism", which Alberto (2015, p. 134) recognises as indispensable to "a responsible banking model".

By highlighting the role of banking in advancing the economic interest of the community whose support was critical for the bank's long-term success and survival (Barnes & Newton, 2016), this thesis demonstrates the importance of ethical qualities in promoting a "higher sense of purpose" in the profession (McGrath & Walker, 2023, p. 800). Alberto's (2015) emphasis on the inseparability of banking professionalism from ethical leadership provides an important input for contextualising the interpretation of professional standards over time. Such standards are the results from the interplay of three vital sources – namely, (1) banking legislation; (2) the core values and guiding principles embraced by corporations, and (3) the prescribed codes of conduct by professional associations. This approach usefully considers how internal constraints (e.g. corporate culture and core values) intersperse with external controls (e.g. professional requirements and state regulations) to establish the behavioural standard. The challenge is that beliefs, values, codes, and regulations are subjective, "self-reporting", and presumably developed for the projection of "an idealised self" (Smith et al., 2017, p. 430). Given this notion,

were professional banking bodies sufficiently autonomous when defining standards and criteria? How far was public interest duly represented during the process? How did the emergence of professional bodies alter the power relations between banks and various groups of stakeholders? How, and to what extent, did professional ethics provide banking companies an interpretive frame for modifying corporate culture, common purpose, and shared valued? How did banks "try to give their activities a particular normative value beyond their technical requirements" (Smith et al, 2017, p. 429)?

The above questions coincide with Carney's (2021, p. 205) argument that wholesome professionalisation is one that aligns compensation with values, increases managerial accountability, and importantly, promotes a renewed "sense of vocation". McGrath and Walker (2023, p. 792) also observe the need for infusing professionalisation with a "pro-social identity, in which there is a recognition of broader obligations to society" that is independent of profit-incentive and the organisational hierarchy of individual firms (see also Grant & Berg, 2012). Professionalisation also enhances the sense that banking is "a community-based activity that serves society" (McGrath & Walker, 2023, p. 799) – and to a greater extent this notion carries stronger appeal to the Victorian context where (most) banking organisations were woven into the social fabric of the community. In this sense, Despotidou and Prastacos (2012, p. 453) fittingly point out the central quality of virtuous professionalisation as one that appreciates "the interconnection of people and views individuals as members of a larger community", who should endeavour "to bring out what is best in them to achieve common interest". In line with these beliefs, Thakor (2019, p. 83) similarly opines that the purpose of banking should be defined in terms of a "pro-social contribution" that links the industry's culture with "explicitly higher social purpose", which in turn should enhance public trust in banking corporations. As far as nineteenth-century banking is concerned, to repair trust successfully there must be renewed respect shown towards the broader social norms, because the economic power and privilege conceded to banking corporations were conditional upon their willingness to protect the community's interests and align their activities with its "normative expectations of conduct" (McGrath & Walker, 2023, p. 793; see Frankel, 1989).

2.2.3 The State of Indulgence?

At the dawn of the Victorian era, the primary purpose of legal intervention was to ensure the public had adequate access to accurate financial information – a principle in

congruence with the doctrine of classical economics that individuals were capable of making informed decisions and looking after their own interests. Insofar as individual responsibility formed an integral part of Victorian social life, non-interference of the state was morally defensible, on the ground that economic affairs were private matters best left to the discretion of affected parties. This section reassesses the validity of the oversimplified, Marxist argument that attributes the state's legal passivity to the attempt of the Victorian upper class to extend their political and economic power over the underprivileged. Such argument is untenable for two reasons. First, as the joint-stock economy continued to advance, aided by the influence and publicity of the press media there was no attempt to "shy away from exposing respected businessmen" who partook in heinous financial crimes that jeopardised the livelihood of a "very great multitude" (Wilson, 2006, p. 1087). Second, legal passivity was more likely the result of the slowness of legislation to "keep abreast" of the financial innovations germinating from rise of joint-stock corporations, creating opportunities for "new types of crimes" while making the old less detectable (Wilson, 2006, p. 1088).

A few studies apply a somewhat Marxist perspective to explain the state's legal inaction, suggesting that the criminal system had been hijacked by the upper class to perpetuate their economic interests and power. Sutherland (1940, p. 7) believes that "white-collar criminals are relatively immune because of the class bias of the courts", with the elites or ruling few dictating the terms of legal implementation and administration. Robb (1992, p. 147) maintains that the Victorians were inclined to attribute criminal behaviour to the impoverished "dangerous classes" but treat financial misconduct of the upper echelon as "a relatively minor social ill". For Cottrell (1980), vested interests of parliamentarians explained why the state and the law were oblivious to bad commercial behaviour. Gatrell (1990) observes that criminal prosecutions fell disproportionately upon low-rank employees but failed to reach fraudulent managers or directors. Lobban (1996) also criticises the criminal sanctions as unduly lenient in punishing key corporate figures. Turner (2014) refers to the cosy alliance between banking and politics: namely, how strongly banking elites could influence and lobby lawmakers in the process of drawing up legislation by forming powerful, well-organised interest groups.

The above studies may have overplayed the class factors, failing to explain why frauds – which were arguably tolerated at first – were subsequently pounded with more concerted and severe punishments by the mid-nineteenth century. Following the

endemicity of financial scandals, the Punishment of Frauds Act was passed in 1857 to make larceny and embezzlement, falsification of company books, and financial misrepresentation officially punishable by penal servitude. Wilson (2006, p. 1079) points out that the criminal court gradually became the "public space" for "deliberating degrees of unacceptability and unlawfulness" in corporate misconduct. With criminal trials proceeding to reinforce "the entire system of trust" based on reputation, respectability, and esteem (p. 1079), there were notable cases where "even the most respected could be reduced to the position of 'common felons' through their professional (mis)conduct" (p. 1087). Over time, with legal cases being treated and sentences applied more consistently by the judges, behavioural norms gradually took shape and became the guiding principles for the business community (Taylor, 2013a). The outcome of legal reforms echoes the belief of Hayek (1960, p. 195) that state intervention – when executed to uphold the rule of law, private property, and contracts – enabled individuals "to plan with a degree" by reducing human uncertainty as much as possible within the capitalist order.

The discussion thus far shows that discovering the meaning of so-called "white-collar crimes" – a term coined by Sutherland (1940) – was largely an experiential process. Taylor (2013a, p. 6), likewise, recognises the establishment of criminal law as a process "socially constructed, embodying particular values and interests in specific contexts". Robb (1992, p. 149) is quite right that Victorian legal reforms were reactive rather than radical, "responding piecemeal to new types of fraud to especially serious cases". Before an offence could be criminalised under statute books, there are questions as to "why certain activities are deemed criminal and not others and why at times and not others" (Zedner, 2004, p. 39). Legal procrastination was not necessarily the result of political deliberation as the class-bias argument is eager to underline. As Carney (2021, pp. 204-5) rightly asserts, "authorities will inevitably lag developments in fast-changing markets". Hayek (1960, p. 202) similarly remarks that institutional innovations are by nature experimental, "slow and gradual even after the essential conditions of a free system have been established", with the state and various parties taking part in an ongoing process of finding the best possible regulatory regime to cope with sweeping socio-economic transformation. Over the century, there was increasing pressure placed upon the criminal law to protrude into commercial dealings, giving rise to "perceptual appreciation" that business activities were "capable of amounting to criminal activity" – and even growing consensus that certain business behaviour "should be criminal" (Wilson, 2006, p. 1077).

This research considers the discursive narratives between the state, policy thinkers, banking companies, journalists, and the investing public as they recalibrated the boundary between lawful and unacceptable practices (see Djelic, 2013). Consider, for instance, how the suffering of the victims of the Royal British Bank scandal was circulated and placed in the public domain by the press, incensing members of public who demanded the letter of the law be "strained to the utmost" to enable a prosecution (*Observer*, 3 May 1857). In his *Facts, Failure, and Frauds*, prolific financial editor David Morier Evans (1859a, p. 5) commented that "unless the extravagant and pretentious habits of the age are brought within more restrained limits", the history of Britain would be one of "the decline and fall of mercantile morality throughout the civilised world". These debates implied a delicate balance between promoting healthy market innovations and wealth creation on one hand, and punishing dishonesty or abuses on the other (Wilson, 2006). This critical issue unpacks a few vital questions for further investigation. How did the state re-evaluate its moral locus in undertaking legal reforms amidst a changing market environment? How, and to what extent, could legislation supplement interpersonal engagements undertaken by corporate leaders to restore organisational trustworthiness? How, and to what extent, did banking companies (re)align their corporate culture, values, and practices with state regulations? These questions invoke interesting discourses about the "proper limits of private action, and thus the proper scope of action" (Wilson, 2014, p. 130), prompting further consideration of how far state coercion was better than individual actions in fostering trust and restoring market discipline.

2.3 The Little Republics: Democratic Rhetoric, Common Good and Corporate Autocracy

Advocates in nineteenth-century Britain were keen to point out that the constitutional restraints on directors and managers, along with checks and restrictions posed by organisational structures, could improve corporate accountability, business efficiency, and the appeal of joint-stock investment (Freeman et al., 2012). The term "little republics" was first coined by Robert Lowe (1811-92) to liken joint-stock companies to a representative democracy, an open and inclusive system within which the interests of all members in the society could be duly represented. As owners and capital contributors, shareholders actively took part in corporate governance and came together to discuss key strategic matters. However, the administrative pattern of joint-stock banks seemed to have

fallen short of the ideals of openness and direct representation they were supposed demonstrate. Progressively, governance became autocratic and evasive, with corporate power being increasingly concentrated in the hands of the executives and shareholders systematically excluded from the participatory politics of corporate affairs. Modern research on corporate governance claims that democratic deficit leads to a loss of social acceptance and thus corporate legitimacy, which could be restored by "internalising democratic mechanisms within their organisations, in particular in their corporate governance structures and procedures" (Scherer et al., 2013, p. 473). Adobor (2020) presents three key antidotes to democratic deficit in business organisations: (1) inclusion; (2) transparency, and (3) shared decision-making – all of which should promote openness and allow stakeholders to exercise control over key agenda that concern their welfare (see Foley & Polanyi, 2006).

This thesis argues that the notions of corporate democratic deficit and weak shareholder activism should be discriminately applied, in the light of the prevailing political economy and institutional settings that governed the narratives of business engagements between banking companies and stakeholders. The interconnectedness between smaller, local joint-stock banks and the community forged a sense of collective identity that was conducive for the promotion of inclusivity, representativeness, and mutual collaboration among all interested parties, thus rendering the term "democratic deficit" somewhat muted. Even if there existed unequal power relations between senior management and stakeholders that undermined corporate openness and accountability, there is a compelling case for unveiling how power could be legitimately exercised (at least in the eyes of the injured parties), and the degree to which open discussion and constructive engagements between conflicting parties helped to restore trust and cooperation. In the event of a crisis, and depending on the contexts and circumstances, democratic openness and collective consultation provide no all-rounded and universal cures. For pragmatic reasons, corporate autocracy in the shape of centralised decision-making and curtailed information-sharing may be justified in consideration of the need for enhanced efficiency, speed, and decisiveness (see Daft, 2000).

2.3.1 Republican Virtues, Trust, and the Common Good

In his study, Alborn (1998) likens joint-stock companies in nineteenth-century Britain to political institutions of those days, in which case both were closely scrutinised for their

actions and held accountable to the parties whose interests they were supposed to represent. Anchored upon the "republican virtues" of vigilance, affiliation, and social solidarity among all members, many post-1826 joint-stock banks were formed to cater for local economic needs. As opposed to the idea of a national branch banking network which did not gain immediate acceptance in England, where the town or county remained the focus of political and social life, these provincial banks adhered to the earlier system of local private finance and pitched their operation within a closely knit community. As long as the traditional pattern of regional self-reliance remained, banking services were confined to a specific region or county, to allow bank officers to keep businesses under close supervision. Given their personal knowledge and participation in the local network, the fact that board members, shareholders, and customers were drawn from the same community meant all parties could monitor each other's actions more closely, thus reducing uncertainties and information asymmetry. Adequate banking expertise, combined with local knowledge, personal vigilance and face-to-face cooperation, provided smaller provincial joint-stock banks a competitive advantage in terms of security and accountability over their large "national" rivals.

The research conducted by modern scholars yield similar findings. Historically, local businesses relied upon relational financing provided by smaller, local depository institutions (Berger et al., 2005). Community oversight works in such a way to ensure stable banking and thus the collective good for all members. First, "in-person customer relationships" provide bank managers the "low-cost endowment of soft information" needed to screen and monitor the creditworthiness of borrowing customers more effectively (DeYoung et al., 2019, p. 100), thus mitigating agency conflicts between management and other stakeholders (Berger & Udell, 2002). Second, because the ownership base of local banks is highly concentrated from which managerial positions are typically recruited, there is incentive for promoting sounder corporate governance that in turn leads to enhanced loan portfolio performance (Sullivan, & Spong, 2007). Lastly, the fear of reputational damage through public recrimination in a close-knit community would act as a deterrent against opportunism or unacceptable behaviour, thus mitigating moral hazards among bankers and borrowers that could otherwise destabilise the whole community (DeYoung et al., 2019).

A limitation of Alborn's (1998) approach to the study of joint-stock institutions is that the political allusion is perhaps too far-fetched, given the limited attempt at connecting the practical conduct of public companies with the prevailing political rhetoric. A few

contemporary studies similarly contend that stakeholder democracy is an organisational concept, conceived of as “a means by which organisational stakeholders are enabled to influence managerial decisions substantially affecting their welfare” (O’Dwyer, 2005, p. 29; see Crane & Matten, 2003; Harrison & Freeman, 1993). This interpretation suggests a case for examining how far the distinct nature of business entities mirrored that of political institutions, and how “republican virtues” were accordingly translated into actions. Gilbart (1836, p. 147), who actively campaigned for the conversion of private banks into joint-stock companies, once argued that this, if exercised “in good faith to *all* concerned would be a great *public* advantage” (*italic* added). Barnes and Newton (2016) show how the practical display of respectability by bank management – coupled with the commitment to delivering local economic benefits – formed the basis on which some early joint-stock banks operated successful ventures via collaboration with their respective community. By conducting their business on personal terms and actively engaging in local industries, local banks became “a part of the fabric of immediate business networks” (Newton, 2000, p. 181).

Other studies also offer similar perspectives by showing the “symbiotic relationships” between local banks and businesses in non-metropolitan economies (Menken et al., 2023, p. 659; see also Gilbert & Wheelock, 2013). Modern sociologists maintain that the secret behind a thriving community is a strong local economy powered by small firms and enterprises owned by “locally oriented and civically engaged citizens” (Menken et al., 2023, p. 659) – whose success and survival depend on the functionality of local banks as “the keystone” that ensures continuous financial and informational support (p. 661). A few interesting questions could thus be asked in consideration of the legitimacy of banking institutions at the local level. For instance, to what extent were bank managers endowed with discretion to respond flexibly to local needs? How far did organisational policies represent the economic interests of various constituents (i.e. shareholders, borrowers, and depositors)? Were directors at the central board too distant from the constituents to dismantle the barrier of distrust and scepticism? These questions demonstrate the importance of local financial facilities in driving the growth of local enterprises, which form the backbone of a stronger community, where different forms of community assets (e.g. natural amenities, human capital, and civic institutions) are effectively mobilised for the betterment of the members’ well-being (Menken et al., 2023).

2.3.2 Joint-Stock Banks, Democratic Deficit, and Corporate Autocracy

The term "stakeholder democracy" recognises firms as "not just private commercial organisations but are also institutions operating within and interacting with the public sphere" (O'Dwyer, 2005, p. 29; Phillips et al., 2003). This notion implies that firms carry with them certain public responsibilities, prompting calls for inclusive corporate governance that embraces "participatory and deliberative democracy" (O'Dwyer, 2005, p. 29; Turnbull, 2010). Similar rhetoric could be heard in the Victorian era, as incorporation became progressively available that promised a new era of corporate transparency and accountability. While an open and accountable organisation relies on stakeholders being able to hold senior management responsible for decisions impacting on their welfare (O'Dwyer, 2005, p. 28), many Victorian joint-stock entities had disappointingly shown otherwise, with a few studies pointing out unequal power relations between the executives and proprietors as the root cause. Alborn (1998), for example, observes the inherent difficulty faced by joint-stock banks in maintaining a good balance between encouraging openness and preventing shareholders from interfering with business routines. Commenting on companies formed after 1844, Johnson (2010, p. 197) sees the power asymmetry between directors and shareholders working "to the advantage of the original owners as they divided their proprietorial rights into shareholder ownership and directorial control". Freeman et al. (2012) maintains that relative to directors joint-stock politics gradually deprived shareholders of the discretion and influence over corporate affairs as the century advanced.

The departure from democratic ideals is mapped out by Freeman et al. (2012) into a few trajectories. The first is traceable to the gradual shift away from annual board election to longer-term directorial appointment. Retiring directors were able to seek re-election or propose candidates of their own choice without much shareholder opposition, effectively circumventing the Joint Stock Bank Act of 1844 that "obliged banks to rotate at least one-fourth of the board yearly and prevented the re-election of the retiring directors for twelve months" (Freeman et al., 2012, p. 89). Second, high share qualifications restricted the pool of directorial candidates, ensuring that only the financially affluent were recruited. Third, many banking and insurance companies also became increasingly opaque, citing the sensitivity of financial information as a source of competitive advantage over their rivals. Prior to the general meetings, directors pre-determined the content, timing, and flow of information, leaving shareholders to be satisfied with whatever information that

had been disclosed to them. Newton (2010, p. 39), however, presents a somewhat different perspective, suggesting that shareholder passivity and seemingly undemocratic practices were evidence of shareholder satisfaction. First, there was no example of shareholders "intervening in the running of a bank" or opposing directorial conduct or policies. Second, candidates to be elected to the board were already approved in advance by incumbent directors, and by custom "only one prospect was put forward". Third, shareholders normally approved the balance sheets and reports presented to the general meetings "without complaint".

This thesis opines that power asymmetry *per se* was inadequate for explaining deficient shareholder activism. The structure of corporate power apart, there are at least three institutional factors which blunted the effectiveness of shareholder activism under the broader canopy of joint-stock politics. First, Searle (1998) and Taylor (2013a) rightly attribute weak corporate governance to the gullibility and greed of shareholders for quick financial gains, and their repeated failure to learn from past lessons. Second, as Sternberg (2004, p. 92) maintains, shareholder activism is costly; it is practically "easier, cheaper and more rational" to dispose share ownership than to attempt active corporate governance. Because of the collective choice problem, without effective communication "each shareholder working alone is likely to be better off by selling out". However, this statement needs to be qualified in relation to the locus of banking business. Alborn (1995, p. 219), for instance, reveals that London banks whose shares were listed on a "busier stock market" had more reasons to fear that their shareholders would sell. Investors of provincial banks, on the other hand, were less inclined to do so. Because within a smaller community many shareholders were also depositors, massive sales of shares were likely to incur self-inflicted losses. Third, unpredictable and inconsistent legal outcomes – combined with the courts' shifting attitudes towards financial misconduct – also discouraged shareholders from confronting fraudulent directors or managers. The aftermath of the Royal British Bank scandal in 1856, for example, showed that shareholders were more anxious about recovering their losses than pursuing justice because of the costliness of filing criminal charges against the directors (Taylor, 2013a).

Given how shareholder activism was contextualised within the constitutional frame of joint-stock politics, this thesis approaches the traits of "democratic" openness and accountability by looking into the stakeholder (or shareholder) engagement process in the event of organisational crisis. According to Backstrand & Saward (2004), the openness and inclusivity of stakeholder engagement depend on (1) how representative stakeholders

are, and (2) how much influence senior management is prepared to confer upon stakeholders. Meaningful engagements, in turn, depend on (1) how well stakeholders are informed about the key problems, and (2) whether there is "a space for competing viewpoints where contributions are equally valued" (O'Dwyer, 2005, p. 30). This thesis explores the nature of stakeholder engagements at the organisational level: how, and to what extent, senior management encouraged "democratic", participatory governance by improving information flows and facilitating stakeholder participation (see O'Dwyer, 2005). Building on this central point, the following questions are worth investigating. For instance, to what extent were stakeholders given discretion over the agenda of consideration? How were "conflicts between organisational legitimacy and stakeholder views" identified and addressed (O'Dwyer, 2005, p. 33; see Gray et al., 1997)? How were views and disputes emerging from dialogues between senior management and stakeholder groups formally incorporated into the decision-making process? How necessary was it to restrict participation because of stakeholders' lack of knowledge to understand and challenge organisational perspectives? This approach duly recognises a few inherent difficulties. First, given the power differentials, Unerman and Bennett (2004, p. 686) argue that meaningful participation is undermined if an "undemocratic managerial prioritising process" takes hold and dictates the engagement agenda. Second, reaching a "democratically driven consensus" is problematic because expectations of different stakeholder groups are far from uniform (O'Dwyer, 2005, p. 33).

2.3.3 Corporate Power: Authority, Accountability, and Assurance

Historically, it was not uncommon that joint-stock systems which concentrated power in the hands of managers or managing directors brought about organisational failures, heightening the risks of "arguments and acrimony between shareholders and management and within boards" (Freeman et al., 2012, p. 86). By the latter half of the century, localised and personalised banking practices gradually gave way to more centralised management and streamlined administration, thus diminishing the power of local supervision. In the words of Alborn (1998, p. 87), "the emerged banking profession" had brought in "exclusionary machinery of modern management" in place of "the inclusive language of democracy", with more distant and impersonal style of administration shifting the balance of power in favour of the executives. Given the concentration of corporate power – and even more so when board members held vested interests across multiple companies –

they were frequently blamed as the source of corruption, inefficiency, dishonesty, and reckless opportunism. As Freeman et al. (2012, p. 86) put it, there was simply "no simple evolution toward a preference for delegation to professional managers". Amidst the outbursts of public indignation and ridicule, the tactfulness of corporate leaders in exercising their legitimate power determined how effectively they could restore confidence and repair complex relationships with stakeholders.

In the immediate term, given that stakeholders "have a reason to trust organisations based upon their engagement experiences and the dissemination of information to them" (Swift, 2001, p. 23), openness and dialogues are – to a certain degree – useful for securing public confidence that all will be accomplished in goodwill. Nonetheless, Baum (1977, p. 44) cautions that there can be no true dialogue in the presence of power asymmetry, and "to recommend dialogue in a situation of inequality of power is a deceptive ideology of the powerful, who wish to persuade the powerless that harmony and mutual understanding are possible in society without any change in the status quo of power". This thesis takes it unthinkable to assume away the inevitability of heated debates or dialogues between conflicting parties when delicate issues had to be resolved. For instance, to the extent that "the issue of accountability is about whether stakeholders have sufficient, accurate, understandable and timely information on which they act" (Swift, 2001, p. 17), how prepared were directors to disclose sensitive information and reveal the real worth of their claim to ownership (Johnson, 2010)? How, and to what extent, were minority shareholders assured that they were protected from what Tocqueville (1835) terms as "tyranny of the majority", particularly when difficult and competing decisions had to be made? How should competing interests from divergent stakeholders be prioritised and treated with fairness and equity? The processes embedded in these questions unveil the "multi-layered and multi-faceted accounts" that enable stakeholders to identify and present "competing perceptions" on main issues that might not have been recognised as problematic before any dialogue takes place (O'Dwyer, 2005, p. 33).

Another delicate, long-term issue is the degree to which agents could be effectively held accountable when power relations are unequal. Unlike trust – which is a product of one's voluntary move to believe that the other party would likewise engage in virtuous behaviour – accountability is a notion emerging from the suspicion that agents might engage in activities that jeopardise the principals' interests (Swift, 2001). Nevertheless, in the presence of power asymmetry this distinction may be overdone, given that stakeholders had little choice but to "trust" and accept – however reluctantly – whatever

terms and information disclosed by the companies. Tricker (1983) maintains that accountability is only meaningful if it is enforceable by contractual arrangements. Because banking is the economic lifeblood for a community, it has a somewhat "quasi-contractual relationship with society at large", and therefore "a duty to account for its actions to society" (Swift, 2001, p. 17). There is also a question about how explicit or tacit a contract should be in specifying the terms on which agents' behaviour should be regulated (Gray et al., 1997). The above issues provide useful perspectives for addressing some interesting questions about the post-crisis contractual relations between Victorian banking companies and the community. For example, how were social contracts negotiated between banking companies and stakeholders? How, and by whom, were the terms of accountability dictated? How far were stakeholders dynamically involved and engaged by directors in the course of negotiating the terms? Could the terms effectively invoke positive changes to corporate governance by inducing the directors to provide adequate justification for their actions (Gray et al., 1987)? To some extent, these questions also reflect an increasingly multi-lateral, stakeholder-driven approach to corporate governance, prompting a reconsideration of the present systems of checks and balances to ensure that companies behave responsibly towards all involved parties (see Solomon, 2007).

2.4 Banking Liability: Regimes, Responsibility, and Credibility

During the first half of the nineteenth-century, commercial activities in Britain and the rest of Europe were guided by the principle of unlimited liability, resting on the belief that "economic undertakings engaged the full responsibility of individuals and even of their kin" (Djelic, 2013, p. 602). Given the broad and diversified base of shareholders, the joint-stock system significantly enlarged and deepened the pool of capital available for productive investment, paving the way for the emergence of large-scale enterprises through the attainment of economies of scope and scale (Baums & Scott, 2005, p. 34). Critics however lamented that the separation of ownership and management that characterised the system, and the cherished culture of shareholder primacy, risked undermining moral and commercial soundness. To satisfy shareholders' desire for maximum financial returns, managers were prone to inflate share values and short-term financial results through the deployment of risky strategies, without paying due regards to long-term fundamentals and capabilities of the organisation (see Ireland, 2010; Kay,

2012). Unlimited liability was therefore widely seen as a vital institutional instrument for restraining appetite for risks of shareholders and managers alike. Shareholders – whose entire wealth is on the line – must exercise caution and ensure that managers conduct the banks prudently (Turner, 2014).

This section does not attempt to review various economic arguments as to why unlimited-liability banking was introduced, or how it pre-empted further economic losses when a bank failed. Rather, it examines how unlimited liability conditioned the network of economic relations and constitutional power in banking organisations, and how well it served as an institutional arrangement to safeguard and balance the competing interests of all affected parties before trust could be effectively restored (see Baums & Scott, 2005). Bearing this objective in mind, it is useful to look at the distinction made by Koslowski (2009, p. 136) as to the different degrees of importance assigned by divergent classes of stakeholders to financial returns, and therefore, their respective perception of fundamental purpose for which the firm is constituted. As opposed to other *stakeholders* who see financial rewards as "a means to ensure the success of the firm as a whole, but not as an end in itself", the *shareholders* are the only group for which "the disciplining instrument of corporate profit and the share price are simultaneously their individual goal". In this sense, as Baums & Scott (2005, p. 33) contend, "it is not the exclusive or even primary purpose of the board to protect the interests of the shareholders, but rather to promote the interests of the firm". There is therefore a compelling case for examining the relevance of unlimited liability in connection to the culture of shareholder primacy, and how they influenced the prioritisation of different economic interests across divergent parties, and thus, the resilience of cooperative relationships within the community as a whole.

2.4.1 Firm as a Rock? The Test of Unlimited Liability

Many nineteenth-century political economists and bankers took unlimited liability as the key to securing banking stability, public confidence and above all – the image as prestigious and reliable institutions. It was generally regarded as "a perfect safeguard" for members of public against possible losses (*Bankers' Magazine*, Jun. 1848, p. 345). The English jurist and statistician Leone Levi (1880, p. 476), for instance, wrote that unlimited liability acted to "inspire unlimited confidence" in depositors that they would be fully repaid if the bank failed. Political economist John Ramsay McCulloch (1856, p. 16) also believed that under the constraint of unlimited liability businessmen would behave

"discreetly, fairly and honourably", building an "unblemished reputation" – an important element by which commercial interests would be best preserved. To Wilson (1879, p. 71), unlimited liability banks enjoyed an advantage over their rivals when competing for customers' deposits:

> A depositor would be much more likely to trust his money with a bank whose shareholders he knew must yield up to him the uttermost farthing that they possessed, in making good losses should the bank fail, than with a bank whose shareholders were liable only to the amount uncalled on their shares.

In most instances, with men of considerable substance making up the body of proprietary at large, unlimited liability appeared to have worked "exceedingly well" in forestalling further escalations in panic by assuring depositors and note holders of the security of their money (*Bankers' Magazine*, Jun. 1848, p. 345; Turner, 2009).

The above Victorian beliefs are echoed in the twenty-first century by Turner (2014), who likewise argues that unlimited liability, when combined with the freedom of incorporation, provided a strong basis for banking stability. A large pool of capital contributed by a well dispersed and diversified base of shareholders assured that the bank's deposits and notes were adequately backed. As to whether unlimited liability afforded better banking security, the historical records were mixed. Notable Victorian bank failures were, in Turner's (2014, p. 118) opinion, a paradoxical illustration of "the effectiveness of unlimited liability in underpinning the stability of the banking system". First, given the size of the fast-expanding banking industry, failures of banks with unlimited liability were uncommon, among which many were attributed to fraudulent behaviour or mismanagement. Second, failures were sporadic that they did not trigger systemic panic and runs on other banks, because depositors – assured ample stock of shareholders' wealth – knew they would receive full repayment. Importantly, Turner (2014) sees unlimited liability as catalyst for *preventing* risk-shifting by bank managers (i.e. maximising returns to shareholders through risky investments at the expense of depositors). How far a bank could withstand adverse shocks also critically depends on (1) the stability of its assets (i.e. securities and loans), and (2) the sufficiency of its cash reserves or other liquid assets to promptly meet withdrawals by customers. These critical decisions inevitably rest in the hands of banks managers, who in the view of Minsky (2008) are prone to increasing leverage ratios by engaging in risky portfolios – a

behaviour that is explained by the incentive structures, risk profiles and governance of banking corporations.

Because banks do not lend their own money but their customers' deposits, they are caught in a "dialectical union of creative entrepreneurial imagination and a sense of reality, objectivity, and thrift", following which they must "strike a balance between sympathy and stringency" (Koslowski, 2009, p. 28). To the extent that shareholders and depositors were not in possession of needful information to impose financial discipline upon bank managers, there were always dangers that risk-shifting would escape undetected. Understandably, bank-loan portfolios were concealed from public knowledge because financial information was confidential. In the case of banking, secrecy originates "from the nature of the matter at issue and from the task of the banks, which is to provide secure and discreet custodianship of value for customers" (Koslowski, 2009, p. 6). To safeguard their own credibility, borrowers did not want information about their investment projects "released into the public domain" (Turner, 2014, p. 23). Banks, on the other hand, also guarded the secrecy of lending portfolios as a source competitive advantage. Poor risk management and over-lending were among the most common errors that triggered episodes of banking troubles during the Victorian age. Taylor (2013b, p. 117) shows that such incidents were anything but rare, often concealed from public knowledge until "serious abuses" were identified.

Ironically, localised banking – which was supposed to mitigate information asymmetry and enhance monitoring – seemed to amplify the failure of unlimited liability *per se* in ensuring financial discipline and prudence. In numerous cases local banks failed to take advantage of their personal knowledge of the customers and community, resulting in credit misallocation (see Koslowski, 2009). Even with the hindsight of prudent management, restricted share ownership and commercial lending within a restricted geographical confine hindered risk diversification. The repercussions of banking liability would be considerable because the costs extended beyond the involved parties and were passed upon the rest of the community (see Koslowski, 2009, p. 167). Given the inherent difficulty in capturing the full costs and consequences of banking crisis, this thesis thinks it worthwhile to reassess the extent and efficacy of banking liability in connection with the community welfare as a whole. For instance, how did unlimited-liability banking ensure entrepreneurial support and prudent risk management in the interest of the community? To what extent could liability rules satisfactorily compensate for the *indirect* damages and distresses suffered by the wider community? Alongside unlimited liability,

how far, and at what level, were there social contracts or ethical constraints negotiated between local banks and the community to mitigate opportunistic behaviour and systemic risks caused by bankers? These questions consider the liability regime not merely in terms of "the sense of legal duties" which constitutes "a legal minimum", but also moral duties and attitudes among market participants "in the economic domain that can be qualified as good" (Koslowski, 2009, p. 8).

2.4.2 Shareholder Constituency, Wealth, and Public Confidence

The aggregate wealth of shareholders in any given joint-stock bank was a critical indicator of its financial robustness. The studies by Alborn (1998) and Turner (2014, p. 109) showed that directors deliberately excluded candidates who were financially inferior, controlling the entry to shareholding membership in such a way that "the aggregate wealth of the shareholding constituency was not diluted". Newton (2010) looks at the role of local networks in determining the choice and composition of shareholders in early English joint-stock companies, showing that the stated residences of the body of proprietary were "predominantly local". Because of the relative ease and accuracy in collecting information about local shareholders, the chances of recruiting only credible investors and customers improved. On the other hand, to the extent that all personal assets and wealth of shareholders were "potentially at risk" (Djelic, 2013, p. 602), they were incentivised to enforce prudent business practices and good corporate governance. Above all, since wealthy shareholders have more to lose, they had "the greatest incentives to act as directors and oversee the shareholder-vetting process" (Turner, 2014, p. 111). From the above studies, it is clear that given the constraint imposed by unlimited liability there is implicitly a strong connection between shareholder composition and the welfare of other stakeholder groups. A recent preliminary study by DesJardine et al. (2023) suggests that by mapping out shareholder heterogeneity, an organisation is able to identify where their divergent interests collide with those of other stakeholders. In this context, unlimited liability certainly conditioned the influence of shareholders over the way in which senior management attended to the concerns of other interest groups.

Given that shareholders or co-partners in some smaller local English joint-stock banks were mostly "local in origin" (Newton, 2010, p. 29), there are interesting questions about the role of local or regional networks in helping directors to shape the composition of shareholders. For instance, what types of shareholder information were of use to

banking companies, and how was information collected, circulated, and appraised by directors for its credibility? In what ways the transmission and sharing of shareholder information was conditioned by local identity and solidarity? To the extent that each partner assumed joint and several unlimited liability, how far were shareholders prepared to trust directors for having the means and wisdom to recruit only qualified investors? The above examples of non-legal interventions deployed by local banks implied that they were aware of the potential problems stemming from imperfect qualitative information about shareholders. Akerlof (1970) sees this as a form of market failure which undermines certainties and raises the economic costs of dishonesty. Kirzner (1979) takes up a different argument, maintaining that imperfect information is simply part of the market process, with which the entrepreneur must inevitably confront and address. Arguably, the composition and background of shareholders were part of what Klein (1974, p. 430) terms as "brand-name capital" mobilised by banking institutions to inspire public confidence.

The stringent selection process aside, critics of unlimited-liability banking argued that if shares were transferrable there remained possibilities that share ownership might end up in the hands of impecunious individuals, thereby undermining "the stability of the wealthy-owners equilibrium" (Turner, 2014, p. 109). Among the critics was Walter Bagehot (1862, p. 397), who contended that liability was *de facto* limited if shareholders' wealth was insufficient to meet the call. As the century progressed, the long-held view that unlimited liability would give joint-stock banks a façade of stability and superiority was increasingly challenged. Opponents argued that unlimited liability had unintendedly dissuaded men of affluence from becoming shareholders. *The Times* (21 Jun. 1848, p. 7), for instance, saw a "rapidly observable, of a substitution of a wholly inferior class in the place of shareholders of wealth". The above arguments, however, failed to consider two preventive measures that severely restricted shareholders' ability to offload their financial obligations through opportunistic share-dumping. First, under the English Banking Co-partnerships Act of 1826, shareholders remained liable for the bank's debts during the first three years after they had disposed their share ownership. Hickson and Turner (2003) also refer to the relative stickiness of share prices of unlimited-liability banks as a proof that post-sale-extended liability was effective in discouraging the sales and purchases of those shares. Second, at the organisational level bank management retained substantial power to ensure that shares could not be sold or transferred freely, which in any event must be approved by the directors or charged at a fee.

2.4.3 Shareholder Primacy, Plight, and Protection

Shareholder values and return on investments appear to be the focal point of the Anglo-Saxon model of corporate governance that underpins the Victorian capitalist order. Critics argue that financial fallouts resulting from the maximisation of shareholder value calls for a fundamental rethink within the industry. Koslowski (2009, p. 144) endorses the idea that increasing the liable capital of banks is an "indispensable imperative" for improving corporate governance and controlling the risk appetite of managers and shareholders alike. The Victorian political economy constantly tied (un)limited liability to the implications on personal responsibility, institutional credibility, and financial stability. Unsurprisingly, as the expansion of the joint-stock economy gathered pace, shareholder liability was at "the centre of a battleground between God and mammon" (Johnson, 2010, p. 137). Limited liability was mainly opposed on the ground that it would encourage financial speculation and deprive the world of commerce of its moral underpinnings. "In the scheme laid down by Providence for the government of the world", wrote McCulloch (1856, p. 10), "there is no shifting or narrowing of responsibilities, every man being personally answerable to the utmost extent for all his actions".

The above arguments began to lose their appeal when banking scandals in the mid-1850s exposed the vulnerability of ignorant shareholders to the deceits and dishonesties of corrupt directors. Enticed by the "glistering prospect of high dividends" and names published under "sufficiently respectable auspices", ignorant shareholders continued to pour in millions of pounds into new banks, many of which were doomed to fail (*Bankers' Magazine*, Apr. 1856, p. 207). Certain quarters remained adamantly unsympathetic. A commentator, for instance, castigated in the *Bankers' Magazine* (1856a, p. 793) that "the public themselves are to blame, if they subscribe to any scheme which is calculated to have a damaging effect upon a community, or upon themselves more particularly". The point was that as owners, all shareholders – "individually as well as collectively" – were expected to fully discharge the bank's liabilities (*Bankers' Magazine*, Sep. 1857, p. 707). On the other end of the spectrum were the sympathisers, who conceded that there were limits on how far shareholders could hold corporate management to account. With bank losses and liability threatening to "reduce many of them to beggary, and make paupers of those who had previously been in easy circumstances" (*Bankers' Magazine*, Jun. 1848, p. 347), consensus was emerging that better protection should be afforded to unsuspecting

and ignorant shareholders, by means of limiting their liability and making directors' misconduct punishable by law.

With the above notions in mind, this thesis seeks to make sense of the changes at play that explained the narratives behind public attitudes towards shareholder protection in relation to the financial commitment of shareholding. For instance, how did joint-stock banks ensure the welfare of depositors while shielding shareholders from huge liabilities? How was the extent of liabilities and losses negotiated? How were competing agenda and complaints among different clusters of stakeholders prioritised in the face of (un)limited liability and perceived injustice? Commenting upon the stakeholder approach which conceives the firm as "a multipurpose organisation", Koslowski (2009, p. 139) is careful to emphasise that it provides "no means of integrating the various goals of the stakeholders, but places them immediately alongside one another with parity of status". The key lesson is that none of the goals of any interest group should be given overriding concern. However, in the case of unlimited-liability banking shareholders' claim was at best "residual in priority and poorly defined" (Baums & Scott, p. 34) – i.e. whatever was left after creditors or depositors had received their due portions. Indeed, one of the main areas to address in this thesis is to demonstrate how far Victorian bank management could possibly – beyond the legal and statutory requirements – satisfy the concern of non-shareholding parties without pressing unduly hard upon the shareholders, in effect mobilising the collective support of all interest groups to navigate the troubled institution through the storm.

2.5 Conclusion: The Essence of Trust

The literature survey advances the debate on the issues of trust in socio-economic relationship between local banks and the community – and to a significant degree, official regulators – by providing historical context and depth to understand the process of fundamental change and certain patterns of continuity over time. The nature of banking and finance is such that it is insufficient to approach these subjects by confining the discussion to the role of the government as watchdog in the marketplace, endeavouring to promote responsible and stable banking institutions as the course of the joint-stock economy evolved. Nor is it sufficient to see the government as a close ally to banking companies, passively serving only the interests of bankers and financiers in the nation (see Williamson, 2004). The debate, in fact, goes far beyond the relationship between the

regulators and the regulated, forming only a part of a much more intricate and muddled picture of the importance of banking in driving industrial capitalism, behind which the vital elements of trust and trustworthiness stretched across “a bewilderingly broad and cross-cutting array” of institutions, instruments, and individuals (Shiller, 2012, p. 13). This central notion forms the backbone of the following chapter, which argues that it is a mistaken idea to reduce the subject of trust – both its inspirations and breakdowns – to simple, mechanical, and abstract terms, insofar as the drivers of capitalist institutions are “real men and women” who assume “certain personae” in relation to their respective roles, responsibilities, and expectations, with each evolving through “a process of continuous invention” in the society (see Shiller, 2012, p. 14).

Chapter 3
Banking Conduct, Changes, and Continuities: A Methodological Comment

3.1 A Cultural Analysis

Established upon the fundamental belief that business organisations are members of a wider cultural framework, this study follows a cultural and narrative perspective to examine how joint-stock banks in Victorian Britain repaired trust and public confidence against a background of crises or scandals. Cultural contexts, this research argues, provide "the very foundation of how we perceive the world and respond to incentives" (Hansen, 2012, p. 705). They become the assumptions on which business organisations or transacting parties make informed decisions. In his study of Victorian capitalism, Johnson (2010) considers the role of laws, norms, and customs of trade and exchange in shaping the conduct and characters of business organisations. Lamoreaux (1995) attributes the emergence and evolvement of business organisations to some conceptual processes and specific socio-cultural contexts, which either create or constrain opportunities for corporate development. As Hollow (2020) observes, an interesting trend that has emerged following a rise in the focus on contextualisation is the growing appreciation of the value of history and historical methodologies to the study of business organisations. Importantly, as the argument goes, a "detailed and contextually sensitive historical research" could potentially challenge and provide new perspectives as to "how and why" business behaviour and practices change over time (Hollow, 2020, p. 80).

This thesis contends that to the extent that the complexity of human behaviour in connection with the wider cultural and social environment is unduly simplified, the functional assumptions of linearity and rationality incorporated in many economic or business models significantly constrain "the way we perceive the world and construct our explanations about that world" (North, 2005, p. 28). Interestingly, Hollow (2020, p. 67) notes that the push for infusing entrepreneurial research with historical insights has partly to do with a desire to challenge the "ahistorical, hypothesis-testing natural science

methodologies" commonly deployed in mainstream entrepreneurial study (see also Forbes & Kirsch, 2011). The cultural and narrative perspective enlarges the scope for understanding how the dynamics of trust repair recast the image and drove the development of joint-stock banks as prominent capitalist institutions in nineteenth-century Britain. Furthermore, by incorporating historical perspectives to understand the role of context in shaping business behaviour (see Hollow, 2020), this approach also opens up the possibility of tracing systemic or institutional changes, especially when new contrasting narratives are persuasive enough to challenge and dominate the existing ones by assigning new and different meanings to events (Hansen, 2013).

According to Pfarrer et al. (2008, p. 731), organisational legitimacy is "a generalised perception by stakeholders that an organisation's actions are appropriate within a socially constructed system of norms and values". Given this argument, there are at least three compelling reasons for applying the cultural and narrative approach in this study. First, the embedded systems of beliefs, values, and ideas provide an interpretative frame through which members ascribe meanings to events, institutions, and practices (Hansen, 2012). In the words of Geertz (1973, p. 5), culture is "not an experimental science in search of law but an interpretative one in search of meaning". To the extent that banking scandals "upset the order of things and urge society to reconsider its cultural, social and economic values and principles" (Hansen, 2013, p. 674), members are constantly engaged in a process of making sense of the events through signification. This process is largely mediated through narratives which in turn shape members' perception and explanation about the events (North, 2005). For instance, how were joint-stock banks compared with private banks for their respective credibility as industrial capitalism advanced? How did the perceived connection between unlimited liability and banking security evolve over time? To what extent the blurring distinction between investment and speculation compound the culture of shareholding? How was the boundary between shareholders' responsibility and protection (re)negotiated over the century? How did the state (re)define its role in reforming the marketplace? Importantly, these suggestive questions point to the fact that meanings ascribed to the conduct, contribution, and economic characters of banking businesses are variable, subjective, and open to reinterpretation from time to time. They are context-specific and must thus be "contextualised and interpreted" (Hansen, 2012, p. 705).

Second, the cultural and narrative approach can also be engaged with the structure and allocation of organisational power. In the opinion of Lipartito (1995, p. 11), "like any

social institution, business can be investigated for its power to ascribe meaning, and thereby constrain, control or claim to represent what is real". Linde (2009, p. 3) observes that as "institutions and their members use narrative to remember ... they work and rework, present and represent the past for the purposes of the present and the projection of a future". Brunnige (2009, p. 11) points to the opportunities for companies using historical heritage "to create and alter brands and to enable organisational and strategic change". Following Hansen's (2012, p. 702) observation that businesses are capable of using history "to create memory and strengthen their organisational identities", this research aims to map out how banking companies recalled and repackaged the history to redeem legitimacy after organisational crises. For instance, how did banks reassert their claim of credibility by emphasising their outstanding history? How did they recover reputation by removing their controversial or blemished past from narratives? To what extent could historical heritage afford bank directors the option and scope for advancing, or perhaps, resisting organisational reforms? In doing so, this study shows that banking companies must locate the sources of power and confront the possible counter narratives by which any effort to reiterate and re-establish organisational credibility could be frustrated.

Third, recurrences of banking scandals are accompanied by moral panics, which often take place within a context infused with cultural meanings and represent "more direct defensive reactions to perceived threats to moral orders" (Hier, 2011, p. 258). Moral panics, as the argument goes, are no mere "irrational social reactions to putative threats" but can be "properly conceptualised as routine forms of social action that contribute to the affirmation and transformation of everyday customs, rituals, conventions, and routines" (p. 258). Given that banking crises are widely publicised and (sometimes) sensationalised, there is therefore a case for examining how moral panics "come about through a complex chain of social interactions involving claim makers, moral guardians and the media" (Hier, 2002, p. 313). For instance, how far was the claim made by William Godwin (1832, p. 173), an English journalist, that company directors were "men fattened on the vitals of their fellow citizens" echoed by members of public? To what degree were bankers and financiers labelled as greedy, incompetent, self-serving, and destructive of business morality and social order? In what ways should bankers be held accountable for their conduct? Hier (2011, p. 258) conceptualises moral panics as a form of moral regulation, which in turn contributes to "the production, reproduction, and transformation of exceptional moral orders by satisfying existential desires for phenomenal security".

Accordingly, discourses about moral panics focus on controlling undesirable activities, serving as an opportunity for reordering the moral system for the banking world.

3.2 Hayek: Freedom, Individuals, and the Spontaneous Order

Focusing on the freedom of action for both individuals and society, Hayek's (1960) *Constitution of Liberty* provides a suitable *theoretical framework* to construct a cultural and narrative analysis of banking practices in nineteenth-century Britain. By approaching individuals as interdependent and thus the need for social cooperation between members within the society, Hayek's conceptual approach to individuals resembles "a deliberate abstraction from social man and the social context of human life" (Miller, 2010, p. 42). By abstraction, Hayek (1960, p. 149) means that an individual normally "responds in the same manner to circumstances that have some features in common", acting with reference to the abstract rules, conventions, or norms in which he is situated. This notion provides a convincing case for understanding individual actions within a broader context of social and communal relationships. In broad terms, Hayek's perspective articulates sufficiently well with Hansen's (2012) argument that culture represents a system of values and ideas that conditions the perspectives and practices of individuals, groups, or organisations. Business culture provides a "set of limiting and organising concepts that determine what is real or rational for management, principles that are often tacit or unconscious" (Lipartito, 1995, p. 37).

Three fundamental propositions raised by Hayek are of relevance to the overarching objectives of this research. First, Hayek (1960, p. 29) claims that the case for individual freedom "rests chiefly on the recognition of the inevitable ignorance of all of us concerning a great many of the factors on which the achievement of our ends and welfare depends". Because of limited knowledge and ignorance, human actions necessarily involve "discovering what is knowable" (Miller, 2010, p. 54) – a process during which trials and errors are inevitable. Hayek's (1948, p. 84) earlier work refers to "the knowledge of the particular circumstances of time and place" (i.e. an individual's acquaintance with his immediate environs) as a source of advantage and condition for social cooperation. Although one's access to unique information may allow him to have certain advantages over others, insomuch as he cannot make decisions "solely on the basis of his limited but intimate knowledge", he must cooperate with others, so as to align his decisions with "the whole pattern of changes of the larger economic system" (p. 84). In

Hayek's view, it is precisely the freedom of actions and social cooperation in the market that allow such dissemination of knowledge and information to take place for all participant's exploration and benefits.

To apply Hayek's repeated emphasis on limited knowledge in this study, to build and rebuild trust was naturally challenging because joint-stock banks and stakeholders alike were respectively constrained by imperfect information. For instance, how did banks and stakeholders collect, exchange, and appraise information about one another? What types of information were of practical use, and how were they shared and disseminated through social cooperation in the marketplace? On what criteria did investing public and depositors assess the credibility of banking institutions? How did joint-stock banks maintain the balance between corporate transparency and secrecy in relation to the disclosure of corporate matters? Hayek's perspective, this research argues, can provide an insight into how different parties actively learned, managed, and overcame information asymmetry through cooperation.

Second, as individuals and groups repeatedly interact and cooperate with one another, unplanned social order and patterns of behaviour gradually emerge, during which "a process of selection" takes place, "winnowing out moral rules that might be destructive to society and preserving those that favour its survival or persistence" (Miller, 2010, p. 74). This is addressed in Hayek's (1960, pp. 58-59) idea of spontaneous order, where "in the relations of men … purposive institutions might grow up which owed little to design, which were not invented but arose from the separate actions of many men". Polanyi (1951, p. 159) holds a similar view that such order emerges out of human interactions "on their own initiative – subject only to the laws which uniformly apply to them all". Hier (2011, p. 526) likewise argues that "all forms of human knowledge are discursively constructed" from repeated encounters, out of which values, norms, and rules are learned, reinforced, and subsumed into the mainstream cultural representation. The key is that these efforts are dispersed, decentralised, and yet remarkably self-coordinating, undertaken voluntarily without a central directive. The role of the state, in this context, "is not to set up a particular order" through its use of coercive power but "to create conditions in which an orderly arrangement can establish and ever renew itself" (Hayek, 1960, p. 161).

Rapid social or cultural changes are likely to interfere with the process of dialectical judgement, during which acceptable and unacceptable practices are identified (Hunt, 2011). Moments of panic, hysteria and fear are regularly – and quite wrongly – dismissed as void of moral or ethical components. To quote Hier (2011, p. 526) again, "as a growing

number of everyday activities became moralised in the form of dialectical judgements about what is right and what is wrong … the boundary separating morality from immorality blurred". This research, however, presents a case for recognising moral panics – if any – as equally relevant for recalibrating the system of values, norms, and customs. In connection with the moral panics accompanying banking scandals, this study utilises Hayek's idea of spontaneous order to analyse the recalibration of banking norms, culture, and practices in nineteenth-century Britain. How were banking entities re-evaluated for their trustworthiness during and after crises? How did banking elites, stakeholders, and other interest groups work together to determine and negotiate the reform agendas of banking institutions? How far were banking reforms driven and reinforced by a sense of commitment to serving society's collective good? These questions reflect the fact that banking crises have serious and wide-ranging repercussions, so much so changes in the regulatory paradigm are deemed warranted (see Cohen, 1972). Even irregular and erratic events, this study argues, are relevant to understanding the (re)stabilisation of moral order and trust over time.

Third, because individuals are part of a system, Hayek (1960, p. 63) contends that they must always function "inside a framework of both values and institutions" which is not of their own making. Without a robust company law during the early decades of the nineteenth century, communal norms, customs, and expectations functioned as a tacit regulatory framework to guide and control the conduct of banking institutions. Individuals acquire and assimilate these behavioural rules by means of observation, imitation, and learning. Miller (2010, p. 72) describes these unspoken regulations as "unconditional demands and not as expedient options", which business organisations are obliged to imbibe to gain public acceptance and avoid reputational loss. Because the system provides a guide for identifying acceptable and unacceptable behaviours, Hayek (1960, p. 62) remarks that "the general observance of these conventions is a necessary condition of the orderliness of the world in which we live, of our being able to find our way in it". Similarly, Hunt (2011) sees "the moral" as relational and therefore finds it necessary to examine the historical context in which the rights and wrongs are discursively constructed. Moral regulations, as such, can be taken as "a long-term process of encouraging others to internalise codes of moral conduct and act on their own behaviour to affirm a sense of phenomenal security in a world of perceived or potential security" (Hier, 2011, p. 530; see also Hier, 2002).

There is also room for analysing how official regulations might interact with unwritten rules and customs to present bankers with new sets of behavioural expectation. Hayek's (1960) endorsement of the government's arbitrary power in enforcing the rule of law does not contradict his defence of individual freedom, noting that it is the character – rather than the volume – of state intervention that matters. To be consistent with individual freedom and the *modus operandi* of free-market capitalism, new laws and legislation must be general, predictable, and equally enforced upon all participants. For most part of the nineteenth century, the ideology of economic liberalism continued to dominate the mainstream of political discourses and public life. Arguably, in response to banking crises and public criticisms, tentative and evolutionary reforms somewhat confirmed the state's political commitment to defending economic freedom by means of restoring trust, order, and discipline to the marketplace. Shifts in regulatory paradigm also reflect the debate over the role of the state as a moral architecture, in conjunction with a call upon individuals to assume the personal responsibility "to manage risk against collectivising discourses that represent the subject position of harm to be avoided" (Hier, 2011, p. 526). Given the difficulty in distinguishing between state and non-state agencies, Dean (1994, p. 152) claims that it makes sense to take moral regulation as a fragmentary and complex process in which "multiple and overlapping jurisdictions" are involved.

3.3 Organisational Trust Repair Model: An Analytical Framework

Repeated episodes of financial crisis in nineteenth-century Britain had undermined public trust and endangered the sector's reputation. Scandals attracted adverse publicity and invoked strong negative sentiments among the victims, but some banks overcame the crisis, offering a case study in trust repair. This thesis endorses the belief of De Jong et al. (2015, p. 32) that there is a compelling case for pushing the boundary of the study of business history beyond its immediate domain and paradigm, so as to "create knowledge by using empirical research to explore, define and test theory". For this purpose, it applies the organisational trust-repair model developed by Gillespie and Dietz (2009) "to build generalisations" and "to understand in a general sense" how Victorian banks rebuilt trust over time, and why some firms performed better in terms of organisational rehabilitation and survival than others (see De Jong et al., 2015, p. 32). The model is built upon three attributes of organisational trustworthiness outlined by Mayer et al. (1995): (1) the *ability* to fulfil key organisational missions; (2) *benevolence* as exemplified in the commitment

to safeguarding stakeholders' well-being, and (3) *integrity* as demonstrated in certain ethical standards. From this claim, Gillespie and Dietz (2009, p. 128) deduce that the legitimacy of an organisation is threatened when it fails "in its responsibility to meet reasonable standards of ability, benevolence, and integrity in its conduct towards its stakeholders". The significance of this theoretical approach is that "the locus of control" for the failure rests with the organisation internally – "even though the context for the failure may involve external influences" (Gillespie & Dietz, 2009, p. 129).

The model incorporates multilevel theory, recognising the interconnectedness of various activities performed across different organisational components and levels (see also Rivkin & Siggelkow, 2003). It incorporates four *internal* components from which stakeholders derive the attributes and signals to form opinions about organisational trustworthiness: (1) leadership and management practices; (2) culture and climate; (3) strategies, and (4) systems, policies and processes. Two *external* components – namely (1) external governance and (2) public reputation – also influence stakeholders' perception of organisational trustworthiness. Table 3.1 provides the definition of each component and shows how the terms are applied or adapted to the context of our study. Given that multiple components form the "collective construct" of perceived organisational trustworthiness, this thesis shows how "dysfunctional interactions and event cycles" resulting in Victorian banking crises could have "multiple contributory causes" and thus required systemic interventions (Gillespie & Dietz, 2009, p. 132).

This approach is characteristically distinct from those that construe trust as "essentially a micro-level phenomenon" based on frequent contacts between individuals (Bachmann & Inkpen, 2011, p. 282). Tomlinson et al. (2004), for instance, relate the victims' willingness to renew trust following a violation to the offender's strategies (i.e. nature of acknowledgement, timeliness of reparative act, and perceived sincerity) and relationship characteristics (i.e. nature of past relationship and probability of future violation). Kim et al. (2009, p. 405) present trust repair as a "negotiation of identity" between trustors and trustees, during which they attempt to resolve "discrepant beliefs" about the latter's trustworthiness through repeated interpersonal engagements. According to Bachmann and Inkpen (2011, p. 282), these "predominantly micro-level contributions" conceptualise trust as a "psychological phenomenon", a mere "attitude or state of mind" encountered by individuals over time in the face of experiences with other parties. In so doing they have neglected the macro, institutional contexts that condition the efforts of individual or collective actors to develop trust in a given business environment.

Table 3.1

Organisational Components and Trustworthiness: A Banking Context

Organisational Components	Contribution to Organisational Trustworthiness	Banking Context
Leadership and management practice	• Senior organisational leaders as role models and key influences over other system components (e.g. rewards, appraisal, cultural values) • Acceptable (including tacitly encouraged) norms and behaviours as informed by organisational authority and accountability	• Banking experiences, specialised knowledge, and competence • Integrity, honesty, and accountability • Benevolence and motivations in relation to stakeholders' interests • Executive shareholding, ownership, and financial interests
Culture and climate	• Shared beliefs, values, and norms about corporate actions and events • Cultural controls and influences on sense-making of (un)trustworthy behaviour	• Commitment towards local and collective economic interests • Short-term vis-à-vis long-term business orientation • Organisational secrecy vis-à-vis transparency
Strategy	• Financial goals, operational procedures, business policies, and behavioural norms as indicative of organisational values and priorities	• Corporate investment in local enterprises and ventures • Provision of depository services and credit facilities • Interest and investment returns • Credit terms and allocation • Financial portfolio and investment
Structures, policies, and processes	• Structures of checks and balances, reporting lines, and distribution of responsibility and authority • Behavioural norms as defined by organisational roles and expectations	• Specification of organisational rules, roles, and power • Organisational power boundary and relations • Allocation of rights, obligations, and liabilities • Prioritisation of divergent interests
External governance	• External governing structures and rules, such as legislation and regulatory mechanisms • Governance rules, professional or industry-specific expectations	• Formation and registration of banking establishments • Corporate disclosure and reporting requirements • Board election and directorial qualifications • Banking professionalism, standards, and expectations
Public reputation	• Evaluations by stakeholders (e.g. customers, industry representatives, the media) about products, services, and treatment of stakeholders • Intra-industry reputation, corporate standing among competitors and stakeholder networks	• Regional paper media coverage and publicity • Local receptivity, support, and solidarity • Corporate local identity and importance • Comparative financial stability and reputational standing • Board and shareholder qualification

On the other hand, Gillespie and Dietz (2009, p. 129) usefully frame organisational trustworthiness as a result of repeated interactions "among agents and groups in a multilevel network", during which certain behavioural patterns are reinforced and accepted as the norm. Because trust is a multifaceted construct that goes beyond what Kim et al. (2009, p. 402) describe as "cognitive and interpersonal processes", this thesis recognises the need for deploying "a macro-level approach" and sees "specific institutional arrangements" as equally pivotal in developing viable strategies to rebuild trust (Bachmann & Inkpen, 2011, p. 284). The pervasive implications of banking and financial crises imply that they are "above all a trust crisis" which extends beyond a breakdown in relationships where individuals "know each other face to face", and accordingly require "macro-level approaches" to repairing business relationships (Bachmann & Inkpen, 2011, p. 282). Institutional arrangements such as legal provisions, organisational structures and social norms create "common orientations", driving interactions between transacting parties into "foreseeable patterns" by establishing explicit rules and tacit knowledge (Bachmann & Inkpen, 2011, p. 287; Seligman, 1997). Giddens (1990) and Luhmann (1979) alike see trust as systemic in character and confirm that institutions are highly influential in (re)building organisational relationships. From this perspective, trust is construed an "organising principle" (McEvily et al., 2003) that coordinates expectations and interaction between market participants, as opposed to a mere attitude or state of mind of individuals (Bachmann, 2001).

This thesis shares the perspective of Bachmann and Inkpen (2011, p. 285) that "powerful and reliable institutions" are crucial for checking the risks of deviant or predatory behaviour. However, it questions their rather far-fetched claim that impersonal structures or arrangements could be (re)constructed as being "functionally equivalent to a personal third party guarantor" that allows individuals "to make a leap of faith and invest trust in a relationship". Whether relevant parties would necessarily find "good reasons" to trust one another simply because institutions have created a "world in common" that governs all market participants is debatable (Bachmann & Inkpen, 2011, p. 285). Quite the contrary, and as subsequent chapters in this study would demonstrate, because institutional arrangements – such as legislation or regulatory frameworks – are relatively slow to adapt, regular face-to-face contacts – which Bachmann and Inkpen (2011) rule out as redundant and inefficient – are in fact critical for suspending suspicion arising from competing interests, asymmetric information, and unequal power relations.

Importantly, the model developed by Gillespie and Dietz (2009, p. 128) fittingly understands trust as a "meso" term, combining "micro-level psychological processes and group dynamics with macro-level organisational and institutional forms". It construes organisational trustworthiness as a collective construct – "a sensemaking heuristic originating at the level of individuals' perceptions but that, in the aggregate of collective impressions, can operate as a shared reputation in the organisation". Following this notion, stakeholders consider multiple agents and actors, together with evidence drawn from multiple organisational components and levels, to evaluate various facets in making judgements about the overall trustworthiness of their organisations (Gillespie & Dietz, 2009). To restore trust effectively, it therefore follows that strategies which "only target the micro-level and call for ethical behaviour" by organisational leaders are insufficient (Bachmann & Inkpen, 2011, p. 283). Accordingly, this thesis moves beyond the specific tactics and responses of transacting parties, to consider how the interpersonal and institutional aspects of rebuilding organisational trust may interact and develop as the contexts of violation and reorganisation vary across time and space (see Kim et al., 2009).

The next theoretical facet of the model is its post-attribution approach to analysing failure – that is, once the failure has undermined organisational trustworthiness (Gillespie & Dietz, 2009). It outlines four stages for effective trust repair: (1) an *immediate response* that acknowledges and expresses regret for the crisis; (2) a systemic and accurate *diagnosis* of the problem; (3) *reforming interventions* across internal organisational components, and (4) a comprehensive and credible *evaluation* of the progress and results of the reforms (Gillespie & Dietz, 2009; Gillespie et al., 2014; Morgeson & Hoffman, 1999). By focusing on substantive actions which accompany the recommended stages, the model presents trust repair as a "protracted process" during which "multiple sources of evidence and actors" across multiple organisational levels operate in such a way that facilitates overall organisational trustworthiness (Gillespie & Dietz, 2009, p. 129). It encapsulates the complexity behind the exchanges and flows of information, the attribution of blame and responsibilities, and engagement with the public and external groups – all of which critically determine the effectiveness of trust repair.

Past studies of Victorian banking show that having the trust and support of the community critically dictate the success and survival of local banks. Barnes and Newton (2016, p. 63) demonstrate that bankers – as "established members of their communities" – were motivated to safeguard their own reputation by conducting themselves "responsibly, honestly and virtuously" in the collective interests of all members.

Insomuch as local business networks conveyed reputation by "word of mouth" and "printed word", Taylor (2013b, p. 682) argues that reputational concern functioned as "a self-regulating device" to ensure good behaviour in commercial transactions. This thesis applies the model to explore the solidarity between local banks and the community in times of crisis, as determined by the preparedness of both parties to identify with each other, and the management's tactful exploitation of the collective identity when seeking to regain public trust. Thus it finds, effective trust repair invokes a critical reflection upon a new agenda that frames the fiduciary conduct of bankers in relation to the economic interests of the local community (see Wilson & Wilson, 2013).

In a separate study, Gillespie et al. (2014, p. 400) acknowledge that trust repair may not necessarily be "a linear process through the four theorised stages, but rather one subject to setbacks", requiring "multiple successive iterations between the discovery, explanation, penance, and reforms stages". This qualification is essential to this study. Firstly, trust and credibility are both context-specific and subject to shifting interpretations as new information emerges: the comment by the press and banking elites, for instance, could sway public opinions about the credibility of the troubled institution. Next, multifaceted business relationships also complicate the trust repair process as competing interests emerge among individuals who are "partially interlocked in a variety of ways" (Downs, 2017; Pearson & Richardson, 2001, p. 659). As Newton (2010) shows, shareholders from the same community could relate to the banking entities as depositors or borrowers at the same time. There were also controversial occasions where directors and managers were debtors to the banks in which they held office. Trust repair thus involved a constant reappraisal of the moral qualities and competence of corporate leadership in uniting different parties through the crisis. The issue is further muddled when unequal power relations between directors and stakeholders enter the equation.

Considering the above observations, this thesis follows the view of Lewicki et al. (1998, p. 440) that trust and distrust are not necessarily "opposite ends of a single continuum". As Gillespie and Dietz (2009) aptly suggest, the underlying mechanisms for trust repair necessitates *both* (1) distrust regulation (i.e. mitigating negative expectations of untrustworthy actions) and (2) trustworthiness demonstration (i.e. sending positive signals of renewed trustworthiness). This notion recognises the possibilities for parties to simultaneously "trust and distrust one another in view of the different experiences within the various facets of complex interpersonal relations" (Lewicki et al., 1998, p. 440). Another theoretical property of the model is its consideration of how senior management

identifies opportunities for trust preservation, a particularly important strategy noted to be a reflexive action taken by leaders when disruption occurs (Gustafsson et al., 2021).

3.4 Cases, Sources and Uses

High-profile bank failures such as the collapse of the Royal British Bank (1856), the Western Bank of Scotland (1857), Overend, Gurney, & Co. (1866) and the City of Glasgow Bank (1878) have been regularly approached by business or economic historians in the past. This research follows a qualitative path and uses these notable failures as the background to examine how other banking companies in key Victorian industrial hubs in Northwest England repaired trust and public confidence in the event of crises or failures. The study uses a mix of banks which succeeded or failed to repair trust as the basis for conducting detailed case studies, in combination with the narrative approach, to reconstruct the social or cultural contexts in which the Victorian society perceived the trustworthiness of banking in relation industrial capitalism, personal autonomy, corporate accountability, and state controls (see Hansen, 2012). Growing local industrial needs and economic complexities also implied the deepening and extension of cooperative relationships between banking firms and local businesses. Considering the complexity of human actions and social processes, contextualisation is important for unpacking the following issues: (1) how the trustworthiness of joint-stock banks as important economic pillars was (re)construed and (re)confirmed by changing economic and socio-institutional environment over time; (2) how the governance of banking enterprises was socialised and (re)integrated into the moral fabric and professional expectations of the Victorian society following each crisis, and (3) how the state perceived and modified its "moral authority" in relation to promoting financially robust and morally responsible banking.

The emphasis in business history "on context and on the particular" (Decker et al., 2015, p. 32) makes the use of case studies an especially appealing method for understanding business organisations "in their time and context" as well as "process of change over time" (De Jong et al., 2015, p. 12). The construction of contextualised cases rests upon the "strong comparative advantage" rooted in the study of business history in engaging "in-depth and rich empirical descriptions" based on primary sources and second literature (De Jong et al., 2015, p. 12). Although case studies are frequently criticised as having "too small a sample" and thus lacking in representativeness, the cases covered in this thesis were carefully selected so as to provide unique insights which other banking

organisations would not be able to provide (see Siggelkow, 2007, p. 20). By moving beyond "purely theoretical motivation" (p. 21), in this thesis the use of case studies keeps modern theories firmly in touch with historical, real-life situations and prevents them from becoming "entirely self-referential" (p. 23). Furthermore, case studies present a gallery of complex realities that may challenge the validity of theoretical models and frameworks which are meant to cut through idiosyncrasies and uncover similarities across cases through simplifications. This is in the view of Siggelkow (2007, p. 21) an "important and insight-provoking violation" that stimulates "inspiration for new ideas", paving the way for modifying and adding new dimensions to existing theories and models. This issue will be covered in greater depth and details in chapter 8.

This thesis chooses and deploys a mix of historical sources from different segments of Victorian society to unpack the density of trust repair efforts, triangulating "multiple perspectives" from diverse parties – lawmakers, political economists, journalists or commentators, stakeholders, and bankers or organisational leaders – to construct a more holistic picture of the buildup of discourses and ideas that underpinned the underlying trust-related issues in Victorian banking (Lipartito, 2014, p. 290). This approach unveils how complementary or conflicting variables emerging from multiple sources interacted with each other, so as to bring to light "how actors of time" understood and responded to their immediate environ, and to uncover the "hidden processes at work" that explained the trajectory of nineteen-century banking (see Lipartito, 2014, p. 286). This section presents a category of sources incorporated in this study that serves to triangulate (1) how banking was portrayed, received, and regulated through legislation, paper media, and personal observation by political economists and banking elites, and (2) how government agencies, organisational leadership, and professional circles combined to exchange information about abstruse practices and narrate the fundamental relationships between banking companies, stakeholders, and regional interests (see Lipartito, 2014).

Systemically preserved and well documented, ***official published records***, such as the proceedings of parliamentary debates, committee publications, and law reports offer extensive sources for analysing the changes in the climate of contemporary political culture in relation to economic and public affairs (Pemberton, 1971). Debates and records about the Banking Co-partnership Act (1826), the Bank Charter Act (1844), the Punishment of Frauds Act (1857), and the eventual extension of limited liability to joint-stock banks (1858), for instance, revealed the changing moral and legal attitudes of lawmakers towards banking practices. These sources provide insightful information as to

how far the state saw the functions of banking as fundamentally distinct that justified the formulation of public policy in the public interest (see Wilson, 2014). Where responsibilities were shouldered by banking entities, these sources offer glimpses of the extent to which the state saw itself as a substitute or complement to improve the character of corporate management as the "primary line of defence" against banking misconduct or instability (Wilson, 2014, p. 133). Official documents also present opportunities for examining the efficacy of new legislation in recalibrating the corporate behaviour and reputability of banking companies, as part of the state's agenda of "articulating law with capitalism" and thus restoring public confidence in the financial marketplace (Wilson, 2014, p. 133).

This study also depends heavily upon different ***cultural sources*** such as newspapers, monographs, quarterly and literary reviews, pamphlets, and trade magazines to contextualise the professional and moral bearing of banking enterprises. *Newspapers*, in particular, are valuable for their detailed and systematic coverage of business or financial news – especially in the event of bank failures or financial turbulence (Taylor, 2014, p. 205). Apart from providing factual accounts of commercial affairs, they also articulated opinions on investment climate, rudimentary and non-specific advice for investors (Poovey, 2002) – and their growing importance was such that "many readers were hanging on their every word" (Taylor, 2014, p. 205). By the 1850s, some financial journalists began to assume the role as the watchdog in the marketplace (Hilton, 1991). Aided also by the repeal of taxes on advertising (1853) and stamp duty (1855), readership and circulation grew further as the Whig Chancellor of the Exchequer William Gladstone repealed the duties on newspapers in 1861. Given its profusion and popularity across the Victorian society, the press media is a rich reservoir of cultural materials to understand contemporary views and sentiments of banking activities and financial investment. More significantly, by exposing financial scandals to public view, newspapers assumed a critical role in mediating corporate reputation, making them a powerful tool of reputational sanctions in the nineteenth-century marketplace. Given the potential biases introduced by city rivalries and local patriotism to shaping how troubled banking institutions were presented by newspapers for public consumption, a wider selection of publications from different regions and cities is necessary for extracting diverse or even opposing interpretations of the events, and thus constructing a more neutral and balanced perspective of the firms' ethical and financial image (Lipartito, 2014).

Pamphlets, *quarterly reviews*, or *trade journals* represent opinions of political or economic elites. First published in 1843, the *Bankers' Magazine*, for instance, will feature strongly in this thesis for its systematic, scholarly, and insightful coverage of banking issues during the century. While Gambles (1999) finds it relatively easy to identify their readership whose political and economic views they were likely to represent, the question is whether these sources were sufficiently broad-based to represent public opinions. To quote Gambles (1999, p. 13) again, although "it cannot be assumed that editors and journalists succeeded in representing or moulding public attitudes they nevertheless strove to define their public and to negotiate a balance between guiding and reflecting public opinion". The fact that these publications were bound and indexed for future uses shows their enduring influence and relevance (Jones, 1996). They provide good sources for identifying how professional discourses converged with the climate of political economy to form an interpretative frame for analysing the business culture, common purposes, and shared values among banking organisations in the marketplace. Prior to the formation of professional bodies in the banking world, these sources are valuable for tracing how values and codes of conduct were (re)articulated to assess the legitimacy of bankers' behaviour and thus help adjudicate disputes between conflicting parties. These documents show how key values gradually became the guiding principles for banking organisations, ensuring improved conduct and compliance by means of disseminating specialised knowledge and insights of the experts (see also Jamal & Bowie, 1995).

This study also relies on ***corporate records*** to obtain insights into the internal conduct of joint-stock banks. However, the research and use of these sources, which were unavailable outside the United Kingdom, was limited by the global lockdown resulting from the pandemic. This thesis relies on the *minutes of annual general meetings*, which contained vital corporate issues such as corporate ownership, the election and dismissal of directors, and the review of corporate performance. A careful analysis of the reports and minutes issued during the years of crisis, in particular, reveals the strained relationships between boards of management and stakeholders, and how banking institutions (effectively) deployed different strategies to restore collegiality and trust. The types of information disclosed – and the preparedness of a banking company to do so – convey how far its true organisational culture was consistent with the spirit of openness, accountability, and truthfulness as purported in its corporate culture. This is one of the key points underlined in this study, given the power of bank management to determine what was to be disclosed in annual statements, and the recurring failures to provide

accurate reports on which information users could form a "considered judgement" (see O'Brien, 2014, p. 223). By providing insights into how disputes were resolved, how liabilities were shared and allocated, and how competing interests were reconciled, minutes of general meetings reveal the conceptualisation and articulation of trust and trustworthiness at the organisational level. These documents are useful for tracing the power relations and engagement between boards of directors and stakeholders when renegotiating the post-crisis terms of corporate governance, especially when advocates of joint-stock institutions seemingly overestimated the efficacy of disclosure requirements in enhancing corporate accountability (see O'Neill, 2014).

Deeds of settlement or *articles of association* contain details about organisational rules, hierarchies, and procedures that frame the overall structure of governance. They cover a wide range of strategic and managerial issues, such as the scope of the executives' duties and power, constitutional rights and obligations among interested parties, and the company's business interests and policies. These sources provide a setting for examining the trustworthiness of joint-stock organisations, especially when complaints about directors' incompetence and abuse of corporate power were rife as to challenge the robustness of the governance framework in regulating the executives' behaviour. They have much to disclose – not just about the role of governance in enforcing the monitoring system and thus ensuring accountability, but also the efforts undertaken by various stakeholders to overcome information asymmetry. Given how corporate relations between different interest groups were structured and defined in the company's constitution, these documents also provide valuable information about the measure of certainty embedded in the procedures for resolving disputes or financial losses, and how they compare to the boards' practical commitment to upholding stakeholders' interests. The directors' show of competence in conducting a bank's regular affairs, and their command of accountability, professionalism, and moral respectability when managing complex relationships with different parties during a crisis, can therefore be captured in relation to the evidence supplied by these sources.

Registers of shareholders – most of which were reprinted in newspapers – disclose the profile of individual shareholders in terms of social standing, financial qualification, occupation, places of residence, and volume of shareholding. Because of the unlimited liability rule, the constituency of shareholders was of critical importance to ensure and project banking security, ensuring that all deposits and notes issued were adequately backed by the proprietary's wealth. Registers yield information about the basis or criteria

on which shareholders were assessed for their credibility before they were recruited. The documents are also useful for examining the proximity between bank management and ownership in monitoring each other's actions insofar they were recruited from the same community. Following the outbreak of a crisis, the registers revealed the composition of the whole body of proprietary and the extent of their financial obligations, thus giving cues as to how far they could meet the creditors' claims. Over the longer term, changes in the constituency as captured in the registers are also of use for marking the alterations in the quality of shareholders and culture of shareholding. Such observation, in turn, gives rise to the debate over the validity of the long-held view that unlimited liability would inculcate sound corporate governance and give joint-stock banks a façade of stability. Tacitly and indirectly, this deliberation is also useful for tracing the changes (or softening) in public attitude towards the culture of shareholding, and how far shareholders deserved better protection by the legislature.

To a limited extent, this study also depends upon the bank and branch ***administration records*** to retrieve the correspondence between headquarters, branches, and customers. According to Orbell and Turton (2001), the regularity of correspondence indicates the cohesiveness of a bank's network. Within a relatively confined network, a local bank which maintained regular face-to-face dealings with customers would find such correspondence less necessary. The emergence of larger banks with extensive provincial branch network over time saw the need for creating a quick system of correspondence with local branch or customers. Information about procedural changes, staff appointments, and new rules or regulations were mainly conveyed from headquarters to local branch through *circulars*, which were then replaced by *instruction books* by the late nineteenth-century century. These documents form good sources for making inferences about a bank's control over administrative affairs and networks. They are suitable for examining, for instance, whether local managers enjoyed sufficient flexibility or discretion to respond to local circumstances. This, in turn, invokes a consideration of the degree to which a bank was prepared to align its corporate policies with local customs and requirements, thereby portraying its capability of representing the interests of the local community.

3.5 A Concluding Statement

On a methodological note, this thesis differs from the conventional, quantitative approach to looking at banking performance based on tightly defined economic criteria. It deploys

cultural narrative analysis to explore major trust-related issues in the banking industry. It also uses various historical sources to reconstruct the nineteenth-century contexts in which the banking companies were situated, thus generating useful information about the main locus of their business interests as exemplified by their respective economic importance and identity in a community. It also provides the opportunity for examining how the features of local networks shaped the circumstances under which trust and distrust were conceptualised, and thus a bank's choice of strategies for repairing trust. This study is aided by the use of the trust repair model theorised by Gillespie and Dietz (2012, p, 210), which suitably applies a multilevel perspective by looking at how "micro-level psychological processes and group dynamics" intersperse with "macro-level organisational and institutional forms" to influence trust repair. This feature provides the room for considering the divergent needs and perspectives of – and as such "how trust antecedents and repair vary" – across different stakeholder groups, as exemplified in a few contextualised, historical case studies.

By placing individual firms at the centre of contextualised analysis, the methodology applied in this thesis also pays attention to how banking institutions interpreted and responded to swings in public opinions, alongside the cues arising from socio-economic and legal-political changes that drove the overall market sentiment. Although there are lessons to be learned from history, the purpose of this approach is not to deduce from the past the blueprint for rebuilding a more trustworthy banking and financial system in the twenty-first century, but mainly to prove that trust repair could take place in different contexts which are unique in their own right, suffused with "inherently subtle and elusive" elements of human behaviour, perceptions, and feelings (Baumol, 1993, p. 7), as conditioned by the general environ in specific time and space (see Hollow, 2020). It will be demonstrated in the following four chapters that as the century advanced, there would be both changes and continuities as to the ways in which banking companies appealed to different stakeholders – and how both parties were constantly engaged in the process of learning to trust and to be trustworthy in the face of conflicts and uncertainty.

Chapter 4
Early Experimentations: The 1830s
A Comparative Study of Two Manchester Banks

4.1 Background

The nationwide banking crisis in 1825-6 was followed by a series of regulatory reforms aimed at bolstering the resilience and reliability of the banking sector. Removals of legal restrictions – coupled with a favourable economic climate in the mid-1830s – set in motion a significant growth of joint-stock banks in England and Wales (Turner, 2014). The enactment of the Banking Co-partnership Act of 1826 marked an important watershed because for the first time in history banking organisations were allowed "to constitute freely on the joint-stock principle" with unlimited numbers of partners in England (Turner, 2014, p. 36). The introduction of the Bank Charter Act of 1833 also paved the way for the formation of joint-stock banks within sixty-five miles of London, thus challenging the monopoly power once commanded by the Bank of England (Taylor, 2013a). Joint-stock banks were slow to catch on at first, owing to the unfamiliarity of the public with "the duties, rights and privileges of the new corporations", and the general doubt in the untested reliability of the new system (Collins, 1988, p. 68; Barnes and Newton, 2016). In the mid-1830s, they began to challenge private banks as the main type of banking. The trend coincided with a rise in the culture of shareholding, trade expansion in overseas, and a burgeoning demand for capital which followed the promotion of new railway companies (Turner, 2014). Nonetheless, the expansion of deposit and credit ushered in by the creation of new joint-stock banks also fuelled speculative activities, feeding into a rise in the share prices of banking and railway companies (Turner, 2014). There was, increasingly, an "adventurous spirit abroad" in commercial ventures and a wave of new joint-stock flotations (Capie, 2014, p. 12). The boom was reminiscent of the bubble years of 1824-5, and observers "were quick to assimilate the new promotions to familiar narratives of speculative mania and unchecked greed" (Taylor, 2013a, p. 46).

In the summer of 1836, the Bank of England set off a wave of monetary pressure in the financial market by twice raising the bank rate from 4 to 5 per cent to alleviate the drain on its gold reserves (Turner, 2014). The curb on monetary growth, which culminated in a depression in the late 1830s, severely tested the resilience of many joint-stock banks. Among those which succumbed to the pressure was the Northern and Central Bank of England. Founded in 1834 with a capital of £500,000 divided into fifty thousand shares of £10 each, the Northern Bank had a head establishment in Manchester and an extensive network of about forty branches (Northern and Central Bank of England, *Deed of Settlement*, 1834, p. 2; *Champion*, 4 Dec. 1836, p. 8). It constituted one of the high-profile bank failures because of poor management and abuse of corporate power by the directors. Another bank which experienced difficulties but survived the crisis was the Manchester and Liverpool District Bank. Established in 1829, it was among the earliest joint-stock banks in the same region. Notwithstanding its massive capital stock of £3 million and ambition to establish a branch bank "in every considerable town of the district", the District Bank was likewise embarrassed by its own chapter of mismanagement (*Manchester Courier*, 6 May 1843, p. 3).

The 1830s was an era in which many joint-stock banks were infected with what Robb (1992, p. 56) describes as "amateurish management". Using the Northern Bank and the District Bank as case examples – both of which were of Manchester origin and could similarly relate their difficulties to deficient banking knowledge – this chapter shows that early joint-stock banks had a steep hill to negotiate before they could regain public confidence. Given the complexity of joint-stock institutions and the challenges posed by a harsh economic climate, this chapter focuses on how bank directors engaged in the "simultaneous management of trust and distrust in a hostile environment" in which different parties are "just as inclined to distrust as they are to trust" (Lewicki et al., 1998, p. 439). Insomuch as both establishments were incapacitated by inexperienced management, this chapter explains why the Northern Bank directors fell in disgrace while their counterparts in the District Bank regained legitimacy. This comparative study attributes the above disparity to different sources of trust failures, following the argument of Schoorman et al. (2007) that the success of repairing trust requires one to understand how trust was damaged in the first place because different types of violations require different reparative responses.

Accordingly, this chapter addresses three overlapping but distinct questions: (1) how ability- and integrity-based violations were articulated, prompting shareholders to form

different assessments about the reliability of corporate reports; (2) how the directors responded to shareholders' suspicion and public criticisms with respect to different attributes of trust failures, and (3) how, in the absence of a robust legal framework, the boundary between publicity and secrecy was (re)drawn, leading to different considerations of how trust should be repaired and credibility restored to the system. The next section outlines the early development of joint-stock banks against a backdrop of considerable economic expansion, and the mounting wariness among lawmakers because of growing market volatility fuelled by banking activities and financial speculation. The third section provides a narrative account of the respective difficulties encountered by the Northern Bank and the District Bank. The fourth section then analyses how differently the integrity of each bank's managing body came under scrutiny, owing to the suspicion that shareholders had hitherto been misled by financial statements of the past. The fifth section recounts the fiduciary incapacity of the management, specifically the failures of the head office to monitor the behaviour of branch managers, allowing imprudent lending to swell considerably. The sixth section examines the adequacy of the corporate structure of joint-stock banks in monitoring the conduct of senior management, and how far the company law had coped with the fast-changing rule of the game in banking. Next, in the context of recurring scandals and crises during the decade, the chapter addresses the tension between the free market and state intervention in charting the regulatory path for joint-stock banks. The final section concludes the discussion.

4.2 The Coming Headwind

Riding upon the political rhetoric of the 1832 Reform Act which extended democratic franchise and electoral representation, the advocates likened joint-stock banks to an inclusive system of participatory politics that represented the ideals of openness, transparency, and accountability championed by the nineteenth-century liberal political tradition (Alborn, 1998). An anonymous writer, for instance, claimed in the *Mercantile Journal* (reprinted in *Bristol Mercury*, 13 Aug. 1836, p. 4) that joint-stock banks were "more open to public inspection and information – there is no mystery about them". The deed of settlement was by default the company's constitution, which laid down corporate rules and demarcated the rights and responsibilities between different categories of organisational members. In annual general meetings, vital corporate issues were openly teased out and discussed in collective consultation. The directors were required to present

truthful reports to shareholders and were held accountable for the firm's performance. The constitutional design was later encapsulated in the term "separation of ownership and control" famously coined by Berle and Means (1932) – under which shareholders were owners of the firm but the power of managing and using its assets was vested in the executives. These were theoretical niceties. In practice, banking was a mysterious business as opposed to the ideals of openness and transparency which many advocates of joint-stock banks were keen to propagate. Banking debacles in the late 1830s proved that the reality was far more in line with the cynicism of Adam Smith (1723-90) that in the joint-stock system directors or managers could not be trusted to treat other people's money with the same vigilance as in the case of a private partnership. The agency theory developed by Jensen and Meckling (1976) maps such a relationship as one between agents and principals, which recognises the possible risk that managers or directors might behave in a self-interested way that endangers owners' welfare.

In the mid-1830s, a wave of asset price inflation and speculative activities swept across the nation as credit growth gathered speed. As Thomas (1934) recalls, between June 1835 and January 1836, as the Bank of England from expanded its stock of credit from £25,678,000 to £31,954,000, many joint-stock banks used their new-found freedom to provide lending in huge excess of their paid-up capital, deposits and circulation. Some banks went as far as rediscounting worthless bills and providing credit facilities to shareholders against the firms' own shares. The President of the Board of Trade Charles Poulett Thomson pointed out that the same period saw the formation of between 300 and 400 new companies, and the nominal capital of new projects reached an enormous scale of about £200,000,000 (*Commons Hansard*, vol. 33, 6 May 1836, c. 688). "Any man", he said, "must be struck with astonishment at the fever which raged at this moment for those speculations".

In his budget speech on 6 May 1836, Whig Chancellor Thomas Spring Rice warned against excess market optimism and urged the public to treat new joint stock banks with "vigilance, caution, and prudence", which had sprung up "in all directions" in a period of "almost unexampled prosperity" (c. 672). Thomson was equally uncomfortable with the extraordinary growth of joint-stock banks, suspecting that without any restraint they were increasingly a threat to the nation's financial stability. Sir Robert Peel of the Tory Party likened the boom to the "mad projects" of 1825, and urged for the enactment of legislation to bring banking growth under control (c. 686). Liberal Member of Parliament William Clay moved for the formation of a select committee to inquire into the soundness of the

banking sector (*Commons Hansard*, vol. 33, 12 May 1836, c. 843). Till then, under the Act of 1826, the mandatory registration with the Stamp Office in London required nothing more than the names of shareholders, public officers, the location of branches, and where bills and notes were issued. As legal laxity led to the emergence of bubble companies, there was "no restriction whatsoever" on the activities of these new establishments (Thomas, 1934, p. 207). Banks enjoyed liberty to extend credit without limit, and "there were no rules governing their constitution, no obligations imposed on them in respect of their capital, and no provisions concerning the publication of their accounts" (p. 205). While speaking in favour of joint-stock principles as "one of the greatest discoveries of modern times" (*Commons Hansard*, vol. 33, 12 May 1836, c. 862), Clay was nonetheless concerned that the "vast and growing system of joint stock banking" had largely been left unmonitored that it had constituted "an uncontrolled element of tremendous power in the nation's monetary system" (c. 843).[1]

Chaired by Spring Rice, the Secret Committee of 1836 required every bank in England and Wales to complete a questionnaire and a balance sheet requiring particular of its assets and liabilities (Taylor, 2013a; Thomas, 1934). Damning evidence emerged that some banks were formed as "vehicles for speculation", and many legitimate ones were poorly managed (*Select Committee Report*, 1836, p. v). In his review, Thomas (1934, pp. 205-6) depicted the endemicity of the underlying problem, revealing that some directors had no "slightest knowledge of banking". Many held no shares in the institutions whose fortunes they were in charge, and used "devious and questionable methods" to meet their share qualifications. Corrupt or careless management helped themselves, their friends, and shareholders to the overdraft facilities without providing adequate security. In Northwest England, the Northern Bank joined rank with the infamous Agricultural and Commercial Bank of Ireland as the "classic instances" of such abuses. Elsewhere in the country, some managers or directors went as far as sinking the company's funds in the shares of other joint-stock institutions, effectively making shareholders "liable not only for that bank's own debts, but also for the liabilities of the other bank in which its funds had been invested". Some other leading joint-stock banks in the region – such as the Bank of Liverpool and the Union Bank of Manchester – weathered the storm because of their sound business and prudent management.

[1] Clay's speech was subsequently published as a pamphlet: William Clay, Speech of William Clay, Esq., MP, on Moving for the Appointment of a Committee to inquire into the Operation of the Act Permitting the Establishment of Joint-Stock Banks (London, 1837).

The debate then was not whether joint-stock banking was too risky a system to adopt – but whether legislation should be toughened to address the far-reaching consequences of banking activities upon the economy. Chapman (1979) argues that erratic practices aside, the profusion of capital, low interest rates, and deficient banking knowledge had compounded systemic risks by giving rise to excessive and unsecured credit. Sir David Salomons (1797-1873), an ardent supporter of joint-stock banks who was one of the pioneers of the prominent London and Westminster Bank, also conceded that the system required "some regulation to enable it to maintain the high character claimed for by its advocates" (1837, p. 37). In is *Practical Treatise of Banking*, James William Gilbart (1794-1863), the general manager of the same company, likewise echoed that failures "have arisen not from any unsoundness in the principles of joint-stock banking, but purely from mal-administration" (1855, p. 175). Both lawmakers and banking elites agreed that the system needed mending because of its economic importance to Britain as a trading nation and industrial powerhouse. As the latter parts of this chapter will explain, far from outlawing the system, the government slowed little political will to regulate the banks, basing their argument on the belief that under the drive of free-market capitalism, shareholder activism in the overall system of corporate governance could improve banking safety and stability more effectively than what legislation could deliver.

4.3 Two Dissimilar, Similar Accounts

Just a little under three years since its formation, overexpansion and imprudent lending drove the Northern Bank to the brink of collapse. In August 1836, its reputation tanked when a publication by Cassels – its London agent – revealed that the bank was in financial troubles, thus compounding the difficulties encountered by the firm to rediscount its bills in the London money market. The squeeze further tightened when the Bank of England refused to rediscount any bill that bore the endorsement of the Northern Bank. Because all its capital had been fully paid up, the bank could no longer raise any money from the shareholders. Strapped for cash, in early December 1836 the firm was forced to turn to the Bank of England for a bail-out. To forestall the looming disaster, the Bank injected £500,000 to secure the "perfect solvency" of the Northern Bank – on the condition that the latter must wind up all its branch establishments except that in Liverpool (*Champion*, 4 Dec. 1836, p. 8). The rescue package briefly restored market confidence. In less than a fortnight, the Northern Bank appealed to the Bank again for another £500,000, and the

news quickly reignited panics across the market (*The Times*, 16 Dec. 1836, p. 2). The Bank of England took upon itself "all the existing engagements" of the troubled entity, forbidding the latter to assume any new engagement until all its outstanding liabilities were liquidated (*Morning Post*, 24 Dec. 1836, p. 2). The aid from London had failed to fend off its ultimate collapse.

On 6 January 1837, the shareholders appointed an inspection committee – consisting of Thomas Harbottle, Thomas Broadbent, James Burt, and Edward Connell – out of the body of proprietary to investigate the company's state of affairs. The *Manchester Times* (7 Jan. 1837, p. 2) described these names as "a sufficient guarantee" that the inquiry would be "fairly, honourably and independently made". They soon found the directors' private ledgers, which documented that they had borrowed extensively from the bank. The *Newcastle Journal* (4 Feb. 1837, p. 3) pressed for an answer to the nature of the advances, asserting that in this pertinent issue "the public, and particularly the shareholders, have a right to be satisfied". As public confidence in the directors began to crumble (*Manchester Courier*, 25 Feb. 1837), and their moral respectability was at stake. During the general meeting on 23 February, repeated probing by shareholders forced Benjamin Braidley, the chairman and a director, to confess that some members of the board had acted upon their "superior knowledge" over shareholders and used the bank's funds for share-trafficking, "acting upon their superior knowledge over many shareholders of limited resources" (*Morning Post*, 25 Feb. 1837, p. 4). The transactions were documented in a private ledger to keep the clerks from knowing about their "share-jobbing tricks" (*Newcastle Journal*, 4 Mar. 1837, p. 3). Knowing that the bank would soon be in difficulties, two directors – John Fernley and John Bingon – had already sold their shares for "a handsome fortune" (*Manchester Courier*, 25 Feb. 1837, p. 3). On 20 April, the shareholders denounced the directors as "totally unworthy of further confidence", and a resolution was unanimously passed to remove them from office (*Morning Post*, 22 Apr. 1837, pp. 3-4).

Another bank which came under the limelight was the Manchester and Liverpool District Bank. Standing "high in general opinion", the company steadily extended its business networks well beyond its head office at Manchester (*Leeds Mercury*, 2 Feb. 1839, p. 8). Nonetheless, on 30 January 1839, about four hundred shareholders who gathered to receive the annual report learned that the bank had sustained no small losses amounting to £375,000, due to mammoth and misguided lending to two manufacturing enterprises (*The Times*, 7 Feb. 1839, p. 6; *Manchester Courier*, 2 Feb. 1839, p. 6; *Liverpool Mercury*, 1 Feb. 1839). In November 1832, the account of a woollen cloth manufacturer named

Taylor, Sons & Gibson opened at the Manchester branch – was found highly unsatisfactory, after which the bank appointed a committee to superintend the firm's affairs (*Manchester Courier*, 2 Feb. 1839; *Preston Chronicle*, 26 Jan. 1839; *Leeds Times*, 2 Feb. 1839). The account opened by Brown & Power at the Stockport branch had likewise turned toxic, and was subsequently placed under the committee supervision in September 1837 (*Manchester Courier*, 2 Feb. 1839). The intervention, coupled with a few capital injections by the bank, did little to revive both firms (*The Times*, 7 Feb. 1839, p. 6). Desperate to salvage what they could "out of the fire", the directors took the whole of their liabilities and carried on their business for some time (*Liverpool Mercury*, 2 Aug. 1839, p. 5). Losses swelled further and exceeded the entire reserved surplus fund that by the end of 1838 both accounts were forcibly closed (*Manchester Courier*, 2 Feb. 1839; *Leeds Times*, 2 Feb. 1839).

The District Bank's reputation suffered another blow when a rumour – which the *Chester Chronicle* (11 Jan. 1839, p. 4) reported to be "credited in the most respectable circles" – began to circulate that the directors – by taking advantage of their "full knowledge of all the circumstances" which later precipitated a sudden fall in the bank's share price – had already sold their shares to a Scottish bank to which they were well connected. The directors firmly denied the accusation, which resembled the charge against Fernley and Bingon of the ill-famed Northern Bank (*Leeds Times*, 2 Feb. 1839; *Morning Post*, 25 Feb. 1837). The District Bank nonetheless suffered no serious business interruption because its general business had been well managed, barring the "superlative blundering" which would have destroyed other mismanaged institutions (*Manchester Times*, 2 Feb. 1839, p. 2). Samuel Fletcher, the chairman and a director, maintained that overall bad debts remained "utterly insignificant", and the firm was "as competent to fulfil its engagements as ever" (*Preston Chronicle*, 26 Jan. 1839, p. 1; *Liverpool Mercury*, 1 Feb. 1839, p. 40). Despite the hostile economic climate, the District Bank garnered an annual profit of £86,000 – a success which Fletcher attributed not to "any adventitious circumstances" but "a regular progressive increase" of the bank's business (*Liverpool Mercury*, 1 Feb. 1839, p. 40).

4.4 Integrity: The Evidence of Guilt

Both the Northern Bank and the District Bank incidents showed that trust – just as Flores and Solomon (1998) posit – fitted not just into "the framework of duties and obligations"

(p. 209) but was also deeply engrained in "the ancient concern for personal character and relationships" (p. 211). Both cases were illustrative of Sternberg's (2004, p. 85) view that business knowledge and experiences are "only incidentally related to the intelligence, judgement and moral courage that are the essential directorial qualities". As distrust began to rise, the managing teams of both banks had to decide how "candid, contrite and cooperative" they should be when disclosing organisational difficulties (Gillespie et al., 2014, p. 390). This section presents two pertinent arguments. First, different attributes of trust violations drove the injured parties to re-evaluate the legitimacy of financial reporting and secrecy differently – and therefore, their respective readiness to renew trust in the light of present information. Second, how stakeholders perceived the management's motives and types of violations also determined the outcomes of crisis disclosure and communication. According to Elsbach and Currall (2012, p. 85), injured parties tend to be more forgiving if failures are attributable to "honest incompetence". This is because incompetence is more recognisable as "both situationally dependent and temporary", while a lack of integrity is seen as "an always-controllable and stable personality trait".

The defensive approach taken by the Northern Bank at the outbreak of the scandal was neither open nor credible in the eyes of the shareholders, thus "compounding and escalating the original trust violation" (Gillespie et al., 2014, p. 390). The directors were slow to account for the company's failure, citing the reason that under prevailing circumstances it was imprudent to provide explicit statements which they considered "necessarily incomplete" (*Leeds Intelligencer*, 7 Jan. 1837, p. 7). No general meeting took place until 23 January – just nine days before the firm was supposed to wind up. Deliberate secrecy and the lack of a credible account for the crisis provided leeway for the press to dominate the narrative of the scandal (Gillespie et al., 2014, p. 391). The tardiness was "extraordinary", wrote the *Manchester Times* (7 Jan. 1837, p. 2), given that shareholders had a very limited window to form their judgement. The *Newcastle Journal* (4 Feb. 1837, p. 3) was equally unimpressed by the directors' refusal to admit reporters to the meeting, during which the board supplied nothing more than "a semi-official document" that gave no proper account for the ongoing situation. Suspicion and uncertainty lingered, as shareholders were obliged to be satisfied with verbal replies to their questions without any official statement until a month later.

As shareholders gathered on 23 February, Braidley declared that under the worst possible circumstance the loss would not exceed £1 per share. The report was greeted with cynicism. Broadbent – together with Stell, a director who took office just over three

months earlier – considered the financial statement "far too favourable" (*Manchester Courier*, 25 Feb. 1837, p. 3). The investigation led Harbottle to the same verdict that the bank had never been in a condition "to make a dividend of one farthing" (*Morning Post*, 25 Feb. 1837, p. 4). Just a few months before the bank imploded, the board declared a dividend of 8 per cent, and "pretended to show" a reserve fund of £40,000 (*Newcastle Journal*, 4 Mar. 1837, p. 3). The last straw came when it was discovered that some directors had misappropriated the bank's funds for share-jobbing. By posting their shares for which they did not pay as security, the directors severely depleted the firm's paid-up capital and put its survival at stake (Taylor, 2013a). The company's opaque bookkeeping was a "deliberate strategy", calculated to hide its dreadful state and the directors' misconduct from public view (Taylor, 2013a, p. 59). The melodrama was of such a scale that two directors – Braidley and Moult, and Lyle the accountant, were summoned before the Secret Committee to account for the scandal. Lyle admitted that bad debt was artificially reduced to allow the fabrication of high dividends from year to year – an offence which Robb (1992, p. 69) denounces in his study of Victorian financial crimes as "the lie to the ideal of safety through publicity".

Both banks differed starkly in their respective approach: while the Northern Bank stubbornly stuck to mystification and constant denials, the District Bank self-disclosed the losses and openly acknowledged the underlying problems albeit after a premeditated delay (Gillespie et al., 2014). Like their Northern Bank counterparts, the integrity of the District Bank directors came under suspicion at first, given the tendency of the public to associate secrecy with malicious intents. Impeded by limited information and market uncertainties, the directors had a "very delicate and important responsibility" to briefly suspend disclosure in defence of the company's credit and shareholders' interests (*Manchester Courier*, 2 Feb. 1839, p. 6). The board had suffered "scorn and reproach" for the delay but were "conscious that they had proceeded in an honest course" (*Manchester Courier*, 2 Feb. 1839, p. 6). While feeling obliged to provide "the fullest and earliest information", the directors only did so when they had in legal possession of the debtors' estates and obtained sufficient details "as made it practicable to report to the shareholders with anything like accuracy" (*Manchester Courier*, 2 Feb. 1839, p. 6). The dilemma clearly displayed a trade-off between accuracy and timely disclosure, when meticulous investigation was required to present shareholders a trustworthy diagnostic account to make informed decisions (Gillispie & Dietz, 2009; Pfarrer et al., 2008).

The (in)accuracy of the company's past financial reports also exposed the directors' conduct to further scrutiny. In July 1836, the District Bank continued to issue new shares and declared a dividend of 7½ per cent although the firm was already in troubled water (*Manchester Courier*, 2 Feb. 1839, p. 6). The reports revealed "a very great surplus fund" and ample financial resources to cover its liabilities, and that dividends could be paid out "without trenching on their resources", when in fact all the funds had been lost (*Leeds Times*, 2 Feb. 1839, p. 8). Shareholders were nonetheless satisfied that the reports were products of pure miscalculation rather than premeditated mischief (*Manchester Courier*, 2 Feb. 1839). The crisis of both banks alike proved that publicity afforded by corporate reporting provided shareholders no absolute protection. Gilbart (1855, p. 172) warned against using published balance sheets as "a fair criterion" for evaluating the financial of an institution. The involvement of directors introduced potential biasness into the process, rendering financial reports "perfectly inefficient as a protection against fraud", he noted. John Ramsay McCulloch (1856, p. 9), a Scottish economist, commented on the ease "to dress up a return, to make a rickety or bankrupt concern appear to be flourishing and wealthy". The retrospective study by Freeman et al. (2012, p. 224) also similarly concludes that directors exploited their strategic control over informational disclosure to prepare "any statement they like for the proprietary". Condensed into "a small number of headings", summary accounts instead created opportunities for the board "to conceal rather than clarify important information". As the latter part of this chapter argues, by the close of the decade, legislators and bankers alike concurred that insofar there were tensions between shareholder agency and bank administration, investors were primarily responsible for their own interests by exercising vigilance. In their view, failures and crisis would teach investors "how their companies worked and remove the threat of shocking disclosures and violent meetings" (Alborn, 1998, p. 112).

As to how the directors exonerated themselves of fraudulent reporting, again the contrasts between both banks were obvious. The District Bank directors referred to their combined ownership of 13,000 shares, which amounted to nearly "one-sixth of the whole stock of the bank", as the weightiest proof of their innocence (*Leeds Times*, 2 Feb. 1839, p. 8). In addition to their "full proportion of the new shares at £5 premium", and the board also took "nearly four thousand shares at £6 premium" (*Manchester Courier*, 2 Feb. 1839, p. 6). Interestingly, the bank owed the directors an amount "more than the entire capital of a great number of joint-stock banks in the country", nulling the suspicion that the board were conspiring against the shareholders (*Leeds Times*, 2 Feb. 1839, p. 8; *Preston*

Chronicle, 26 Jan. 1839, p. 1). Conversely, by selling the bank's shares for quick gains before the crisis broke out, the Northern Bank directors ignited shareholders' wrath for slighting their duties in doing "what was right and just" to defend the "deep interest" of the firm (*Manchester Courier*, 25 Feb. 1837, p. 3). The *Newcastle Journal* (4 Mar. 1837, p. 3) reproached that the directors, having been assigned a position of "solemn trust and responsibility", had instead abused their power for "their own personal aggrandisement". "The directors might be ignorant of banking", the paper decried, "but in share-jobbing the unfortunate shareholders to their cost have found they have been wise as serpents".

Interestingly, to the very end those who retained their integrity and good conscience were still well-spoken of, despite their fiduciary failure. On the day of his sudden death on 3 April 1845, the *Manchester Courier* (3 Apr. 1845, p. 8) wrote of Braidley as a "benevolent and worthy gentleman". A native of Durham, he came to Manchester at an early age and took up apprenticeship in a firm of linen importers. In 1813, Braidley became actively involved in the Bennett Street Sunday School – an institution to which he remained devotedly committed until "his latest hour". In 1835, he was twice nominated Conservative candidate for Manchester but failed to win the seat. By becoming a commission agent, Braidley acquired substantial wealth but lost the greater part of it through the failure of the Northern Bank. The local daily described his connection with the bank as "unfortunate", resulting in him being "most unjustly" attacked by his enemies. "If ever there was a being in the world who never ought to have had an enemy" – the paper commented – "he was the man" (p. 8).

4.5 Competence: The Trouble with the Novice

The Northern Bank and the District Bank affairs took place in "a period when the inexperience of the managers in banking affairs was obvious" (*Liverpool Mercury*, 2 Aug. 1839, p. 5). In both cases, a want of banking knowledge and expertise at the top of organisational hierarchy begat a flawed branch management system, giving rise to what Child and Rodrigues (2004, p. 144) dub as a "double agency" problem. This arises "when the process of holding agents to account for the attainment of goals given to organisations involves two sets of accountability and control relationships, reflecting the presence of agents at two main levels". The first agency problem emerged when directors and managers failed to protect the economic interests of stakeholders. The second was traceable to the failure of local managers across the branch network to act in compliance

with the rules and policy at the head office. In the light of these issues, this section addresses two trust-related implications when different organisational agents failed to live up to their callings. It begins by examining the fragility of "role-based" trust, which in theory should enhance organisational trustworthiness by reinforcing the positive expectations that organisational agents are technically competent to discharge the duties and obligations accompanying their roles (Kramer, 1999, p. 578). The section then goes on to consider the degree to which organisational rules and controls could reinforce trustworthiness and accountability by creating "shared understandings regarding the system of rules regarding appropriate behaviour" (p. 579).

Robb (1992, p. 20) suspects that in the nineteenth century "anyone could form a banking company, regardless of experience or financial resources or business probity". The fact that none of the Northern Bank directors had any previous banking knowledge did not check their ambition to establish "a very extensive business" by opening branches "with amazing speed", and lending more generously than its rivals (Joplin, 1837, p. 117). Seltzer (2018) observes the regularity with which aggressive branch banking coincides with a slide in prudence associated with rapid credit growth and indiscriminate risk-taking. Like the directors and their friends, shareholders were privileged to enjoy almost unlimited access to credit. The investigation by the Secret Committee revealed that some of the advances "were out of all proportion to the means and standing of the persons concerned" (reprinted in Thomas, 1934, p. 285). Moult testified to the "shameful" credit policy: three (unnamed) individuals alone owed the bank a total of £124,000, posting the company's own shares as security. The number of branches – some of which were as remotely situated as in Bristol and Nottingham – were more than what the head office could effectively monitor and control (*Newcastle Journal*, 17 Mar. 1838; *Manchester Courier*, 24 Feb. 1838; *Leeds Intelligencer*, 9 Sep. 1837). Without proper inspections, inexperienced branch managers overindulged borrowing customers with "great sums of money which they ought never to have had" (*Leeds Intelligencer*, 9 Sep. 1837, p. 7). Braidley intimated that the bank had never been in a habit of refusing to grant a loan. Broadbent pointed out the "miserably bad" situation at branches where heaviest bad debts were incurred: at Leeds alone, losses amounted to £82,000, whilst Nottingham and Sheffield each suffered a loss of £20,000 (Thomas, 1934, p. 285).

Weak banking knowledge and a profligate corporate culture exposed the directors' failure to appreciate their "position of reposed trust" to manage risks responsibly (Wilson & Wilson, 2013, p. 68). Failing to understand the risks they were dealing with, the

directors “reduced their business to gambling” and passed the costs of failures on to the rest of the society (Graafland & van de Ven, 2011, p. 614). The press stridently criticised the management for their reckless expansionist programme, accomplished with little regards to the interests of stakeholders. *The Times* (2 Dec. 1836, p. 2) reproved that “no bank could be in a situation to make so humiliating an appeal for assistance without having previously incurred great losses, and done an enormous amount of bad business”. The *Morning Post* (3 Dec. 1836, p. 2) blamed the woes on its “injudicious management”, describing its branch network as “too complicated and unwieldly for the power of its conductors”. The *Newcastle Journal* (31 Dec. 1836, p. 2) reported that the branch agents demonstrated their zeal by “the multiplication of issues and discounts” rather than “cautious methods of business and a careful selection of customers”. By overextending itself, the Northern Bank had in effect become too swollen to be of any economic value to the community (see Wilson & Wilson, 2013).

The District Bank directors were also chided for their “mistaken hope” in trying to salvage two failing enterprises by impetuously taking over and carrying on their business (*The Standard*, 1 Aug. 1839, p. 3). A shareholder named Thomas Gisborne mocked that the directors had *de facto* made themselves “calico printers and wool staplers”, squandering an enormous amount of capital on trades which the bank knew nothing about (*Liverpool Mercury*, 1 Feb. 1839, p. 4; *Leeds Times*, 2 Feb. 1839). Gisborne criticised the directors for knowing “nothing whatever of the concerns of the bank”. “Of the twelve or fourteen directors”, he fumed, “nine of them were dumb dogs, and that the other three would not bark” (*Leeds Times*, 2 Feb. 1839, p. 8). The bank’s branch management system was also a farce: in many cases, credit limits and bad debts far exceeded the amount permitted by the head office, and the soundness of an account was judged solely on the volume of credit without giving due consideration to its remunerative character (*The Times*, 7 Feb. 1839). Given the bank’s heavy concentration of capital on two fledging enterprises via the Manchester and Stockport branch, *The Times* (7 Feb. 1839, p. 6) insinuated that the management had been unduly swayed by local influences:

> The prejudices which invest a provincial town – the selfish interests which actuate a manufacturing community – the personal jealousies that dry or clog the useful intercourse of life in every narrow neighbourhood are felt by a local bank, and, if not actually participated, must at least be regarded and humoured.

As in the case of many local banks who saw themselves as "representatives" in their respective regions, it was common that a "real sense of local pride and independence" had lured many shareholders and customers away from other larger counterparts "with a head office hundreds of miles away" (Alborn, 1998, p. 103). Retrospectively, it was perhaps unsurprising that the District Bank endeavoured to perpetuate its "relatively local sphere of influence" by keeping its customers afloat as long as possible.

The District Bank affair also exemplified the failure of the company's rules, procedures, and reporting lines to hold organisational members in check (Gillespie & Dietz, 2009; Perronne et al., 2003). The inspection committee intimated that shareholders had perhaps inadvertently expected too much of the board because directorial duties were improperly defined (*Liverpool Mercury*, 2 Aug. 1839). Inexplicit job scope had also led Jackson, the general manager, to be overcharged with responsibilities (*Liverpool Mercury*, 2 Aug. 1839). Contrary to the oft-repeated scene that a manager was "almost always made the scapegoat" in the event of a crisis, the directors instead lavished "the completest and most unqualified exoneration" on Jackson (Grindon, 1877, p. 257). While the committee testified to his "zealous consideration" of the bank's interests, they bemoaned that "the excess of his zeal" had turned out to be his "greatest fault", driving him to undertake whatever course which he deemed might be accomplished with any chance of success (*Report of the General Board of Directors*, 29 Jan. 1840). In 1840, Jackson left the bank with a broadly intact reputation, which later led to his appointment to a "high position" as a bank manager in the Isle of Man (Grindon, 1877, p. 257). Following the District Bank mayhem, no one was publicly held accountable, given the board's inability to identify the personal responsibilities and public obligations occasioned by fiduciary failures (*Leeds Times*, 2 Feb. 1839; Jaffer et al., 2014b). The affair exemplifies an important lesson that "any method of enhancing trustworthiness is without direction" unless the objectives of the agent's role are properly defined and understood, (Jaffer et al., 2014b, p. 352; Miller, 2011).

4.6 Governance, Transparency, and Accountability: The Limits of the Law

The growing importance of joint-stock banks presented legislators with new challenges of adapting the existing regulatory framework to the rapidly changing rules of the game. Growing business and organisational complexity made it more difficult for investors to monitor the behaviour of directors and detect "derelictions of duties" (Robb, 1992, p. 3).

Unequal power relations and information asymmetry rooted in the constitutional design of joint-stock corporations compounded the culture of secrecy in banking and finance, thus undercutting the capacity of the company law to make the new system more transparent and accountable. As Alborn (1998, p. 105) observes, in banking "certain things could not be talked about" in a system which was supposed to feature "full and open discussion", and it was not uncommon that "controversial" issues were excluded from their meetings. Notable bankers did not see this as an immediate threat to the sector's credibility. To Thomas Joplin (1837, p. 49), a director of the National Provincial Bank of England, "to tear the veil from the mysteries of banking too suddenly" would prove too risky for new joint-stock banks, many of which were coping with the delicate transition from the old regime of secrecy associated with private banking to "one of greater publicity". Gilbart (1855, p. 172) also warned that complete publicity "lays the bank open to attacks from its rivals or opponents". Financial confidentiality, meanwhile, offered banks strategic advantages over their rivals (Freeman et al., 2012; Robb, 1992). Gaa (2009) also agrees that secrecy is a requisite component of corporate governance that prevents sensitive information from escaping to the public. Given the legal limitations in establishing a "basis of trust", this section considers how the press media and participatory politics in joint-stock banks challenged directors' control over informational disclosure and complicated trust repair efforts (Gillespie & Dietz, 2009, p. 132).

First, insofar the company law did not require joint-stock banks to present any audited report to shareholders at large, the press took up "the key issues of disclosure and investigation", acting as an extra-legal force to bear upon the companies to ensure good conduct and bring corporate abuses to light (Tambini, 2015, p. 124). Consistent with this perspective is Borden's (2007) analysis of the role of financial journalists in exposing corporate scandals and matters of public concern, which answers to legal limitations in cementing the system of governance. As Taylor (2013b, p. 701) asserts, "in disseminating opinion and information on the companies that competed for the public's capital", to some extent the press was able "to make up for the lack of legal control from the courts and the legislature". Far from "discreetly ignoring debates on contentious topics" – such as the pay, privileges, and performance of the management, the press provided "multifaceted accounts" of the proceedings of general meetings, turning the "internal politics" of joint-stock corporations into "public property" (Taylor, 2013b, p. 685). Tambini (2015, p. 136) recognises this as "a clear institutional role" of the press in holding public companies to account and warning investors about the downside risks in the market. "A simple way to

understand this role", as the argument goes, "is to see it as a framework of rights and duties that have been developed in the context of legal and regulatory disputes and form the institutional framework which governs and shapes professional practice".

Indiscriminate attempts by the Northern Bank directors to enforce secrecy when the crisis broke out amplified distrust and provoked public inquisition further when the affair was of considerable public interest (Kramer, 1999). Taylor (2013b, p. 686) observes that newspapers "were alert to rumours of difficulties or rifts and were more likely to send along reporters when they sensed a scandal". As the dark secret began to unfold, the directors filed a lawsuit against *The Times* and the *Morning Post*, accusing them of circulating rumours "with a view to discredit the bank" (*Lancaster Gazette*, 31 Dec. 1836, p. 1). Given that the directors' integrity was already at stake, their injudicious attempt to silence the press backfired. By contrast, the District Bank directors seemed to have rightly anticipated the danger of stoking public anger had the losses been disclosed by the third party in a manner over which they had little control (*The Standard*, 1 Aug. 1839). *The Times* (5 Jan. 1837, p. 5) reasoned that because "ignorant or careless administration" of a joint-stock company was a matter of public concern, the public "have a right to the knowledge of it" so as to avoid the ensuing pitfalls. In the event of a fraud, the case for "full exposure" was stronger still – and at any rate "the whole must come out in due time", the paper insisted.

Because legislation could only prescribe legal duties and mandate "an ethical minimum of obedience to the rule of law", it cannot articulate "any duties concerning the intentions and virtues of economic actions" (Koslowski, 2009, p. 24). Victorian newspapers filled the gap by acting as "a key reputation intermediary", providing the ethical lens through which the public scrutinised and appraised the moral character of corporate leaders (Taylor, 2013b, p. 682). Companies with a good reputation thrived and survived. While as "a self-regulating device" the concern for reputation would not necessarily induce directors to conduct themselves trustworthily, the Northern Bank directors were severely punished with reputational losses for their bad behaviour (Taylor, 2013b, p. 682). Censures and criticisms were packed with recurring emphasis on the "duty of loyalty" which attended the directors' role in advancing the interests of the company and stakeholders (Baums & Scott, 2005, p. 37). On the moral lapses of the Northern Bank management, the *Joint Stock Banker's Journal* (reprinted in *Newcastle Journal*, 27 May 1837, p. 3) castigated that they had failed to recognise "the very high standard on integrity" expected of directors, and "the man who lowers this character in his own person, is guilty

not only of his own individual degradation, but of a public injury". The *Newcastle Journal* (4 Mar. 1837, p. 3) reported that "the *exposé* of the manner in which this bank has been conducted is one of the most shameful and infamous that could possibly be imagined".

Second, if legislation had failed to compel bank directors to come clean, then the constitutional provision for shareholder investigation would do the job. On one hand, the Victorian boardroom was likened to the notion of "honourable secrecy" found in British political life (Vincent, 1998). By the decree of the *Deed of Settlement* (1834, p. 7), the Northern Bank only allowed shareholders to inspect any books or accounts via the intermediation of an inspection committee, which they had the power to appoint out of the proprietary. The District Bank prescribed similar clauses, obliging auditors to "observe secrecy in respect to the state of the accounts of individuals" (Manchester and Liverpool District Bank, *Deed of Settlement*, 1831, p. 16). By contrast, general meetings and formal enquiries provided shareholders the platform to expose the management's actions and dealings to public gaze, and on this score joint-stock companies were compared to "a sort of ideal republic" (Alborn, 1995, p. 205). This provision was commonly available when the constitution did not accommodate individual rights of inspecting the accounts. Although a shareholder in a public company was increasingly recognised as "an individual owner of property" rather than as "a member of a collective association", throughout the century general meetings remained a "sacrosanct" institutional feature which embellished the joint-stock economy with a façade of openness and accountability, during which shareholders exercised their rights to understand corporate matters more perfectly (Freeman et al., 2012, p. 170).

Transparency appeared to go hand in hand with responsible management (Freeman et al., 2012). Fletcher was keenly aware that the District Bank affair was of considerable public interest, warning that "[t]he eyes of the public and the shareholders generally are upon us" (*Manchester Courier*, 2 Feb. 1839, p. 6). A shareholder and new director named James Heald held the committee of investigation – of which he was a part – a vital corporate organ to conduct an inquiry until "a full light" was cast upon those toxic accounts which had been misguidedly carried on under "the system of secrecy" (*Manchester Courier*, 2 Feb. 1839, p. 6; *The Standard*, 1 Aug. 1839, p. 3). Composed of nine members – including two auditors and four newly elected directors – the committee devoted "seventy hours with scarcely any interruption" to the investigation, to the end shareholders might receive "as complete a report as possible" (*Manchester Courier*, 2 Feb. 1839, p. 6). The directors, meanwhile, furnished the committee with "every facility"

and crucial information, vindicating their trustworthiness that promised greater transparency.

As Freeman et al. (2012, p. 237) construe, however, the shift to indirect representation by the committee of investigation in fact paradoxically signalled a decline in corporate transparency, because shareholders must learn "to take much more on trust" that the elected representatives would undertake the task with competence and honesty. While the Northern Bank investigators were empowered by shareholders to call for any books, documents, or writings "without any hindrance or denial whatsoever", they were pledged to secrecy "in respect to the state of accounts of individuals with the bank" (*Deed of Settlement*, 1834, p. 7). As an inspector, Harbottle bemoaned that it was "a delicate matter for them to make any statements relative to their discoveries" (*Manchester Courier*, 25 Feb. 1837, p. 3). The "gentlemen of the highest integrity" who formed the committee and new directory were apparently the strongest assurance that shareholders' interests would be justly represented (*Manchester Courier*, 24 Feb. 1838, p. 3; Freeman et al., 2012). Unconvinced, a shareholder named Ogivie moved for the appointment of auditors to re-examine the accounts – a move which the new directors took as "an affront" to their honour (*Manchester Courier*, 24 Feb. 1838, p. 3). The case exemplified here is an illustrative example of shareholders' suspicion of the inspection committee, especially where transparency was generally lacking (Freeman et al., 2012).

4.7 Trust: By Means of Learning or Legislation?

Contemporary perspectives often attribute financial crisis to the lack of robust state regulations (Graafland & van de Ven, 2011; Gillespie et al., 2012). The early Victorian pattern, however, differed markedly from the contemporary recognition of "strong forms of regulation" as the *conditio sine qua non* for restoring public confidence in banking companies (Gillespie et al., 2012, p. 200). Indeed, the budget speech by Spring Rice on 30 June 1837 revealed the fading zeal of the Whig government to clean up the banking industry, citing that the crisis was "rapidly passing away" (*Commons Hansard*, vol. 38, 30 Jun. 1837, c. 1725). Neither did the inquiry of the Select Committee of 1836 translate into tangible banking reforms. William Hutt, a Liberal Member of Parliament, regretted that the nation's monetary system had not been placed under "a searching and complete revision" (c. 1732). This section presents two perspectives which explained the government's reluctance to place banking enterprises under more rigorous regulatory

controls. There was first the capitalist order in early Victorian Britain, which emphasised the importance of shareholders' responsibilities to invigorate banking governance. Second, commercial affairs were largely seen as private matters between the contracting parties. How these perspectives worked out in practice showed that government regulations did not share as much importance as the role of individual parties in driving responsible banking behaviour.

The Whig administration framed its economic policies around the nineteenth-century belief that underlined the moral duty of shareholders to discharge their financial obligations as owners in public companies. Unlimited liability would incentivise shareholders – especially those who were wealthy because they had more to lose – to actively participate in the company's governance and monitor the management closely, leading to the belief that there was little need for "investor protection legislation" (Hickson & Turner, 2005, p. 178). In fact, the Northern Bank fallout showed that many wealthy shareholders were just as equally inexcusable and deplorable as the management. Together with the directors and their friends, they owed the firm an astounding total of £443,000. Exploiting the legal loophole that no partner could sue another for a debt, they refused to pay their dues and "got off practically scot-free" (Thomas, 1934, p. 292). Public sentiments swung against the shareholders as they tried to "wriggle free from their liabilities" (Taylor, 2013a, p. 58). Even those who were of "the humbler walks of life" and had "suffered markedly" did not receive much sympathy (Thomas, 1934, p. 292). Spring Rice argued that under the current law, "parties might be ruined to an extent scarcely calculable … a door would be opened to fraud, and considerable difficulty and derangement would be created in the commercial world" (*Commons Hansard*, vol. 40, 6 Feb. 1838, c. 818). Enabling the banks to recover payments from shareholders or customers thus became a "more pressing issue" than banking reforms (Taylor, 2013a, p. 58). A bill was subsequently introduced and pushed through both Houses to allow public officers "to sue shareholders for debts on the same terms as non-shareholders" (Taylor, 2013a, p. 58).

The government's conviction was indisputably clear: it was up to individual banks and shareholders at large – and not lawmakers – to make or break the new-found system. As Spring Rice disclosed in his budget speech in May 1838, no legislation "could protect the public from the effects of commercial vibrations" (*Commons Hansard*, vol. 42, 18 May 1838, c. 1418). The *Manchester Times* (11 Nov. 1837, p. 2) echoed the sentiment, commenting that "[n]o act of parliament can provide against such contingency", and

shareholders were responsible for putting "men devoid of talents and integrity" in charge. The Chancellor told the House that the *Report* – published after the inquiry by the Select Committee of 1836 – was meant to furnish amateurish joint-stock banks with "the benefit of the example and experience of the older banks" (*Commons Hansard*, vol. 44, 27 Jul. 1838, c. 720). It did not, as Taylor (2013a, p. 59) remarks, culminate in "a roadmap for legislation". Clay's major recommendations in the *Report* – namely audit, publicity, and limited liability – attracted limited support (Taylor, 2013a). Interestingly, some bankers endorsed Clay's recommendation for improved publicity and audit, so as to distinguish themselves as public entities from their private competitors whose accounts were largely kept secret. Still, with most legislators and bankers approaching the crisis as a "correctable problem of shareholder ignorance" instead of systemic flaws, it was not until the 1840s that banking reforms became tangibly noticeable (Alborn, 1998, p. 112).

Second, legislation played little role in helping banking companies and stakeholders to resolve matters of grievance insofar as they were regarded as private matters. What drove the course of actions was participatory politics in public companies, as demonstrated via the iterative exchanges between the directors and various stakeholders. The assertiveness demonstrated by inquisitive shareholders was itself an expression of their reluctance to be passive recipients of wisdom from the directors (Alborn, 1998, p. 112). What was clear from the Northern Bank incident was the constantly changing status of trust and distrust in the relationship: at any rate, trust is "continually under negotiation … built out of (and destroyed in) routine frustrations, promises, and commitments" (Flores & Solomon, 1998, p. 223). Between 1837 and 1838, the odds continued to stake against the new management. As the investigation went on, more losses emerged from unexpected quarters, as shown in the worse-than-anticipated financial result delivered on 31 August 1837. Dissatisfied with the "very illusory statement", a shareholder wrote to the *Manchester Guardian* (21 Feb. 1838, p. 3), urging his "fellow-sufferers" to press for "a correct and tangible statement" in the forthcoming half-yearly general meeting, during which the estimated value of the firm's assets was embarrassingly slashed by a whopping £45,000 – most of which was attributable to "one large account, in which the grossest deception has been practised" (*Manchester Courier*, 24 Feb. 1838, p. 3). A motion was unanimously passed that the former directors should return the gains from the sale of the bank's shares, and the silver plate obtained from shareholders "under false pretences" (*Manchester Courier*, 24 Feb. 1838, p. 3). It is clear from the iterative exchanges that inferences deduced from corrupt regime in the past, and the shocking

discovery of fresh losses, also inevitably led the shareholders to revise their expectations about the trustworthiness of the present management (Kramer, 1996).

The District Bank, on the other hand, fared much better. The fact that the directors kept their shares and identified themselves with the shareholders' loss gave them much stronger moral authority to unite and mobilise the support of all disgruntled parties. The board claimed full responsibility, considering it "unworthy of them to shrink from the difficulties into which they had brought the bank" (*Preston Chronicle*, 26 Jan. 1839, p. 1). Bound together by share ownership, both directors and shareholders were effectively "all in one boat", following which all parties must cooperate and abstain from actions that could "swamp that boat" (*Leeds Times*, 2 Feb. 1839, p. 8; *Manchester Courier*, 2 Feb. 1839, p. 6). Once the problem was identified and "mutually recognised", the management and shareholders worked together "by way of a serious understandings and renewed commitments" (Flores & Solomon, 1998, p. 223). In the half-yearly meeting on 31 July 1839, the board presented a plan for reorganising managerial controls over "every department and every branch" (*The Standard*, 1 Aug. 1839, p. 3). With "a rigid system of discipline" in place to bring branch managers under closer inspection, the reform produced the intended results (Gilbart, 1855, p. 183). By the middle of the century, the District Bank had developed a pool of staff "with equal levels of training and education" to manage the branches (Barnes & Newton, 2018, p. 463), facilitated by local managers with good managerial literacy and knowledge of the community (*Board of Directors Minutes*, 26 Feb. 1859 – 15 Sep. 1871).

Notwithstanding the scandals and setbacks, joint-stock banks remained on the course of gaining public confidence. Given only "a small number of failures", Spring Rice was confident that "the principle of joint-stock banks was good, and would prove beneficial to the country" (*Commons Hansard*, vol. 44, 27 Jul. 1838, c. 720). With unlimited liability remaining firmly in place, the *Manchester Times* (11 Nov. 1837, p. 2) stressed that "the public has not lost one shilling by the failure of these banks". Although a comprehensive banking reform did not follow, the crisis had arguably left behind a lesson and legacy for stronger banking governance. Yet, where information and balance of power are asymmetrical, empowering shareholders to monitor the behaviour of bank management is notoriously problematic. In this context, trust is more than mere "contractual relationships" (Flores & Solomon, 1998, p. 210), where shareholders or ordinary users are dependent upon the executives for their specialised expertise and virtues (Graafland & van de Ven, 2011). Another lesson is that there was essentially a twofold, mutual

response to the dynamics of trust and distrust after each crisis. First, directors must overcome stakeholders' negative inferences that their (renewed) trust might again be abused. Second, stakeholders who chose to renew their trust must simultaneously accept the risks this decision may entail, and wilfully overcome the instinct to distrust induced by violations of the past (Flores & Solomon, 1998, p. 216). No piece of legislation, it seemed, was versatile enough to encapsulate the constantly evolving dynamics, where contexts differed across institutions from time to time.

4.8 Conclusion

The gradual rise of joint-stock stocks in the 1830s was beset by a few eye-grabbing scandals – among which the Northern Bank was named one of the most notorious transgressors. The reputation of the District Bank briefly suffered too for its own account of mismanagement. In Northwest England, only the Northern Bank had failed beyond recovery. The comparative study of this chapter reveals three key findings. First, to the extent that banking troubles arose primarily from deficient banking knowledge and corrupt management, shareholders were more prepared to renew their trust if they believed that the crisis had more to do with *ability* failures rather than outright *integrity* violations. The proof of integrity or absence of malicious intent rested mainly with the readiness of directors to take responsibility, endure losses, and identify themselves with shareholders' interests as exemplified by the extent of their shareholding.

Second, the public dimension of a joint-stock company, when combined with the sensitivity and confidentiality of financial information, presented bank management with the challenge of striking a delicate balance between publicity and secrecy. When crisis assailed, attempts to withhold sensitive but crucial information – even in the genuine interest of protecting the company or shareholders – were almost certain to invite backlash. As the influence and importance of banking in the economy grew, so did the quest for information by stakeholders and members of public. Whereas shareholders had limited constitutional power to penetrate into the firm's internal affairs, the press assumed a role in the overall framework of corporate governance by uncovering corporate scandals and warning readers of devious schemes (Tambini, 2015). Moreover, in conjunction with the pressure for openness exerted by the press, the fact that proceedings of general meetings had become a subject of public interest also challenged and undermined directors' control over information. In the absence of mandatory corporate reporting, it was under the

influences and constraints of such extra-legal forces that the threshold between trust and distrust was constantly renegotiated and modified between conflicting parties in the face of new evidence and information.

Third, banking scandals in the 1830s did not prompt the government to extend "the reach of criminal laws" to the Victorian boardroom (Taylor, 2013a, p. 64). While the directors had certainly received their due retribution in terms of damaged reputation, the government firmly held shareholders legally liable for the company's losses. The press and members of public also pinned a fair share of blame upon the shareholders for failing to discharge their duties as owners of public corporations with care and vigilance. No legislation was enacted for the protection of shareholders insofar as bank failures, "though dramatic, were ultimately seen as private matters between shareholders and directors" (Taylor, 2013a, p. 64). The high-profile investigation led by the Select Committee was by no means a precursor to banking legislation, as shareholder activism remained by default the most ideal policy in nurturing a sound and stable banking system. For this reason, the notions of trust, trustworthiness, and accountability were not conveyed by the letter of the law but through the remedial actions taken by bank management adapted to the circumstance unique to each company. In the following decade, it would take a few more commercial outrages to test the robustness and reliability of joint-stock banking.

Chapter 5
From Trials to Troubles: The 1840s
The Bank of Manchester and the Royal Bank of Liverpool

5.1 Background

After taking power in 1841, the new Tory administration led by Peel took a more interventionist approach to overhauling the banking system. It began with the enactment of the famous Bank Charter Act in 1844 to curtail the excessive issuance of paper notes by both country and private banks in England and Wales (Turner, 2014). In the same year the Joint-Stock Bank Act was introduced to bring the new institutions under more satisfactory form of corporate management. Despite the reforms, banking scandals which attended the boom-and-bust cycle in the 1840s revealed the fundamental weakness and poor management of many joint-stock banks. The frequency of banking scandals proved an embarrassment to the proponents of the Peel reform, who congratulated themselves on enacting a system they touted to have protected the public against the danger of excessive issuance of paper currency, while providing the essential financial accommodation to various commercial and agricultural interests at favourable rates of interest (*Bankers' Magazine*, Oct. 1845). The Bank of Manchester collapsed in 1842 through its amateurish board and dishonest managing directors (see Grindon, 1877). In 1846, the Newcastle Joint Stock Bank, the Leeds and West Riding Banking Company, the Leeds Commercial Banking Company, and the Sheffield and Retford Banking Company suspended payment in consequence to the collapse of the Railway Mania (*Bankers' Magazine*, Feb. 1846). The North of England Joint Stock Bank collapsed in early March 1847, having locked up a vast amount of its capital in questionable and inconvertible securities, and failed to write off its mounting bad debts (*Bankers' Magazine*, Apr. 1847). Seven months later, as the commercial panic raged on, the Royal Bank of Liverpool, the North and South Wales Bank, and the Liverpool Banking Company alike experienced a stoppage and briefly closed their doors.

Knowing how to repair trust and mitigate distrust is a key demonstration of critical management competency (Lewicki & Bunker, 1996). Using the Bank of Manchester and the Royal Bank as case examples, this chapter shows that broken trust could be restored (Gillespie & Dietz, 2009). The key questions of this chapter focus on two distinct issues: (1) how troubled banking institutions responded to stakeholder perception of its damaged legitimacy as shaped by press publicity, and (2) how they rebuilt fractured internal relations with stakeholders by reforming organisational components and reconciling competing interests through discreet use of corporate power. The next section revisits some changes in banking legislation in 1844 – namely the enactment of the Bank Charter Act and Joint-Stock Bank Act, in response to the alleged regulatory defects which led to bank failures and financial turmoil in the preceding decade. This section also reviews the degree to which legislative reforms mirrored the growing perception of joint-stock companies as public entities, consistent with the moral dimensions and corporate transparency intrinsic to banking enterprises. The third section outlines the respective crisis facing the Bank of Manchester and the Royal Bank of Liverpool, briefly describing the context in which trust violations took place in each case. The fourth section revisits a similar subject explored in chapter 4, showing that violations of different kinds (i.e. lapses in integrity and competence) led to different assessments by stakeholders regarding the trustworthiness of organisational leadership. The next section then discusses trust violations with respect to bankers' failures to discharge their duties as financial stewards. In the light of asymmetrical power relations and competing interests between different classes of stakeholders, the sixth section analyses the challenges intrinsic to trust repair efforts. The seventh section compares the underlying factors that led to different outcomes in the efforts of resuscitating each bank. The final section brings the chapter to a close.

5.2 The 1844 Reform

In the early 1840s, there were expressed interests – among the policymakers and leading bankers alike – to toughen banking legislation so as to nurture the growth of joint-stock banks on a stronger and sounder basis. Two central pieces of legislation were introduced in 1844 alone to claw back some of the freedom which joint-stock banks had once enjoyed. First, the inauguration of the Bank Charter Act marked an important step undertaken by the new Tory government to regulate note issues by banking institutions. In his parliamentary speech, Peel wasted no opportunity to emphasise the significance of the

reform, that "[t]here is no contract, public or private; no engagement, national or individual, which is unaffected by it" (*Commons Hansard*, vol. 74, 6 May 1844, col. 720). By restricting the power of provincial and country banks to issue notes, the Act had in effect granted the Bank of England the sole and exclusive privilege to do so. However, even so, the Bank was not spared from the restraint imposed by the new legislation, insofar it could only issue notes in proportion to its gold reserves and holding of government securities (Turner, 2014).

Second, the Joint-Stock Bank Act of 1844 was also passed to reorganise the fundamental corporate constitution and governance (Thomas, 1934; Turner, 2014). Among other things, the legislation brought the freedom of forming new joint-stock banks to an abrupt end. No more institutions of more than six partners, from henceforth, should be established "except by letters patent granted by the Crown after Petition to the Privy Council" (Thomas, 1934, p. 411). Each charter could not extend beyond twenty years and was subject to "numerous and onerous chartering stipulations" (Turner, 2014, p. 40). The new Act required banking companies to publish monthly statements of assets and liabilities, and have their accounts audited by at least two auditors appointed by shareholders. Annual financial statements – together with the auditors' report – must be presented to shareholders in general meetings. These new rules aside, none of William Clay's three "cardinal principles" underlined in the *Report* by the 1836 Committee was written into the new Act – namely (1) limited liability for shareholders; (2) a mandatory fully paid-up capital, and (3) a standardised balance sheet presented "for the guidance of the public and of their customers" (Thomas, 1934, pp. 410, 412).

The decision to retain unlimited liability for shareholders was unsurprising, for Peel himself believed that members of public would have "a great security" if all partners were liable to the full extent of their wealth for the debts of the bank with which they were affiliated (*Commons Hansard*, vol. 74, 6 May 1844, c. 746). Nineteenth-century political economists took this institutional design as the key to ensuring banking stability, securing public confidence, and above all – projecting banking institutions as prestigious and reliable. Gilbart (1859, p. 219), for instance, stressed that "it gives greater security to the public". "It is not enough that a bank is ultimately safe", he contended, "the public should believe that it is safe" (p. 220). Legislation (e.g. the English Co-partnership Act of 1826) and organisational rules ensured that no shareholders could shirk their financial commitment through opportunistic share dumping or transfers.

The emphasis placed by the Act on the publicity of corporate information also echoed the development in the 1840s, during which the former cultural and legal perspective that once construed corporate affairs as "purely 'private' matters" had begun to be challenged (Wilson, 2014, p. 137). Joint-stock banks were increasingly reckoned as incorporating "public dimensions" – and even more so if their conduct of business was inseparably tied to wider public interests (Wilson, 2014, p. 150). Paradoxically – and perhaps quite rightly, Peel also conceded that public disclosure of corporate information offered no immediate remedy to the root causes of corporate misconduct:

> It has been frequently proposed to require from each bank a periodical publication of its liabilities. But I have seen no form of account which would be at all satisfactory – no form of account which might not be rendered by a bank on the very verge of insolvency, if there were the intention to conceal a desperate state of affairs (*Commons Hansard*, vol. 74, 6 May 1844, col. 747).

In the following decades joint-stock banks continued to assume substantial discretion to decide what should be disclosed, resulting in inconsistent financial reporting practices which would remain unresolved until the close of the century (Robb, 1992).

The key dispute was whether the reforms had effectively plugged any obvious regulatory gap and improved the banking system as a whole. As this chapter will unfold, prudent and sound banking did not solely depend on legislation; it necessitated bankers to understand the significance of their fiduciary functions and appreciate the trust conferred upon them in credit allocation and risk management. Proponents of joint-stock banks like Gilbart, framed banking institutions as engines of moral uplift in their towns. By extending credit to the honest and industrious, and withholding it from spendthrifts and gamblers, "bankers perform the functions of public conservators of the commercial virtues" (Gilbart, 1849, p. 13). Fellow banker Gavin Mason Bell (1840, pp. 43, 68) saw joint-stock banks as "moral and religious institutions" for precisely the same reasons; when directors were not men of strict integrity, they had the "power to ruin the fortunes of others, and to inflict much commercial evil upon the community". Using two Victorian cases, the following section shows that banking scandals were more than mere legal and regulatory issues. They provoked a rethinking of the importance of individual integrity, calibre, sacrifice, and commitment in the process of trust restoration.

5.3 The Drama Unveiled

In October 1842, having lost the whole of its paid-up capital of almost £780,000, the board of directors came to terms that the Bank of Manchester could not be carried on (*The Standard*, 11 Oct. 1842). The news triggered considerable panic and became "the sole topic of all conversation" (*Preston Chronicle*, 22 Oct. 1842, p. 2). The abscondence of Edmund Burdekin, one of the managing directors, with a huge sum of £13,000 to America, further fuelled public outrage (*The Standard*, 11 Oct 1842; *Preston Chronicle*, 22 Oct. 1842). On 14 October, about 200 shareholders gathered at Hayward's Hotel, Bridge Street, to receive more gloomy reports from the directors. Prior to this, the loss of trust in the management was already widespread such that a shareholder, in a letter printed in the *Manchester Courier* (15 Oct. 1842, p. 8), anonymously penned the following:

> …it behoves us to take decisive measures at the approaching annual meeting, to rescue ourselves from the present management, as it is impossible any longer to place confidence in persons who have consented to our capital being squandered in such an unwarrantable manner.

The proprietary consisted of about five to six hundred shareholders, among whom many were men of substance. *The Standard* (11 Oct. 1842, p. 1) reported that many had "invested their all" and were required to pay a call of £2 per share to meet all its liabilities. The disgraced institution turned to the Manchester and Liverpool District Bank and Denison & Co., its London agents, for financial aid. It also entered into an arrangement with the District Bank to take over most of its current accounts, ensuring that no business transactions would suffer interruptions (*Manchester Times*, 15 Oct. 1842, p. 2; *Manchester Guardian*, 15 Oct. 1842). The bank suffered a run but promptly met all claims, narrowly averting a stoppage (*Freeman's Journal*, 12 Oct. 1842).

Formed in December 1828 on "the best presumptive evidence" that it would facilitate the trade of Lancashire, the Bank of Manchester enjoyed public confidence "in a super eminent degree" because of its huge paid-up capital and a "very respectable constituency" (*Bradford Observer*, 24 Oct. 1842, p. 4). Its capital stood at £2,000,000, in 20,000 shares of £100 each (*Manchester Times*, 15 Oct. 1842; *Manchester Guardian*, 15 Oct. 1842). Behind the imposing façade, however, there were serious issues at stake. The bank began to author its own chapter of trouble since the mid-1830s, during which "delusive

appearance of prosperity" drove the management to indulge in extensive discounting and lending (*Bradford Observer*, 20 Oct. 1842, p. 4). As economic prosperity ebbed, bad debts began to accumulate until the whole of the bank's paid-up capital was steadily consumed. Direct liabilities totalled £1,800,462 and estimated net assets stood at £1,794,214, making a net deficiency of £16,248. When added to the loss of the entire paid-up capital (£780,000) and the reserved surplus fund (£19,000), the total loss exceeded a staggering £800,000 (*York Herald*, 12 Nov. 1842).

As a watchdog in the marketplace, newspapers swiftly laid the details to public gaze and ridiculed the board for their incompetence and bad behaviour. The managing committee – consisting of six of the twelve directors – came under fire for contracting two toxic accounts. The *Sheffield Independent* (22 Oct. 1842, p. 2) and *Manchester Courier* (15 Oct. 1842, p. 8) revealed that the bank lent a large (unspecified) sum to Hilton, out of which "thousands of pounds" were lavished on a property at Darwen upon which the bank seemed to have no proper claim, and the remainder distributed among "coal mines, print works, paper works, and open halls". In 1840 the bank granted a whopping £180,000 to Joseph Raleigh & Co., despite their struggle in raising a mere £500 credit elsewhere (*Manchester Courier*, 15 Oct. 1842). More damagingly, the *Manchester Times* (15 Oct. 1842, p. 2) described the financial report presented by the managing committee to the board in 1841, which showed an intact paid-up capital of £741,000 and a surplus fund of £19,000, as "entirely fallacious" and mere "false figures and garbled statements". The board – and the managing committee in particular – were immediately suspected of conspiring to defraud the shareholders. The directors pleaded innocence and ignorance, accusing the committee instead for masking the bank's true state of affairs.

Certain individuals on the managing committee, which was formed in 1836 to mitigate further losses incurred due to Burdekin's recklessness, soon attracted public attention (*Manchester Courier*, 15 Oct. 1842). Over the years, death and resignations steadily reduced the quorum, until the committee was largely in the hands of Richard Roberts and the infamous Burdekin, who racked up bad debts by perpetuating the accounts of Hilton and Raleigh. John Smith, the auditor from the start until the last report was presented in June 1841, failed to detect the bank's underlying difficulties. To make up the quorum, two long-serving directors – Joseph Dyer and John Brown – joined the committee and were unaware of the company's dire conditions. While Smith endorsed the report without suspecting any wrongdoing, Dyer also ignorantly vouched for its reliability during the general meeting in the same year (*Manchester Times*, 15 Oct. 1842,

p. 2). Incensed by a blend of deception and ignorance, the shareholders vigorously attacked the management for driving the once prominent institution to an abysmal state. It would take nearly a decade to bring the bank's affairs to a satisfactory close, under the guiding hand of new leadership that steered the entire proprietary through an arduous and painful process of liquidation.

The latter half of the 1840s saw the British economy bracing for another financial storm after years of strong growth propelled by a regime of cheap credit. Intensifying monetary pressure compelled the Bank of England to restrict discounting and lending, thus setting off a wave of mercantile failures in September 1847 (Turner, 2014). The credit squeeze hit the country's joint-stock banks particularly hard. Among the sufferers was the Royal Bank of Liverpool, which turned to the Bank of England for an advance upon bills. The aid was refused in cash but granted in stock, which was subsequently liquidated for cash, precipitating a sudden fall in the price of the bank's shares – an inauspicious sign which the public interpreted as a looming calamity (*Manchester Courier*, 16 Oct. 1847). Attempts to secure further support failed, and on Monday 18 October the Royal Bank suspended payment (*The Times*, 19 Oct. 1847).

News of this sent "an electric shock" through the town (*Liverpool Mercury*, 19 Oct. 1847, p. 8). Alarmed depositors began to press upon other local banks for their money (*Manchester Courier*, 4 Dec. 1847; *Liverpool Mercury*, 26 Oct. 1847; *Chester Chronicle*, 5 Nov. 1847). The Liverpool Banking Company and the North and South Wales Bank, which had extensive operations in Liverpool, both also temporarily suspended business, while the Bank of Liverpool survived £100,000 of deposits being withdrawn because of its name "being somewhat similar to that of the Royal Bank" (Turner, 2014, p. 75). Though the monetary pressure soon abated, the sudden reversal of the Royal Bank's fortunes – its shares had been trading at a large premium just weeks prior – bewildered the local community (*Liverpool Mercury*, 19 Oct. 1847, p. 8).

Founded in 1836 with £2 million nominal capital, its shares were 1,000 each – an unusually high denomination which set it apart from most of its more "democratic" rivals – with £500 per share paid up, designed to attract a wealthy proprietary and ensure the bank's resilience (Alborn, 1998, p. 109; Royal Bank of Liverpool, *Deed of Settlement*, 2 May 1836, p. 2). Indeed, the local press described its body of shareholders as "one of the richest in England" (*Liverpool Times*, reprinted in *Manchester Courier*, 20 Oct. 1847, p. 669). The bank's ownership reflected Liverpool's status as a "provincial outpost of 'gentlemanly capitalism'" (Belchem, 1998, p. 1). About 32 per cent of its shareholders

were merchants, brokers, or involved in shipping – while a further 26 per cent described themselves as gentlemen (*Liverpool Mercury*, 19 Oct. 1847, p. 8). By contrast, just six per cent were tradesmen. As was typical of provincial banks at the time (Alborn, 1998, pp. 102-3), these proprietors were overwhelmingly local. Of 199 shareholders, 129 (65 per cent) were Liverpool residents, and a further 23 (11.5 per cent) came from the environs of the town (see Figure 5.1). The board, dominated by Liverpool merchants, successfully embedded the bank in the town's business culture. Unlike many other new joint-stock banks, it chose not to establish a regional branch network, catering primarily to Liverpool itself, "whose commodity and export trades had made its commercial activities more diverse than in Lancashire as a whole" (Anderson & Cottrell, 1975, p. 604; Newton & Cottrell, 1998). Yet it was its enthusiastic support of local enterprise that led it to disaster.

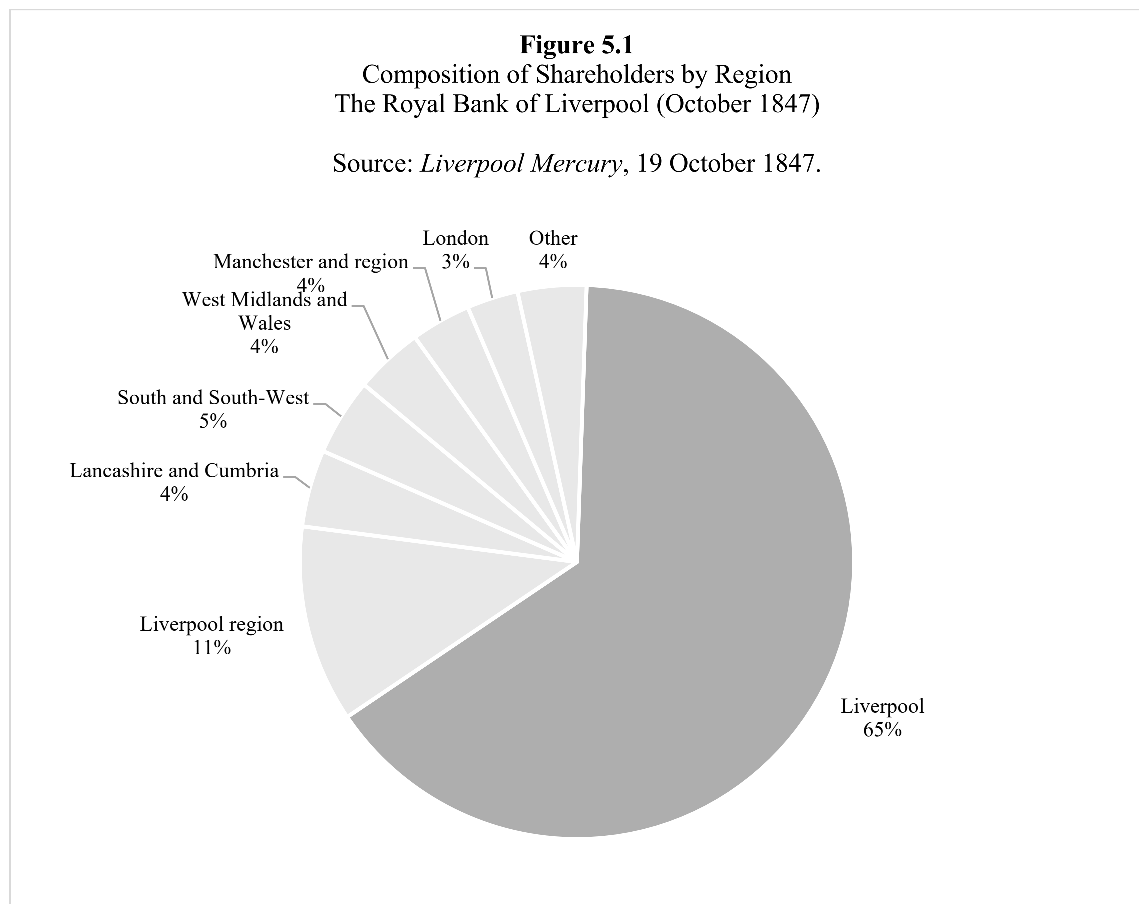

Figure 5.1
Composition of Shareholders by Region
The Royal Bank of Liverpool (October 1847)

Source: *Liverpool Mercury*, 19 October 1847.

About a week after the stoppage, a committee of shareholders started working with the directors to investigate the bank's situation. At a general meeting on 30 October, the committee confirmed the reason for the bank's predicament: it had extended around £523,000 of its paid-up capital of £646,000 to Barton, Irlam, & Higginson – a prominent

Liverpool mercantile house led by Jonathan Higginson – and had made further large advances to two other local businesses (*Liverpool Mercury*, 2 Nov. 1847; *Bristol Mercury*, 23 Oct. 1847). It was this lock-up of capital that led the bank so exposed during the credit squeeze. The shareholders faced three options: wind up the bank, amalgamate with another local bank, or attempt to resuscitate the bank by raising enough additional capital from shareholders to get it over its present difficulties (*Liverpool Mercury*, 2 Nov. 1847). Despite considerable criticism in some quarters, and the pessimism expressed by the *Manchester Guardian* (3 Nov. 1847, p. 4) that the chances of restoring the bank to solvency were "exceedingly small", a majority of shareholders and depositors in fact proved willing to work with the directors to revive the bank. At the meeting a proposal to liquidate the bank was voted down by a margin of about ten to one (*Liverpool Mercury*, 2 Nov. 1847).

The prospects for resuscitation improved further at a second meeting of shareholders a week later, on 6 November, when the committee reported that a re-examination of the accounts had seen a considerable reduction of the bank's liabilities, and that the assets available "had been much underrated in the former report" (*Liverpool Mercury*, 9 Nov. 1847, p. 4). The committee's recovery plan consisted of two policies allowing prompt settlements of depositors' accounts without imposing an excessive financial burden upon the shareholders (*Liverpool Mercury*, 5 Nov. 1847). First, depositors would have their money refunded in four equal instalments over nine months with interest paid. Second, instead of enforcing payments by making calls upon shareholders' wealth, the management issued four thousand preference shares of £100 each to raise the £400,000 needed to meet depositors' claims (*Liverpool Mercury*, 9 Nov. 1847). Later that month, amidst rising optimism, the bank announced that it planned to resume business on 1 December. At a third meeting on 29 November, the chairman confirmed that this would happen, in a remarkable reversal of the bank's fortunes. The rest of the chapter explores how the directors in each bank reengaged stakeholders to restore trust.

5.4 Positive Discrimination

Competence and integrity are fundamental qualities against which one's trustworthiness is assessed (Barber, 1983; Schindler & Thomas, 1993). The Bank of Manchester's scandal exposed the board's failure in both. The Royal Bank's debacle, on the other hand, had to do with the board's misplaced judgement while their moral standing was far less of an

issue. According to Reeder and Brewer (1979), relative to competence failures, stigma that follows integrity lapses proves more difficult to negate. The question is, what are the "cognitive underpinnings of trustworthiness perceptions" that explain the relative ease for leaders to recover from lapses of competence than ethical violations (Elsbach & Curran, 2012, p. 218). With reference to Wojcizke's (2005, p. 157) position that "morality and competence constitute two separate and basic clusters of traits in the perception of leaders", this section explains how and why stakeholders attributed different meanings to lapses in competence and integrity respectively, and hence their distinct perceptions of organisational trustworthiness (Butler & Cantrell, 1984; Elsbach & Elofson, 2000). This clearly shows that injured parties were by no means "passive bystanders" but individuals capable of making informed evaluation in relation to the facts of transgression and the appropriateness of the directors' response (Kim et al., 2009, p. 409; Gustafsson et al., 2021). Different strategies, therefore, were required in each bank (see Kim et al., 2006).

Following the fall of the Manchester bank, the directors were careful to go only as far as acknowledging their neglect and incompetence, and resolutely distanced themselves from the slightest hint of ethical misconduct (see Kim et al., 2009). Relative to ethical violations, inadequate task performance is normally attributable to deficient skills and abilities, a temporary condition that may be "remedied with time" (Elsbach & Curran, 2012, p. 221; Tomlinson & Mayer, 2009). John Spencer, the chairman and one of the directors, candidly acknowledged the bank's "most disastrous" state, having incurred considerable losses stemming from "many bad debts of substantial amounts" (*Manchester Courier*, 15 Oct. 1842, p. 8). Pinning the blame squarely on the managing committee for issuing misleading reports, the board pointed to their own combined ownership of 11,000 shares as "proof of their having themselves been deceived", rendering them the "heaviest sufferers" as a result (*Manchester Courier*, 15 Oct. 1842, p. 8). They clung on to the troubled firm and refused to divest a single share. Given the separation between control and ownership in joint-stock establishments, because the major concern was whether directors were sufficiently incentivised to protect the company's well-being and properties which they did not (directly) own, the most immediate and tangible proof of the board's innocence therefore critically hinged upon how far their own interests were aligned with the shareholders'. As will be shown later, the injured parties were evidently more forgiving towards those who lacked competence, as long as the latter were willing to own responsibility (Meindl & Erlich, 1987; Sutton & Galunic, 1996).

The directors elicited a spectrum of different responses from shareholders, depending on the nuances emanating from the nature of their wrongdoings. Dyer and Smith, for example, drew relatively tempered criticisms in the face of their apparent failures. A vocal shareholder named Thomas Greig believed that Dyer, as an "unlucky holder" of 2,500 shares who lost nearly £40,000, was "a sufferer to a great extent" and "not culpable of dishonesty" (*Manchester Times*, 15 Oct. 1842, p. 8). His connection with Manchester and then the bank was rather unique. An inventor of American origin, Dyer left for Britain in 1811, briefly residing in London and Birmingham before settling permanently in Manchester in 1816, after which he increasingly took interest in the local affairs (Sutton, 2004). Five years later, he co-founded the *Manchester Guardian* with a cotton trader, John Edward Taylor, with the support from the Little Circle, a Manchester-based group of non-conformist Liberals. In 1831, Dyer was then elected to the Manchester Literary and Philosophical Society, after which he became a vice-president (1851-68). Forced by the failure of the bank he co-founded, he sold Leegate Hall, his textile-card factory, and other properties in Manchester to meet the calls on his shares, vastly reducing his once sizeable fortune (Sutton, 2004). Likewise, while Smith's individual loss stood at about £15,000, the loss to his family was "two or three times the amount" (*Manchester Courier*, 15 Oct. 1842, p. 8). A director named John Potter also defended Smith, asserting that the shareholders owed him "a great debt of gratitude", without whose "indefatigable exertions" the troubles would have "increased tenfold". Smith's endorsement of the report was not entirely a mistake of his own making, his brother Thomas Smith explained. This was because the inherent nature of the auditor's duty – arguably a situational factor outside his control – had prevented him from detecting the underlying troubles.

The Manchester scandal was typical of the oft-repeated instances in which wreckages of mismanagement were camouflaged behind "a false appearance of prosperity" (Robb, 1992, p. 60). Greig was scandalised that the bank was already on the verge of bankruptcy since 1836 but the board continued to declare dividends ranging from 6 to 9 per cent from year to year (*Morning Chronicle*, 8 Feb. 1843). The *Manchester Courier* (15 Oct. 1842, p. 8) reported that the company's audit was nothing more than "calling over the bills, and seeing what amount of cash there was in the bank on a certain day". The *Sheffield Independent* (22 Oct. 1842, p. 2) called it "the merest farce, consisting merely of calling over the accounts, a task of an hour or two". The *Liverpool Mercury* (28 Oct. 1842, p. 8) summarised the notoriety of the auditor's failure as follows:

> A summary is read at the periodical meeting of shareholders, put to the vote, and agreed to within the hour, without examination or comment, the bias of all corporate bodies leaning singularly in favour of their directors.

Among the newly elected directors, Brown echoed the criticism, remarking that the task was nothing more than ensuring "numerical accuracy" (*Manchester Courier*, 15 Oct. 1842, p. 8). Potter also castigated the auditors for failing to provide an accurate assessment of the bank's financial status (*Manchester Courier*, 15 Oct. 1842).

Arguably, the case advanced by Graafland and de Ven (2011, p. 613) that accuracy is "the central virtue in the pursuit of truth" raises an important question as to how far misinformation had put the directors' integrity on the firing line. Due to unstandardised procedures in nineteenth-century corporate reporting and the sacrosanct culture of financial secrecy embedded in banking, published statements provided "surprisingly few details" and were often "little of direct use" (Collins, 1984, p. 44). Manipulation of financial statements was not uncommon, artfully orchestrated to induce a change in the behaviour of shareholders as management intended (Gaa, 2009; Taylor, 2013a). The failure to disclose material information may be "unintentional or intentional", depending on the management's motive (Gaa, 2010, p. 183). The true condition of the Manchester bank utterly contradicted Roberts' claim in 1841 that it was "the noblest in the town" (*The Times*, 9 Nov. 1842, p. 5). A shareholder named Curtis accused the committee of producing a fallacious statement knowingly "for some sinister purpose" (*The Times*, 9 Nov. 1842, p. 5).

As the accused masterminds, Burdekin and Roberts were shown little mercy. Such discriminatory response is unsurprising because victims tend to interpret unethical conduct as an outward demonstration of the moral character indwelling the offenders' personality (Elsbach & Curran, 2012; Tomlinson & Mayer, 2009). Greig led a scathing attack on Roberts, accusing him of perpetrating deceits and "fraudulently abstracting money from the bank" (*The Times*, 9 Nov. 1842, p. 5). To defend his innocence, Roberts cited his personal loss of £40,000 together with his family's assets, all of which "had been swallowed up in the wreck" (*Manchester Times*, 12 Nov. 1842, p. 3). The estimated values of the securities had been "in their general correctness and fidelity", he alleged, until they had depreciated considerably amidst "an extraordinary and long-continued depression of trade". The shareholders erupted in rage when a statement disclosed that Roberts had owed the bank £72,701. A director named Norris recalled that in October 1841 Roberts

refused to let the auditors examine the accounts, contending that "unless the directors could have the entire confidence of the bank they had better resigned and let the affairs of the company be wound up" (*The Times*, 9 Nov. 1842, p. 5). Given Roberts' active involvement in the committee, few believed that he was ignorant. Insofar as the past statement was riddled with "hypocrisy and fraud", Norris charged Roberts for "intentionally deceiving" the whole proprietary (*Manchester Courier*, 15 Oct. 1842, p. 8). A shareholder named Walker denounced Burdekin as a disgrace to the bank: his management was "discreditable and ruinous", and his private character, "notoriously irregular" (*Manchester Courier*, 15 Oct. 1842, p. 8). The verdict was beyond dispute: Burdekin had misappropriated the bank's funds "to his own purposes", and the full extent of his "fraudulent transactions" remained unknown (*Sheffield Independent*, 22 Oct. 1842, p. 2).

In the case of the Royal Bank – as with bouts of banking crises now and then – excessive risk-taking was "the core of the problem" (Jaffer et al., 2014c, p. 10). The injured parties appeared to have accepted that role failures – and not ethical violations – were the primary cause of the debacle. What seemed acceptable risks to the directors were subsequently revealed to be ruinous. At the first meeting of shareholders on 30 October 1847, three of the bank's directors, William Shand, Emanuel Zwilchenbart, and Charles Middleton, all Liverpool merchants, issued a written statement explaining how Higginson was able to build up such a disastrous account with the bank. In June 1846, when the amount owed by Higginson was about a third of what it was eventually to become, Jeremiah Chaffers, the bank's manager, had advised the directors against making any further advances because of his failure to provide adequate securities. The directors, however, overruled Chaffers on the grounds that Higginson, who was also a shareholder, was a man of "honour, wealth, and integrity" (*Liverpool Mercury*, 2 Nov. 1847, p. 6). Subsequently, absent from work for seven months due to poor health, Chaffer's duties were filled by chairman of the board Sir Thomas Brancker (1783-1853). As a self-declared "regular old Tory", and once the Mayor of Liverpool in 1831 and alderman in the reformed Town Council, Brancker was a major figure in Liverpool politics and society (*Liverpool Mercury*, 15 Feb. 1853, p. 4). His considerable influence and standing had done practically nothing to steer the bank in the right direction, however. Instead, he allowed Higginson's account to swell much further. Though not "wanting to cast an undue share of blame upon him", the other directors stressed that Brancker alone possessed full knowledge of customers' accounts (*Daily News*, 1 Nov. 1847, p. 2). They wanted to

“solemnly assure the proprietors everything was done as was supposed at the time for the best” but admitted that allowing Higginson to borrow so much was “a grievous error of judgement” (*Liverpool Mercury*, 2 Nov. 1847, p. 6).

The willingness to admit mistakes is consistent with the finding of Gillespie and Dietz (2009, p. 137) that denials or “duplicitous impression management” can significantly undermine organisational credibility. It certainly did not spare the board from scathing criticism from the shareholders, many of whom were reportedly “disgusted with the management” (*Manchester Guardian*, 6 Nov. 1847, p. 7). William Thompson, a London Member of Parliament and director of the Bank of England, traced the confusion to “an utter departure from all the established and recognised principles of banking”, and accused the board – and Brancker in particular – of “gross mismanagement” (*Liverpool Mercury*, 2 Nov. 1847, p. 6). Other shareholders echoed similar complaints. Liverpool ironmonger Joseph Cooper deeply regretted his belief that the directors were “sharp enough and keen enough” to be entrusted with the management of the concern (*Liverpool Mercury*, 2 Nov. 1847, p. 6). Captain Jones, a retired officer of limited means, complained that the directors had been vested with too much power “to make advances either with or without security” (*Liverpool Mercury*, 2 Nov. 1847, p. 6).

Exculpated from ethical failings, the board’s preparedness to endure substantive losses by retaining their shares was a tangible signal of honest intentions (Bottom et al., 2002). As the largest shareholder, Brancker’s refusal to part with his shares was evidence that he held a substantial stake in promoting the prosperity of the establishment. He was determined “to stand or fall with the bank”, vindicating his innocence of intent to conspire against the public (*Liverpool Mercury*, 2 Nov. 1847, p. 6). Though arguing that the episode demonstrated “so humiliating a picture of incapacity” (*Liverpool Mercury*, 5 Nov. 1847, p. 6), the press was satisfied that “not a shadow of a stain rested on the purity of intention, or on the personal honour of the directors and managers” (*Manchester Courier*, 3 Nov. 1847, p. 2). Even the bank’s severest critics in the London press accused the directors of incompetence rather than corruption. “Was there ever such perversity, such grievous imbecility, or recklessness all united?” queried the *Morning Advertiser* (1 Nov. 1847, p. 2). This was crucial, for distrust originating from ethical breakdown – which has to do with moral flaws rooted in personal characters – are more difficult to mitigate than that associated with fiduciary failures (Kim et al. 2004).

Similar to the Bank of Manchester, the Royal Bank was criticised for its entrenched culture of secrecy. As was typical, the bank denied shareholders the right of inspecting

the company's accounts, documents and writings, "except such as may be produced for that purpose at any meeting of proprietors" (Royal Bank of Liverpool, *Deed of Settlement*, 24 Dec. 1847, p. 42). To the extent that shareholders' knowledge about the company's affairs was restricted to the reports and summary accounts produced for the general meetings, the management "could conceal troublesome reality for some time" (Freeman et al., 2012, p. 225). It is therefore not difficult to appreciate the misgivings the stakeholders had about the bank. Cooper complained that there had been "hitherto too much secrecy about the bank", and shareholders had "a right to expect the strictest investigation into the manner in which their affairs were managed" (*Liverpool Mercury*, 9 Nov. 1847, p. 4).

It was therefore significant that after the bank suspended, the directors worked and shared control with the committee of shareholders, chaired by Booker, to investigate the affairs through the critical weeks of suspension. Though the directors initially preferred managing the crisis behind closed doors, barring reporters from the first meeting of shareholders on 30 October, when the meeting resumed a week later, it was with reporters present, the board having agreed to a resolution to that effect by shareholder Samuel Holme (*Liverpool Mercury*, 9 Nov. 1847). This is highlighted by Gillespie and Dietz (2009, p. 137) as the "critical and urgent step" for the board to provide timely, accurate, and transparent communication to the stakeholders about the crisis. The tactical change, in fact, also recognised the "public interest functions" that journalists could play within the "broader system of corporate governance", holding companies to account and subjecting directors' conduct to public scrutiny (Tambini, 2015, p. 128).

5.5 Untrained, Unqualified, and Unprincipled

According to Graafland & de Ven (2011, p. 611), the vocation of bankers is fundamentally bound up with the "virtues of quality and accuracy" because of the underlying "phenomenon of risk-taking" in the industry. Prudent and professional bankers only undertake a decision of which they are thoroughly acquainted with the risks involved. They improve wealth by "real skill in trade or profession, and not by excessive risk-taking" (p. 611). Even without malicious intent, the virtue of accuracy is violated when bankers fail to understand the nature and significance of their fiduciary duties. From this perspective, because "the relevant virtue" is tied to representing and taking care of stakeholders' interests, this section demonstrates the negative implications on

organisational trustworthiness as bankers grossly underestimated the risks involved in credit misallocation, encouraging excessive indebtedness with significant spillover costs upon the rest of the society. In the context of the joint-stock culture in which optimising return on investment and shareholder value had progressively become an accepted norm, the core argument in this section is whether bankers had pursued profits without paying regards to their professional responsibility (Graafland & de Ven, 2011).

At the Bank of Manchester, in less than a week the diagnosis was promptly concluded to counteract any "rumour machine" that had the tendency to amplify negative report over which the board had limited control (Gillespie & Dietz, 2009, p. 139). Doubtless, deficient banking knowledge and expertise led the company to its ultimate downfall, for which Greig charged the directors with the "sin of omission" (*Manchester Courier*, 15 Oct. 1842, p. 8):

> It must be perfectly well known to any rational man, any one who understands the importance of banking, that it was utterly impossible for one man, or twelve men, going only once or twice a week, to know what was going on in a bank; it must be done by one man who had a constant eye to the accounts, and the way those accounts were kept.

In a lengthy letter addressed to the shareholders, Smith intimated that the managing directors' failure to make "regular daily, and even hourly, attendance" at the bank had blunted their capacity to form an "accurate knowledge" of the firm, with most directors having "very limited knowledge of banking business", and its early success emboldened them to follow measures "which subsequent has shown to have been ill-advised" (*Manchester Courier*, 11 Feb. 1843, p. 3).[2] By 1836, under the charge of Burdekin bad debts had swollen to such a degree that a managing committee was formed to put the bank upon "a better footing". When the company failed, above seventy shareholders were females, making approximately 14.6 per cent of the firm's entire body of proprietary (*Manchester Times*, 29 Oct. 1842, p. 4). About five of them were widows. It was one of "the most disgraceful proceedings that ever human nature saw in England", a shareholder named Stubb derided, "that the shareholders, especially females and orphans, should be robbed by these people" (*Manchester Courier*, 11 Feb. 1843, p. 3).

[2] The letter was reprinted in *Manchester Courier and Lancashire General Advertiser*, 11 February 1843, p. 3.

As Shah and Napier (2019, p. 349) note, many nineteenth-century directors coming from the "upper echelons of society" were "essentially amateurs", and the requirements imposed on directorial candidates were anything but rigorous. The *Leeds Mercury* (13 Oct. 1849, p. 4) editorialised as follows:

> Heretofore the qualification of a director or an auditor has, in most cases, been the supposed long purse, instead of the long head, of the candidate for office. Unfortunately for shareholders, they have had to pay very dearly for their experience.

In the case of the Manchester bank, because directorial roles were underappreciated, practically little had been done to ensure that the board had the necessary calibre or qualifications (Sternberg, 2004). Embarrassingly, managerial defects had been flagged long ago. In 1829, Joseph Macardy (see chapter 1) warned the directors that "there is not an individual amongst you who understands the title of the duties of a bank director; nor of the nature and organisation of a public company", denouncing their knowledge as bankers as "purely intuitive" (*Manchester Courier*, 29 Apr. 1843, p. 2).[3] The fact that the directors were men of "great zeal" and "best intentions" offered no protection to the shareholders (*Manchester Courier*, 29 Apr. 1843, p. 2).[4] The Bank of Manchester was Macardy's first project in the region, and his initial and "thoroughly judicious" recommendation was that the company "should embrace a large portion of the neighbourhood" via an extensive branch network (Grindon, 1877, p. 251). Having had his proposal rejected by the board, in January 1829 Macardy severed his tie with the directorate and went on "courageously" to adventure other banking projects in the following years (Grindon, 1877, p. 251). His active campaign for a joint-stock bank headquartered in the region ultimately saw the fruition of the District Bank and the already-defunct Northern Bank (see chapter 4).

While the managing committee contrived to hide toxic accounts from the directors, the board's lack of vigilance and decisiveness also conveniently allowed Burdekin and Roberts to carry out their exploits unimpeded (*Manchester Courier*, 15 Oct. 1842). Dyer,

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[3] The letter was quoted in part in *Manchester Courier and Lancashire General Advertiser*, 29 April 1843, p. 2.

[4] The opinion of Smith was quoted by Joseph Macardy in his letter published in *Manchester Courier and Lancashire General Advertiser*, 29 April 1843, p. 2.

for once, identified the problems and was determined to bring Raleigh's account to a close, expressing his astonishment that "how sane men could have allowed them to get nearly fifty thousand pounds into the debt of a bank" (*Manchester Courier*, 15 Oct. 1842, p. 8). Burdekin and Roberts, in response, assured him that Raleigh would "turn up a trump", and the bank "shall lose nothing by him". Closing the account would invite financial catastrophe, they warned, because the bank relied heavily on "an enormous amount of outstanding paper" received from Raleigh to finance its daily transactions (*Manchester Courier*, 15 Oct. 1842, p. 8). Dyer caved in. Deluded, the directors deemed that the managing committee were "fair and just" in their dealing, and that half of the bank's capital would remain intact even after the bad debts were written off (*Manchester Courier*, 15 Oct. 1842, p. 8). Failing "to ask questions necessary" in the interests of the firm and shareholders, the directors unknowingly permitted the committee to perpetuate the "unsatisfactory status quo" (Sternberg, 2004, p. 85).

The board's failure to hold the managing committee in check heightened a recurring concern that "unfettered agents" are dangerous when given to opportunistic behaviour and self-serving agenda (Nordberg, 2010, p. 176). In his *Logic of Banking*, Gilbart (1859, p. 226) reminded his readers the importance of putting the manager's "daily exercise of the administrative power" under the managerial principles prescribed by the directors, and reserving key corporate matters for their "special consideration". Such division of power reflects a governance structure established on "the premise of mistrust" (Todd, 2010, p. 59), pivotal for mitigating exposure to "the individual failings or dishonesty of managers" (Robb, 1992, p. 60). As with a few other joint-stock banks, the blunder of the Bank of Manchester was that "decisive measures" were delayed in hope for better times which never came (*The Times*, 24 Oct. 1843, p. 6). Smith intimated that losses could have been avoided during the 1837 panic had the managing committee closed the accounts "at whatever risk or cost" (*Manchester Courier*, 11 Feb. 1843, p. 3). However, under Burdekin's control the committee continued to temporise, until successive years of bad harvests ushered in a period of commercial distress, during which some customers became too impoverished to repay their dues.

The Royal Bank crisis, meanwhile, portrayed a possible conflict of interest that explained the directors' profligate lending policy. Prior to emancipation, Barton, Irlam, & Higginson had been one of the biggest slaveowners in Barbados, and their extensive sugar and cotton interests placed them firmly in the same business networks as members of the Royal Bank board (Butler, 1995). Several directors had interests in the West Indies, most

notably Josias Booker, who was one of the bank's founding directors in 1836, though he had stepped away from the board by the time of the bank's suspension. Booker had made his fortune in British Guiana, and following a dispute with Liverpool shipowners, in 1835 he and his brothers founded the Booker Line, their own shipping company, to transport raw sugar from their plantations (Slinn & Tanburn, 2003). In partnership with his brother James, Thomas Brancker was a leading figure in Liverpool's sugar refining industry: until it burnt down in 1843, their factory was one of the largest in the country, "employing some hundreds of men" (*Morning Chronicle*, 29 Dec. 1843, p. 3). While Lamoreaux (1996) has shown that preferential lending was not necessarily a rash and precipitous policy, the suspicion was that the directors were far more attuned to the interests of Liverpool's mercantile elites than the wider business community. One anonymous critic writing in the *Liverpool Mercury* (5 Nov. 1847, p. 6) mocked that the bank's "aristocratic" pretensions, which had meant that it had been "rather exclusive in the choice and number of its friends". Of the town's banks, it had developed a reputation as "the least accommodating to the public generally", and now the reason was clear: having locked up all its resources with Higginson, it simply could not afford to lend to others. The paper lamented that "so important an establishment should have crippled its great means of usefulness to thousands of safe men of business, by accommodating one accumulator so enormously" (*Liverpool Mercury*, 2 Nov. 1847, p. 8).

The charge resonated with the bank's customers. At the first general meeting following the suspension, Cooper accused the management of "favouritism": while the bank was enormously liberal to a failing enterprise, the board had repeatedly denied him an advance of a few hundred pounds "until he gave his own personal security into the bargain" (*Liverpool Mercury*, 2 Nov. 1847, p. 6). One subscriber wrote to the press suggesting that the crisis would have been averted had the bank's accounts been presented to the directors in anonymised form. Their judgement would not then have been clouded by their unreliable assessments of the debtors' "honour and means" (*Liverpool Mercury*, 9 Nov. 1847, p. 6).

The bank kept Higginson's account open for so long on the "security" of the huge stocks of cotton he was holding, in the belief that prices would continue to rise. Though they did, Higginson refused to sell, hoping that prices would increase yet further, and when they dropped, the firm quickly went bust. It was the Manchester press that was the most scathing in its criticism of the bank's actions in lending so freely to Higginson. As the *Manchester Examiner* (2 Nov. 1847, p. 4) put it, "instead of maintaining an

independent position, and lending its aid to the public generally as it ought to have done", it allowed itself to be drawn into a massive and ultimately fatal cotton speculation. As well as depriving Liverpool businesses of accommodation, this policy caused economic havoc in the wider region, particularly in Manchester. According to the *Manchester Courier* (30 Oct. 1847, p. 4), the cotton speculations of merchants like Higginson caused shortages and price fluctuations which "had done more injury to the manufacturing markets, and thrown more operatives out of employment than any other circumstance". The *Manchester Guardian* (20 Oct. 1847, p. 2) even believed that if the Bank of England had propped up the Royal Bank knowingly allowing it to continue doing business along these lines, "the act would have been not merely foolish, but criminal".

The Manchester press recognised the two towns' very different perspectives on the legitimacy of speculation, noting that "it has always been a hard task to reconcile Liverpool notions about cotton with those entertained in Manchester (*Manchester Examiner*, 2 Nov. 1847, p. 4). Indeed, there was not national commercial culture at the time: what was disapproved of as excessively reckless, risky, and irregular in one region could be regarded as legitimate and acceptable elsewhere (Moss, 1997, p. 377). In this case, these ethical differences were underpinned by the clash between Manchester manufacturing interests and Liverpool mercantile interests (Belchem, 1998, p. 2). But in the wake of the suspension, even the bank's Liverpool stakeholders were forced to admit much of the Manchester critique, Samuel Holme telling his fellow shareholders that only when the bank had learned the lessons of "prudence and moderation" would trade "be really profitable, because it would be really legitimate, and founded upon labour, instead of that most baseless of all visions, reckless speculation" (*Liverpool Mercury*, 30 Nov. 1847, p. 5).

5.6 Leadership Shakeup and Restitution

Because the power relations between the board and shareholders were anything but equal, the dynamics behind the directors' attempts to regain their trust reflected the belief of Flores and Solomon (1998, p. 210) that "trust relationships are bidirectional" but not necessarily symmetrical. Against a backdrop of unequal power relations, to redeem legitimacy the directors actively engaged the stakeholders in conversation and monitored their changing expectations. Power asymmetry may undermine stakeholders' ability – broadly defined in terms of specialised expertise, access to information, and involvement

in strategic decision-making – to protect their own interests but would not necessarily preclude meaningful dialogues altogether. The affairs of the bank echoed the view of Flores and Solomon (1998, p. 218) that trust can be created and destroyed "through dialogue, in conversation, by way of promises, commitments, offers, demands, expectations and tacit understandings". Therefore, to argue there could be no true dialogue is to deny trust as "a dynamic aspect of human relationships" (p. 206) – which must be initiated, maintained, and repaired from time to time. There were iterative interactions between different parties, during which the firm assessed the appropriateness of its actions and revised them accordingly in retrospect to stakeholders' feedback (Pfarrer et al., 2008). "This discourse", in the words of Pfarrer et al. (2008, p. 732), "serves to crystallise key demands and questions, promote certain views, shape opinions, and diffuse them across multiple constituencies". Following the view that trust repair is a "stakeholder-driven process" (Pfarrer et al., 2008, p. 730), this section argues that the effectiveness of repairing trust is dependent on stakeholders' perception, as they form judgement and provide feedback in relation to the appropriateness of the firm's remedial actions. Given the complexity arising from multiple stakeholders with divergent interests, the firm must "recognise the revolving demands of stakeholders throughout the reintegration process and take appropriate actions along the way to reflect these changes" (Pfarrer et al., 2008, p. 730).

Insofar as the Bank of Manchester's leadership became conspicuous targets for criticisms, some administrative changes quickly followed, with "men of talent and ability, of respectability and character" filling the posts (*Manchester Courier*, 15 Oct. 1842, p. 8). During the general meeting on 14 October, the shareholders applauded the appointment of William Haynes and William Smith, who replaced John Brown and John Smith. William Stell also took over Roberts' post but Dyer retained his office. Potter and Spencer, who joined the board shortly before the scandal broke out, were re-elected. A shareholder named Kaye was confident that the name of Potter, a Liberal Politician who was one of the largest shareholders and would later become Mayor of Manchester (1848-51) – was "a guarantee" to the board's credibility (*Manchester Courier*, 15 Oct. 1842, p. 8). His involvement in the local affairs began when he was given his father's aldermanic seat on Manchester Town Council in 1845 (*Daily News*, 27 Oct. 1858). On 20 October 1843, following Greig's urge for the formation of a committee that "would go strenuously and actively into the business of the bank", a shareholder committee consisting of John

Bannerman, John Burton, Samuel Walker, and John Johnson was appointed with "full powers" to investigate the bank's affairs (*The Times*, 24 Oct. 1843, p. 6).

Prior to this Greig reproved the directors for having committed "a very serious fault" by putting the wrong persons in charge for so long (*Manchester Courier*, 15 Oct. 1842, p. 8; see also *Morning Chronicle*, 8 Feb. 1843; *Morning Post*, 8 Feb. 1843). By and large, the moral reputation of Roberts and Burdekin was irrecoverably damaged. Greig described Roberts as "a low designing villain" (*Manchester Times*, 12 Nov. 1842, p. 3), while the *Manchester Courier* (11 Feb. 1843, p. 8) called Burdekin "the reputed father of the mischief". Gillespie et al. (2014, pp. 396-7) posit that "the contrite communications, detailed diagnosis and rehabilitative reforms necessary to repair trust are unlikely to be initiated, let alone embedded", insofar the presence of "perceived culprits" continued to undermine the probity of any "open and objective approach" to restoring trust. The repeated attempts by Burdekin and Roberts to carry on the toxic accounts were indicative of "defensive routines and self-serving biases" which weakened organisational stability (Gillespie et al., 2014, p. 396). Roberts' refusal to allow the auditors to inspect the accounts signalled his "ego defences" to fend off "any detection or correction of errors" (Gillespie et al., 2014, p. 396). The "changing of the guard" thus proved the bank's determination to drive meaningful changes (Gillespie et al., 2014, p. 396), signalling a decisive break with the corruption and incompetence witnessed under the old regime. William Smith asserted that the new board stood "on a perfect equality with the rest of the shareholders, a perfect exemption from blame" (*Morning Post*, 8 Feb. 1843, p. 6; *Manchester Courier*, 11 Feb. 1843, p. 3).

On 9 October 1844, the shareholders met with "a better fortune" dawning upon the bank (*Morning Post*, 11 Oct. 1844, p. 3), with the chairman George Chappell addressing the meeting "with far different feelings than he had entertained twelve months ago". Following a series of successful asset liquidations, the half-yearly balance sheet as at 31 December 1843 showed significantly reduced liabilities from £440,936 to £314,778 – a positive outcome that broadly matched the committee's expectation, justifying their cautious optimism that shareholders should anticipate "no further loss" (*Manchester Courier*, 12 Oct. 1844, p. 2). Walker was pleased that "everything that was possible has been done" to improve the bank's finances, believing that within a year the firm "would no longer occasion any anxiety as to the final result" (*Manchester Courier*, 12 Oct. 1844, p. 2). The shareholders also drew "a very marked distinction" between the old and new administration. Managing director William Smith, for instance, was lauded for his

constant exertion "to extricate the shareholders from the difficult and dangerous situation" (*Manchester Courier*, 12 Oct. 1844, p. 2). Stubb characterised him as the community's most "judicious, upright, and business-like" gentleman (*Manchester Times*, 21 June 1843, p. 6). Overall, while the previous management was criticised for their "want of talent", the new leadership commanded considerable respect and confidence for tactfully winding up the bank's affairs in fairness to all parties.

However, with the arrival of better news, shareholders began to urge for the publication of debtors' accounts (*Manchester Courier*, 12 Oct. 1844, p. 2). The demand was understandable, considering how the old regime exploited secrecy "to cover their own shameful management". A shareholder named Millington insisted on "every particular as to the outlets of their property", arguing that secrecy was no longer warranted to prevent others from turning information to the bank's disadvantage (*Manchester Courier*, 12 Oct. 1844, p. 2). Greig, for his part, was concerned about "the whole secret" behind the proceedings of debtors who failed to honour their due, arguing that with many ladies having been reduced "from affluence to poverty and destitution", to pass the debtors' names "entirely in silence" was morally indefensible (*Manchester Courier*, 12 Oct. 1844, p. 2). It was in keeping with "common honesty, justice, and morality" – he maintained – that money should be recovered to the widows and orphans "whose all had been sacrificed" (*Manchester Courier*, 12 Oct. 1844, p. 2; *Morning Post*, 11 Oct. 1844, p. 3). For their ignorance and helplessness in mending their broken means, such victims were exculpated from any moral blame normally pinned on greedy shareholders. The proprietors at large were sympathetic and willing to do for them everything that "ought to be done" (*Morning Post*, 11 Oct. 1844, p. 3).

The directors did not oppose publicity "in the slightest degree" but were expressly concerned about its potential risks on the bank's ability to recover payments (*Manchester Courier*, 12 Oct. 1844, p. 2), as Chappell pointed out as follows:

> Persons had entered into engagements to pay instalments at certain periods; they had hitherto kept those engagements; it was for the shareholders to judge whether they would not be more likely to continue to do so if those engagements were kept secret, than if they were exposed to the world – they being men in business, whose credit might thus be damaged.

Furthermore, under the bank's *Deed of Settlement* the directors were to "faithfully and impartially" uphold the confidentiality of individual accounts – a pledge that required absolute legal compliance as the bank's legal counsellors reiterated (*Manchester Courier*, 11 Oct. 1845).

In response to the suspicion that the directors might leverage insider knowledge for personal gains, the board deployed two distinct strategies to defend their credibility. First and importantly, the directors argued they were the largest shareholders and had paid their calls, vindicating that they had "never ceased to hold their interest in it, and share in its adversity" (*Manchester Courier*, 24 Oct. 1846, p. 7). Potter stressed that "not one gentleman at the board" was indebted to the bank, and none had received a shilling for their directorship (*Manchester Courier*, 12 Oct. 1844, p. 2). As Freeman et al. (2012, p. 98) remark, even without a crisis, "such was the faith in the sense of responsibility that substantial shareholdings would engender that shareholders were sometimes more enthusiastic than boards about driving the directorial qualification upward". Seeing "no real benefit" from publicity as long as the bank remained in debt, a shareholder named Dobson was afterwards content to leave the directors to wind up the concern at their discretion (*Manchester Courier*, 12 Oct. 1844, p. 2). Nield was also in favour of giving directors the authority to determine the time at which "a full account" would be duly presented for "full liberty of access" (*Manchester Courier*, 12 Oct. 1844, p. 2). Makinson, however, was keen on fixing a time to "induce the debtors to come forward" and repay their due. Second, Dyer referred shareholders to their constitutional power to investigate the directors' conduct by appointing a committee, avowing that "[n]one of the directors felt the slightest disinclination to the full examination and publication of their own accounts with the bank", and that they were "individually disposed to answer every question relating to the interests of the shareholders as fully as they possibly could" (*Manchester Courier*, 11 Oct. 1845, p. 12). By the close of 1845, shareholders' confidence further improved, with the liquidation of assets generating a surplus of £50,000 to be distributed among the proprietors. The restrictions on share transfers were rescinded, and the improvement was such that Chappell declared the bank was effectively "out of danger, out of debt" (*Manchester Courier*, 11 Oct. 1845, p. 12).

The Royal Bank directors employed similar strategies with some tweaks. As Flores and Solomon (1998, p. 211) assert, "trust and trustworthiness involve sincerity". A mere signal of benevolent intentions "without an objective penitential act" is liable to be interpreted as cheap talk (Bottom et al., 2002, p. 500). To this end, in the middle of

November it was announced that the directors would be tendering resignations at the general meeting at the end of the month, to give shareholders the opportunity to elect a new board (*Liverpool Albion*, 15 Nov. 1847, p. 4). But though the credibility of individual directors, most notably Brancker, was beyond repair, but the bank largely remained in the control of Liverpool's mercantile elites. Of those elected on to the board at the meeting, two – Josias Booker and John Bibby – had been founding directors in 1836, and others, including John Highfield, were also former directors. Chaffers was also to stay on as manager. The only genuine break from past policy was to include Samuel Holme on the board as a sole representative of the town's tradesmen. Thomas Dover, a Liverpool merchant, explained that he "should not like to see the whole of the directors filled up with tradesmen – they would not be bold and spirited enough – but it was desirable to have a tradesman to act as a check" (*Liverpool Mercury*, 30 Nov. 1847, p. 5). But other than this, the shareholders were confident in the truthfulness and integrity of men like Booker, Bibby, and Highfield to rebuild the institution successfully.

Having identified and acknowledged the problem which led to the crisis, the directors actively engaged different groups of stakeholders to address their financial concerns. This coincides with the importance attributed by Gillespie and Dietz (2009) to the willingness of organisational leadership to take responsibility for the consequences of their errors and show genuine concern for the victims (see also Korsgaard et al., 2002). The work of Kähkönen et al. (2021) shows restoration of trust requires a demonstration of organisational competence (especially at board level), evidence that stakeholders are held in high regard (through consultation and care for their best interests) and the degree to which the offending institution is considered to abide by conventionally accepted moral principles. As with the case of the Bank of Manchester, effective engagement and negotiation were largely constrained by the institutional characteristics which governed the constitutional responsibilities and relationship between the board, shareholders, and depositors. While depositors were assured by the rule of unlimited liability that they would receive full payment, shareholders shouldered much of the burden as every farthing of their wealth became the "guarantee for the ultimate payment of the debts of the bank" (Gilbart, 1859, p. 219; Turner, 2009), in which case the directors had the power to raise the needed funds by invoking shareholders' wealth. The bank, by its own corporate rules, also deprived shareholders of the power to transfer shares without the approval of at least three directors (Royal Bank of Liverpool, *Deed of Settlement*, 2 May 1836, p. 2). This restriction, intended for preventing share ownership from passing into the hands of "men

of straw", blocked the exit for shareholders in the event of failure (*Manchester Examiner*, 21 Jun. 1845, p. 6).

Despite initially issuing a call on the shareholders, the directors quickly changed tack, resorting to a less oppressive methods, issuing £100 preference shares for voluntary subscription, not restricted to existing shareholders. This initiative reflected the directors' awareness of the potential rise in shareholders' dissent or distrust if payment was enforced through the use of coercive power. This method also allowed the bank to signal its departure from the "aristocratic" policies that had landed it in difficulties. Holme, a local builder and proud to be part of "the great tradesman body of Liverpool", thought it "absolutely indispensable that the basis of the operations of the bank should be extended". The £100 preference shares would help achieve this: "it would be like a pyramid, the more extended the basis, the firmer would be the apex" (*Liverpool Mercury*, 9 Nov. 1847, p. 4). The shareholders were very clear about what was happening: John Torr, a Liverpool broker, said they were "calling in tradesmen to their assistance as holders of £100 shares" (*Liverpool Mercury*, 9 Nov. 1847, p. 4). Holme believed that when revived, the bank, established on its broader base, "would start into a new and useful existence, and be of immense service to the town at large" (*Liverpool Mercury*, 30 Nov. 1847, p. 5).

To the extent organisational survival is determined by how closely remedial actions are matched to the demands of various stakeholders (Pferrer & Salancik, 1978), the most tangible challenge facing the Royal Bank was how to arrive at an early settlement of depositors' accounts with "the least possible inconvenience to the proprietors … in equity to all parties interested" (*Liverpool Mercury*, 5 Nov. 1847, p. 6). Because the constitutional relationship was such that the demand of depositors could only be satisfied at shareholders' expense, the management had to ensure that both parties were justly relieved and recompensed – in keeping with the warning of Gillespie and Dietz (2009) that poor treatment of neglect of any interest group could tarnish the firm's overall reputation. This risk was especially profound when considered in relation to the fragility of trust after the crisis, and the tendency for trust-destroying events to exert more influence over one's judgement than trust building ones (Slovic, 1993). As a result, after the suspension the bank quickly published a scheme by which the depositors would be paid their money in full in four instalments over the course of nine months, at interest of five per cent. The main dangers to forestall were depositors launching lawsuits against the directors or shareholders for immediate payment, or pressing for liquidation (*Liverpool Mercury*, 29 Oct. 1847).

Apparently reassured by shareholder declarations that they would repay the depositors "to the uttermost farthing", even if they must surrender "their last shilling of property", the depositors in fact proved very accommodating (*Manchester Courier*, 3 Nov. 1847, p. 2). A meeting of depositors on 4 November was characterised by a lack of recrimination, and those present agreed to the bank's terms (*The Times*, 5 Nov. 1847). Given the inconvenience of having to do without their money for several months, however, they voted to request six per cent interest instead of five (*Liverpool Mercury*, 5 Nov. 1847). While some shareholders, such as Holme who also acted as representative for several female shareholders, were sympathetic to this request, wider opinion was reportedly against offering depositors more than five per cent (*Liverpool Albion*, 8 Nov. 1847; *Liverpool Mercury*, 9 Nov. 1847). But though denying the six per cent, the directors and committee of shareholders otherwise proved responsive to the depositors' needs, allowing them far swifter access to their money should they require it (*Liverpool Albion*, 8 Nov. 1847, p. 6). Upon reopening (as this chapter would unveil later), the bank adopted a sliding scale, where small sums would be immediately payable, sums over £500 available in seven days, with progressively longer waits for larger sums; those withdrawing over £5,000 would have to wait six weeks (*Manchester Courier*, 27 Nov. 1847). As Gillespie and Dietz (2009) suggest, trust repair efforts took more than overcoming negative expectations among the victims: it was equally important to generate positive expectations that the offenders were genuinely repentant and willing to offer reparations for their mistakes accordingly. Tailoring crisis response strategies to stakeholders' needs can convey a positive signal to the injured parties that the organisation is prepared to take direct responsibility (Coombs & Holladay, 2008).

5.7 Second Chance?

Between 1847 and 1850, the legal position of the Bank of Manchester and prospect of resuscitation dominated the general meetings agenda. Because the stringency of the Joint Stock Bank Act (1844) had made it "quite impossible" to form new companies of such character, the bank's charter thus carried "a value of no small importance" that might be "turned into a good account" (*Manchester Courier*, 16 Oct. 1847, p. 3). In spite of Manchester's growing importance as an industrial hub, a harsh economic climate and teetering market confidence dampened the keenness of all parties to resuscitate the bank. The board, for instance, "did not think the present a time to appeal to the proprietors with

any prospect of success" (*Manchester Times*, 19 Dec. 1848, p. 6). Potter called the proposal for an immediate resuscitation "idle and absurd" (*Manchester Courier*, 16 Oct. 1847, p. 3). At the special meeting on 18 December 1848, a show of hands revealed that all shareholders unanimously rejected resuscitation, who were satisfied so long as they could receive the full value for their shares "derived from a fair estimate of the assets" (*Manchester Courier*, 12 Oct. 1850, pp. 9-10).

The lack of appetite for "any risk greater or less" among the injured parties appeared to indicate that trust had never been fully repaired (*Manchester Courier*, 12 Oct. 1850, p. 9). The salience of negative inferences derived from past violations had seemingly reinforced a sub-optimal level of trust, underlining the argument of Kim et al. (2006, p. 50) that trust-destroying events tend to "carry more weight in judgement" than trust-building ones. Since trust had plunged "below its initial level", it required a greater magnitude of increase before trust could be fully restored. Though sound plausible, these arguments nonetheless understate the profound influence of uncertain economic prospects – coupled with years of painful and protracted liquidation process – in undermining the willingness of shareholders "to take a risk in the relationship" (Mayer et al., 1995, p. 715; Slovic, 1993). The board's cautious and conservative approach could have played a part, too. On the critical matter the directors consulted the shareholders regularly and steered clear of any suspicion of overstepping their legitimate power, "in case by so doing it might turn out to the disadvantage of the shareholders" (*Manchester Courier*, 16 Oct. 1847, p. 3). Refusing to "make any bargain" without the shareholders' consent, Chappell stressed that the decision was entirely in *their* hands.

The attribute of trustworthiness requires the agent to diligently live up to the commitment, an undertaking motivated by a goodwill to safeguard and uphold the principal's interests (Baier, 1986; Gold, 2014). By 1849, most "troublesome, litigious, vexed questions" arising from disputed properties and lawsuits had largely been solved (*Manchester Courier*, 13 Oct. 1849, p. 10). The "observable actions" taken by the directors to address shareholders' concerns had won them much applause and praise (Pfarrer et al., 2008, p. 740). As all directors held on to their shares and "kept their posts to the last", Greig considered the new management "highly honourable and commendable, and worthy of every confidence on the part of the shareholders" (*Manchester Courier*, 13 Oct. 1849, p. 10). Dyer described Chappell's services as "so earnest, so incessant, and so valuable", having travelled a distance of 2,314 miles and walked more than 500 miles to inspect properties and superintend their sales "to the best advantage" (*Manchester*

Courier, 13 Oct. 1849, p. 10; *Morning Chronicle*, 11 Oct. 1849, p. 2; *Manchester Times*, 21 Oct. 1848, pp. 1-2). In Potter's view both Spencer and Dyer had "conscientiously and fully" fulfilled their duties, compensating for their "mistakes and errors" when they were part of the old management (*Manchester Courier*, 12 Oct. 1850, pp. 9-10). Whether their actions were motivated by genuine altruism or mere self-interest to protect their own reputation was arguably irrelevant. Even if "undertaken for purely selfish reasons", Gold (2014, p. 135) maintains that such pursuits ultimately drive the agent to act in the principals' interests. The outcome was unmistakably positive, with the shareholders unanimously voting a sum of £700 to the board as "an honourable testimony", for serving seven years "in an honourable, intelligent, and straightforward manner" without receiving "one farthing of remuneration" (*Morning Chronicle*, 11 Oct. 1849, p. 2; *Manchester Courier*, 11 Oct. 1849, p. 10).

As for the Royal Bank, its history of reckless lending for a handful of favoured clients made repairing trust far from straightforward, but not impossible. Although the bank had threatened its own legitimacy by failing to fulfil its key mission, this failure was eclipsed by the success of the bank's exploitation of the collective identity shared between the firm and the wider community (Gillespie & Dietz, 2009). Though highly critical of the way the company had been managed, the Liverpool press nevertheless saw its survival as a matter of local pride. "To suppose the Liverpool joint-stock banks insolvent", the *Liverpool Mercury* (19 Oct. 1847, p. 8) protested at the start of the crisis, "would be to suppose Liverpool insolvent", with millions of property of its own within its own boundaries".

Critically, the option of liquidating the bank quickly identified with London interests and was therefore easily dismissed. Its main advocate at the first shareholders meeting, William Thompson, was a London alderman and director of the Bank of England. Thompson came under fire from Liverpool shareholders, such as John Mellor, a corn dealer, who claimed that Thompson "would be glad to shut up every joint-stock bank in the kingdom" as unwelcome competition (*Liverpool Mercury*, 2 Nov. 1847, p. 6). Voices in the local press agreed. "This is a question in which Liverpool, and not London, is interested", argued "An Observer" in the *Liverpool Mercury* (5 Nov. 1847, p. 6): "we have had quite enough of the management of the Bank of England of late". Associating Thompson's position with a tendency to panic and a "want of nerve", the writer argued that working to resuscitate the bank was the way for Liverpool's townsmen to demonstrate their independence and virtue, proving to London that "Liverpool men can look at

difficulty in the face, and what is more, have the courage to grapple with, and overcome it" (*Liverpool Mercury*, 5 Nov. 1847, p. 6). Goertz and Diehl (1993) illustrate the historical continuity of enduring rivalries, such as that between Liverpool and Manchester, and between the northwest region and London. Regional rivalries lead to mistrust and can drive organisations and stakeholders to take decisions based more on confounding their rivalries than their own interests (Colaresi & Thompson, 2002; Leng, 2000). As noted in the work of Baskin (1988), regional rivalries are prone to amplifying tensions and uncertainty, which can be especially difficult in building trust in financial markets where there is asymmetry of information.

Blithely ignoring the fact that over a fifth of the shareholders were women, proponents of resuscitation frequently presented the crisis as a test of manhood. At a shareholders meeting, Josias Booker declared, "Cease your alarm – struggle with your difficulties like a man – is it not more manly to face your difficulties and grapple with them than to turn your back on them like a dastardly coward?" (*Liverpool Mercury*, 9 Nov. 1847, p. 4). The call to solidarity was a success, as bank and community were prepared to identify with each other in the time of crisis. The proximity afforded by a localised network re-echoed "the sense of shared expectations", and reinforced the confidence that such expectations would continue to be shared by all parties for the common good of the region (Sabel, 1993, p. 1139). There was thus a clear determination to rally together in the face of external criticism. It appeared that distrust resulting from the crisis could be easily seen off – as long as the bank and local businesses were locked together in search of mutual benefits (Moss, 1997).

Local pride aside, financial interests were an equally vital force in pulling all parties together. There was concurrence as to how their interests should be addressed, to stave off liquidation, which "would involve and place in jeopardy" – as Holme warned – "a great number of mercantile firms" (*Liverpool Mercury*, 5 Nov. 1847, p. 6). Stakeholders ultimately accepted Booker's portrayal of the situation: "there exists between the proprietors and the customers of this bank a reciprocity of obligation. The well-being of both are intimately connected" (*Daily News*, 30 Nov. 1847, p. 3). Moreover, the bank's benefits were not "confined to depositors, or shareholders, or customers, but, directly and indirectly, to the community at large" (*Liverpool Mercury*, 30 Nov.1847, p. 5). The shareholders and depositors stood or fell together: "resuscitation by one united effort would be by far a more sensible option than muddling through a painful and protracted process of liquidation" (*Manchester Courier*, 10 Nov. 1847, p. 714). "With fresh tackle,

and good management, and the blessing of Providence", he added, "the royal barque will weather the storm, and once more cast anchor at the station whence she has been driven by adverse winds" (p. 714). To the extent that both the management and stakeholders shared "similar or even identical perceptions" that the bank had been instrumental to the community, and that it could safely resume business, renewed cooperation became a feasible option to all parties (Bottom et al., 2002, p. 498).

5.8 Redrawing the Boundary of Power

The imposition of checks and balances on the executive's power and behaviour is an example of distrust-regulation mechanisms dealing with the misconduct or abuses of organisational members that lead to a crisis (Gillespie & Dietz, 2009). By replacing the old norms or practices with a new "admissible range" of behaviours (Gillespie & Dietz, 2009, p. 134), the enactment of tougher rules is "an immediate and highly visible signal" to stakeholders that the organisation is committed to inducing a behavioural change in its members, and avoiding the same mistakes in the future (Eberl et al., 2015, p. 1207). Self-imposed rules and restrictions also reinforce the belief that the management have learned the lesson and are intrinsically motivated to undertake the necessary reforms and conduct themselves differently (Gillespie & Dietz, 2009; Nakayachi & Watabe, 2005). In this regard, the absence of historical evidence from the Bank of Manchester makes it difficult to produce a meaningful comparative study. However, this section uses internal reforms introduced at the Royal Bank to present a rather interesting finding: although limiting the scope of legitimate authority was both essential and useful for removing negative inferences about the potential abuse of corporate power in the short-term, it was nonetheless a poor proxy for long-term organisational trustworthiness (Shapiro, 1987).

As part of the resolutions, significant rule changes were implemented at the Royal Bank aiming to prevent future problems. The toughening of rules indirectly acknowledged that trust could be misplaced and power vested in the wrong candidates. The fact that the directors' miscalculation had brought widespread repercussions saw a need for placing their conduct under stringent regulations, so as to "protect the shareholders from results such as they have lately had to deplore" (*Liverpool Mercury*, 30 Nov. 1847, p. 5). Reforms included the creation of a new management structure consisting of seven unpaid directors, who would appoint not only a manager, but also two paid directors, who were expected to work from ten till four every day (*Liverpool Mercury*,

30 Nov. 1847, p. 5). The new structure saw a compartmentalisation of decision-making process. The paid directors and the manager would form a permanent committee, which assumed the power to decide on matters pertaining to day-to-day business affairs. The new rules stipulated that only the paid-up capital, not deposits or other funds, could be employed for advances, prohibited advances beyond £20,000 without any security, and capped the allowable credit to any firm or individual on any security at £50,000. Credit would be withdrawn on the objection of any permanent committee member, while the ordinary directors would oversee the committee's decisions and could overrule the committee on a majority vote. The paid directors and manager would be denied all credit facilities, while no directors or the manager would have a vote on giving credit to any business partner or family member (Royal Bank of Liverpool, *Deed of Settlement*, 24 Dec. 1847, pp. 15-16).

The reforms were well received. Before the details were announced, *The Times* (15 Nov. 1847, p. 3) reported that they would place the general management on a basis "destined to exert an important and salutary influence upon the fortunes of the bank". After the general meeting, the *Morning Chronicle* (1 Dec. 1847, p. 6) argued that the resolutions, "if they are strictly adhered to by the directors, appear calculated to place the bank once more in a sound position". The reforms also helped to rebuild bridges with wider interests in the region. The *Manchester Courier* (1 Dec. 1847, p. 4) thought that limiting credit to £50,000 would be hailed in that town "as some guarantee that the money of this bank will not again be employed in raising the prices of raw produce against us, so as to interfere with the legitimate trade of this district".

Despite the rule adjustments, the directors kept most of their previous powers. The revised *Deed of Settlement* (24 Dec. 1847, p. 22), for instance, retained the clause that the board – with the sanction of at least three directors – could still introduce from time to time "whatsoever rules, by-laws, or provisional regulations they may think expedient". The new constitution did not significantly rebalance the power relations between directors and shareholders. Attempts to give shareholders more say over the running of the bank, such as powers over the paid directors, were blocked at the meeting. Booker claimed that it would be unworkable to appoint anyone if they were "liable to be turned out by proprietors who, it was impossible, could know the real workings of the bank" (*Liverpool Mercury*, 30 Nov. 1847, p. 5). Indeed, though the denomination of bank shares was slashed from £1,000 to £200 in order to encourage a wider proprietorship, those who held less than five shares would not have any voting rights at meetings (*Liverpool Mercury*,

30 Nov. 1847, p. 5). When combined with the sophistication and culture of secrecy in banking, entrenched directorial power meant that shareholders, as was true of joint-stock banking more generally, had limited informed inputs to evaluate or monitor the true financial condition of their companies (Freeman et al., 2012).

While the measures adopted appeared credible enough to signal a decisive break with past habits and had enabled the bank to renew confidence in the short term, there was little evidence that the bank had systematically evaluated the effectiveness of its reform initiatives over the longer term. Without a systemic evaluation, Gillespie and Dietz (2009, p. 141) consider it doubtful that "outstanding problems in the organisational system" could be detected and resolved adequately. Broadly speaking, Gilbart (1859, p. 173) argued that "it is the height of folly" to suppose any deed of settlement could protect a bank from incompetent or fraudulent management. Given "the difficulty of specifying abstract standards of competence … and of teasing out abuses of trust from mere differences in the talent or commitment of the agent" (Shapiro, 1987, p. 638), regulatory controls were too impersonal, inflexible, and context-specific to address "generalised value incongruence" arising from unprofessional and unethical conduct (Sitkin & Roth, 1993, p. 303). Eberl et al. (2015, p. 1223) also caution that while ensuring rule compliance is a "quick-fix and short-term measure" for rebuilding trust, it often does not go far enough to address the lack of a "shared understanding of integrity" in order to evoke a fundamental change in organisational behaviour. Hazy distinction between investment and speculation in particular limited the efficacy of organisational rules in defining morally permissible in the banking and financial world. The danger and prospect of falling victim to either incompetent or deceitful management therefore remained tangibly real, as subsequent events would show.

Precisely twenty years later, the ultimate – and terminal – collapse of the Royal Bank in October 1867 seemed to imply that "all manner of stringent provisions' contained in its *Deed of Settlement* "have been useless" (*The Economist*, 16 Nov. 1867, p. 1294). *The Times* (23 Oct. 1867, p. 5) reported as follows:

> To inspire perfect confidence for the future, [in 1847] an entire reorganisation had been adopted, and it will now be an important question whether the peculiar conditions then framed with the view of completely preventing a recurrence of mismanagement have from that time to the present been faithfully fulfilled.

On investigation, it appeared that the causes of the bank's failure were disturbingly similar to that which triggered its suspension two decades ago. This time, it went into a contract to carry on insolvent shipping companies, again harping upon a "mischievous hope that by advancing a little more, what is already advanced may be recovered" (*The Economist*, 16 Nov. 1867, p. 1294). Credit was recklessly extended upon inconvertible shipping property. Above all, both the paid directors had borrowed huge sums from the bank which they failed to repay, together with the brother of the bank's manager (Turner, 2014). As *The Economist* (16 Nov. 1867, p. 1294) commented, to prohibit lending by a bank to its directors or managers is "easier said than done": insofar as they "have the custody of the till … if they want to help themselves they can". Notwithstanding the rules introduced following the embarrassment in 1847, a concatenation of misconduct and maladministration reappeared and finally broke the "old established concern" which once enjoyed "a high reputation for safety and dignity" (*Liverpool Courier*, reprinted in *Leeds Mercury*, 26 Oct. 1867, p. 2).

5.9 Conclusion

Both the Bank and Manchester and the Royal Bank failed at a time when there was expressed dissatisfaction from many quarters with the performance of joint-stock banks. The Peel government believed that tougher legislation was needed to enhance robustness and security of the banking system, by means of erecting entry barriers and weeding out the poorly managed institutions. Parliamentary intervention did not produce the intended result, however. Unlike modern banking crises during which a collapse in public confidence was commonly averted by government bailouts (Turner, 2014), the 1840s witnessed a few troubled banking entities – and the Royal Bank being one of them – successfully re-emerged from temporary suspensions through renewed cooperation between different parties. Even though the Bank of Manchester was not re-established until 1852 (see chapter 7), given the colossal loss and the prolonged liquidation process, the growing cordiality in the sustained relationship between the management and shareholders in bringing the company to a satisfactory close was fairly impressive. These remarkable outcomes were achieved with practically no recourse to legal apparatus of the day. Insofar as scandals weaken corporate legitimacy and undermine public confidence, these notable examples showed that the survival of troubled banking institutions was

highly contingent upon the robustness of their relationship with different clusters of stakeholders.

The process of repairing trust was of course not without difficulties. This chapter highlights some unique aspects in banking institutions that complicated the efforts to rebuild damaged internal relations with diverse stakeholders, often requiring self-imposed penalties, restraints, and a display of individual commitment which commensurate with public expectations of the moral calling residing in bankers. The first had to do with information asymmetry rooted in banking, arising from the obligation to pledge secrecy to customers' financial information. Because stakeholders were liable to interpret selective disclosure as malicious, and given their hypervigilance and susceptibility to paranoid cognitions and sinister attribution error at the start of the crisis, a demonstration of genuine benevolence and goodwill by the directors was therefore of critical importance (Kramer, 1996). Next, because trust failures and panics resulting from banking crises tend to be widespread and disruptive across the real economy, the success in defusing the impact of negative publicity depended critically on the management's effective capitalisation upon the shared perspective and identity between the company and local community. Thirdly, to the extent that unequal power relations bred the suspicion of corruption and abuse, and that the management must address competing agendas and expectations among different interest groups, trust restoration was facilitated by the board's endeavour to actively engage stakeholders through dialogues, to offer reasonable relief and reparation, and to tactfully abstain from exercising corporate power.

Another important lesson is that insofar as adverse economic conditions are often cited as handy excuses for the collapse of banking institutions, there appears to be an unchanging principle that "failure was a morally justifiable outcome of irresponsibility in the face of reposed trust" (Wilson & Wilson, 2013, p. 72). Criticisms developed in the 1840s that (some) bankers had grossly underestimated the importance of risk management and credit provision. Such functions and their embodied values extended beyond the letter of the law under which banking entities were held liable in the event of trust failures. Among others, while the collapse of the Bank of Manchester took place under the "unreformed" regime of light-touch regulation, post-1844 banking crises illustrated the famous remark by the English financial journalist Hartley Withers that "good banking is produced, not by good laws, but by good bankers". Something far more than "parliamentary enactment" was needed (Thomas, 1934, p. 415). The sense and scope of responsibility vested in Victorian banking institutions were invariably conditioned by

the working of the moral principles, in which banking practices came under constant public scrutiny and appraisal as articulated by the press media. To repair trust effectively, troubled institutions must recognise their "calling" within the community not to harm individuals, taking responsibility for the systems in which they functioned and of which they had specific knowledge (see Herzog, 2019, p. 535). This recognition emphasised the obligations of banking companies to vindicate themselves as "occupants of positions of responsibility" capable of acting in the best interest of the community (Wilson & Wilson, 2013, p. 72). Indeed, the following decade would again witness a spate of banking scandals that triggered a sense of moral panic and prompted the state to act more resolutely by making misrepresentation more easily punishable by law.

Chapter 6
Lessons (Un)learned: The 1850s
The Liverpool Borough Bank and the Same Old Mistakes

6.1 Background

On 17 February 1856, the discovery of the lifeless body of John Sadleir on Hampstead Heath in London led to the unfolding of one of the most obnoxious financial scandals in Victorian Britain (*The Times*, 18 Feb. 1856). Sadleir was no ordinary man: he was the Member of Parliament for Carlow, and one of the founding members of the Tipperary Joint-Stock Bank, which became an astounding success story by the mid-1840s. It followed that Sadleir – in complicity with his brother James who sat on the board – had misappropriated more than £280,000 from the bank to fund his speculative ventures in commodities and railway shares (O'Shea, 1999; Taylor, 2013a). When his schemes had failed and the bank was destroyed, he took his own life by drinking prussic acid, leaving many shareholders and depositors in utter financial ruins (*The Times*, 18 Feb. 1856). In September 1856, the nation was outraged by another lurid scandal when the Royal British Bank – a joint-stock concern formed under a Royal Charter in 1849 – collapsed. Notwithstanding a limited paid-up capital of only £15,000, the bank had advanced a whopping £100,000 against the security of some iron and coal-mining ventures in Glamorganshire, Wales (Thomas, 1934). The manager, Hugh Innes Cameron – alongside a few other directors – had borrowed heavily from the bank to finance their failed speculation which haemorrhaged no less than £50,000 (*The Times*, 4 Sep. 1856; *The Economist*, 6 Sep. 1856).

In autumn 1857, more bank failures followed when the commercial storm broke upon the nation (Thomas, 1934). On 27 October, the Liverpool Borough Bank became the first institution which succumbed to the crisis, only to be closely trailed by the Western Bank of Scotland and the Northumberland and Durham District Bank in the following month. The Borough Bank had accumulated an alarming volume of bad debts in the preceding

decades, and its exposure to American trade and shipping – which suffered deeply during the panic – compounded its parlous condition further (*Liverpool Mercury*, 28 Oct. 1857). The sign of trouble began to emerge in 1854, when many of its borrowing customers involved in colonial shipping trade were pounded with heavy losses, threatening to wipe out the bank's entire reserve fund (*Liverpool Mercury*, 28 Oct. 1857). It soon became apparent that the management had been massaging the financial reports for years, so as to inflate the values of loans securities and hide the bad debts from public view as long as possible (*The Times*, 28 Aug. 1858; 21 Oct. 1858; 29 Jan. 1859).

By 1847, the rapid expansion of joint-stock banks was itself a vindication of its superiority in facilitating the nation's burgeoning trade and industrial activities. However, banking reforms undertaken in the 1840s – which were supposed to stamp out fraud and protect investors via the enforcement of publicity and disclosure – had failed to check malpractices in corporate reporting. The series of banking failures in the 1850s discussed above led to serious questions about how boards of directors had neglected – and sometimes knowingly exploited – the interests of shareholders (Nordberg, 2010). Whilst legislation and the mechanisms of corporate governance should in theory restrain the behaviour of organisational agents (i.e. directors and managers), in practice there remains a wide range of actions where they "exercise discretion and decide what is fair" (Nordberg, 2010, p. 176). Repeated incidents in which banking institutions abused the trust which was intrinsic in their economic functions gave rise to what Taylor (2013a, p. 109) terms as "a new urgency in debates, a growing sense of moral panic". Herzog's (2019, p. 531) "responsibility-based account" of banking ethics suggests that bankers are essentially responsible towards both their customers and the society as a whole. As Flores and Solomon (1998, p. 209) reckon, "it is not just the character of individuals that is in question here but the character of relationships and institution". Smith et al. (2017, p. 413) similarly posit that as one of "the most powerful occupations" banking should discharge its "paramount duty to the public interest in important social and economic institutions".

Using the Liverpool Borough Bank as a case example, this chapter seeks to understand how legislators, bankers and the wider public construed and responded to the underlying problems in banking governance and legislation during the 1850s crisis. The decade witnessed serious attempts by the state to criminalise corporate delinquency, offering investors "a protection infinitely more effectual" amidst further waves of economic deregulation (*Morning Post*, 23 Sep. 1856, p. 4). As opposed to the preceding chapters which explicitly focus on the challenges and constraints encountered by bank

management during the process of repairing trust, this chapter takes a step back to consider from a broader perspective the (re)interpretation of organisational trustworthiness and accountability during the decade, following the failures of legislation and corporate governance to make banking institutions more robust and reliable. For this purpose, this chapter uses some contemporary perspectives of organisational trust – in connection with Sternberg's (2004) critiques of the best practices of corporate governance – to understand the complexity of trust-related issues across multiple agents and levels. There are three broad questions to answer in this chapter: (1) how far a breakdown in corporate governance explained the firm's failures; (2) how ethical and legal discourses influenced the credibility and relevance of corporate information in relation to making intelligent judgements on corporate matters, and (3) how, and by whom, the terms of accountability and transparency in relation to corporate disclosure were determined in the face of competing informational needs among different stakeholders. To answer these questions, this chapter also considers how the publicity role of the press, the toughening legal attitude of the state, and the opinions of commentators, had mingled to (re)define the expected traits, standards, and practices in trustworthy and responsible banking. In so doing, the chapter provides a contextualised framework for understanding the crisis as an event contributed by individual, organisational, and systemic factors, which plays out "in the full glare" of the print media and puts the interests of the public at stake (Gillespie et al., 2012, p. 192).

The chapter is broadly outlined as follows. The next section maps out the growing public concern in the face of recurring banking frauds and failures in the mid-century, citing the widespread suffering of shareholders and the legislation's failure to curb the excesses committed by the boards. The third section recounts the maladministration that brought about the downfall of the Borough Bank, and the legal implications the management had to encounter for publishing misleading financial reports. The fourth section analyses the breakdown of trust in the light of fiduciary failures of the elected leadership in forestalling perverse lending policies, which also escaped largely undetected under the surveillance of annual general meetings. From the case materials, the fifth section demonstrates the oft-repeated problems of relying on corporate reports to assess banking performance, which in turn led to clashing opinions about using supplementary measures such as independent audits and statutory regulations to restore financial accountability. The next two sections unfold the impact on trust repair dynamics introduced by the use of legal machinery to resolve disputes between bank management

and stakeholders. This development, which reflected the state's growing concern about the credibility and trustworthiness of Britain as a trading nation, was evidenced in two ways: first, the tougher stance taken by the legislators to punish misrepresentation, and secondly, the streamlining of the liquidation process which afforded directors and shareholders the power to jointly appoint official liquidators under the Joint-Stock Company Act of 1857. The concluding section highlights how institutional (or legislative) consolidation interfered with the interpersonal aspects of trust repair efforts in shaping the trustworthiness of banking companies in the decade.

6.2 Legislative Failure, Governance Breakdown, and Moral Panic

As the *Bankers' Magazine* (Apr. 1856, p. 208) described, the 1850s was a decade of "banking mania" riddled with "inconsiderate and wild speculation". Newspaper columns and financial monographs attacked many joint-stock banks for their disappointing if not deplorable performance. David Morier Evans (1859b, p. 37), a prolific financial journalist known for his exhaustive exposition of commercial issues, noted that while many corporate failures in the 1857 crisis were attributable to overspeculation, "the darker portion" was taken up with "the records of fraud, and of a recklessness which was equivalent to fraud". *The Times* (26 Nov. 1857, p. 7) saw the system saturated with "gangs of reckless speculators and fictitious bill drawers", fuelling public anger that corruption had "eaten into the heart of British commerce". The extent of trust deficit was evident, suggesting the endemicity of decay in commercial morality. The *Glasgow Herald* (18 Sep. 1858, p. 4) launched no small excoriation against the directors of public companies for spreading "ruin and havoc far and near", and gambling with "the destinies of their constituents" whose trust they had barefacedly abused. "Better for the small tradesman to tie up his earnings in a stocking and hide it in his bed", *The Times* (9 Sep. 1856, p. 6) mocked, than to become depositors in banks "conducted on such lax principles".

The Borough Bank failure sat uncomfortably among a litany of scandals, and its own chapter of discredit seemed to be microcosm of a wider, broken system urgently in need of fixing (see Taylor, 2013b). A few noticeable changes had transpired during the decade, which were important for contextualising the crisis. First, legal reforms thus far had failed to snuff out the temptations of senior management who enjoyed "great latitude as to the investment of funds" to tamper with financial reports (Robb, 1992, p. 57). Apart from "outright embezzlements", balance sheets were falsified, and dividends paid out of capital,

"in which assets and liabilities seem like so many figures, selected for no other object than that of illustrating a strong disproportion" (Robb, 1992, p. 37; Evans, 1859b, p. 37).

Next, while shareholders were still criticised for failing to grasp an "accurate conception of the history of failed institutions" (*The Times*, 26 Nov. 1857, p. 7), public attitudes were clearly changing. This time, shareholders were largely viewed as passive victims falling prey to covert and pre-meditated conspiracy rather than greedy speculators who were oblivious to the dangers lurking beneath the system. Following the fall of the Royal British Bank, shareholders and depositors alike attracted public sympathy, as "their savings, the small pittances of old age", went up in smoke. The scandal inflicted "serious loss upon a very considerable body of customers", many of whom were "small traders and private individuals of limited means" (Evans, 1859a, p. 269). "In the annals of commercial fraud, we have never heard or read of more outrageous acts of rascality than they have perpetrated against the customers and shareholders", *The Times* (24 Sep. 1856, p. 6) thundered. Another article published in the same paper empathised that frauds and scandals of the decade had reduced many "from a state of fancied independence to complete poverty", who constituted only "a subordinate part" of the whole misery (*The Times*, 26 Nov. 1857, p. 7). Interestingly, the growing sympathy towards suffering shareholders also coincided with a mounting consensus among lawmakers that unlimited liability could not secure honesty in commerce (Taylor, 2013b).

Also, the Whig administration led by Lord Palmerston faced mounting pressure to subject corporate fraudsters to more severe legal punishments (Taylor, 2017; see *The Observer*, 7 Sep. 1856; *Blackburn Standard*, 17 Dec. 1856). The *Daily Telegraph* (6 Sep. 1856) urged that the board "should be made examples of, for the benefit of their brother joint-stock directors". "If there is one class of persons more than another whom society for its security should keep under lock and key", wrote *The Times* (24 Sep. 1856, p. 6), "it is just such men as the offending directors and managers of the Tipperary and British Banks". The Attorney General, Richard Bethel of the Liberal Party, thundered in the House of Commons that "few had been bold enough to submit a proposition on the subject", although the need for legislation was "universally felt" (*Commons Hansard*, vol. 145, 8 Jun. 1857, c. 1372). As scandals after scandals unleashed a wave of public criticisms demanding firm and just actions against what Bethel described as the "gross and most distressing exhibitions" of abuses which had become a conspicuous notoriety "to the opprobrium of the country" (*Commons Hansard*, vol. 145, 8 Jun. 1857, c. 1372),

legislative priorities began to shift "from prevention of fraud to punishment of fraud" (Taylor, 2013b, p. 108; see also Wilson, 2014).[5]

6.3 Lies, Losses, and Lawsuits

On 15 September 1857, the collapse of the value of railway securities in America left many British holders of about £80 million worth of its stocks and bonds in serious financial limbo. British banks – particularly those based in Liverpool and Glasgow whose economic fortunes were closely tied to trade links with America – suffered depletion in gold reserves and dwindling public confidence (Turner, 2014). On 27 October, the Borough Bank became the first institution to collapse in Northwest England. Founded in 1836 with a massive paid-up capital of £950,000 (its nominal capital stood at £1 million), the bank gained its lustre as one of the most well-established joint-stock banks in the region (*Liverpool Mercury*, 28 Oct. 1857). Years of large and indiscreet advances, over-reliance on bill discounting, and hefty losses resulting from the bank's disproportionate involvement in colonial shipping trade in 1854 – had finally caught up with it (*Paisley Herald*, 3 Sep. 1858). The bank's wealthy and respectable body of shareholders was a pledge to depositors that they would fully receive their money in four instalments over two years with an annual interest of seven per cent (*Morning Post*, 28 Oct. 1857; *The Standard*, 1 Nov. 1857). The firm was placed under the Joint-Stock Companies Act of 1857, which granted the shareholders and depositors the joint power to appoint liquidators to wind up the concern (*Manchester Guardian*, 11 Nov. 1857; *The Times*, 13 Nov. 1857).

The executive structure of the Borough Bank soon became a target of public criticisms. The board consisted of twelve directors, out of whom a managing committee of two managing directors and a manager was formed, who had exclusive access to the company's accounts. In 1854, Joshua Dixon, a native to New Orleans known for his banking experience among the Liverpool mercantile quarters, joined the board (*Paisley Herald*, 4 Sep. 1858). Three years later, he became a managing director – a position that

[5] *Commons Hansard*, 3s, 145, col. 1372 (8 June 1857); see also Wilson, *The Origins of Modern Financial Crimes*. Taylor (2017) usefully outlines the gradual toughening of the laws in dealing with corporate abuses. In 1857, the Parliament made a breakthrough and passed the Punishment of Frauds Act with little debate, making three main offences effectively punishable by criminal charges: (1) larceny and embezzlement, (2) falsification of company books, and (3) dissemination of false statements. Under the Act, the criminal law was now extended to directors and managers, covering both crimes of misappropriation and misrepresentation. Taylor (2017, p. 7) describes this legislation as an important watershed, given that "for the first time, company frauds were defined and punished in the statute books".

subsequently made him keenly aware of the bank's dreadful condition (*Glasgow Herald*, 1 Sep. 1858). Bad debts amounted to a staggering £334,500, which threatened to wipe out the entire reserve fund and cause a further capital loss of £30,000 (*Glasgow Herald*, 1 Sep. 1858). The discovery led Dixon to believe that no dividend could be declared. However, fearing a sudden collapse in public confidence and a possible run on the bank, the directors rejected Dixon's statement as speaking too unfavourably of the company's condition (*Manchester Courier*, 29 Jan. 1859). Overruled, Dixon reluctantly gave his assent to publish a report which was contrary to his finding (*Paisley Herald*, 4 Sep. 1858).

The report, which was published on 28 July 1857 – just a little under three months before the Borough Bank succumbed to the commercial pressure, soon became a hotly controverted issue at which point the directors' reputation – and Dixon's in particular – took a hit. According to the report, the paid-up capital stood at £1 million, the reserve fund £101,775, and the net profits for the year £69,318 – out of which £61,679 were distributed as dividends (*Glasgow Herald*, 1 Sep. 1858). While admitting that the entire reserve fund had been consumed by the loss incurred in 1854, the report assured the shareholders that the bank's "good genuine business" would allow the directors to declare a dividend of five per cent without trenching upon the capital (*Glasgow Herald*, 8 Nov. 1858, p. 3; *Liverpool Mercury*, 28 Oct. 1857). About a month later, two warehousemen by the name John Scott and Robert Robinson subsequently purchased a total of ten £5 shares, described as of "great value" in the report (*Morning Chronicle*, 28 Aug. 1858, p. 3). When the bank unexpectedly collapsed, on 26 August 1858, represented by a Liberal barrister Edward James the disgruntled pair took Dixon to court, on the allegation that he had "fraudulently contrived and published" a misleading statement (*Morning Chronicle*, 28 Aug. 1858, p. 3). The defendant was tried before Sir Samuel Martin of the Liberal Party, who was appointed the Baron of the Exchequer in 1850. Upon finding that Dixon's own assessment was contrary to that disclosed in the published statement, the special jury ordered him "to repay the purchase money" amounting to £142 (Taylor, 2013a, p. 119).

Dixon appealed against the sentence, and the case came before the Court of Queen's Bench on 4 November 1858, with John Campbell, the Chief Justice and a Liberal political figure, presiding over the hearing (*Glasgow Herald*, 8 Nov. 1858). The verdict was upheld, on the ground that Dixon had knowingly consented to publish an untrue report. Whereas in the past shareholders in civil suits "had typically struggled to win over judges and juries", the Borough Bank verdict marked a change in attitudes that shareholder

protection had begun to receive more serious attention in common law and equity suits (Taylor, 2013b, p. 119).

The liquidation process, which began under the Joint-Stock Companies Act of 1857, also met difficulties. The legislation was supposed to wind up the concern in a way which would "press the least severely upon the shareholders" and realise the assets "as fully as possible" in the interest of creditors (*Liverpool Mercury*, 10 Dec. 1858, p. 6). A shareholder committee was formed to receive information from the liquidators – Joshua Dixon, John Brancker, Peter Serjeantson, Philip Rawson, and Harmood Banner – from time to time. At the general meeting on 9 December 1858, the liquidators presented a report which shareholders found of little relevance. A vocal shareholder named John Bramley relentlessly pressed the board for information about the financial status of some borrowing customers and proprietors – including the director Robert Crosbie – who laboured to be discharged from their liabilities to the bank (*Liverpool Mercury*, 10 Dec. 1858). Lengthy discussion ensued and the meeting was adjourned to 16 December, when liquidators and shareholders collided in their views on the power and extent of disclosure afforded by the Act of 1857 (*Daily News*, 10 Dec. 1858, p. 2).

As the 1860s dawned, liquidation began to gather momentum. In September 1861, the Borough Bank had discharged £102,858 of its liabilities. By the close of the following year, the largest debts owed to the bank had been mostly settled – among which was Messrs. Fernie Brothers, a shipping company of Liverpool, had repaid the whole sum with interest of about £420,517 (*The Standard*, 19 Dec. 1862; *Daily News*, 19 Dec. 1862). In late 1863, the remaining collectible debts were mainly composed of bad or doubtful accounts, which required "constant vigilance and attention" but could not be hurried through in consideration of their delicate impact on shareholders (*Liverpool Mercury*, 18 Dec. 1863, p. 3).

6.4 Agency Failure

Boards of directors are supposed to be shareholders' "first line of defence in governance" Mehran et al., 2011, p. 9), as they represent the entire corporation which in turn constitutes "the property of the shareholders in aggregate" (Sternberg, 2004, p. 43). However, the Borough Bank crisis was among other financial scandals during the decade that illustrated the problematic principal-agent relationship in Victorian banking, and a crude exposé of the fact that the quality of directors as corporate governors is "considerably less in

practice than it is in theory" (p. 91). More specifically, there was "a simple failure" on the directors' part to understand their role in mobilising their assets and power to protect the interest of shareholders (p. 85). This section looks at how far the crisis was attributable to a breach of fiduciary duties by bank management, which prompted a rethinking of the (in)capacity of the governance structure to monitor the behaviour of senior leadership and hold them to account. It uses contemporary management theories to examine the Victorian articulation of the failure of organisational controls to regulate distrust.

As Freeman et al. (2012, pp. 94-5) observe, by the 1840s a sequence of joint-stock scandals involving "undeniably affluent directors" had already challenged "the automatic right of the wealthy to rule" and led to "the floating of meritocratic ideas". In the case of the Borough Bank, not even the name of the philanthropic William Rathbone (1819-1902), with his distinguished background as a notable merchant and Liberal politician, could secure the company's soundness and stability. A few business tours to America in the 1840s kindled his interests in commercial affairs and made him an ardent advocate of free trade. In late 1841, he became a partner of his father's firm, Rathbone Brothers & Co., whose fortunes were dwindling then. With his brother Samuel Greg Rathbone, he successfully revived the company, broadening its operation and establishing branch houses in China and an agency in New York. A fleet of clippers was built to accommodate its rapidly consignment business. Rathbone was a notable figure on the board of the Borough Bank, a large shareholder and the chairman of the directors, whom the *Liverpool Mercury* (reprinted in *Leeds Mercury*, 14 Nov. 1857, p. 3) described as "one of the most upright, honourable, and benevolent of townsmen", given his relentless commitment to poverty relief and philanthropic activities in the town. Failing to detect the coming stoppage, Rathbone persuaded a lady "a short time ago" to purchase the bank's shares to the extent of £5,000. When the bank failed, he returned her money in full and transferred her shares to his own name, acting in "so noble a manner" that the daily extolled him as a gentleman deserving the "highest admiration". Both "in public and in private", as the paper remarked further, Rathbone's behaviour was characterised by a "high sense of honour" – a fact especially well known to his inner circles of acquaintance.

However, the bank's woeful state revealed that the directors needed far more than what Sternberg (2004, p. 43) terms as "influential contacts" or "specific business experience". As the shareholders met on 29 December 1859, John Bramley-Moore (1800-86), who was also a Conservative politician, a notable local figure because of his chairmanship of Mersey Docks and Harbour Board, vociferously exposed a series of

malpractices which had gone unnoticed for years (*Glasgow Herald*, 31 December 1859). Two directors audited and signed the 1847 balance sheet, after which annual statements were never again "duly and properly" certified for their accuracies. It was not until April 1849 that the management started to keep a minute book, and the entries thereafter were "meagre and miserable in the extreme". Since 1841, many bad or doubtful accounts which the directors feared to lay before the shareholders had been "carried on from year to year as good". A sum of £28,078, for instance, was lent to a brewer on a lease which was "worse than worthless"; another £34,000 was advanced without any security to a person unworthy of credit for "a tithe of that amount", and a further £44, 59 to a surgeon, whose gallipots Bramley-Moore sarcastically presumed the directors would be happy to accept as security. Prior to this, *The Economist* (18 Sep. 1858, p. 1044) also similarly remarked that the bank had undeniably "lent itself to overtrading". Members of public also suspected that the directors had given "too great facilities to speculators" (*The Huddersfield Chronicle*, 31 Oct. 1857, p. 7). Bramley-Moore's attacks were forceful and influential, probably because of his active involvement in the region's economic and political affairs. In 1841, he was elected an alderman by the Liverpool borough council – a post which he retained until 1865. Bramley-Moore's ambitious and expansionist strategies also drove the Liverpool dock committee to becoming the most prominent and established port authority in the nation (Sutton, 2004).

The fact that the Borough Bank directorship was taken up by wrong candidates could be explained with reference to two agency problems termed as adverse selection and moral hazard (Eisenhardt, 1989), which tend to worsen in the face of imperfect information and market uncertainties. Adverse selection has to do with the shareholders' limited capacity to evaluate the ability of agents (i.e. directors) to perform their duties. Moral hazard occurs when shareholders cannot ascertain if board members had duly acted "in furtherance of the contractual objective" (Bourke & Bechervaise, 2003, p. 68). In the absence rigorous regulations, good names and morals were the basis on which directorial candidates were judged for their suitability (Johnson, 2010). The *Bankers' Magazine* (Mar. 1850, p. 131) revealed the absurdity of the appointment process:

> One director is chosen because he is engaged in active business on his own account, and is supposed to know what is going on in commercial circles; another is elected because he is not in business, and is therefore free from the rivalry of trade and the temptation to speculate. One man is chosen because he

has spent all the past years of his life in India or Van Diemen's Land; and another gentleman is elected because he happens to be a Member of Parliament, or a distant relation of some railway potentate.

Commenting on the Borough Bank crisis, *Paisley Herald* (4 Sep. 1858, p. 3) wrote that the directors' only contribution was "the sanction of their high names, and the lustre which could be shed about the bank by their undoubted respectability" (see Table 6.1). *The Economist* (18 Sep. 1858, p. 1044) similarly remarked that those who pledged their names to the management "trusted too much to the wisdom and prudence of others, and suffered their names to be used as guarantees for a safe and legitimate transaction of business, in regard to matters of which they could not have personal knowledge". While agency problems seem to approach imperfect information as a symptom of a dysfunctional market in need of corrections, Kirzner (1979) nonetheless sees it as a common market process which all participants must experience. This argument seems to explain why the Whig administration (as this chapter will discuss later), on the whole, was more concerned about making frauds punishable by law than improving market information.

Table 6.1
Liverpool Borough Bank
Board of Directors (1856-7)

Chairman:	William Rathbone	
Deputy Chairman:	Christopher Bird Jones	
Directors:	Edward Benn	Duncan Kay
	John Cropper	David Lamb
	Robert Crosbie	Joseph Pater
	Joshua Dixon	James Ruder
	Robert Edison Harvey	Thomas Sellar
Manager:	John Peter George Smith	

Source: *Liverpool Mercury*, 28 Oct. 1857, p. 5.

Second, the bank's managerial structure partly had much to contribute to the organisational decay. Those who were not part of the managing committee – or the "outside directors" so called – had little knowledge about the true state of the company. Dixon's knowledge (quoted in *Lloyd's Illustrated Newspaper*, 14 Mar. 1858, p. 5) as an

insider was particularly illuminating, acknowledging that the problem was by no means unique to the Borough Bank:

> … the practice of the directors of this bank in respect to not having an insight into its affairs is not by any means unusual or exceptional. It is not the only bank in the kingdom where the outside directors know little or nothing at all.

As "gentlemen of eminence and standing in the town, high in the mercantile world" (*Paisley Herald*, 4 Sep. 1858, p. 3), the directors "knew little or nothing" about the bank's affairs and appointed two managing directors who "knew a great deal about them", who in turn delegated the duties to another manager that "really knew and directed everything" (*Glasgow Herald*, 1 Sep. 1858, p. 3).

As Gilbart (1859, p. 226) pointed out, in Victorian joint-stock banks active administrative power was commonly vested in the manager, or a few managing directors, and in certain cases, "a changeable committee". To forestall errors and abuses, in all cases directors prescribed the general principles and rules of governance, and "all very important matters are reserved for their special consideration". Sternberg (2004, p. 85) offers a contemporary perspective that it requires moral courage on the part of directors "to cope with confrontation" by asking hard questions, obtaining satisfactory answers, and taking needful actions in the best interest of shareholders. The Borough Bank affair epitomised the vulnerability of public companies to individual failings as Freeman et al. (2012) have observed. The concentration of informational power in the managing committee had seemingly undermined corporate accountability, where confidential matters were "kept under lock and key" and thwarted opportunities for early error detection (Trebilcock, 1998, pp. 759-60). The agency failure was twofold: no board members were in possession of the expertise and information to perform the duty to question and challenge the managing committee, who at the same time were unfortunately ill-informed about their functional responsibilities (Sternberg, 2004, p. 87).

6.5 Profits or Puffery? The Failure of Financial Accountability

The Joint-Stock Bank Act of 1844, which required banking companies to publish annual audited statements, was proven a broken reed that it had failed to improve corporate governance and accountability. The 1850s scandals demonstrated the skilfulness of bank

management in courting stakeholders' trust or public confidence through false pretences. Predictably, the Borough Bank's farcical book-keeping went down badly at a time when fraudulent financial reporting had tarnished numerous banking institutions. Robb (1992, p. 148) outlines that between 1856 and 1900, "there were no legal specifications as to the keeping of proper books and accounts, nor was there a mandatory audit for most joint-stock companies". Because senior leadership assumed the power to determine the structure and substance of financial reporting, Thomas (1934, p. 585) notes that it was easy for those who were intent on fraud "to deceive or to obtain the collusion of other members of their own concern". Staubus (2005, p. 5) questions the usefulness of financial statements, insomuch as they contain "errors so material as to require restatement" that they fail to guide investors in matters pertaining to capital investment. Through historical lenses of mid-Victorian society, this section examines with the aid of contemporary theories how far the purposes and procedures of financial reporting ideally resonated with the underlying values of corporate accountability and transparency. In so doing, it considers some arguments about the challenges and limitations of financial accountability in relation to the impact on shareholder activism in improving banking governance.

At the outset, the move by the Borough Bank directors to pressurise Dixon into publishing a somewhat less petrifying report reflected the oft-recurring concern that corporate reporting was festered with half-truths. The objectivity of the report was also called into questions because they were prepared by auditors who were at the same time directors of the company (*The Times*, 12 Sep. 1856). The *Bankers' Magazine* (Jan. 1856, p. 5), in fact, referred to the 1850s scandals as examples of "how utterly futile is the dependence upon directorial reports – published and audited accounts, or even the payment of respectable dividends, as a criterion of the prosperity or the solvency of a joint-stock bank". From the contemporary perspective afforded by Staubus (2005, p. 15), corporate misinformation constitutes an institutional flaw, where the liberty premised upon free-market capitalism has been "sabotaged by defects in systems of corporate governance" that had invested excessive power in the board members, who were *de facto* "the servants of the owners". An undue reliance on audited financial reports to construct a neutral assessment of corporate performance gives rise to a perverse incentive on the part of senior management "to render favourable reports on their stewardship" (p. 5). As the argument goes, "when the corporate governance system calls upon the management to report on its own management, so the motivation to report financial information that makes management look good is built into the system" (p. 6).

Upon the belief that publicity baffles every fraud and irregularity, mandatory corporate disclosure and audits are supposed to enhance transparency and underpin trust among stakeholders (see Johnson, 2010) that secures the company's long-term success and survival. Meanwhile, because senior management have strategic advantages when deciding matters of disclosure, external auditors help mitigate information asymmetries and moral hazard by judging whether financial statements are worthy of "a seal of approval" (Gaa, 2009; Shah, 2003, p. 179). Insofar as corporate reporting and audits are rule-bound, they harness "the constitution of trust" (Bachmann, 2006, p. 541). From this angle, the urge for independent and external audits in the mid-nineteenth century mirrored the contemporary belief that auditing – alongside the rise of legislation and professional bodies – is closely aligned with "impersonal structures" and forms a part of the broader "expert systems" that facilitate institutional trust and trustworthiness (Bachmann & Inkpen, 2011; McKnight et al., 1998, p. 119). Paradoxically, by introducing external auditors as intermediaries, shareholders' oversight of governance matters became less direct and more distant (Freeman et al., 2012). This is because audits are performed in a "grey zone" and "cannot be fully accounted for with reference to a rule system", and as a result shareholders are obliged to trust the auditors for their competence and integrity in fulfilling their missions (Mueller et al., 2015, p. 1195). By the middle of the nineteenth century, the reliance on summarised accounts and audited reports presented at the general meetings in fact signalled a further lurch towards financial secrecy and a decline in shareholder activism by the middle of the nineteenth-century.

For one thing, advocates of capitalism criticised that bureaucratic intervention had sometimes unknowingly undermined the foundation of individual responsibility in the marketplace. As *The Times* (12 Sep. 1856, p. 5) quite rightly pointed out, corporate publicity enforced by means of legislation had promulgated "a false confidence" that stifled "the habit of private vigilance":

> It was damaging whenever an event occurs from which men should be taught to gather for themselves a wholesome lesson, to seek to divert them from the true uses of the adversity by representing that it has happened not from any want of wisdom on their part, but from the neglect of statesmen to frame preventive checks.

To make things worse, “a multitude of regulations” had instead confused the general public and given devious schemes “increased openings for evasion” (*The Times*, 12 Sep. 1856, p. 12). The strongest safeguard available to shareholders was entrusting the entity to men of competence and integrity, with regular internal check by personnel who had the insight and knowledge necessary to forestall misconduct. Against this notion, *The Observer* (29 Nov. 1857, p. 2) was baffled by the regularity at which unsuspecting shareholders accorded to their directors “every mark of consideration, or even of gratitude” and happily placed all efforts towards resuscitation “under their auspices”. The article condemned the “overacted unanimity” at each general meeting, during which “every allusion to the ‘interests of the district’, the ‘proud display of public spirit’, and the necessity for avoiding all ‘hostile feeling’” had seemed to lull all parties to a sense of false security.

Criticisms targeted at the exaggerated power of financial audits in detecting frauds also grew increasingly vocal. The *Bankers' Magazine* (Dec. 1856, p. 797), for instance, penned the following:

> When those who are daily concerned in the management of a banking company are deceived in the estimate they may have formed of those doing business with the bank, how is it possible for strangers to the internal workings of the establishment, by a cursory glance at the bank's books, to arrive at any conclusion on the subject?

To *The Economist* (9 May 1857, p. 503), to appoint (external) auditors was just another “pretended caution, which above all others has been a fruitful source of deception”. Their duties were “a mere mockery and delusion”, the paper contemptuously remarked. Criticisms of a similar tone continue into the following centuries. The historical study by Thomas (1934, p. 584) exposes the auditors' limited ability to enforce “a sound system of check”, as growing banking operations and branch networks had rendered “any attempt at thoroughgoing audit not only a matter of extreme difficulty and heavy expense, but also one which was almost bound to be unsatisfactory”. Sternberg (2004, p. 71) also believes that auditors only play a “peripheral role” and have little to do with detecting frauds or operational problems within the wider governance framework. Their primary function is to provide a “true and fair” picture of corporate performance – a formal task which does not require them to be “general purpose detectives” (p. 73). The faults

attributed to the auditors have usually been those of the senior management or even shareholders themselves. By the mid-nineteenth century, complaints about legal laxity in punishing financial irregularities were becoming too loud to ignore (*The Times*, 12 Sep. 1856).

6.6 The Unlawfulness of Half-Truth

The civil charge against Dixon coincided with the emergence of legal discourses about what constituted misrepresentation. According to Wilson (2014, p. 133), financial misconduct in numerous joint-stock banks had undermined public confidence amidst the growing importance of banking to support industrial capitalism, and the notion of "financial crime" began to take root within Victorian consciousness as public anxiety and anger grew. Banking abuses were among the most recognisable outrages "as criminal offences old and new became part of its highly ambitious agenda of articulating law with capitalism" (p. 134). This section approaches the punishment of frauds and misrepresentation in the decade as a socially constructed process which incorporated particular values and principles, as legal agenda and public opinions (as expressed in the press media) formed a mainstream view to condemn misrepresentation and redefine financial accountability (see Taylor, 2013a). Because financial disclosure involved how corporate power is used in relation to the interests of stakeholders, this section also deliberates how banking scandals had unleashed a sense of moral panic, which in turn shaped the legal and cultural vantage of financial accountability. This contextualisation matters because the Borough Bank scandal took place at a time when the government began to mobilise legal machinery more forcefully to punish misrepresentation and frauds, amidst the growing concern that the nation's commercial morality was on the path of rapid degeneration. Legal punishments had, in effect, become a moral necessity, given Britain's reliance on reputation as a global industrial powerhouse and trade at that time.

First, intentional alteration of financial reports is not uncommon that it is done for various reasons, depending on the firm's situations and motives (Gaa, 2009). As shown in the case of the Borough Bank, legal implications set in once the neutrality of reports was violated, to the intent that it might induce the shareholders to behave as the board desires. With the bank being found in a state of "complete mess of ruin and desolation", James called the report "a gross misrepresentation" (*Paisley Herald*, 4 Sep. 1858, p. 3). Justice Hill accordingly concurred that Dixon had published "a falsehood with guilty

knowledge and fraudulent intent" (*The Economist*, 18 Sep. 1858, p. 1044; *Glasgow Herald*, 1 Sep. 1858, p. 3). Lord Campbell also rejected the management's rationalisation that losses had to be disguised so as to stave off a potential collapse in public confidence (*Elgin Courant*, 4 Feb. 1859, p. 3). The report was misleading that any "common person" or "man of business" would believe a dividend could be declared without straining the bank's capital (*Manchester Courier*, 29 January 1859, p. 11).

Ironically, by acknowledging his awareness of the bank's position being "far worse than he ever dreamed of", and that the capital had been "irretrievably lost", Dixon *himself* felt "he had done wrong and regretted the conduct he had pursued" (*Elgin Courant*, 4 Feb. 1859, p. 3). The fact that he was only appointed a managing director on 4 July 1857 – just twenty-four days before the report was published – did little to excuse him from his failure to act according to "the warning of his own conscience and common sense" (*Paisley Herald*, 4 Sep. 1858, p. 3; *Glasgow Herald*, 8 Nov. 1858). Having held Dixon guilty of "knowingly concurred" in a false report with "an intention of deceiving" (*Glasgow Herald*, 31 Dec. 1859, p. 4), Lord Campbell maintained that it was indefensible the firm had induced members of public "to become purchasers of shares and to run the risk of its bankruptcy" (*Elgin Courant*, 4 Feb. 1859, p. 3).

According to *Southampton Herald* (5 Feb. 1859, p. 7), the final verdict had "important bearing" on the legal responsibility of directors "in regard to speaking the truth". Commenting on the scandal of the defunct Commercial Bank of England whose directors were similarly charged for misrepresentation, Lord Wensleydale concurred that "it would be both a legal and a moral fraud", so long as the defendants presented a fact which was "true for a fraudulent purpose", while at the same time "not believing that fact to be true" (*The Economist*, 4 Sep. 1858, p. 977). Justice Maule remarked that "if a man, having no knowledge whatever on the subject, takes upon himself to represent a certain state of facts to exist … with a view to secure some benefit to himself or to deceive a third person, he is in law guilty of a fraud" (*The Economist*, 4 Sep. 1858, p. 977). As judges began to treat cases and apply the sentences more consistently, the boundary between acceptable and unacceptable behaviour became more distinctly drawn (Taylor, 2013a).

Second, the 1850s also witnessed legal articulations conflating with social inputs and situational factors to shape the legitimacy of the joint-stock economy, with Victorian periodicals actively underlining the legal and ethical benchmark for corporate reporting (see Kramer, 1999). In so doing, Taylor (2005, p. 238) asserts that "the Victorian populace was able to articulate its sense of moral superiority to its social betters, whose turpitude

was exposed for all to see". For long, as the *Law Review* (May-Aug. 1859, pp. 230-1) lamented, many directors of public companies were "nearly, if not quite irresponsible, for all that they said or did whilst seated behind the boardroom door", often escaping "with comparative impunity". Following the Royal British Bank scandal in September 1856, newspaper columns were crammed with "withering editorials", condemning the toothless criminal law to hold corrupt directors to account (Taylor, 2017, p. 6). *The Times* (12 Sep. 1856, p. 5) decried as follows:

> Until the wilful concealment of losses, the misappropriation of proprietary funds, and offences of this description generally, are made penal, and the prompt and inexpensive procedure of a criminal court can be invoked, it will be vain to hope for any improvement.

When Lord Campbell sentenced the Royal British Bank directors to imprisonment for false pretences, the public rejoiced that the law had finally "awakened" (*Law Review*, May-Aug 1859, pp. 230-1).

Because most offenders were drawn from "the cream of a very tightly configured social structure which was regulated by morality and class" (Wilson, 2006, p. 1075), there was growing need for ensuring that "a man's wealth and power do not put him beyond punishment" (Levi, 1991, p. 268). Delighted, *The Times* (30 Aug. 1858, p. 6) welcome the Borough Bank verdict as a step towards restoring "good faith and honesty", believing it would be received with "great satisfaction by all honest men". *The Economist* (4 Sep. 1858, p. 977) commented that with frauds undermining "credit and good faith between man and man", it would be "still more absurd and injurious" to leave the directors unpunished. By holding Dixon liable, the English law had acted in defence of "the first principles of natural justice and morality", the paper remarked. "The principle is as clear as it is just", *The Times* (30 Aug. 1858, p. 6) assented, "that if a man by a misrepresentation which he knows to be false at the time of making it induces another to commit any act, he is bound to indemnify him for any loss he may sustain by any such representation". The norm was emerging that a man was legally bound by his statements to "either to carry them into actual effect, or to make restitution and indemnity, by way of damages, to the injured party" (*The Economist*, 4 Sep. 1858, p. 977).

Negative press publicity also went hand in hand with legal sentences to punish public figures for their unacceptable behaviour. Taylor (2005, pp. 240-1) outlines how punitive

"public interrogation and ridicule" of this sort could be, given that "well-born, educated men" would more keenly feel than common felons the reputational cost of public humiliation. In less than three years, the Royal British Bank directors had fallen "from being admirable expositors of the science of banking to being embarrassments to the banking community" (Alborn, 1995, p. 201). By comparison, Lord Campbell remarked that the Borough Bank affair was one of much "reputation as well as pecuniary loss" (*Elgin Courant*, 4 Feb. 1859, p. 3). The *Glasgow Herald* (18 Sep. 1858, p. 4) censoriously asserted that Dixon and the board through "innumerable misrepresentations" had destroyed shareholders' interests with "such perfect impunity". *The Economist* (29 Jan. 1859, p. 112) caught the mood and hammered home the message:

> … the most skilful deceivers have usually been men who, fearing a downright lie, have fitted their language so adroitly to what they know to be the real facts of the case, as, whilst misleading any man ignorant of them, yet to be capable of a construction consistent with those facts when they shall at last have been dragged to light.

From the Royal British Bank and the Borough Bank scandals emerged a distinction between "those found guilty of falsifying information and others found guilty of uttering information knowing it to be false" (Wilson, 2006, p. 1088). Notwithstanding the difference, the verdict – both legally and socially – revealed the embarrassments to which a well-respected, public figure could be exposed.

6.7 Distrust, Secrecy, and Legal Constraints

Gaa (2009) argues that firms are regularly torn between making material information public on the one hand, and keeping certain information confidential on the other. However, the fact that the suffering of Victorian stakeholders had "intruded into the public domain" was itself a challenge to the legitimacy of financial secrecy (Taylor, 2005, p. 232). As influenced by unequal power relations within the broader system of corporate governance, the strategic decisions about post-crisis disclosure are also bound up with ethical deliberations because of the dissimilar impact on different interest groups with competing demands and objectives (Gaa, 2009). This section assesses the impact on trust repair efforts made by the Borough Bank management, when legal constraints resulting

from the intermediation by the Court of Chancery had reconfigured the power relations, conflicts, and motives which in turn determined the firm's choice of disclosure.

Given the lack of progress and information, the general meeting called on 9 December 1858 was pervaded with growing discontent as shareholders' patience began to wear thin. Bramley-Moore was pleased with the presence of reporters, remarking that there had been "far too much secrecy" (*Daily News*, 10 Dec. 1858, p. 2), leaving shareholders "groping in the dark, not knowing where we were going to" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). Since the bank had collapsed, the liquidators only summoned the shareholder committee once in August 1858 to present a "a brief statement" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). The December meeting was called at such a short notice, Bramley-Moore protested, that shareholders could not examine but approve whatever "mass of figures" laid before them. Finding the report not containing "a particle of information", shareholders concurred that they had not become "any wiser" by its publication (*Liverpool Mercury*, 10 Dec. 1858, p. 6). More queries arose when it became known that the liquidators had sent a list of defaulters to the Chancery for a release from their liabilities – which included the director Robert Crosbie who could only repay £7,000 against £10,000 he owed to the bank (*Liverpool Mercury*, 10 Dec. 1858). The management accordingly granted Crosbie a relief by accepting the reduced payment, against "a great feeling of disgust at the circumstances of the case" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). Together with other shareholders, Bramley-Moore adamantly insisted: "We ask for publicity, and publicity we shall have" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). The directors dithered, arguing that "in the present depreciated condition of all kinds of property" publicity would expose the debtors to discredit and thus send the bank deeper into jeopardy (*The Times*, 14 Nov. 1857, p. 6). Bramley-Moore, however, insisted that "no [further] advantage can come from concealment", arguing that "as parties sufferings" the shareholders were entitled to receive "frank and full" information (*Liverpool Mercury*, 10 Dec. 1858, p. 6). The controversy demonstrated the way in which demand for publicity contravened the interests of borrowers who prioritised confidentiality, implying that they too assume a role in "the structuring of the corporate governance mechanism (Hickson & Turner, 2005, p. 176). Koslowski (2009, p. 105) maintains that secrecy forms an integral part of the bank's "own brand of professional confidentiality" and "the rights of personality" – with the latter deserving especial legal protection "to prevent infringement of personal rights or invasion of the private sphere". Such legitimacy nonetheless becomes challengeable because of the very "public nature" of banking crises (Wilson,

2006, p. 1083). On the wider scale, because a complex banking system facilitates financial exchanges between market agents and forms the backbone of the economy, a banking crisis, as *The Times* (26 Nov. 1857, p. 7) remarked, was more than an earthquake, a mere "great public calamity" for which no one could be held responsible.

Arguments arose as to whether the Act of 1857 prohibited liquidators from allowing individual shareholders to inspect the company's books without the Chancery's authority (*Liverpool Mercury*, 10 Dec. 1858, p. 6).[6] Turner asserted that "there was no limit whatever in any clause or act of Parliament which restricted the liquidators in making out that statement to any limits whatever" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). Having consulted the chief clerk of the Master of the Rolls, Bramley-Moore concurred that the liquidators were at liberty to supply "all the information they thought fit", although they were "perfectly justified" in denying shareholders the access if it impeded the proceedings (*Liverpool Mercury*, 10 Dec. 1858, p. 6). Frustrated, he pressed for an adjournment of the meeting, so as to provide the liquidators "time and opportunity" to prepare the required information – "and not, as now, to put us off with side winds about the advantage of the bank" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). The complaint echoed that of an anonymous writer named "A Member of the Stock Exchange" (1853, p. 46) that corporate gatherings had become "mere matters of form" when reports were provided "ten minutes before the meetings", in effect depriving shareholders of their capacity "to make valuable suggestions, and to put to questions, the replies to which might be of interest".

At the adjourned meeting on 16 December, reporters were barred from taking notes of the list of doubtful and bad debts laid before the shareholders, fearing that its publication "would be injurious to the liquidation" (*Daily News*, 17 Dec. 1858, p. 3). It also soon became clear that the liquidators had a tightrope to tread. On one hand, they were allowed within their locus to power to provide the "fullest information", provided that disclosures were not "calculated to prejudice the interests of the bank" (*Daily News*, 17 Dec. 1858, p. 3). They were, meanwhile, prohibited by the legislation to determine whether the directors were "guilty of dereliction of duty", unless shareholders had applied to the Master of the Rolls to investigate the bank's past transactions (*Daily News*, 17 Dec. 1858, p. 3).

[6] *Liverpool Mercury*, 10 Dec. 1858, p. 6; according to the seventh clause of the Act, "when an order has been made for winding up a company compulsorily, the court may make such order as they think just as to the inspection, by creditors and contributories, of the books and papers of the company, and such books and papers may be inspected in conformity with such order of the court, but not further nor otherwise than by the order of the court".

By mediating access to corporate information, legal arrangements had in effect divested shareholders of direct oversight over corporate management. The liquidators came under attack for acting arbitrarily, contrary to the expectation that they should consult both directors and shareholders "as to the best mode" of conducting the bank's affairs (*The Times*, 13 Nov. 1857, p. 7). Turner was disappointed that the shareholder committee – which was supposed to function as an independent "consultative body with which the liquidators could communicate from time to time" – had lapsed into "merely a kind of blind to the general body" (*Liverpool Mercury*, 10 Dec. 1858, p. 6). *The Times* (14 Nov. 1857, p. 7) similarly criticised the committee being obsessed with "picking as much as possible out of the fire" without properly investigating the causes of the failure.

Although the legal solution afforded by the Act of 1857 was less consultative than what the shareholders had desired, the outcome was far more conciliatory than the combative melodrama of the Royal British Bank, where "shareholders and depositors cut each other's throats for the benefit of none but the lawyers" (*The Times*, 14 Nov. 1857, p. 6):

> As no member of the former class could see his way to saving himself, by any kind of sacrifice or effort, from utter ruin, there was naturally no disposition to make any effort or sacrifice at all; so that resources which should have proved the security of the depositors were virtually unavailable (p. 7).

In the case of the Borough Bank, "timely and obligatory" legal procedures (*The Times*, 14 Nov. 1857, p. 6) had largely secured "unanimity and union between all parties concerned" (*Newcastle Journal*, 14 Nov. 1857, p. 8), by means of protecting shareholders from "personal arrest" just while assuring depositors of full payments (p. 9). Empowered by the Chancery, the liquidators realised the assets "as fully as possible" in the creditors' interests, enforcing payments from a minority few without inflicting excessive financial distress upon the entire propriety (*Manchester Guardian*, 11 Nov. 1857, p. 5; *Newcastle Journal*, 14 Nov. 1857, p. 8).

In the early 1860s, through the liquidators' "patience and tact", the firm had significantly reduced its liabilities and recollected most of its largest debts (*The Standard*, 19 Dec. 1862, p. 6). Seemingly, legal mediation had harmonised conflicting needs of divergent stakeholders and reduced potential discrimination against any group (Sitkin & Roth, 1993). Political inquiry and the mobilisation of legal apparatus had also gradually

become "an institutionalised and ritualised process of trust problematisation and (potentially) restoration" (Mueller et al., 2015, p. 1176). However, given that legalistic remedies are impersonal and increase "the perceived distance between different parties", they undermine interpersonal relationship by replacing "reliance on an individual's 'good will with objective, formal requirements" (Sitkin & Roth, 1993, p. 376). Arguably, active engagements coloured by intense moral and interpersonal appeals as witnessed in the earlier chapters are ostensibly missing here, perhaps pointing to how the "structural barrier" posed by legal remedies had made the relationship less direct, and reduced the importance of transaction history and familiarity which once reinforced the foundation of trust (Sitkin & Roth, 1993, p. 376).

6.8 Conclusion

The Borough Bank failed at a time when numerous cases of banking misconduct dominated public opinion and legal discourses about the fundamental problems in banking governance and legislation, giving rise to serious reflection upon issues pertaining to trust and accountability across the industry. Banking misconduct aroused considerable public anxiety and political attention because of their connectedness to the stability of the financial system that formed the lifeline of industrial capitalism. This crucial position underpinned the fact that banking companies carried with them a public dimension, from which the quality and behaviour of management had profound impact on public interest on a much wider scale. While it was scarcely plausible that the government and members of public desired to reverse the growth of joint-stock banks, there was nonetheless a growing concern that defective governance within individual institutions were responsible for triggering systemic crises and imposing widespread socio-economic costs on the rest of the economy. For one thing, the problems posed by adverse selection and moral hazard were of particular concern within the governance system, in which shareholders did not have adequate information and insight to form astute judgement as to the fiduciary fitness of the executives. Next, repeated occurrences of intentional manipulation of financial reports reinforced shareholders' suspicion that, as insiders, directors and managers would exploit informational edge for their own gains. The use of external auditors and inspectors – as agents who could control other agents (i.e. directors and managers) on behalf of shareholders – thus became an alternative measure for regulating distrust (Shapiro, 1987). Then, the very public nature of banking

disasters – as expressed in terms of the destitution and ruins inflicted on different ranks and classes of society, and the disrepute brought upon Britain as a trading nation – drove the government to punish financial misconduct more assertively through legal sanctions.

The debate about the inadequacies of existing governance practices and legal framework also indicated that trust and accountability in banking companies began to be structured (albeit loosely) around an *institutional* dimension. Meanwhile, extra-legal apparatus remained relevant in articulating banking legitimacy with respect to one's *interpersonal* standing (e.g. moral quality, social respectability, and individual responsibility). Both domains were not necessarily mutually exclusive. For instance, the verdict of Victorian judges on financial irregularities were (partly) informed by their appreciation of business morality and respectability in financial dealings, which in essence formed the ethical foundation and subjective references for trust and accountability (Garnett, 1998; Wilson, 2006). The press also criticised the ineptness of the company law to stamp out corporate abuses, invariably exerting pressure upon the state to toughen up legal machinery to punish unacceptable behaviour. Over time, as legal rulings were more consistently enforced and applied, and the parameters of acceptable norms in commerce gradually became more discernible, legal intervention helped restored confidence among market participants by reducing uncertainties caused by deviant behaviour (Taylor, 2013a).

On the other hand, there remained opinions that *institutional* trust was no substitute for *interpersonal* trust exercised under the guide and learning of one's moral responsibility. The imprisonment of the Royal British Bank directors – and the civil charge against Dixon – were examples of the government's warning to the commercial circles that certain modes of conduct would not be tolerated (Taylor, 2007). Another important legal milestone was the phasing in of the Joint-Stock Companies Act of 1857, which reorganised the liquidation procedures and resolved the concerns of different interested parties in a more predictable and stratified manner. Beyond this, both the government and press media had little appetite for using legislative intervention to improve banking governance. The idea that organisational credibility could be enhanced by employing external auditors and inspectors attracted little support still. The government remained reluctant to supplant the role of shareholders in safeguarding their own interests – an attitude informed by "a highly moral view of the responsibilities of shareholders", and a desire "to uphold the traditional regulatory roles of participants in commercial activity" (Taylor, 2007, p. 723). Equally, financial journalists and

commentators maintained that no legislation and external bodies could replace individual vigilance and circumspection in addressing trust-related matters. While legalistic remedies and external inspection seemed to have gained limited enthusiasm as favoured solutions in the 1850s, the crisis in the following decade would prove whether they would be well-suited enough to restoring lost trust.

Chapter 7
Safe as Houses? The 1860s:
The Consolidated Bank *vis-à-vis* the Preston Banking Company

7.1 Background

Perhaps it was a blessing in disguise that the prudent, principled, and prominent English banker and philanthropist Samuel Gurney (1786-1856) did not live long enough to witness the collapse of the long-established, renowned Overend, Gurney & Co. on 10 May 1866 – a firm which he took control in 1809 and turned into a giant bill broker "second to none" in London (Orbell & Turton, 2001, p. 424). Once an "old sound business", the "younger men now in charge" held bills of doubtful and toxic character, stuffing the firm's portfolios with "a sorts of flimsy paper" (Capie, 2014, p. 14; Turner, 2014). When the establishment became a limited-liability company in 1865, the loans – which amounted to £3.5 million – were worth only an estimated £711,500 (*The Economist*, 24 Nov. 1866). The firm was *de facto* insolvent by at least £4 million. As Walter Bagehot later commented in his *Lombard Street* (1873, p. 19), "these losses were made in a manner so reckless and so foolish, that one would think a child who had lent money in the City of London would have lent it better". The crisis triggered a wave of "sheer, violent panic" (Turner, 2014, p. 81) across the money markets that *The Times* (12 May 1866, p. 12) described the event as "Black Friday". The Overend failure was just a starter, for a few joint-stock banks would soon follow it down into the hall of shame, reinforcing the impression that mismanagement and misconduct had remained a stigma since joint-stock banking took off just about four decades ago.

On 11 May 1866, the English Joint Stock Bank became the first victim which failed following the collapse of Overend, Gurney & Co. Within just a little over two years since its establishment in January 1864, the bank grew rapidly and developed a large branch network composing of twenty-seven branches. Its tragic end somewhat resembled that of the Royal British Bank: three directors, and the general manager Samuel Finney, were

charged for conspiring against shareholders by falsifying the financial statements (Turner, 2014). The directors were also suspected of using the company's funds to artificially prop up the bank's share price since November 1865 (*The Times*, 20 Apr. 1869). The next casualty was the Bank of London, whose failure on 24 May 1866 was again precipitated by reckless advances, among which the Atlantic and Great Western Railway failed to repay £500,000 (Gregory, 1936). The most colossal failure was that of the Birmingham Banking Company on 14 July: its liabilities were a staggering £1.8 million against a meagre paid-up capital of £280,000. The manager owed £75,000 to the bank and five of the directors helped themselves to the credit facility (Crick & Wadsworth, 1936). On 21 October 1867, the Royal Bank of Liverpool – which once suspended payment but escaped liquidation during the 1847 crisis – failed again for lending massively to two insolvent firms (*Manchester Guardian*, 21 Oct. 1867). Two paid directors and the brother of the manager also failed to repay their debt to the bank.

Amidst a plethora of banking scandals, *The Economist* (23 Jun. 1866, p. 732) pessimistically editorialised that reviving a bank with a tarnished credit or ruined reputation was "as impossible as mending an egg". Against such defeatist spirit the Consolidated Bank and the Preston Banking Company stood out as exceptionals which suffered a stoppage but swiftly rebounded during the 1866 panic, confirming the contemporary management insights that trust can indeed be restored (see, for example, Gillespie & Dietz, 2009; Pfarrer et al., 2008). Formed with limited liability in 1863, the Consolidated Bank was a result of the amalgamation of the Bank of Manchester (re-established in 1852) with a London private bank named Heywood, Kennards, & Co. (*Manchester Courier*, 29 May 1866; *The Times*, 29 May 1866). Its managerial structure, consisting of directors from both Manchester and London, reflected the firm's expansionist agenda in serving broader commercial interests (see Table 7.1). The Manchester shareholders held 56,731 shares valued at £10 each, on which £4 had been paid, making a paid-up capital of £226,924 (Grindon, 1877, p. 298). Heywood contributed an equal sum, doubling the total to £453,848. By contrast, in 1844 the Preston Banking Company was incorporated by Royal Charter with unlimited liability and a paid-up capital of £100,000 (*Preston Chronicle*, 21 Jul. 1866). It enjoyed considerable confidence in the agricultural districts, and by mid-century it had steadily extended its business networks to Lancaster, Blackburn, Blackpool, Lytham, Garstang, Ormskirk, Fleetwood, and Southport (*Manchester Guardian*, 20 Jul. 1866).

Table 7.1
Consolidated Bank, Limited
Board of Directors (October 1863)

Chairman:	John Pemberton Heywood (London and Liverpool)	
Deputy Chairman:	Richard Smiths (Manchester)	
Directors:	James Bannerman (Manchester)	Edward Langworthy (Manchester)
	Matthew Curtis (Manchester)	Ivie Mackie (Manchester)
	Thomas Fairbairn (London)	John Pender, MP (Manchester)
	Alexander Finlay MP (London)	William Peacock (Manchester)
	Thomas Hankey (London)	John Pickersgill (London)
	Frederick Hankey (London)	James Aspinall Turner, MP (Manchester)
	John Kennard (London)	Benjamin Wilson (Mirfield)
	Coleridge Kennard (London)	James Wyllie (London)
	Adam Kennard (London)	
Managing Director:	Coleridge Kennard (London)	
Joint Managers:	John Farrer (Manchester)	Joseph Rice (Manchester)

Source: *The Economist*, 24 Oct. 1863, p. 33.

Using these cases for comparative purposes, this chapter considers the relative importance of interpersonal engagements and institutional arrangements over different stages of trust repair by addressing two pertinent issues: (1) how, and to what extent, formal and legalistic remedies were useful for restoring corporate credibility and overcoming public distrust, and (2) how the strategic choice of rebuilding trust via a mix of "interpersonal channels" and legalistic avenues were conditioned by conflicting expectations from different stakeholder groups. Considering trust failures as context-specific, this chapter argues that the rationale and effectiveness of different trust repair strategies also depended on how stakeholders and members of public interpreted the causes of organisational crises.

This chapter underlines two central arguments. First, while formal or institutional arrangements (e.g. the use of contracts, organisational rules, external audits, and legal procedures) serve as "administrative or symbolic substitutes for trust that can enhance the legitimacy of an otherwise suspect", they are less effective in addressing context-specific problems and reinforcing the rapport between the involved parties (Sitkin & Roth, 1993, p. 369). Secondly, and as such, informal and interpersonal initiatives (e.g. moral and interpersonal appeals) via dialogues, persuasions, and constant engagements with

stakeholders remain a complementary essential, given that the success of restoring trust and cooperation is necessarily cognisant of the mutual interdependence between different interest parties. Kee and Knox (1970, pp. 358-9) define this mutuality as "a trust situation" in which two parties are "to a certain extent interdependent with respect to the outcomes defined by their joint choices and one of the parties is confronted with the choice between trusting or not trusting the other". This chapter relates the above arguments to a few key developments in the mid-Victorian era. First, recurring crisis and scandals did not prevent joint-stock banking from becoming an established hallmark of Victorian capitalist edifice. What followed the rapid growth of joint-stock banks was a gradual relocation of the centre of corporate politics away from general meetings to the executives, with "more autocratic forms of government by directors and managers" replacing shareholder participation in corporate affairs (Freeman et al., 2012, p. 109). Second, the extension of limited liability to banking institutions since 1858 – coupled with the increasing role assigned to the Court of Chancery in winding up corporate affairs – also altered the dynamics of power and trust relations between different interest groups (Taylor, 2013a).

The chapter is organised as follows. The next section reviews the progress of joint-stock banking amidst changes propelled by the extension of limited liability and increased involvement of the Chancery in the proceedings of liquidation. The third section provides the historical narratives behind the suspension of the Consolidated Bank and Preston Banking Company, due to a poorly executed takeover and serious concentration of risks in lending portfolios, respectively. The fourth section considers the fiduciary failures in each bank and evaluates the appropriateness of corporate structures and policies in demarcating the executive power of decision-making. The fifth section focuses on the aversion of the interested parties in each bank towards the use of legal solutions afforded by the Chancery, and thus their decision to turn to external, reputable banking elites to untangle and harmonise competing interests within the banks. The sixth section looks at how the management appealed to the renewed support from stakeholders by evoking local patriotism and underlying economic values of the institutions. The chapter then proceeds to compare and contrast different responses, strategies, and degrees of commitment exhibited by each bank to carrying out organisational reforms. The final section brings the chapter to a close, pointing mainly but not exclusively to the relevance of interpersonal appeals in complementing legal and institutional façade to draw all interested parties together and drive them towards a common pursuit of organisational reintegration.

7.2 No Turning Back: The Progress of Joint-Stock Banks

The manner in which prominent leading banks rose above the monetary panics in the late 1840s and 1850s proved that they could withstand periodic financial storms so long as they were conducted prudently (Thomas, 1934; *Bankers' Magazine*, May 1846). As a new chapter of banking history began in the 1860s, the slow but sure decline of private banks seemed to confirm that they could no longer provide the economic and financial facilities befitting the country's needs in the nineteenth century (Thomas, 1934). On the contrary, given its larger and stronger basis the joint-stock system remained firmly on course to become the cornerstone of the national economy. As *The Economist* (8 Aug. 1863, p. 1) confidently echoed, with "a good proprietary", the networks of joint-stock banks were "capable of almost indefinite extension". The company law was reformed and adapted to facilitate and support the gradually maturing system, on which the economic prosperity and power of the nation were critically depending.

The mid-1850s saw the waning faith in unlimited liability as the golden rule in safeguarding the moral foundation and financial robustness of the joint-stock economy. The moralist view that shareholders were the authors of their own misfortunes – and that they must yield up their uttermost farthing until all creditors were fully repaid – was slowly giving way to the realisation that their capacity to enforce sound corporate governance was arguably limited. For one thing, both bankers and lawmakers were unsure of how far limited liability – as feared in the preceding decades – would necessarily fuel reckless speculation and dull the vigilance of shareholders. Although in principle a "decided opponent" to limited liability, Samuel Jones-Loyd – a Liberal politician and banker attached to the London and Westminster Bank – confessed that he struggled to justify why joint-stock banks should not be granted the equal privilege. Thomas Hankey of the Liberal Party, a shareholder who would later become one of the directors at the Consolidated Bank, cautioned that unlimited liability had quite the contrarian effect of undermining the prestige of joint-stock establishments by "deterring the great mass of respectable and cautious men" (*Commons Hansard*, vol. 148, 11 Feb. 1858, c. 1170).

In 1858, the Limited Liability Act – which had already become law in 1856 – was finally conferred upon the banking industry (Grindon, 1877). However, the take-up was slow, for many joint-stock banks adhered to the belief that unlimited liability remained a superior institutional feature that attracted the confidence of depositors (Acheson & Turner, 2008). As two of the oldest joint-stock banks in Manchester, the District Bank and

the Manchester and Salford Bank held on to the old principle, consistent with some prominent metropolitan joint-stock banks in London (Grindon, 1877). Among those that bucked the trend was the Consolidated Bank, which on 15 October 1858 adopted limited liability. Contrary to the general cynicism, the bank's deposits rose, and the base of shareholders became more widely distributed in the following years. Another example was Overend, Gurney & Co., a discount house in London, which adopted limited liability in 1865 but failed in the following year. As the *Bankers' Magazine* (Dec. 1861, p. 864) noted, it was only "in the progress of time", in the event of another monetary panic, that the resilience of limited-liability banks would be tested and revealed accordingly. Arguably, limited-liability banking was introduced "as a doubtful experiment": with many opponents prophesying its failure, even the most earnest advocates "did not venture to anticipate for it more than a qualified success" (*Bankers' Magazine*, Aug. 1865, p. 905).

The introduction of the Joint Stock Companies Act of 1862 had significant implication upon the contractual relationship between management and stakeholders in the liquidation process. It streamlined the winding-up procedures by vesting the Chancery with the "default authority" to liquidate companies in different ways: (1) forced liquidation by the court, (2) voluntary liquidation outside the court, and (3) voluntary liquidation under the supervision of the court (Taylor, 2013a, pp. 132-3). The new legislation also granted the Chancery the power to enforce payments with interest from the management who defrauded or misapplied the corporate money. "Most significantly", as Taylor (2013a, p. 133) observes, "if it appeared that any director, manager, officer, or member was guilty of a criminal offence, the court could, either on the application of anyone interested in the winding-up or of its own volition, direct the official liquidator to prosecute, the costs to be paid out of the company's assets". The reform agenda marked the government's resoluteness to facilitate the expansion of joint-stock banks by fixing the legal impediments which muddied the outcomes of liquidation. Notwithstanding the efforts, whether market participants were prepared to turn to the supposedly improved system for solution was quite a different matter.

7.3 A Tale of Two Banks

Since its establishment, the Consolidated Bank had been reputed as a "perfectly sound and healthy" institution (*Daily News*, 30 May 1866, p. 7). The bank's predecessor was the Bank of Manchester which failed disastrously in 1842. When the old entity was

reconstructed with its existing royal charter and new capital in 1852, it had since then been conducted "with much caution and circumspection" by an experienced directory (*Daily News*, 30 May 1866, p. 7). Its track record of "great prudence" continued when it went on to absorb Heywood in London to form the "Consolidated Bank". In autumn 1863, the bank expanded further by acquiring another London private bank named Hankey's & Co. and relocated to its premises in Fenchurch Street in the following year. The move allowed the Manchester establishment to tap a larger pool of banking talents and fill its board with "the most experienced members" (Grindon, 1877, p. 298; *The Times*, 29 May 1866, p. 10). The extensive connections enjoyed by the Hankeys in Norwich also provided the Consolidated Bank the advantage of opening a branch in that city (Grindon, 1877). With limited liability, the company's expansionist strategy attracted mixed responses. *The Economist* (8 Aug. 1863, p. 1), for example, commented with confidence that "a bank with limited liability is far wider and stronger than that of an ordinary private bank". A reader named "Vox" was sceptical, writing in a letter addressed to the *Bradford Observer* (13 Aug. p. 7) that "limited liability is good for shareholders, but not for the general public". Indeed, as the Consolidated Bank continued to grow in size and scale, it was about to encounter its greatest trial.

The timing could not have been worse. Scarcely had the nation emerged from the financial catastrophe precipitated by the Overend failure in May 1866, the Consolidated Bank was on the brink of disaster following its hurried acquisition of the impaired Bank of London. Established in 1855 as an unlimited concern, the London bank had been a large and profitable business until it locked up a considerable portion of its capital in a few miscalculated advances (*The Times*, 24 May 1866). In the weeks leading up to its suspension on 24 May, a sizeable volume of deposits and current accounts was withdrawn, while the bank's securities were illiquid to meet immediate financial claims (*Daily News*, 24 May 1866). Prior to its failure, an agreement was reached whereby the London bank directors would transfer the current and deposit accounts of its customers to the Consolidated Bank. On 27 May, the latter withdrew from the agreement, on the ground that the directors had discovered serious errors in the list of assets issued by the Bank of London (*Manchester Courier*, 29 May 1866; Turner, 2014). While the Consolidated Bank remained solvent, it was forced to temporarily close its doors and enter voluntary liquidation due to legal contentions stemming from the controversial deals (Turner, 2014). It followed that the firm was willing to settle the claims of all account holders but refused to undertake the liability owed to the bill holders of the failed London bank, sparking

allegations that the directors were partial to certain groups of creditors (*The Times*, 29 May 1866).

The closure of the Consolidated Bank spooked the market, after which a steep decline in its share price caused shareholders a hefty loss of "no less than a million of money" (*The Times*, 29 May 1866, p. 10). The "great inconvenience" caused by the suspension to its customers aside, the "legal difficulty" was in fact the board's greatest fear (*The Standard*, 29 May 1866, p. 7). Although the bank had ample assets to satisfy its customers' claims, it was almost certain that it could not resume business so long as the legal disputes dragged on. In the ensuing weeks, the board convened regular meetings with shareholders and creditors, actively engaging in dialogues so as "to arrange for a reconstruction" (*The Standard*, 29 May 1866, p. 7). Barely had the dust settled, another banking disaster was about to implode in the region.

On the morning of 19 July 1866, a crowd of anxious inquirers thronged the Preston Banking Company at Fishergate. A notice was posted at the main entrance, announcing that "[i]n consequence of pressure in the money market, and temporary embarrassments, this bank is compelled to suspend operations for the present" (*Manchester Courier*, 20 Jul. 1866, p. 3; *Preston Chronicle*, 21 Jul. 1866, p. 5). The Preston community had in the past witnessed two notable bank failures: the collapse of Messrs. Wilson, & Clayton in 1842, and that of Messrs. Pedder just a little under two decades later (*Manchester Courier*, 20 Jul. 1866). These were private banks, nonetheless, and in neither instance had the scale of calamity exceeded that of the Preston bank (*Preston Chronicle*, 21 Jul. 1866). Given that the bank "had considerably the largest business" in the town and "a very large connection" in the district, the stoppage had caused no small disquietude throughout North Lancashire (*Manchester Guardian*, 20 Jul. 1866, p. 3). Prior to the suspension, a rumour had already been in circulation that the managers struggled to recover loan payments, fuelling "the general feeling of mistrust in banks that has lately prevailed" (*Preston Chronicle*, 21 Jul. 1866, p. 5). Whispers emerged that the Preston bank was besieged by a series of runs more than its financial resources could cope. A total of £40,000 was withdrawn within two days that a stoppage seemed inevitable (*Manchester Courier*, 20 Jul. 1866).

Until then, as the *Preston Chronicle* (21 Jul. 1866, p. 4) remarked, the Preston bank enjoyed the reputation of being "one of the best businesses in the north of England", "the best investments for the shareholders", and "the most advantageous for the legitimate trade". On the whole the bank had been charting a stable and successful path until the

Lancashire Cotton Famine in the early 1860s severely paralysed Preston's cotton textile industry (Orbell & Turton, 2001). The bank's overconcentration on cotton trade – coupled with the huge advances it made on inconvertible securities – left the company highly vulnerable to the turmoil (*Preston Chronicle*, 21 Jul. 1866). A staggering sum of £400,000 was locked up in advances to two failed enterprises at Blackburn. Crippled, the bank later suspended payments, when some hard-pressed cotton manufacturers overdrew their accounts or mortgaged their properties (*Leeds Mercury*, 21 Jul. 1866). The board quickly worked with shareholders and creditors alike to revive the bank, striving to avert liquidation under the Court of Chancery. The company underwent somewhat painful reorganisation, primarily by closing down branches at Blackburn and Lancaster, downsizing its taskforce, and recruiting a new management team. After a five-week suspension, the bank successfully resumed business, although the closed branches never opened again (Orbell & Turton, 2001).

7.4 Rules, Role Autonomy, and Discretionary Power

The joint-stock system was arguably known for the constitutional limits and role constraints it imposed upon the executives (Freeman et al., 2012). An anonymous commentator (1836, p. 109) once wrote in defence of joint-stock banks that "by a subdivision of labour, much useful work is accomplished, and a final determination on all subjects arrived at, in a comparatively short space of time", leading to improved business efficiency and financial outcomes. Organisational rules enhance trustworthiness by making one's behaviour more consistent and predictable (Gillespie & Dietz, 2009; Kramer & Lewicki, 2010). They also define organisational role by limiting individual autonomy, thus preventing organisational members from behaving opportunistically. At the same time, a role is far from "a set of rules that are slavishly adhered to", because it is susceptible to different interpretations, especially in the context of multiple parties with conflicting expectations (Perrone et al., 2003, p. 422). Following the stoppage of the Consolidated Bank and Preston Banking Company, the *Manchester Courier* (5 Jun. 1866, p. 3) expressed that "government by a board of directors is not a divine institution", and "not necessarily the final outcome of administrative inventiveness and wisdom". This section discusses how the underlying corporate structures and policies shaped and defined organisational role through the enactment of rules, guidelines, and procedures for decision-making and communication between members. Because organisational rules

and procedures were limited in their capacity to encapsulate unforeseen contingencies, questions arose as to whether the executives, with considerable scope for discretionary corporate power, could be trusted to make sound and fair decisions in the best interest of multiple stakeholders with ostensibly irreconcilable objectives.

Prior to the stoppage, the Consolidated Bank had been embarking upon a series of amalgamations and rapidly expanding its business networks beyond its centre of origin in Manchester (see chapter 6.3). As Mehran et al. (2011) caution, as business complexity grows, the knowledge and techniques required to cope with growing activities and portfolios progressively come under duress and strain, thus exposing the executives to greater risks of fiduciary oversight or conflicting role expectations. Expectedly, the directors caught flak for absorbing the business of the London bank. *The Times* (29 May 1866, p. 10) remarked that "[a]t any period a negotiation with a failing concern must, in the banking world, be one of extreme delicacy", and the hurried agreement with the London bank was "an impulse of insanity". The paper went on to criticise the directors for making a crucial decision without "the slightest foundation of security", and that the deal was "as careless and uncertain as if they had been framed for the very purpose of inviting difficulty". *The Economist* (2 Jun. 1866, p. 641) termed the mistake as "extraordinary", "almost revolutionary", and a "commercial suicide". The directors would not have entered into the agreement, the *Daily News* (29 May 1866, p. 9) asserted, had they correctly foreseen that the London bank stoppage "would prove the signal for an immediate run upon themselves".

According to the *Daily News*, (29 May 1866, p. 9), by acquiring the Bank of London the Consolidated Bank had in fact "undertaken more than it had courage or power to perform". To the extent that trust is conceptualised in reliability, predictability, and fairness (Perrone et al., 2003), the directors' choice "to give any preference to one class of creditors rather than another" from the London bank immediately threw the board into legal disputes and ridicule (*The Economist*, 2 Jun. 1866, p. 641). The shareholders, meanwhile, were distressed because their fortunes were "entirely at the mercy of any similar minority of directors". Against the assertion of Perrone et al. (2003, p. 425) assert that organisational agents demonstrate fairness by arriving at "mutually acceptable solutions for upholding the spirit of implicit commitments", the directors' outright refusal to honour the liabilities laid bare their failure to demonstrate discretion and competence as their role autonomy required (Perrone et al., 2003). Worse still, as the London bill holders threatened to apply an injunction from the Court of Chancery against any

preferential payments, "for three or four days" the directors "took no precautions to have the question quietly arranged, or to fortify themselves against any discredit that might arise" (*The Times*, 29 May 1866, p. 10).

To obfuscate the problem further, the London board took upon themselves "the grave responsibility" of closing the bank without consulting their Manchester colleagues (*Manchester Courier*, 29 May 1866, p. 6). *The Economist* (23 Jun. p. 732) called the move "fatuous" and a "wild folly". Henry Pochin, an alderman and a prominent shareholder who once led a consortium of Manchester businessmen in the formation of a few iron, steel and coal companies, sympathised with the Manchester directors who were unknowingly embroiled in the deal arising from "among a small section resident in London" (*Daily News*, 29 May 1866, p. 9). He found the bank unsatisfactorily conducted, "so that three, four, or five directors could walk about the streets, and at once constitute themselves into a managing power". The *Manchester Courier* (16 Jun. 1866, p. 2) criticised that the London directors had taken "a very imprudent step" and plunged the bank into "a very great difficulty". *The Times* (29 May 1866, p. 10) struck the board for their want of tact, calling the closure "one of the most extraordinary errors ever committed by men of business" that had caused losses of property "with such rapidity". A concern subsequently emerged that certain senior figures had been wielding too much power to make critical decisions "without the concurrence and support of the directors at large" (*Manchester Courier*, 16 Jun. 1866, p. 2).

The decision to shut down the bank was meant to be a mere contingency plan to liberate the firm from unanticipated constraints, which at that time had already impaired its routines. Several contemporary management scholars concur that one's circumvention of organisational rules to make arbitrary decisions is sometimes necessary and even desirable. As Eberl et al. (2015, p. 1221) opine, rules cannot prescribe an exact pattern of behaviour in a given situation because they are largely "formulated in abstract terms". Ortmann (2010) agrees that sometimes violation of rules is necessary to provide organisational members the flexibility to act under unprecedented circumstances. Wittgenstein (1953 cited in Eberl et al., 2015, p. 1221) likens rules to signposts, which "show the way, but do not determine action", and hence are subject to different interpretations as situations vary. Against all possible outcomes rule-breaking is inevitable and "cannot be fully pre-empted by even the most tightly defined prescriptions" (Eberl et al., 2015, p. 1221). It is therefore pointless to enact additional rules to determine "when to break a rule", which in turn is an issue in its own rights that must be decided on

"informal norms" (p. 1222). Role autonomy, in this instance, is crucial for overcoming organisational shocks which "cannot be specified in their role a priori" (Perrone et al., 2003, p. 423; Williamson, 1975), in which case the use of individual discretion provides signals to others about the agent's trustworthiness.

A way that organisational agents exercise their role autonomy is taking personal initiatives and making independent decisions by circumventing organisational rules (Perrone et al., 2003). They use their experience and expertise "to influence internal constituencies to accept and support the agreements reached with stakeholders" in the event of unanticipated eventualities (Perrone et al., 2003, p. 425). However, the arbitrary actions taken by the London board without consulting their Manchester colleagues backfired. As *The Economist* (2 Jun. 1866, p. 641) reported, "[n]o proceeding could have been more calculated to affright the public and restore the condition of panic from which we had barely escaped, than the arbitrary conduct of a minority of directors". *The Times* (29 May 1866, p. 10) echoed that "the emergency found the [London] directors so totally underprepared that they could do nothing but decide to close their doors", jeopardising "millions of property" and reigniting the fear from which the whole nation "was happily just emerging". Shareholders suffered hefty losses as the bank's share price tanked, and the inconvenience suffered by depositors alike was "incalculable". As the *Bullionist* (reprinted in *Liverpool Mercury*, 11 Jun. 1866, p. 7) similarly remarked, "their entire capital is locked up entirely, and partly lost beyond all redemption, and that obtaining is next to impossible".

The *Daily News* (29 May 1866, p. 9) also drew readers' attention to the "kind of personal conflicts" emerging between the London and Manchester board. As the Manchester directors strove to "do all in their power" to reorganise the business in the town, speculation began to emerge that the company would be "completely severed from any London establishment" (*Manchester Courier*, 1 Jun. 1866, p. 2). Although a split did not ultimately materialise, the underlying lack of synergy and coordination between London and Manchester seemed to imply the need for curtailing role autonomy to eliminate internal inconsistencies. Unlike other industries, in banking there appeared to be a strong case for tighter supervision and coordination at the organisational level, owing to the wide dispersal of risks among multiple participants. "That the directors must have earnestly desired to act for the best cannot be doubted", *The Times* (29 May 1866, p. 10) commented, "but it may be questioned if a similar sacrifice of property was ever effected with such rapidity, or under circumstances less rational".

The Preston suspension, on the other hand, had more to do with the lack of risk diversification and over-lending upon inadequate securities. The story was analogous to those of the preceding decades that banking institutions could "alter the risk composition of their assets more quickly than most non-financial industries", concealing their financial troubles by repeatedly extending loans to borrowing customers who struggled to service their loans (Levine, 2004). The Preston bank lent £400,000 to two tradesmen connected with the cotton trade in Blackburn – one of them was a yarn agent and another a cotton spinner (*Preston Chronicle*, 21 Jul. 1866). Prior to the suspension, the *Manchester Courier* (20 Jul. 1866) reported that the management had been pressing heavily for outstanding accounts in Blackburn, which the public believed to be advances on cotton transactions. Heavy discounting of the Blackburn bills had dented the bank's character within the financial community in London and Liverpool (*Preston Chronicle*, 21 Jul. 1866). In several quarters it had extended advances "to an unwise extent" and most of its securities were inconvertible (*Preston Chronicle*, 21 Jul. 1866, p. 5). As *The Times* (20 Jul. 1866, p. 11) echoed, the company's difficulty had been perpetuated by "long-continued advances to individuals on the security of mills and other property, which, however inherently valuable, are wholly useless in an emergency as a banking asset".

Given the Preston bank's position as "the general depository of the funds" of many local commercial houses and public bodies, the suspension had far-reaching ramifications (*The Times*, 23 Jul. 1866, p. 7). Tradesmen and workers of slender means were among those who most keenly felt the pain and inconvenience (*Manchester Guardian*, 20 Jul. 1866). A shareholder named Cooper harshly castigated that the bank's lending policy was "a disgrace to the town and to men of business" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Such "perfect madness", he fumed, had sunken so colossal an amount of money collected from agricultural districts into a "bottomless pit", putting "the lifeblood of the working class" at risk (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Large employers who had their money locked up in the bank were forced to suspend their works and deprive the workers of their rightful wages. With the loss of the entire share capital, shareholders consisting of "persons of substantial position and means" were anticipating a punitive call on their wealth (*Manchester Courier*, 20 Jul. 1866, p. 3). Of all 113, seventy-two shareholders were actively engaged in the cotton industry – including the chairman William Humber (*Manchester Courier*, 20 Jul. 1866; *Blackburn Standard*, 25 Jul. 1866). A reader named Argus criticised the bank's heavy involvement in cotton-

related enterprises and called for “an entire fresh appointment”, seeing that “the old directors have managed so badly” (*Preston Chronicle*, 4 Aug. 1866, p. 6).

The role autonomy of the managing board, and the unforeseen contingencies resulting from the impact of the crisis, had combined to expose the inadequacies of the governance structure to facilitate reliability-based trust (see Williamson, 1975). Insomuch as the role autonomy is determined through “on the job experience accrued” over their tenure in the organisations, it is their knowledge and power that give them the discretion to “make and uphold commitments” (Perrone et al., 2003, p. 424). However, as the *Preston Chronicle* (21 Jul. 1866, p. 5) reported, it was those directors who once commanded the reputation as “shrewd and cautious men of business”, and knew “the rock upon which so many similar establishments had foundered”, had ironically run the vessel ashore. Because a role is contingent upon a “set of recurrent behaviours appropriate to a particular position in a social system” (Polzer, 1995, p. 495), it connects the actions and attributes of the role occupant to the wider organisational system and society that define the acceptable behaviour (Barley, 1990). According to Shiller (2012, p. 55), the public “has a sense of the centrality, sobriety, and safety of banks”, knowing that bankers are in a “guidance or management role for the whole community” because of their economic influence and importance. The Preston bank crisis shows the lapses of competence in organisational leaders, that afterward proved disruptive to the local commerce as a whole. As the following section would show, it would take the involvement of a few external agents to mend the troubled bank.

7.5 Investigation: The Appeals of Professionalism

In the 1860s, although banking professionalism had not perceptibly materialised, something was clearly changing. Both cases of the Consolidated Bank and the Preston Banking Company denoted a notable shift to external parties with specialised and professional qualities to conduct post-crisis investigation. Alongside a rise in the appeal of professionalism, the boards found it equally important to unite all stakeholders towards a common course of reintegration through equitable financial arrangements, in preference to liquidation under the Chancery – a strikingly similar strategy to that deployed by troubled banking entities (the Royal Bank of Liverpool, for instance) in the preceding decades. This section addresses the functionality of institution-based trust, as embedded in impersonal structures such as the legal machinery and external expert systems, in

facilitating the process of trust repair (Bachman & Inkpen, 2011; Zucker, 1986). In this context, institution-based trust deals with one's readiness to believe that "the necessary impersonal structures are in place to enable one to act in anticipation of a successful future endeavour" (McKnight et al., 1998, p. 475). This section also discusses the role of integrative agreements formed between senior management and stakeholders in repairing trust. The projection of a credible image of commitment, fairness, and equity by the management, and the commendation and approval provided by the professionals, were equally vital for reinforcing the legitimacy of the agreements, thus facilitating trust repair efforts.

At the Consolidated Bank, legal challenges began to mount when the directors refused payments to the London bill holders. While the board claimed that their decision had the backing of the "opinion of two eminent counsels", the bill holders applied to the Chancery and obtained an injunction, under which the Consolidated Bank must undertake all the liabilities, effectively pre-empting any "preference of one class of creditors over another" (*The Times*, 29 May 1866, p. 10). On 28 May, the board submitted a petition to the Chancery to wind up the company's affairs, and Sir Richard Torin Kindersley was appointed official liquidator to administer the proceedings (*The Times*, 9 June 1866). His former appointments as Master in Chancery (1848) and Vice Chancellor (1851) made him a reputable equity judge in the nation. Within a week after the stoppage, the liquidators had paid about £1 million sterling from the bank's assets and contribution by shareholders to the Bank of England. As financial resources were sufficient to meet the bank's liabilities, the directors began to mull the possibilities of reopening the bank and retracting the administration of the affairs out of the Chancery (*Daily News*, 5 Jun. 1866; *The Times*, 9 Jun. 1866).

On 8 June, a committee was formed of a few Manchester directors uninvolved in the debacle to gauge the chances of resuscitation (Gregory, 1936). However, the progress was frustrated by legal disputes with the London bill holders, with the *Manchester Courier* (11 Jun. 1866, p. 2) hinting at the danger of "a long and protracted litigation" following the alleged preferential treatment given to a class of creditors over the other. Clashes intensified as the Bank of London denied the Consolidated Bank the right to withdraw from the agreement. The accounts taken over from the London bank also posed considerable difficulties in determining "in each individual case the nature and extent of the liability of the Consolidated Bank" (*Manchester Courier*, 11 Jun. 1866, p. 2). An agreement was eventually reached that the Consolidated Bank would return all assets

formerly owned by the London bank, and the bill holders were given the option of choosing between two banks they would "rank against".

A safe and effective resuscitation critically depended on the directors' success in acquiring unanimous support through compromise and cooperation from all interested parties. The board proposed that all debts to be repaid in four equal instalments over twelve months, "so as to secure the liability of all the present shareholders for the protection of the creditors" (*Manchester Courier*, 11 Jun. 1866, p. 2). The paid-up capital was to be buttressed further – either by issuing 50,000 shares at par, or making a call of £2 per share on the existing shares. The board also appointed a few "competent and clever persons, independent persons, and men of the highest standing" – including Kirkman Hodgson and John Peel – to jointly investigate the viability of the plan (*Manchester Courier*, 16 Jun. 1866, p. 2). The *Daily News* (23 Jun. 1866, p. 7) credited them as "men of first-rate business talents". Hodgson was a Liberal politician whose insight and acuteness in the banking world commanded the respect of William Gladstone. Once a partner in the mercantile firm of Baring Brothers & Co., Hodgson later became Deputy Governor (1861-3) and then Governor (1863-5) of the Bank of England. Peel was also a Liberal politician and had since 1863 been elected Member of Parliament for Tamworth. Although a centralised expert system that facilitates "standardisation across contexts" and provides "a key coordinating function" of the twenty-first century remained a distant prospect still (Barret et al., 2005, p. 19), it now became noticeable that the involvement of high-profile figures with banking and commercial experiences *did* inspire renewed confidence (Sztompka, 1999, p. 63).

Sztompka's (1999) sociological perspective on the transfer of trust explains how testimonies presented by professionals or the expert system could translate into renewed trust in the troubled organisation and its key leaders. Hodgson's professional experience and credentials, for example, gave considerable weight to his positive verdict of the Consolidated Bank. According to "the highest legal and the highest monetary authorities in England", he said without naming, the terms presented by the directors were "a wise and business-like and well-digested one" (*Manchester Courier*, 16 Jun. 1866, p. 2). To the extent that stakeholders trusted Hodgson and Peel for their competence and impartial judgement, they also trusted the emergent system in which the investigators were given the charge (Sztompka, 1999). In this sense, trust in the audit and investigative functions transcended different levels: from the interpersonal exchanges between the experts, executives, and stakeholders (Anderson-Gough et al., 2000), to the institutional trust that

society placed in the experts (Power, 1999). Potentially, as Gillespie and Hurley (2013, p. 199) suggest, trust repair at both the "micro-organisational level" and the "macro-level of the financial system" could be mutually reinforcing, as mediated through stakeholders' engagement with the system through individual firms.

A comparable pattern also emerged in the Preston Banking Company, which also engaged professionals and embarked upon similar strategies to pre-empt the involvement of the Court of Chancery. On 21 July, the first shareholders' meeting was convened to move the company out of "the present emergency" (*Preston Chronicle*, 28 Jul. 1866, p. 4). The board denied the reporters admittance, decreeing that nothing should be made public until the bank's position was satisfactorily understood. A committee was formed of six shareholders – Joseph Livesey, Robert Ascroft, James Hogg, James Whitehead, James Naylor, and Edward Rodgett – to investigate the affairs and the possibilities of reopening the bank. Extending over three weeks, the investigation was aided by David Chadwick, a gentleman of Manchester well-known to the banking and financial community. His involvement reinforced credibility of the proceedings, because of his presidency at both the Manchester Statistical Society and the Manchester Institute of Accountants, and more crucially, his past supervisions of many banks "in similar circumstances" (*Preston Chronicle*, 25 Aug. 1866, p. 2; *Lancaster Gazette*, 4 Aug. 1866). Chadwick began his career as an accountant in 1843, and rose to prominence as one of the nation's most prolific industrial financiers, so much so he was called in 1867 before the Select Committee to present his assessment of the Limited Liability Act. In 1866 alone, his firm, Chadwick, Adamson, McKenna & Co., investigated no less than four joint-stock banks: the Agra and Masterman's, the Bank of London, the Consolidated Bank, and lastly, the Preston Banking Company (Cottrell, 2004).

As shareholders met again on 25 July, a preliminary investigation revealed that the bank was financially "very much better than it was anticipated" (*Preston Chronicle*, 28 Jul. 1866, pp. 4-5). Revised estimated losses were halved, cutting shareholders' contribution to about a quarter of the initial projection of £200 or £250 per share. The reduced contribution was sufficiently ample to make a handsome working capital of £100,000. Ascroft vouchsafed for the accuracy of the statements prepared by Chadwick's firm, whose reputation in conducting financial investigation was such that "it would be superfluous for him to make any observations" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). The largest shareholder and a director named Bickerstaff warned that losses would quadruple had the bank wind up under the Court of Chancery (*Preston Chronicle*,

28 Jul. 1866). Livesey was confident that the establishment was "far from being in a hopeless condition", citing the examples of other banks which succumbed temporarily to financial difficulties but had since "overcome their difficulties, retrieved their character, [and] afterwards made fortunes" (*Preston Chronicle*, 28 Jul. 1866, pp. 4-5). "With good management in future, and a little forbearance on the part of all interested", he remarked, the Preston bank could similarly escape "the disgrace of absolute and permanent insolvency".

The committee worked with the board to propose two measures for carrying on the company, "in preference to an official or voluntary liquidation under the Court of Chancery" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). First, creditors would be fully repaid in four equal instalments over two years with an annual interest of five per cent. Second, shareholders were recommended to pay £100 per share in two instalments, providing approximately £200,000 to enable the company to discharge its remaining liabilities. A letter composed by "Argus" endorsed the proposals, intimating that some wealthy shareholders "will watch an opportunity to wriggle out", and that "the security of the depositors has no right to be depreciated" (*Preston Chronicle*, 4 Aug. 1866, p. 6). Accordingly, in addition to the bank's rule which prohibited any sale of shares without the directors' approval, a resolution similar to that of the Bank of Manchester in 1842 was promptly passed to bar shareholders from transferring their shares until all creditors were fully paid (*Preston Chronicle*, 4 Aug. 1866, p. 6; *Carlisle Journal*, 7 Aug. 1866, p. 2).

In the case of the Preston bank, the institutionalisation of the instruments for containing distrust coincided with the perceived demand for the intervention of external parties, who could be trusted to conduct investigation with accuracy, objectivity, with integrity (Mueller et al., 2015; Shapiro, 1987). As will be discussed in greater depth in the latter part of this chapter, Chadwick's appointment as the bank's first professional accountant appeared to signal the *beginning* of a new culture of accountability which promulgated a more streamlined or "perfect administrative control of institutional and professional life" (O'Neill, 2002, p. 46). The borough's mayor Charles Roger Jacson and a notable depositor named Edward Rodgett, "two gentlemen" in Lancashire who commanded "great confidence", were also appointed provisional liquidators (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Like Chadwick, they agreed to take the post "without fee or reward" – an arrangement which the board deemed "far better than having some accountant who would have to be paid for his services". Partly motivated by the bank's endeavour to introduce "a system of economy in every department" (*Preston*

Chronicle, 1 Sep. 1866, p. 5), Livesey believed that including them in the future management "would strengthen the directorate and give prestige to the concern" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866).

The discussion thus far shows that institution-based trust rests upon the belief that the activities of agents are compatible with the competence, integrity, fairness, and objectivity expected of their professional standing or qualifications (Sztompka, 1999). In the 1860s, although professionalism still remained a loosely defined term because of the absence a centralised body to prescribe standards and exercise disciplinary power, banking was slowly morphing into more tightly defined groups of individuals in possession of specialised expertise and technical competence, whose pursuit of vital economic activities and functions was governed by values of independence, autonomy, and moral obligations towards stakeholders (Smith et al., 2017). Until professionalisation became more formally recognisable by the end of the nineteenth century, face-to-face, in-person "trust-related interactions" between all interested parties in the face of adversity and all possibilities, remained a requisite component of trust repair efforts (Sitkin & Roth, 1993, p. 369).

7.6 Interactions: Sticking Together

In theory, the risk of trust failure could be contained by prescribing shared procedural norms and standards of behaviour (Bachmann, 2001). Legal procedures resemble "formal protections that characterise the public legal order" (Edelman, 1990, p. 1406), and thus projecting "the appearance of legitimacy and responsiveness" (Sitkin & Roth, 1993, p. 370). However, both case examples in this chapter reveal the aversion of most parties towards using the Chancery as the intermediary, citing the costly and lengthy process of litigation and the uncertain outcomes it could entail. Additionally, legalistic remedies also lead to "increasingly formalised relations", especially in times of crisis when conflicting parties "haggle over" the rights and procedures (Sitkin & Roth, 1993, p. 367). At "crucial junctures" or "field configuring events", trust is primarily constructed at interactional level (see also McInerney, 2008). Bachmann (2001, p. 463) also points out that an absence of "strong forms of system trust" enshrined in legislation and standardised policies results in greater reliance on interactional trust, cultivated through the display of competence, integrity, equity, and communicative skills. Building on these notions, this section shows how "more interpersonal and community-based forms of trust" usefully filled the gap and

complemented institutional arrangements, where the executives actively engaged and worked with the injured parties to ensure smooth and safe resuscitation (Mueller et al., 2015, p. 1173).

On 11 June, the Consolidated Bank management held separate special meetings with the shareholders and depositors, during which it soon became obvious that under a condition of interdependence, a positive outcome was contingent upon the consent of all parties (Sitkin & Roth, 1993). The Chairman, James Aspinall Turner, was explicitly against reopening the bank without shareholders and creditors accepting the directors' offer, so as to keep the whole concern from being delivered over to "the tender mercies of the Court of Chancery" (*Manchester Courier*, 16 Jun. 1866, p. 2). An anonymous shareholder from a London merchant of "the highest standing" urged that the directors' mistakes "must now be buried in the past" so that the bank might speedily recommence business (*The Times*, 20 Jun. 1866, p. 7).[7] Another shareholder named Simeon thought it was "in the interest of all that they should be united" to extricate the bank from the present difficulty. Pender, also a shareholder, was optimistic that the bank would soon awake and "occupy as good position as it had ever yet done". Although admitting that the London directors were "personally responsible for an error of judgement", the shareholders unanimously accepted the terms to avoid a "lengthy and costly litigation" through the Chancery, serving only to spread "a lawyer's feast" (*The Times*, 20 Jun. 1866, p. 7).

A few dissentient creditors stood in the way. Webster questioned if accepting the offer would give the London directors "a clean sweep and amnesty for all the mistakes committed" (*Manchester Courier*, 16 Jun. 1866, p. 2). Heywood also insisted that depositors had no reason to suffer "a positive loss" for which the directors were largely responsible. Two large creditors named Fields and Higgins, however, gave their "cordial assent" to the proposals and urged their peers to do likewise (*Manchester Courier*, 16 Jun. 1866, p. 2). Hanley argued that "they should act as lunatics" if they turned down the offer (*Manchester Courier*, 16 Jun. 1866, p. 2). A few letters written in support of the directors by a few notable merchants were read aloud in the meeting.[8] Thomas Clegg of Quilter, Ball, & Co. of Manchester, for instance, was confident in the bank's ability "to meet all demands upon it". Ahurst, Morris, & Co. thought it wise for all parties to "pull together" to revive the bank. Fearing that "it might be many years before they got any money at all"

[7] The letter was published in *The Times*, 20 June 1866, p. 7.
[8] The letters were read in response to the Chairman's speech during the meetings and published in *Manchester Courier and Lancashire General Advertiser*, 16 June 1866, p. 2.

if the Chancery was involved, all creditors gave their support "with singular unanimity" (*The Times*, 22 Jun. 1866, p. 6).

To improve the chances of a successful resuscitation, the board urged shareholders to subscribe the remaining 50,000 shares, so as to increase the existing stock of paid-up capital from £600,000 to £1 million (*The Times*, 23 Jun. 1866; *Manchester Courier*, 28 Jun. 1866), with the directors expressing their readiness to take up 25,000 shares if necessary. The proposal attracted mixed opinions. *The Economist* (23 Jun. 1866, p. 732) cautioned that having a large pool of capital when the business was still on the mend would tempt the board to make "a good dividend" via risky strategies. Given that the bank had just suffered a setback, the directors "have now no character for wisdom to lose", and the move would be "detrimental to their credit as well as hazardous in its results", the paper warned. However, inspectors Hodgson and Peel opined otherwise, arguing that further capital injection was necessary before the bank could be reopened "with hopes of profit to the shareholders and security to the public" (*Manchester Courier*, 28 Jun. 1866, p. 2). As June drew to a close, the shareholders confidently took up most of the new shares.

The discourse thus far proves that interdependence is a "trust related feature", under which "expectations about another's trustworthiness only become relevant when the completion of one's own consequential activities depend on the prior actions or ongoing cooperation of another person" (Sitkin & Roth, 1993, p. 369; see also Deutsch & Krauss, 1962). As shown in the Royal British Bank fiasco, the refusal of each party to compromise and cooperate resulted in amplified losses to all, measured in terms of costly litigation and delayed compensation (see Kee & Knox, 1970). Trust-related interactions were therefore primarily concerned with exploring the common ground on which affected parties exercise forbearance in the interest of maintaining long-term cooperation (Argyris, 1982). Importantly, according to Butler (1983), higher levels of mutual trust tend to emerge when relational trust behaviour from the other party is reciprocated. Until the end of 1866, the directors declined any remuneration, and shareholders agreed not to press for "a single penny of their dividends" until they had repaid the creditors "every farthing" (*Manchester Guardian*, 25 Jan. 1867, p. 3). Furthermore, scepticisms about the efficacy of the Chancery appeared to magnify the relative merits of goodwill, flexibility and individual autonomy – all of which were crucial for encouraging all parties to engage in collective reintegrative strategies. As Bachmann (2001, p. 360) posits, in a lightly regulated market with entrenched uncertainties in the legal procedures and outcomes,

market participants "need to secure the effectiveness of the coordination of their mutual expectations and interactions on the basis of individual experiences and resources".

Similarly, the fate and future of the Preston Bank rested with the endorsement of stakeholders of the proposed terms, without whose "indulgence and forbearance" the company could not hope to resume business", Livesey warned (*Preston Chronicle*, 25 Aug. 1866, p. 2). Under the *Deed of Settlement*, because no shareholder could get clear of their obligation "until every farthing was paid", fears surfaced that those of "slender means" would be "pounced upon" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). By accepting the terms, for at least a year the shareholders must be satisfied with much smaller dividends, as opposed to the customary twenty per cent in the past (*Preston Chronicle*, 1 Sep. 1866). To the creditors, the fact that the bank was constituted under unlimited liability, and that most shareholders were men of substance, were an assurance that they would be paid in full – although to some "it might be an inconvenience to have to wait for it" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Livesey cautioned that the involvement of the Liquidation Court and the Chancery would result in delayed payments "probably at very distant time", resulting in prolonged distress and destitution – especially among those of limited means. This scenario would be "the very worst thing that could come", he stressed, and the bank "would be in a far better condition for being disposed of and transferred than if it were shut up" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866).

In August, with the bank's financial position turning out to be better than expected, the interested parties were decidedly favourable of carrying on the company that they might preserve "a connection and business of so great intrinsic value" in Preston (*Lancaster Gazette*, 4 Aug. 1866, p. 2). The management strategically evoked their sense of local patriotism, emphasising that by revitalising the firm they would "feel proud that Preston had still a bank of its own" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Chadwick echoed that allowing the bank to fail would be "the greatest mistake in the world" and "an eternal disgrace" to the town, particularly given the relative ease of resuming the company's business (*Preston Chronicle*, 26 Aug. 1866, p. 2). Livesey's exemplary moral character also made him a fitting candidate to appeal to stakeholders' confidence. As a devout Christian, he was one of the most steadfast advocates of temperance in the century, believing that economic progress must proceed hand in hand with moral reform. Interestingly, despite his limited ownership of just a few shares, the shareholders recognised him – together with Ascroft – as among the most noble and

notable figures within the committee who had undertaken “a great amount of work in connection with the labour of resuscitation” (*Preston Chronicle*, 25 Aug. 1866, p. 2).

Thus far it is conspicuously clear that although disadvantaged by information and power asymmetry, stakeholders were by no means passive actors but capable of making informed assessment about the trustworthiness of the management, which in turn leads to “postures of trust or suspicion” (Gillespie & Hurley, 2013, p. 178). Aided by cues and signals emanating from multiple sources (e.g. past interactions, personal traits, press reports, and professional representation), they were able to gauge whether they could trust particular agents or institutions, and identify the extent of counter-measures they might undertake to protect themselves against possible harms (Gillespie & Hurley, 2013). Modern management scholars also concur that perceived trustworthiness is usually “a strong antecedent to trust” (Gillespie & Hurley, 2013, p. 179; see also Mayer et al., 1995). Within a “large socio-technical system” (Gillespie & Hurley, 2013, p. 179), banking consists of many trust relations established upon both personal and impersonal exchanges across multiple boundaries. In the presence of unlimited liability and prohibition of share transfers which effectively undercut shareholders’ ability to escape losses, the “impersonal, distance-enhancing, and context-specific” nature of legal intermediation through the Chancery was poorly positioned to foster individual goodwill and consent among affected parties (Sitkin & Roth, 1993, p. 376). Individual characters and experiences in interpersonal interactions, as a result, became a supplementary proxy for attributions of trustworthiness (Barber, 1983; Zucker, 1986).

7.7 Intervention: Putting the House in Order

Internal reforms are necessary to prevent the recurrence of similar mistakes, so as to reintroduce trustworthiness into the organisational structure (Gillespie & Dietz, 2009). Over-leveraging and poor lending policies reflected the Preston bank’s failure in risk management and capital allocation. The Consolidated Bank’s crisis, on the other hand, exposed a lack of synergy, control, and integration between its managerial units when responding to organisational emergency. In the words of Gillespie and Hurley (2013, p. 198), “proactive attempts to repair trust at the organisation level have been shown to be more convincing than passive acceptance of externally enforced rules and regulations” (see also Tomlinson & Mayer, 2009). The objectives are twofold: (1) to convince stakeholders that the organisations have learned the lesson and are willing to address

internal failures, and (2) to reposition themselves and rebuild external reputation (Child & Rodrigues, 2004; Dietz & Gillespie, 2011). This section shows how far each bank had travelled to repair its flawed managerial functions (Pfarrer et al., 2008). It goes on to demonstrate the tactfulness of the management in using its public relations functions – through dialogues and mutual understanding – to convey the objectives of organisational reforms and sense of renewed optimism to stakeholders (Bowen, 2000; Grunig, 2000).

With the support of all parties, the Consolidated Bank successfully reopened its doors on 2 July (*The Times*, 30 Jun. 1866). Just about a month later, during the half-yearly meeting the deputy chairman Turner proudly pointed out the rarity of banks that have closed their doors would find themselves "in the same happy position" again, intimating that "what is past is past" and every party should "look to the future" without viewing the crisis "with a very critical eye, or heap blame upon one man or another man" (*Manchester Guardian*, 1 Aug. 1866, p. 3). He did not consider the deal with the Bank of London "an insane junction" as *The Economist* (23 Jun. 1866, p. 732) once described – but a strategic opportunity that had now put the bank on a trajectory of expansion (*Manchester Guardian*, 1 Aug. 1866). With many customers of the London bank transferring their accounts to the Consolidated Bank, the *Manchester Guardian* (25 Jan. 1866, p. 3) testified that there was "a considerable accession of business from other quarters". Hankey was impressed by how swiftly the Consolidated Bank had recovered from a crisis "with so few scars", and by reorganising itself the company had now become "one of the first institutions" in the metropolis (*Manchester Guardian*, 25 Jan. 1867, p. 3).

In 1867, the swift recovery of the Consolidated Bank amidst a sluggish economy was "a strong proof of its unimpaired credit, and that there was before it a good and satisfactory future" (*Manchester Guardian*, 25 Jul. 1867, p. 2). In addition to "a very satisfactory increase" in the balances on current and deposit accounts, the bank's capital further burgeoned to £800,000 to accommodate its growing business. In the same year, the bank sustained "a great loss" through the death of Turner, whose "energy, great shrewdness, and business ability" had contributed to the company's ongoing success and stability after the crisis (*Daily News*, 24 Jan. 1868, p. 8).

Returning to the Preston bank, a series of shareholders' meetings in late August saw a few but vital reorganisations of the firm. First, a range of cost-saving strategies was deployed to improve the firm's operational efficiency, culminating in a downsized taskforce and the closure of the branches at Lancaster and Blackburn (*Preston Chronicle*, 1 Sep. 1866). The board also proposed an increase in the number of directors from six to

seven, accompanied by a drastic reduction in share qualification from twenty to five (*Preston Chronicle*, 25 Aug. 1866). The former directors resigned, prompting new appointments to ensure renewed discipline and good management (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Dalby, described by the committee as "a gentleman of great banking experience", was appointed the new manager (*Preston Chronicle*, 1 Sep. 1866, p. 5). Edward Rodgett, John Bickerstaff, Charles Jacson, Joseph Livesey, Thomas Hincksman, George Hargreaves, and James Whitehead also became directors upon the committee's recommendation. Livesey's appointment, in particular, inspired much confidence that some former customers decided to return (*Preston Chronicle*, 1 Sep. 1866). Third, the committee also nominated Chadwick to be the auditor for the ensuing year, marking the first appointment of a professional accountant, rather than a shareholder, to the position (*Preston Chronicle*, 25 Aug. 1866).

The Preston bank crisis underscored the unchanging principle that a competent and functional management was key to organisational stability and trustworthiness (Gillespie & Hurley, 2013). The reforms revealed the board's consciousness that the bank had become stigmatised with "bad management" (*Preston Chronicle*, 1 Sep. 1866, p. 5) – another rude awakening that "brains and wealth" did not always go together, and "men reputed to be rich" were not necessarily fitting candidates for directorship (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). The committee stressed the need for "a constant, careful consideration" of the company's business – a point which Livesey accordingly echoed, emphasising that the bank's future prosperity depended on "improved management" "more than anything else" (*Preston Chronicle*, 1 Sep. 1866, p. 5). Directors were required to attend "not just an hour or two weekly, but for some time, every day", he said. Importantly, the role autonomy of the executives would also be restricted by the influence which other organisational units may exert upon them (Perrone et al., 2003). To maintain financial prudence, Livesey proposed the formation of a consultation committee composing of "right, good hearted, earnest businessmen" to assist the management without unnecessarily encroaching upon its legitimate scope of power (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). The proposal reflected a humble acknowledgement of the struggle encountered by senior management to recognise and understand all the details within an increasingly large and complex organisation, and thus the need for introducing supervisory mechanisms "to monitor each other, raise concerns, criticise, and question upwards" (Gillespie & Hurley, 2013, p. 199).

Confidence gradually returned as the reform proposals proved to members of public that the new management was determined to purge the bank of its blemished past (Seeger & Ulmer, 2001). Dalby was optimistic that sound management, aided by the bank's "good connection" and strategic position in a centre of "great commercial and manufacturing enterprise", would re-establish the company on a stronger foundation (*Preston Chronicle*, 1 Sep. 1866, p. 5). A committee member named Naylor remarked that with improved management the firm would re-emerge from "those quicksands in which their beautiful vessel had well-nigh been lost" (Preston Bank, *Report of Shareholders*, 27 Jul. 1866). Bickerstaff believed the bank would rise again as "one of the best in the country" (*Preston Chronicle*, 1 Sep. 1866, p. 5). A shareholder called Smith echoed that the vessel that was once "run ashore" had been "gotten off and fairly launched again". Interestingly, the frequency at which maritime metaphors were deployed to describe bank management may well reflect the riskiness of the world of finance, and that the safety and survival of every member of crew on board critically hinged on the captain's wisdom and foresight. Doubtless, cases were many that some captains by their misjudgement had inadvertently driven the vessels into the heart of a storm. Ironically, it was not unusual that the chances of survival significantly improved when the crew – no matter how grudgingly – chose to work with the captains to steer the vessels out of hazard to haven once more.

7.8 Conclusion

The intermittent setbacks suffered by the Consolidated Bank and the Preston Banking Company, and the manner in which they were dealt with, paradoxically confirmed the irreversible progress made by the joint-stock banking system in nineteenth-century Britain. In relation to the observation of Noteboom (2012, p. 9) that "[o]ne can trust individuals, organisations, institutions and systems", this chapter demonstrates the transmissibility of trust across the individual, organisational, and institutional dimensions. The most noticeable change witnessed during the decade was the growing reliance on the expert system to deal with trust-related issues. The speciality and skills required in the management of banking institutions became more closely identified with the quantum of professionalism that was markedly different from other branches of commerce. To the extent that injured parties trusted external investigators to be competent and impartial in their judgement, it also became increasingly likely that they would extend and extrapolate their trust to the emerging expert system (Anderson-Gough et al., 1999). Furthermore,

distrust in the accuracy of annual statements prepared by corporate leaders may have gradually raised the demand for external auditors over time, who in turn were entrusted with the mission to inspect the company with accuracy, objectivity, and integrity (Mueller et al., 2015). As Shore and Wright (2000, p. 77) comment, the reliance on external and independent audit leads to the "displacement of a system based on autonomy and trust by one based on visibility and coercive accountability". Although this statement may be somewhat far-fetched in the 1860s, the emerging signs appeared to suggest that stakeholders increasingly view external professionals as agents who could hold other agents (i.e. senior management) to account on their behalf (Shapiro, 1987). There was seemingly a gradual transition towards professionalised administrative control, which would then become the "new accountability culture" in the twenty-first century (O'Neill, 2002, p. 46).

Notwithstanding the change discussed above, this chapter also observes a few strong continuities in the pattern of trust repair. First, legal remedies remained a far less preferred option, as manifested in the aversions of interested parties to wind up the company's affairs through the intermediation of the Chancery. Sitkin and Roth (1993) caution that legal avenues tend to undermine the interpersonal foundations of a relationship by supplanting individual goodwill with formalised and procedure-driven solutions. As Granovetter (1985, p. 489) likewise concurs, they "do not produce trust, but instead are a functional substitute for it", and fail to recognise the value of "concrete personal relations and the obligations inherent in them [to] discourage malfeasance". On the contrary, the management responded to competing expectations by cementing the relationship between all contracting parties, hence proving the relative importance of personal contact, persuasions, and social bonds in dismantling structural barriers and distance as interposed by organisational hierarchies and power relations (see Shapiro, 1987). While legal procedures may arguably improve the certainty of outcomes by streamlining the actions of divergent stakeholders via bureaucratic and top-down mechanisms, they are of limited capacity to harmonise multifaceted inter-party relationships constituted by highly dense social processes, especially in the presence of imperfect information, unequal power relations, and competing interests. In this instance, the desire and decision to trust (again) were established upon the social interactions between economic actors, during which trustors revised their assumptions and assessments about the trustees' behaviour, who at the same time formed conjecture about the possible actions which the trustors would find preferable (Sitkin & Roth, 1993).

Second, processes of trust repair unveiled in this chapter also resembled those witnessed in the 1830s and 1840s: banking entities which proactively diagnosed their own internal deficiencies and implemented reforms stood a better chance of rebuilding organisational trustworthiness more effectively (Gillespie & Dietz, 2009) – at least in the immediate term. Voluntary attempts to repair organisational defects have been shown to be more credible than passively accepting rules enforced and imposed from without (Gillespie & Hurley, 2013; see also Tomlinson & Mayer, 2009). Given the short span of time covered in this chapter, and to the extent that it was important to ensure consistency between organisational components and units to reinforce the sense of renewed trustworthiness, the question remained whether the banks had carried out adequate periodic evaluation so as to determine the effectiveness of organisational reforms. The complex socio-technical environment which enshrouds the banking and financial sector makes it difficult for senior management to push through all reform agendas at one stroke, let alone ensuring that disputes and tensions between different stakeholder groups would not derail the ongoing efforts. Because "power and politics are very much at the heart of the reality of repairing system trust", the convolution of vested interests within a "large multi-agent, multi-level system" poses a risk that painful but important measures would be "conveniently left out" (Gillespie & Hurley, 2013, p. 199). Another critical aspect of trust repair left unaddressed in this chapter is the identification of agents which presumably possessed the required insight and authority to conduct independent evaluation of organisational reforms. This reverberates the importance presented by Gillespie and Hurley (2013, p. 199) of framing trust repair as "a long- term, social, technical and political process where success can only be declared after repeated evaluation and testing over a significant period of time".

Last and ironically, another recurring issue in the 1860s was the extent to which bankers could and should be empowered to make corporate decisions which carried far-reaching consequences. The study in this chapter again verifies that organisational leaders – irrespective of their presumed specialty and purview – were not infallible due to their imperfect acquaintance with the dynamism in a multi-faceted system. Child and Rodrigues (2004, p. 149) thus reason that an inclusive internal control system that facilitates participation and transparency (in the form of information-sharing) is thus required, encouraging organisational members to monitor each other, raise concerns, and subject senior management to scrutiny. This was in theory, for one barrister told a parliamentary committee in 1850 that in the politics of joint-stock companies "the

shareholders are delivered over, bound hand and foot, to the mercy of the directors" (Ludlow, 1850, p. 6). The entrenched complexity and culture of secrecy mean that in many respects joint-stock banks were "the least democratic of all", and shareholder activism gradually conceded to more autocratic governance over the century (Freeman et al., 2012, p. 139). A larger scope of role autonomy ascribed to senior management may sometimes be justified under the pretext of engaging "in new areas of business or in branching" (Freeman et al., 2012, p. 139). As demonstrated in the study thus far, conflicting objectives arising from diverse stakeholders added to the duress and nuances of banking governance, thus undercutting the usefulness of "hard and fast rules" in curtailing managerial autonomy (see Mehran et al., 2011, p. 11).

The rest of the nineteenth century witnessed further concentration of economic and financial power in banking institutions, promulgated by a wave of amalgamation which began in the mid-1870s and continued right into the early twentieth century. The 1866 setback did not check the Consolidated Bank's ambition to extend its business territory. By 1877, its paid-up capital had reached £800,000 and its reserves £145,000. With such financial prowess, it had three established branches in Salford, Manchester, and Charing Cross, London. From the 1880s, in pursuit of "a vigorous policy of branch expansion" (Orbell & Turton, 2001, p. 163), the bank opened offices in Patricroft, Pendleton and Longsight (1887), Leigh and Tyldlesley (1888), Radcliffe (1892), Deansgate at Manchester (1893), and Salford Cattle Market (1894). In 1896, the Consolidated Bank merged with Parr's Banking Co. & Alliance Bank, assuming a new name Parr's Bank Ltd. The Preston Banking Company trod a similar path, attracting more than £1 million of deposits in 1880, although it did not adopt limited liability until 1883. By 1894, it had opened ten full branches and sixteen sub-branches (Orbell & Turton, 2001). In the same year the bank reached another milestone when it amalgamated with London & Midland Bank, forming "the twentieth largest provincial bank", with deposits reaching £1.8 million and paid-up capital £200,000 (Orbell & Turton, 2001, p. 442). By the close of the century, as with the case of many other provincial banks, both the Consolidated Bank and the Preston Banking Company had extended their reach far beyond their local origins whose interests they were (once) closely identified with. As local banks expanded in size and scope, members of public found themselves having to trust – and distrust – in the wisdom and acumen of the growingly distant agents to secure their financial interests.

Chapter 8
Construction, Destruction, and Reconstruction: An Analytical View of Trust Repair in Victorian Joint-Stock Banks

8.1 Introduction

This chapter applies the organisational trust repair model constructed by Gillespie and Dietz, 2009) to (1) understand the sources of trust failures in Victorian joint-stock banks and (2) evaluate the effectiveness of some institutional trust repair strategies. It shows how far broken trust could be successfully restored, unravelling the issues and complexities encountered under different constraints during the process. Deducing from the case studies detailed in the preceding chapters (4 – 7), this chapter discusses the usefulness of the model in diagnosing a few systemic factors contributing to trust breakdowns in banking institutions, and pointing out remedies for restoring organisational trustworthiness (Gillespie et al., 2012). With the aid of the model, it identifies how banking agents and different organisational components interacted with each other in the process of repairing trust, critically reflecting on how organisational members and institutions responded (differently) to crises and trust failures. This property has at least two important and challenging implications, as Gillespie et al. (2012) have rightly observed. First, because banking crises inflicted suffering and losses on a broad range of socio-economic interests and participants, trust repair could only be more meaningfully appreciated by understanding the multiple, cross-level factors by which the strategies were conditioned. Next, to the extent that responsibility was indeterminately defined and diffused across multiple agents or organisational components, trust repair required consideration of the context in which strategies were likely to vary between interpersonal and institutional settings.

The chapter is structured as follows. The next section considers the need for adapting the model to incorporate some features peculiar to the banking and financial industry – namely (1) interlocking relationships with different classes and concerns; (2) a principal-

agent relationship highly skewed by information asymmetry; (3) a strong predisposition to high-risk, high-return investment strategies driven by financial incentives that answer to shareholder primacy, and (4) dense interconnectedness of banking activities with systemic impact across the real economy. Using the multilevel theory incorporated in the model, the next five sections (8.3 – 8.7) address the underlying trust violations emanating from different systemic components, and the constraints imposed by banking characteristics on trust repair efforts in each, broadly classified as follows: (1) organisational leadership and reputational sanctions, (2) corporate power, controls, and accountability, (3) shareholder activism, information, and public scrutiny, (4) corporate local identity, cohesiveness, and public reputation, and (5) government regulations. In recognising that banking crises have "systemic as well as individual and organisational causes" (Gillespie et al., 2012, p. 192), these sections also discuss the comparative rationale and effectiveness of some immediate and short-term strategies for repairing trust employed by different banking entities. The final section concludes the thesis by pointing out the relevance of the model in explaining some historical patterns in Victorian banking, and how the past can equally inform and revise the contemporary understanding of trust and trustworthiness. It also highlights some underlying limitations of the study in addressing some ongoing and unsettled trust-related issues in the banking and financial industry.

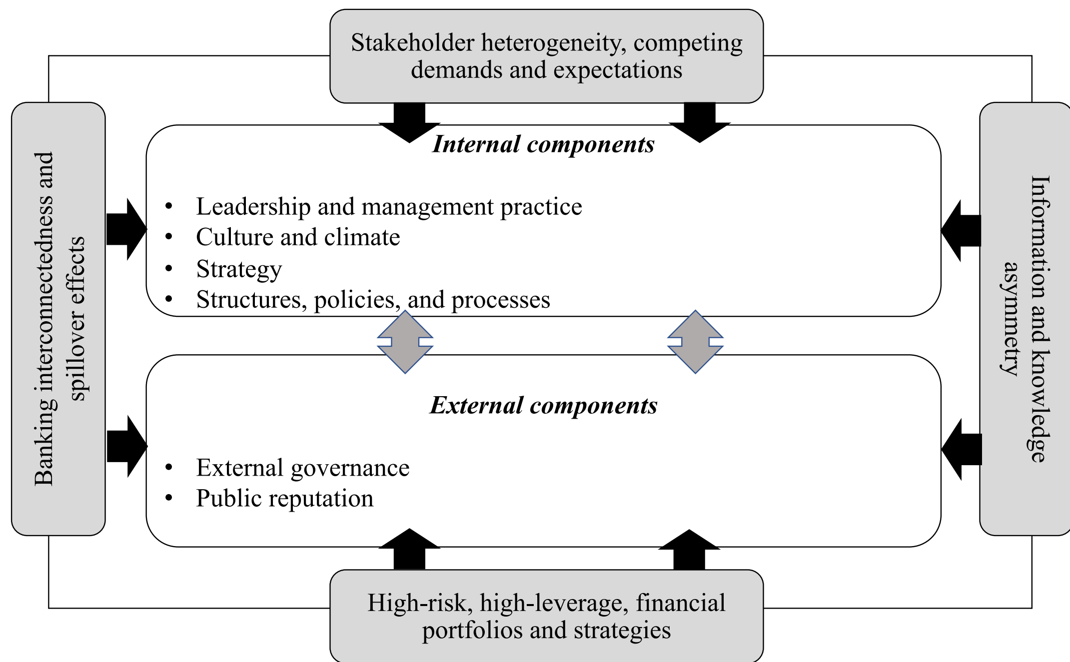
8.2 Trust Repair Model and Banking Peculiarities: Some Adaptations

As briefly outlined in chapter 3, the organisational trust repair model depicts "a multilevel, system-based perspective" for understanding organisational trustworthiness and the process of trust repair (Gillespie & Dietz, 2012, p. 194). Stakeholders' assessment of an organisation's trustworthiness is informed by signals emanating from multiple components of the organisational system. The model describes organisational failures as "systemic in nature", with deficiencies in multiple institutional components contributing to the breakdown (see Figure 8.1). This helps explain why not all banks failed or suspended payments, albeit all came under the strain of commercial crises. The case studies also confirm the belief of Gillespie and Dietz (2012, p. 194) that bankers' incompetence or unethical behaviour did not occur "without an opportunity". Rather, they had to be analysed and explained in conjunction with – among other factors – poor or corrupt leadership, inappropriate financial strategies, weak governance and control, or

deficient regulatory framework (see Gillespie & Dietz, 2012, p. 94). As explained below, the thesis finds it necessary to adapt the model to encapsulate some features unique to banking, which compound the dynamics behind the internal and external components in the event of trust failures (see Figure 8.1).

Figure 8.1

Organisational System Components and Impacts of Banking Characteristics on Public Perception on Organisational Trustworthiness



First, the bank's balance sheet shows that the duties and virtues of bankers are essentially polarised and contradictory. On the liabilities side, and as debtors to deposit customers, bankers are expected to be risk-averse, conservative, and prudent in handling monied properties invested in on-demand deposits. On the assets side, bankers are creditors to borrowing customers – a role in which they are expected to be adventurous and take necessary risks when providing advances for new commercial ventures. As financial intermediaries between depositors and borrowers with opposing financial perspectives, bankers must therefore reconcile their competing interests by balancing "different duties and virtues of risk-reduction and risk-assumption" (Koslowski, 2009, p.

20). These dual role expectations demonstrate that "material appropriateness of the banking system calls for a synthesis of risk-aversion and willingness to embrace risk, of sober risk-control and bold openness to risk-capital and risky investment" (Koslowki, 2009, p. 27).

The soundness, stability, and trustworthiness of banking institutions are informed by how effectively bankers could reconcile and balance their dual role expectations. As Koslowski (2009, p. 26) cautions, there is always a temptation of "shifting this balance too far in one direction" – either yielding too much to the demand of deposit customers in risk-free investments, or being overgenerous to borrowing customers without appropriate risk controls. The sharp decline in the perceived trustworthiness of banking institutions which follows a financial crisis has normally much to do with credit misallocation, in which the savings of depositors were lost in risky lending or malinvestment. As Koslowski (2009, p. 27) argues, the failure to abide by prudent lending principles is unethical, since easy credit cannot benefit borrowing customers without infringing the interests of deposit customers.

Second, the principal-agent relationship in banking and finance is structured by a high degree of information or knowledge asymmetry. Unlike tangible goods, the abstractness and complexity of financial products imply that ordinary users are incapable of forming accurate assessments of risks and values (Jaffer et al., 2004c, p. 10). According to Sandler (2002), such asymmetry has intensified over the years, owing to a long-cherished culture of secrecy in the industry, increasing use of technical jargon unknown to users, and growing complexity of financial products. Moreover, given that financial investments "contain promises about delivering returns far into the future", it is almost impossible to ascertain the real value and risks until a significant period has lapsed (Jaffer et al., 2014c, p. 10). This also provides the manager with leeway to camouflage downside risks over long periods of time (Noe & Young, 2014). Therefore, the industry is "trust-intensive" insofar as users are heavily reliant upon the expertise and honesty of the providers, whose motives and actions they nonetheless cannot perfectly monitor (Jaffer et al., 2014d, p. 33). According to Jaffer et al. (2014c, p. 10), "both uncertainty and asymmetric information led to great temptations for those who possessed knowledge or expertise to behave dishonestly".

Another source of information asymmetry – which is considerably more evident in this thesis – stems from the confidentiality of financial portfolios and client information. As insiders, bank directors or managers are in control of certain information, which they

knowingly keep from public knowledge for legal or strategic purposes (Shiller, 2012). A culture of enforced secrecy curtails the capacity of stakeholders to hold the management to account (Jaffer et al., 2014c). Violations of trust take place when they abuse their corporate positions and exploit insider knowledge for their own or any third party's enrichment – an act which Koslowski (2009, p. 64) describes as "a more or less universal characteristic of corruption". All forms of corruption violate the "position of trust" underlying the principal-agent relationship, and beget "perverse incentives" which divert the attention of agents or fiduciary to those activities which do not represent the interests of principals (Koslowski, 2009, p. 65). Because information knowledge carries with itself the power over stakeholders against a backdrop of uncertainties and risk-taking, this thesis believes that *integrity* and *benevolence* have more influence on the success of restoring trust than *ability* alone could achieve.

Third, bank managers tend to embrace high-risk, high-return investment strategies because the downside risks fall disproportionately on depositors or creditors. Noe and Young (2014) present detailed argument as to how self-interested, profit-driven managers can easily devise portfolios which maximise financial returns for clients – and hence larger bonuses for themselves – in the short term, while imposing high and well-hidden risks which take years to recognise. The fact that financial products are too complex to understand, and that banking and financial institutions are oblique in their operation, also makes it difficult and costly for stakeholders to monitor their investment directly. Without commensurate financial incentives, managers would not be sufficiently motivated to monitor risks, on the presumption that the probability of losses or catastrophe remains comparatively low (Jaffer et al., 2014c, p. 12).

Last but not least, banking and financial activities are known for generating spill-over effects – which are widely diffused, dynamic, and destabilising – on other market participants (Armour & Gordon, 2014). Given the interconnectedness of the banking system, losses and panics stemming from individual bank failures tend to spread to other healthy institutions, thus disrupting payment facilities and credit flows across the real economy. Typically, a crisis could transmit and permeates through the system as a result of a liquidity mismatch exemplified in the bank's balance sheet. This is particularly the case if the bank's capital is largely locked up in loans and advances (i.e. illiquid assets) in the face of a sudden surge in demand for liquidity (i.e. liabilities) by deposit customers (Turner, 2014). As confidence evaporates, depositors withdraw their savings on a massive scale, forcing the bank to liquidate its long-term assets in a way that is "destructive of

value" (Armour & Gordon, 2014, p. 236). The sudden collapse in asset prices and the slump in confidence in other banks (resulting from the inference made by deposit customers) thus combine to trigger a crisis within the financial system (Turner, 2014).

Figure 8.2

Constraints of Banking Characteristics on Trust Repair Efforts

Banking Characteristics:

- Stakeholder heterogeneity, competing demands and expectations
- Information and knowledge asymmetry
- High risk, high-leverage financial portfolios and strategies
- Banking interconnectedness and spillover effects

Respectability: Competence, Integrity, and Reputation

Accountability: Corporate Power, Control, and Procedures

Transparency: Shareholder Inspection, Information, and Publicity

Equity: Conflicts, Prioritisation, and Reconciliation

Legality: Prevention, Punishment, and Protection

Legend:

sources of constraints
interconnection

A destabilised system results in wider socio-economic disruptions because banks facilitate payments and diffuse credit across the real economy (Armour & Gordon, 2014). Following bank failures, a sharp devaluation in asset prices and credit contraction also lead to a collapse in private investment and the value of the stock of wealth in the private sector. The result is a recession induced by a systemic failure, with the resultant effects felt across the real economy (Bernanke, 1983). Given that the macroeconomic and social losses are much larger than those suffered by bank shareholders, risky and imprudent pursuits by banking institutions thus impose massive external costs on the rest of the economy (Bernanke, 1983). The combination of these features makes trust failures in banking particularly challenging to overcome: failures at the organisational level could potentially mutate into a systemic crisis. In the following sections, the thesis argues that

the unique characters of banking largely conditioned how trust repair efforts were undertaken from different aspects – namely: (1) individual respectability; (2) corporate accountability; (3) organisational transparency; (4) proprietorial equity, and (5) official legality, briefly illustrated in Figure 8.2.

8.3 Respectability: Competence, Integrity, and Reputation

Because banking is crucial for ensuring efficient payments, prudent risk management and credit allocation, "those who participate are part of a community to which they make a meaningful contribution" (Herzog, 2019, p. 533). With their economic power and specialised expertise, bankers assume a "duty of loyalty" to demonstrate "undivided and unselfish loyalty" to parties who were less capable of detecting "violations of any applicable forms" (Koslowski, 2009, p. 12; Awrey & Kershaw, 2014, p. 281). Among Victorian bankers, however, there were noticeable recurrences of trust failures which concern "matters of competence or integrity", thereby condemning banking companies to dysfunctional risk management and financial difficulties (Kim et al., 2004, p. 106). In the absence of a robust and comprehensive regulatory framework, this section first presents the importance of reputational sanctions – as mediated by various cultural sources such as newspapers, banking manuals, and pamphlets – in articulating and reinforcing the values and ethos governing the banking industry. It argues that in Victorian Britain reputational damages inflicted by negative publicity was in fact more punitive than monetary penance, and such was especially the case if bank failures had (more) to do with moral breakdown. The section then compares how professionalisation and local business networks informed banking conduct and motivated the commitment of individual bankers to support important institutions connected with the practice of their profession. The thesis argues that banking entities are inseparable from moral underpinnings because of their unique dimensions – namely, the specialised knowledge and economic power which they could wield over a multitude of stakeholders.

As Shiller (2012, p. 38) comments, given that the public has "a sense of the centrality, sobriety, and safety of banks", they turned to bankers for their specialised role in steering the whole community towards economic stability and commercial expansion. During the first-half of the century, because there was no established ethical and administrative benchmark "among a decidedly mixed crowd of financiers", individual bankers assimilated the practices of their peers and dismissed each failure or crisis as "an

unfortunate case of rules not being followed" (Alborn, 1995, p. 199). To fill the regulatory gap, reputational sanctions were a somewhat formidable tool to regulate bankers' behaviour by condemning and excluding those who did not abide by the rules of exchange (see Jaffer et al., 2014b). Growing circulation and readership strengthened the role of newspapers in mediating individual and corporate reputation in the marketplace, exposing high-standing corporate figures to public censure and humiliation, and in certain cases terminating the careers of "some of the biggest names involved" (Taylor, 2013b, p. 687; Taylor, 2012). Expulsion from "polite society" was in fact widely regarded as "a more serious penalty than imprisonment" (Robb, 1992, p. 165). Taylor's (2005, p. 251) study also confirms that the stigma and public humiliation suffered by Victorian bankers were so condemnatory that criminal prosecutions were "widely believed to be superfluous". "Being for the most part well-born, educated men", as the argument goes, "they would feel these penalties far more keenly than would common felons". Notwithstanding its "tinge of class-prejudiced special pleading", this argument does point to the severity of reputational costs as a form of extra-legal punishment during the century.

In banking, integrity, objectivity, confidentiality, diligence, competence, and professionalism are among the most commonly cited values to guide behavioural choice (De Bruin, 2014). Among these values, this thesis has shown that a good number of Victorian bankers came under stern criticisms for their sheer incompetence and inexperience (i.e. ability failures). An article published in the *Bankers' Magazine* (Jan. 1845, p. 202), for instance, fumed that many lacked the knowledge and habits consistent with "the character of their office". Another mocked that "a well-known mercantile or even a political name" was sufficient "to secure the votes of the proprietors" (Jul. 1848, p. 422). Another thundered that "any one and every one is qualified to be a banker without premonition whatever" (Oct. 1856a, p. 796). Increasingly, the belief was gaining ground in the 1850s that "a banker should be a banker, and nothing but a banker", in recognition of the high degree of specialism and delicateness involved in the profession that requires undivided attention and energies to "one class of operations" (Gilbart, 1859, p. 48).

By the 1860s, even with the lessons gathered from past bank failures, there remained no conclusive definition as to what "a healthy and constructive banking system" should be (Alborn, 1995, p. 210). With many bankers showing little regard to the system or responsibility, 'A Depositor' of *The Maze of Banking* (1863, p. 28) expressed his thought as follows:

> We have joint-stock banks everywhere… [but] we have never had the skeleton of a healthy specimen brought into the dissecting room… [T]he ruins show such a shattered wreck, that it is impossible to build a correct system from the disordered remains.

In his *Lombard Street* published in 1873, however, Walter Bagehot noted otherwise, opining that "many excellent men of business were quite ready to become members of boards of directors, and to attend to the business of companies, a good deal for the employment's sake" – and such persons were "much on the increase" (p. 125). Being a "professional" with a calling and standing in a "promissory relationship" within society implies the banker's commitment to safeguarding individual interests and taking responsibility for the system within which he functions (Herzog, 2019, p. 534). Expectedly, the public dimension of banking activities meant that public anger and frustrations were likely to be far more manifest and evident, given the bankers' failure to appreciate the scale of damages and dysfunctionalities arising from capital misallocation and distortion of commodity prices (see Herzog, 2019, p. 534).

On a different level, the reputational damage and censures were noticeably more evident in the case of moral conflict and corruption, as revealed in the Northern Bank and the Bank of Manchester scandals. Schifferes and Knowles (2013, p. 48) note that "greedy bankers were a far more exciting topic for the popular press" than the failure of banking governance and regulations. As the *Bankers' Magazine* (Feb. 1846, p. 267) observed, what went missing in many professed bank directors or managers was the virtues of "sterling honesty and integrity", and a resolute self-denial to "the manly frivolous and extravagant pleasures". In the event of a crisis, while morally respectable figures "could sometimes evade ignominy", those who had "taken from the till" could expect no public forgiveness (Taylor, 2005, p. 251). Such outpouring of moral outrage was particularly evident in the 1850s during which a swathe of bank failures was trailed by "a growing sense of moral panic" (Taylor, 2013a, p. 109). Victorian banker Gavin Bell (1840, p. 67) asserted that bankers assumed a weighty moral obligation because they had been appointed to "a solemn trust" to represent the interests of numerous parties. To reiterate, banking is in its own right strongly connected to "a moral or ethical phenomenon" for two reasons (Koslowski, 2009, p. 3). First, asymmetries of information and expertise in the principle-agent relationship reinforce "a kind of self-commitment" on the part of the agents to act in the best interests of ordinary and less informed market participants (p.

281). Second, because the safety of individual properties and societal welfare is consequent upon how banking institutions exercise their economic power and expertise, it follows that there must be a commensurate “consciousness and moral awareness” in the conduct of business (p. 3).

The arguments detailed in this thesis thus far also contravene the claim made by Stiglitz (2015) that short-sighted firms tend to prioritise financial gains and care little about reputation. From Gold’s (2014, p. 148) perspective, “in the absence of accompanying social sanctions”, one may be inclined to treating financial sanctions merely “as a price rather than punishments”. O’Neill (2014, p. 187) contends that “the realities of earning professional respect, or losing professional respect, of being respected or shamed, ultimately expelled and ostracised, can have greater weight”. More importantly, because of its extensive and enormous impact upon the real economy, this thesis shows that the high moral intensity of banking augmented the power of reputational sanctions transmitted via press publicity. Strong socio-economic ties between provincial banks and local communities sharpened the moral reproach accompanying each banking scandal, as the *Bankers’ Magazine* (Aug. 1856, p. 470) commented:

> With deposits amount to millions, and the enormous engagements based thereon, the directors … would be liable to serious reprehension if they failed to recognise the actual position in which they stand in relation to the public and customers.

As the latter part of this chapter will discuss in greater detail, to repair trust effectively, senior management must acknowledge the importance of harmonising rehabilitation effort with pro-social motivations, recognising the inseparable link between their actions and the public interest (see O’Brien, 2014, p. 228). As words of mouth travelled across the community of which local banks formed an integral part, it placed an even greater onus upon the governing body to ensure that every decision was “morally responsible and defensible” (Koslowski, 2009, p. 3).

In the 1870s, banking conduct and crises became issues to be addressed “within a technically competent community”, with bankers recognising their conduct as increasingly defined by professionalism in a highly specialised industry (Alborn, 1995, p. 204). Consequently, the discourses of what constituted sound banking practices gradually moved away from the heart of the local community, as bankers began to digress from the

moral premises and communal expectations that once defined the utility and credibility of their profession. The demand for banking professionalism is primarily driven by an "unspoken assumption" that it would enhance banks' "loyalty to the public interest" and thus their trustworthiness as vital social and economic institutions (Smith et al., 2017, p. 413). According to De Bruin (2014, p. 271), values and codes of conduct define the "public function" of a profession by underlining the activities and obligations which society or clients could reasonably expect from it. They enhance the reputation and identity of a profession, insofar as members share the beliefs and aspirations which provide meaning to their moral ties and sense of purpose (Frankel, 1989). Professionalisation also promotes "procedural motivations", behind which bankers perform their roles "according to accepted standards" defined by the professional bodies to which they belonged (Jaffer et al., 2014c, p. 17). This improves the predictability in the agent's behaviour in terms of what can normally be expected of a person acting acceptably (Gabarro, 1978).

By contrast, this thesis has shown that it took more than impersonalised and remote professionalisation to promote meaningful trust, as exemplified in the willingness between bankers and clients to take a risk in renewing collaborative relationship and be vulnerable in the face of past failures (Mayer et al., 1995). Bankers who have direct contact and long-term relationship with clients tend to develop empathy and a "motivation not to harm them", because of their personal acquaintance with the potential victims and awareness of how they would be injured (Herzog, 2019, p. 535). The density of local business networks also heightened public perception that the banks – as influential and powerful entities over key socio-economic agenda in the community – assumed a paramount duty in serving and supporting local stakeholders (see Smith et al., 2017). In the context where banking was a community-centred business (see Shiller, 2012), a desire to behave trustworthily could – albeit arguably – arise from an altruistic concern with the well-being of other people. Even if bankers are concerned only with their own interests, they could be motivated to conduct themselves credibly because of the reputational advantages and "high value placed by individuals on the probation of others" (Jaffer et al., 2014c, p. 17; Gold, 2014). Whatever the character and origin of motivation, the approach taken by this thesis underlines the importance of capturing the dynamism of trust and distrust behind the interdependence between heterogenous parties to accomplish individual or organisational goals.

Importantly, the knowledge asymmetry embedded in the industry and the systemic harms it could inflict on the society also imply that it is practically impossible to distance bankers' competence and economic power from moral principles. As the *Bankers' Magazine* (Oct. 1856b, p. 601) remarked, with so much power and influence vested in the bank, "the only guarantee" for sound and prudent banking hinged upon the "integrity and moral rectitude of those placed at its head". Modern scholars also agree that ethics remain a "form of insurance" against predatory behaviour by self-serving bankers (De Bruin, 2014, p. 270; Jamal & Bowie, 1995). Are the features and facets of professionalism sufficiently versatile and rigorous to regulate and moralise banking as a whole, given its fundamentally different characteristics from other somewhat conventional industries? Herzog (2019, p. 535) sees little connection between professionalism and agents being "more interested in the well-being of others and in the prevention of systemic harms". Smith et al. (2017, p. 430) is likewise cynical that professionalisation would encourage "better, pro-social behaviour" – unless both the entity and individual bankers are "cognitively and behaviourally" committed to transforming the industry into "something more beneficial than risky business" propelled by blind pursuits of profits (p. 427). Professional ethos alone is unlikely to make a significant difference, for motivational structures and surrounding settings also determined bankers' behavioural norms and how they frame their tasks (Jaffer et al., 2014b). As experiences in Victorian banking revealed, the structure of corporate governance and organisational controls in place had from time to time failed to check and pre-empt individual opportunism and unwarranted risk-taking.

8.4 Accountability: Corporate Power, Control, and Accountability

The *Bankers' Magazine* (Oct. 1847, p. 495) once optimistically argued that as a "regular system of check upon check", the joint-stock system afforded "the most perfect and prompt control over all". The recurrences of Victorian banking crises, however, sparked repeated questionings of its robustness as an "infallible guarantee for good management". By the mid-nineteenth century, general attitudes "continued to be pervasive" (Freeman et al., 2012, p. 78), with sceptics – such as William Thompson (1854), an Edinburgh shipbroker – arguing that "joint-stock companies never will successfully compete with private enterprise and management in any well-known business, and within the range of ordinary capital" (quoted in Freeman et al., 2012, p. 78). With growing organisational complexity and anonymity blurring the legitimate functions of the governing body,

O’Neill (2014, p. 173) claims that corporatisation blunts interpersonal trust which once provided “the cohesion and compliance” in relatively primitive societies. Using the agency theory, this thesis has explored a recurring concern within Victorian banks regarding the concentration of power in the managing body, which shareholders perceived as exclusive and too imperious to challenge. In so doing, it revisited the deep-seated separation of control from ownership in joint-stock banks and examines the trustworthiness of senior management. Deducing from the case studies, the thesis has shown that confused role functions and power distribution among organisational leadership led to crises and failures. It also questioned the dominant narrative that shareholder primacy – aiming at maximising short-term shareholder value via risky financial venture – was primarily responsible for wrecking banking stability and trustworthiness. It then questioned the effectiveness of organisational reforms in delivering tangible and meaningful long-term improvement in corporate governance.

Evidence gathered from the cases – especially the District Bank, the Bank of Manchester, and the Consolidated Bank – shows that poorly defined fiduciary duties and boundary of power weakened the capacity of organisational structures and processes to monitor the executives and hold them to account. For this study it is useful to consider the work of Armour and Gordon (2014, p. 242) that distinguishes between two classes of controllers. Executive officers or bank managers are normally tasked with making strategic decisions and susceptible to the temptation of “high-powered incentives” derived from remuneration packages, which in turn are tied to the share price of the firm. Directors, on the other hand, monitor the performance of managers. Because the directors’ remuneration is not linked to the share price, their incentives are “much more low-powered, driven by personal integrity and reputational concern”. It is also vital to relate the present study to the collectivity model of governance developed by Shah and Napier (2019, p. 346), which traces the source of corporate power to the company’s general meetings, during which shareholders elect directors to manage the organisation on their behalf. The directors, who were not actively involved in the “day-to-day management” of the company, in turn hired managers to undertake the conduct of the business. Although typically there was “clear separation” between the board and managers, the balance of power began to shift when directors took on managerial roles, thus reducing their influence and independence in monitoring management (p. 347). Armour and Gordon (2014, p. 242) also highlight the danger of “genteel pressures of camaraderie” – together

with the collegiality between directors and managers – blunting objectivity and prudent oversight.

Gilbart (1859, p. 228) once tersely asserted that the constitution of joint-stock banks appeared "theoretically absurd". In numerous cases directors lacked "ordinary care and business-like attention", and their "general respectability" on which shareholders relied for the protection of their own interests, was "quite insufficient" (*Bankers' Magazine*, Jun. 1848, p. 346). Managers, notwithstanding their superior expertise and knowledge, were accountable to the directors and followed their instructions (*Bankers' Magazine*, Sep. 1844, p. 347). The directors, in turn, were placed under "the control and instruction" of a body of proprietors whose banking knowledge was even more inferior (Gilbart, 1859, p. 228). On the other hand, there were cases where the managing directors and manager formed "a secret committee" who alone had exclusive knowledge about the banks (Gilbart, 1859, p. 229). A reader named Justilia commented in the *Bankers' Magazine* (Jan. 1857a, p. 86) that it was not uncommon directors generally lacked "the science or practice of banking", and thus the foolishness to assume that banks were safe as long as the managers were endowed with "a larger share of virtues than we generally meet with in frail humanity". Gilbart (1859, p. 226) agreed that "the want of experience" would not necessarily produce "dangerous consequences" when directors appointed a vigilant and competent manager. As detailed in this thesis, cases of bank mismanagement originated from a few channels: some banks failed in the hand of the manager; some were destroyed by an exclusive and elusive committee composing of the manager and managing directors, and in other cases a few directors who dictated corporate decisions against the manager's will (see Gilbart, 1859, p. 228).

Contemporary scholars associate the Anglo-Saxon model of banking governance with a culture of short-termism and financial excesses because of its narrow focus on creating shareholder value. Studies of modern financial crises also trace numerous cases of governance failures to "some of the most sophisticated banks operating in some of the most developed governance environments in the world" (Ard & Berg, 2010, p. 1). In a financial market in which portfolios and capital can be easily reshuffled between competing institutions, directors may pander to the demand from influential shareholders who look for lucrative short-term returns. In Victorian Britain, the growing popularity of joint-stock banking unleashed "a revolution", simultaneously producing "permanent good" and "the individual spirit of speculation" (*Bankers' Magazine*, Apr. 1856, p. 202). "It is the fashion now", the *Bankers' Magazine* (Jul. 1856, p. 413) moaned, "to anticipate

large dividends and bonuses, whatever may be the respective resources of the establishment concerned". Bank managers engaged in risky ventures to boost short-term financial results, so as to avoid being seen as underperforming relative to their competitors. From Kay's (2012, p. 10) perspective, in the twenty-first century similar "hyperactive behaviour" has successfully inflated the share values without improving the "fundamental operational capabilities of the business". Because information and knowledge are asymmetrically structured between management and shareholders, the stock market is not "informationally efficient", rendering share prices a poor proxy of shareholder value (Armour & Gordon, 2014, p. 234). The entire incentive structure undermines trustworthiness of the banking industry by "rewarding the wrong things, and measuring the performance to be rewarded in the wrong ways" (Jaffer et al., 2014b, p. 367). As the Victorians had painfully witnessed, the "very spirit of competition", and the obsession with "immediate profit" without considering the consequences or liability entailed, posed considerable risks and injuries to long-term stakeholders (*Bankers' Magazine*, Jul. 1856, pp. 413-14; see also Armour & Gordon, 2014).

This thesis, however, presented a few findings which somewhat moderate the above arguments. As posited by the agency theory, unlimited liability and high shareholding qualification provided – at least in theory – the necessary financial incentives to manage the firm prudently, thus deterring opportunistic or predatory behaviour. The common argument stretching across all case studies was that large share qualifications aligned the interests of directors and shareholders by obliging the former "to hold a significant stake in the firm" (Freeman et al., 2012, p. 96). Although the arrangement – which was meant to improve standards of governance by attracting "men of substantial capital and good character" to occupy the board (p. 93) – had failed to ward off mismanagement, the thesis has shown that in the aftermath of each crisis large investments held by the directors reinforced their legitimacy in the eyes of all stakeholders. "Such was the sense of responsibility", as Freeman et al. (2012, p. 98) observe, "that substantial shareholding would engender that shareholders were sometimes more enthusiastic than boards about driving the directorial qualification upward". Furthermore, with a limited scope of operations and "a less dispersed shareholder base", the banks under this study were featured by a strong and distinct local identity (Freeman et al., 2012, p. 99). Consequently, directors, many of whom were also prominent local figures, were motivated by reputational concern to act in the best interest of the community. As will be discussed at greater length in the latter part of this chapter, such local identity and commitment played

a critical role in forging collegiality between the management and stakeholders along the path of organisational rehabilitation.

Finally, from the perspective of contemporary management theorists, by "setting the tone from the top", as role models senior managers who violate stakeholders' trust with impunity often pose the most immediate threat to organisational trustworthiness (Crane & Mattern, 2019, p. 193). Multilayer organisational relationships imply that one's credibility could take a knock through violations committed by other organisational members (Jaffer et al., 2014b). The *Bankers' Magazine* (Dec. 1844b, p. 143) aptly noted the transmissibility of negative perceptions when distrust and speculation were running wild. As uncovered in the cases of the Northern Bank and the Bank of Manchester, even individuals with "characters and integrity unimpeached and unimpeachable" could at times unexpectedly suffer "the slings and arrows" targeted at the misconduct of others. To eliminate the further spread of distrust and obstacles posed by the old guards, radical changes in organisational leadership (see, for instance, the Bank of Manchester crisis) were warranted at times to enable prompt diagnosis and rehabilitative reforms (Gillespie et al., 2014, p. 397; Hilger et al., 2013). Albeit to a less extent, similar responses were observed in the Royal Bank of Liverpool and the Preston Banking Company. These actions signified a willingness to embrace accountability and organisational change, breaking the banks from their scarred or scandalous past.

Even with tightened rules and sharpened roles, Jaffer et al. (2014b) question the long-term effectiveness of legalistic measures in containing the risks of future violations. For instance, were the rules comprehensive and adaptive to ward off violations of different character? Was the threat of punishment sufficiently significant to pre-empt predatory or opportunistic behaviour? To what extent had legalistic measures reinforced the shared corporate values and strengthened the desire of all organisational members for a good reputation? In this study, the ultimate collapse of the Royal Bank of Liverpool in 1867 (see chapter 5) – twenty years after it had reorganised its managerial structure and policies – echoes O'Brien's (2014, p. 177) postulation that organisational procedures and rules are ill-positioned to improve corporate accountability – "unless at some point trust is placed in some claims or some persons, institutions, or processes". "It is unlikely", as Awrey and Kershaw (2014, p. 296) argue, that such reforms "would have prevented any of the major bank failures during the crisis, or indeed have altered the board composition of many of those failing banks". The culture of risk-taking and opportunism inherent in the world of banking and finance dampens the incentive for engaging trustworthy behaviour (Jaffer et

al., 2014b). “There are always temptations”, as O’Neill (2014, p. 186) warns, “to cut corners, to hurry procedures, to do a less good job than is needed, and to cover up for friends and colleagues”. Corporate accountability thus extends beyond strict compliance with organisational rules and procedures *per se*, and should be intelligently construed with reference to the broader frame of corporate governance, legislation, and professionalism. Robust corporate accountability requires a comprehensive reappraisal of the robustness of the existing system to cope with the conflict of interest, to provide remedies for failures, and foster a culture conducive for ethical and responsible banking (O’Neill, 2014).

8.5 Transparency: Shareholder Inspection, Information, and Publicity

Intermittent crises appeared to have exposed the failure joint-stock banks to live up to public expectation in providing the “most perfect and prompt control” to forestall abuses or misconduct (*Bankers’ Magazine*, Oct. 1847, p. 495). It was sometimes argued that shareholders’ properties were “entirely at the mercy” of the managing body, whose actions they nonetheless had little power to monitor (*Bankers’ Magazine*, Jun. 1848, p. 346). This thesis confirms the finding of Freeman et al. (2012, p. 111) that over the century the “constitutional balance” had shifted in the board’s favour, systemically divesting bank shareholders of their powers over key strategic and governance matters. In particular, with organisational rules explicitly barring shareholders from accessing important documents or account books, an enforced culture of secrecy deprived them of the ability to make an informed and independent judgement about corporate performance (see O’Neill, 2014). In the light of checks and balances in joint-stock politics skewed by asymmetric information and power, this section presents two important findings about how ongoing tensions between publicity and secrecy shaped the dynamic of trust repair in Victorian banks. First, “simple and straightforward” financial statements presented during the general meetings had paradoxically undermined transparency because they concealed rather than disclosed important corporate information (Freeman et al., 2012, p. 224). Second, with the press peering “behind the corporate veil” and the market’s heightened sensitivity to financial news, general meetings emerged as the platform on which the relative merits and demands for publicity and secrecy were hotly contested (Taylor, 2013b, p. 694). These meetings, being considered a “public occasion” and “sacrosanct” in joint-

stock politics (Freeman et al., 2012, p. 170), posed a challenge for directors in deciding the timing and extent to which sensitive information should be disclosed or withheld.

With the joint-stock mode becoming more widely adopted in preference to the traditional private banking "premised on partnership" (Wilson, 2014, p. 148; see Cassis, 2009), formal enquires mediated through shareholders' meetings were "important demonstrations of intrusion into business dealings and directorial conduct" (Wilson, 2006, p. 1077). In relation to this constitutionalised forum, a rash of failures and shocking disclosures in the 1830s led both legislators and bankers to the consensus that improved publicity of financial statements – as underlined in the *Select Committee Report* of 1836 (see chapter 4) – would keep shareholders adequately informed of how their companies functioned. The founder and chairman of the Sheffield Banking Company Samuel Bailey (1837, pp. 212-3), for instance, endorsed the report for its sound exposition of "the true principles of banking", using "statistical facts" and "economic principles" to enlighten those engaged in trade and commerce. Advocates of joint-stock banks touted the proposal as a distinct advantage that set them apart from private banks where privacy was jealously guarded. However, Alborn (1998, p. 112) associates the call for administrative reform with "a movement toward streamlined administrative structures that enacted barriers between the bank manager and the proprietary". The line between shareholder activism and interference could be "a narrow one", and it is not unknown in the case studies (for instance, the Northern Bank and the Bank of Manchester) that sometimes "a sensitive board could easily take umbrage when they felt the line had been crossed" (p. 119). Progressively, shareholders became less assertive in the participatory politics of joint-stock banks and more reliant upon their "elected officials" for information and wisdom. As shown below, this transition marked a gradual shift from direct inspection of accounts by shareholders to "more formal scrutiny" by *ad hoc* or regular auditors (Freeman et al., 2012, p. 213).

The findings gathered from the case studies are largely consistent with the findings of Freeman et al. (2012) that show a gradual curb on shareholders' rights of inspection. Rules were explicitly enacted in the banks' constitution to bar them from accessing important documents or account books. As a consequence, with shareholders having to rely on summary accounts and audited reports presented at the general meetings during which they had limited time to investigate the statements in greater depth, they were deprived of the ability to form an independent judgement about corporate performance (see O'Neill, 2014). Arguably, insomuch as shareholders believed that high dividends

were "the most important and best-protected benefit", they subsequently became less critical of the published reports (Freeman et al., 2012, p. 123). The "language of openness and straightforwardness" used by boards did not necessarily translate into transparent governance, as the management kept a firm hand on the form, content, and extent of disclosure, dictating the agenda and subjects under consideration (Freeman et al., 2012, p. 224). Practically in all cases – except the Consolidated Bank and Preston Banking Company – there were recurrences that statements which were once vouchsafed for their fairness and accuracy turned out to be "high pretensions" of growing prosperity, craftily engineered by so-called "men of rank" lacking moral rectitude and common honesty (*Bankers' Magazine*, Jan. 1857b, p. 4). Robert Stewart (1853, p. 5) criticised the approach to audit as "superficial and unsound", drawn up merely to certify "the correctness of the accounts". The *Bankers' Magazine* (Jan. 1856, p. 7) also concurred that the entire process was "worse than useless", "a mere matter of form" involving nothing than "dotting up of certain figures" furnished by the directors.

Notably, in banking where a system of "mystery and concealment" rendered shareholder oversight "necessarily more indirect", the "standard mechanism" for holding the governing body accountable in the event of a crisis was to form a shareholder committee vested with the power and independence to conduct investigation (Freeman et al., 2012, p. 227). The introduction of an intermediary (i.e. the committee) into the relationship between the management and proprietors nonetheless represented a further departure from direct shareholder involvement to virtual or direct representation (Freeman et al., 2012). Shareholders were obliged to trust and depend on "elected representatives" to perform the investigative job with competence and independence (p. 237). Thomas Corbet (1841, pp. 97-8), questioned the credentials of shareholders in undertaking such a task, warning that where knowledge was deficient "fools take the lead, and wise men are reduced to the condition of, and are obliged to content themselves with being lookers-on". Stewart (1853, p. 14) also dismissed their role as merely hunting down "some weak or wrong points" in the management. Notwithstanding the criticism, typically shareholders displayed little doubt as to the committees' rigour and independence in unearthing controversies and conflicts of interests. Composing of Victorian gentlemen with credible moral standing and commercial stature, the committees demonstrated professional scepticism and questioning minds, seeking to obtain a full understanding of all relevant facts and evidence that exposed the management's

representation to public scrutiny (see O'Brien, 2014, p. 224). Post-investigation inquiries often presented managing bodies a delicate challenge regarding disclosure and secrecy.

Even with diminished shareholder power and participation in corporate affairs, the constitutional structure of joint-stock politics still afforded a platform for conducting rigorous post-mortem inquiries, as demonstrated through "lively proceedings" at the general meetings (Freeman et al., 2012, p. 143). Formal enquiries into directorial conduct mediated by shareholders' meeting were "important demonstrations of intrusion into business dealings" (Wilson, 2006, p. 1007). The growing importance of banks as "investment propositions" – which in turn reinforced public perceptions of banking's increasingly "public utility" – also amplified the pressure and demand for transparency in times of crisis (Wilson, 2014, p. 148). As narratives in this study had revealed, given that public mind was in "a state of alarm", openness and honesty in giving a full account of the company's crisis forestalled the dangers of unfounded rumours turning into "fact and circumstance" (*Bankers' Magazine*, Jan. 1857b, p. 7). Transparency was also pivotal to shield the management from any suspicion of wanting "to deprecate or escape from an ordeal" (p. 8). On the other hand, insomuch as the governing body was responsible for the crisis, self-exculpation in the evidence of guilt and "duplicitous impression management" stoked public resentment and suspicion (Gillespie & Dietz, 2009, p. 137; Gillespie et al., 2014; Kim et al., 2004). Denials and obfuscation alienated stakeholders who, upon frustration, turned to the press for attention (see Pfarrer et al., 2008).

The emergence of the press as a watchdog in the marketplace corroborated the "liberal ideology" in Victorian Britain, anchored upon the belief in the power of publicity "to educate and encourage rational debate", and its ability to remedy the failure of company law to protect investors (Taylor, 2013b, p. 700; Taylor, 2012). Just as nineteenth-century directors were skilful at hiding secrets from shareholders, Evans (1845, p. 134) reminded his peers that their "chief qualification" was to fearlessly expose "anything like fraud or foul dealing", "watching over the commerce of the country" in the interest of the general public. As Taylor (2013b, p. 699) confirms, over the century the British press retained "a fair measure of public trust" for its "distinguished record" of exposing corporate scandals to public gaze. Given the public perception that corporate affairs "were to some extent public property", under the constant pressure of the press and shareholders the boards were certainly mindful of the strategic importance of transparency in dispelling rumours and suspicions during crises (Taylor, 2013b, p. 686). Using the Royal British Bank's scandal as a lesson, the *Bankers' Magazine* (Oct. 1856b, p. 602) warns that in days

of "competitive influence and slanderous whispering", failures to disclose pertinent information was liable to further erode the credibility of a troubled entity. According to Gillespie et al. (2014, p. 391), by gaining control of the "dominant narrative", the press deprived the management the opportunity "to actively manage the data manipulation problem internally without prominent external control and reputational damage" – a painful and costly lesson that the Northern Bank directors had learned. In this sense publicity was a "pragmatic move", initiated by the management to ward off "the risks of garbled or false information going out to the public" (Taylor, 2013b, p. 686).

Insights from the case studies – especially the District Bank, the Manchester Bank, and Liverpool Borough Bank – revealed that a system relying on "full and open discussion" posed a paradoxical problem for banking where secrecy and publicity were equally prized and cherished (Alborn, 1998, p. 105). Directors also deemed prudent to withhold certain sensitive information, fearing that indiscriminate publicity could destabilise public confidence and trigger "a very direct and powerful impact" on market behaviour (see Tambini, 2015, p. 123). The requisite need for secrecy was particularly acute when one considered the "potentially powerful position" of journalists within a broader framework of corporate governance (Tambini, 2015, p. 123). On balance, the study supports the supposition of Gillespie and Dietz (2009) that openness, meticulous investigation, voluntary disclosure, and a credible explanation formed a necessary part of the trust repair process. Nonetheless, the narratives inferred that transparency and disclosure were discreetly staged and timed before the scale of the problem could be more accurately ascertained. As the following section will discuss, tactful interactions and continuous assurance were essential to negate possible resentments or frustrations resulting from selective secrecy. This allowed shareholders to form more accurate perspectives of the firm's status, creating a crucial connection to organisational rehabilitation in the following stages (Pfarrer et al., 2008).

8.6 Equity: Conflicts, Prioritisation, and Reconciliation

Another important finding in this study is the presence of "multiple constituencies" with competing demands, giving rise to longstanding and heated debates about whose interests should be prioritised after each organisational crisis (Awrey & Kershaw, 2014, p. 298). In practice, not all concerns are likely to be given immediate attention, and there are gaps between "those stakeholders that the firm is normatively obliged to acknowledge, and

stakeholders that are actually approached in dialogue, consultation, or partnership" (De Bruin, 2014, p. 261). This is because divergent interest groups are normally ranked according to their respective power, legitimacy, and urgency (Mitchell et al., 1997), with priority given to stakeholders whose interests and goals are perceived as "pressing and requiring immediate attention" in the event of conflict (De Bruin, 2014, p. 261). Against this backdrop, this section demonstrates the importance of senior management adopting a pluralistic approach by which the interests of all stakeholders were carefully weighed and deliberated, "without any legal direction to prioritise one constituency over another" (Awrey & Kershaw, 2014). It then considers a few obstacles to effective stakeholder engagement – namely, new market information, rumours and hearsays, and shifting public perceptions – all of which could frustrate and thwart the process of trust repair.

Owing to the conflicting role expectations faced by bank management, and the constraints of unlimited liability on shareholders, it was challenging for the governing body to fulfil what Dodd (1932) terms as "the quasi-public responsibility" of treating all stakeholders with fairness and equality, as exemplified in the cases of the Royal Bank of Liverpool, the Bank of Manchester, the Consolidated Bank, and Preston Banking Company. The most pressing issue was finding ways to promptly meet the claims of depositors and noteholders, using the aggregate wealth and unlimited liability of shareholders to provide a pivotal reassurance of the bank's security (Hickson & Turner, 2005, p. 186). Socio-occupational evidence revealed that most shareholders were gentry, merchants, and professionals, coming from the wealthiest strata of Victorian society (Turner, 2014, p. 114). The fact that depositors and noteholders were fully repaid clearly vindicated the ample wealth of shareholders to meet the banks' liabilities. More importantly, across all case studies, the crises did not result in opportunistic dumping by shareholders *en masse*, given the constitutional rule which preserved the "equilibrium of wealthy bank owners" by prohibiting share transfers (Turner, 2009; Turner, 2014, p. 108). The "post-sale extended liability" imposed by the Banking Co-partnership Act of 1826 also prevented opportunistic dumping by shareholders, making them liable for the bank's debts for three years even after they had sold their shares (Turner, 2014, p. 112). Unlimited liability, coupled with the restrictions on the transfer or relinquishment of share ownership, meant that shareholders bore the brunt of the cost, although depositors and noteholders also suffered short-term inconvenience due to delays in receiving their money.

To complicate stakeholder engagement further, situational factors lying beyond the control of senior management also altered the level of vulnerability and thus the level of

trust between conflicting parties in the face of divergent interests (Zafari et al., 2020). The *Bankers' Magazine* (Oct. 1847, p. 493; Dec. 1857, p. 997), for example, remarked how a discovery of new losses, collapse in asset prices, and "hostile state of public feeling" stirred up by sharp-tongued commentators or disgruntled parties, may bring "new moments of embarrassments" into play (see for instance, the Northern Bank and the Bank of Manchester). The narratives of the case studies are also broadly consistent with Thompson's (2015, p. 180) observation of the critical role assumed by the press in establishing the "parameter of market consensus" and signalling "the prevailing mood of the investing community". Modern scholars emphasise the need for formulating strategies to enable trust and contain threats from the external environment that may undermine ongoing engagement efforts (Zafari et al., 2020), paying attention to how stakeholders revise their values and expectations in the face of market turbulence and informational changes (De Bruin, 2014). The speed at which news travelled across a cohesive community via words of mouth and press publicity, and the strong correlation between banking institutions and the financial market, implied that local banks must remain attentive to potential threats and opportunities, as well as signals that reflected the underlying shifts in collective market perceptions (Zafari et al., 2020, p. 283; Weick & Putnam, 2006). Such "mindfulness" is essential for avoiding conflicts and "keeping relationships alive", suggesting the importance of frequent communication that helps monitor the resilience of organisational affiliations and thus the opportunities for (renewed) collaboration (Zafari et al., 2020, p. 283).

Being able to avoid prioritising "one constituency over another" was among the few strategies which successfully put a few banks – namely, the Royal Bank of Liverpool, the Consolidated Bank, and the Preston Banking Company – on the path to recovery. Their success echoed the assertion of Jaffer et al. (2014d, p. 57) that it is "lawful, legitimate and expected" that organisational leaders should respond to different clients with divergent but equally legitimate needs without partiality. Sandwiched between classes of stakeholders with distinct difficulties and demands, the credibility of senior management hinged on achieving a satisfactory compromise with one group (i.e. depositors and noteholders), without pressing too hard upon the other (i.e. shareholders). To contain distrust, directors kept their shares and remained stuck with the firm until they had successfully navigated it through the crisis, proving that their incentives were aligned with those of shareholders (Hickson & Turner, 2005). A high level of interdependency and commitment, alongside constant interactions and abstinence from the use of coercive

power, helped nurture a favourable atmosphere in which injured parties were willing to take the risk and collaborate with the management again, with the expectation that in the presence of vulnerability their trust would not be abused (Zafari et al., 2020).

The case of the Manchester bank offered an excellent example that while dialogues between the management and injured parties often began with sparks of anger and resentment – a situation attributed by De Bruin (2014, pp. 262-63) to "a clash in expertise and expectations owing to value ambiguity and differentiation perspectives" – the case studies show that stakeholder engagement, when mindfully handled, reduced antagonism and distrust. By identifying the core issues at stake, both Dryzek (2000) and Habermas (2006) agree that stakeholder engagement improved the quantity and quality of information, with interested parties meticulously discussing the urgency and legitimacy of divergent concerns. Zafari et al. (2020) holds a similar view that regular interactions with diverse stakeholders allow senior management to frame the underlying issues more accurately and negotiate or modify terms where necessary. Given the multiple perspectives presented by other parties, stakeholders gained a holistic understanding of the issues at stake, thus fostering a greater sense of empathy for each other's concern. By increasing the proximity between the management and injured parties, open dialogues and active stakeholder involvement improved the legitimacy of organisational leaders when guiding the company to the best possible solution (De Bruin, 2014). Most significantly, a strong sense of local patriotism and identity gave the managing body an advantage to rally different injured parties behind a common objective of reviving the bank as a local monument of economic pride, thus building more resilience, cohesiveness, and stability into organisational relationships amidst market uncertainties (see Zafari et al., 2020). Throughout the process, they worked together to make sense of potential threats and opportunities, (re)negotiating the terms where necessary to enable quick decision-making (Zafari et al., 2020). This pattern somewhat resembled what Williamson (2000) terms as "non-calculative social contract" meant to consolidate socio-economic bonds between all parties and restore discipline in the management.

Interestingly, the introduction of the Joint-Stock Companies Act of 1857, which granted shareholders and creditors the power to appoint liquidators to wind up a concern in the spirit of "unanimity and union between all parties concerned", did not induce a profound change in the pattern of conflict resolution (*Bankers' Magazine*, Dec. 1857, p. 995). Citing the uncertainties and costliness which legal processes entailed, the banks analysed in this thesis – the Consolidated Bank and Preston Banking Company, in

particular – remained strongly in favour of engaging all organisational members "in one general effort of cordial cooperation" to resolve conflicting agendas as explored above (p. 997). Local patriotism appeared to have forged a social contract to promote collaboration between banking entities and the community, during which local cultural norms were inculcated to promote socially desirable behaviour and regulatory outcomes (see Awrey & Kershaw, 2014, p. 292). As commercial networks and customs differed from place to place, the process of negotiating a so-called social contract in pursuit of broader societal welfare was left to the discretion of individual banks, with each adopting "divergent perspectives respecting, *inter alia*, whether and to what extent various activities generate systemic risk and how best address it" (Awrey & Kershaw, 2014, p. 292).

Over the long-term, addressing the varied interests of stakeholders while navigating conflicting role expectations continue to pose a challenge for bank management. As the *Bankers' Magazine* (Feb. 1858, p. 85) emphasised, principled bankers understood the need for harmonising shareholders' pursuit of high returns from (risky) lending with depositors' expectations of secure and profitable long-term investments. Although for most part of the nineteenth century unlimited liability had served to contain a culture of greed and short-termism by enforcing rigorous moral expectations and financial responsibilities upon management and shareholders, the design was not without obvious drawbacks. As the *Bankers' Magazine* (May 1857, p. 375) once remarked, the guarantee of full repayments offered "no compensation for the distress occasioned by the intermediate delay". Institutional arrangements – such as contracts and liability rules – could only deal with opportunistic behaviour and direct financial losses sustained by individual stakeholders, without encapsulating the spill-over costs of banking crises suffered by the wider society (Armour & Gordon, 2014). Commenting on the competitive pressure under which financial intermediaries pander to shareholders' craving for quick returns, Kay (2012) is pessimistic about the workings of anonymous markets in fostering long-term cooperation, given the tendency of market participants to maximise their own gains at the expense of others. On the other hand, trust is precipitated upon a behaviour demonstrably committed to investing for the long term (see Jaffer et al., 2014b). In the twenty-first century, there is a call for "a form of stewardship" in which bank managers go beyond their duty of care as stipulated in contractual agreements, and undertake longer-term investment to enhance organisational values (Kay, 2012; Mayer, 2013).

8.7 Legality: Prevention, Punishment, and Protection

As Victorian lawmakers responded to banking crises by introducing or amending legislation from time to time, questions arose as to how far the government should travel to restrain private enterprises whose activities nonetheless incurred enormous ramifications across the real economy. Wilson (2014, p. 129) believes that the Victorian legal framework for capitalism must be construed as "being predominantly private but also as having public dimensions" – an argument endorsed in this thesis given the importance of banking institutions in securing economic expansion and the stability of a nation's payment systems. As underlined in this study, the unique and influential position occupied by banking in a capitalist economy acted as a catalyst for the government's growing assertiveness to act in public interest (Wilson, 2014, p. 147). This development can be mapped onto two distinct but intertwined trajectories. First, in conjunction with the use of shareholders' meetings as a forum to inquire into directorial conduct, banking companies were legally obliged to present financial reports so as to bring commercial dealings under closer public inspection. Second, there was also an increasing urge for using the "public space" afforded by the legal apparatus for "deliberating degrees of unacceptability and unlawfulness" in the joint-stock economy as "important matters of public concern" (Wilson, 2006, p. 1079). As this section will discuss, the complexity behind the nature of banking relations was such that over the century legal interventions always grappled with the disputed boundary between private enterprises and public concerns (see Wilson, 2014, p. 136). To maintain confidence, Victorian lawmakers also faced the challenge of keeping legislation abreast of rapidly changing market conditions without encroaching upon the freedom of financial innovation.

As the nineteenth century rolled on, the "public profile" of banking became increasingly apparent as a sizeable number of joint-stock banks failed to function as "principal depositories of financial savings and primary allocators of credit", thereby inflicting considerable injuries upon the wider society (Wilson, 2014, p. 147). When "permissive legislation" in the 1830s had apparently failed to procure shareholders' access to corporate information (Alborn, 1998, p. 112), in the following decade corporate disclosure became the heart of regulatory responses to banking scandals. Alongside the Joint-Stock Companies Act of 1844, the introduction of Joint-Stock Bank Act in the same year represented a shift towards "state-assisted publicity", marking a "different level of intrusiveness" into banking affairs (Wilson, 2014, p. 138). The *Bankers' Magazine* (Sep.

1844, p. 347) welcomed the move, opining that “publication and periodical examination of accounts are good preventives against fraud and culpable negligence”. Arguably, the change also signified the end of an era when corporate conduct was looked upon as “purely a matter of private concern and operation” (Wilson, 2014, p. 137), following the “heightening awareness” that banking conduct had to be transparent and prudent because of its importance and impact over a wide constituent of society (p. 150). This view began to permeate as contractual relationships between different parties became more formally established and entrenched with the growth of joint-stock banking. To the extent that openness and transparency were recognised by members of public as positive moral attributes, the importance of (re)building public confidence via mandatory disclosure “extended beyond the interests of the actual parties involved, and clustered around the integrity of commerce itself” (Wilson, 2014, p. 149). It was this “nineteenth-century awareness” of the impact of business corporations spanning beyond the immediate contracted parties that explains the “contemporary recognition of public interest in aspects of private enterprise” (p. 150).

Given the relapses of misleading financial reports (as extensively detailed in the cases of the Northern Bank, the District Bank, the Bank of Manchester, and the Liverpool Borough Bank), the legacy of Victorian corporate reporting resonates with the view of contemporary scholars who see interim statements as a poor approximation of long-term organisational performance. By swamping ordinary stakeholders with “a mass of details” and increasing the “noise” in the banking system, rule-based disclosures make it difficult to form accurate assessments about corporate performance (Jaffer et al., 2014a, p. 117). To the extent that disclosure rules provide companies the loopholes to “arbitrage regulations to fit their strategies and practices” (p. 109), financial intermediaries are exposed to the temptation to exploit informational power over stakeholders to mask incompetent performance or predatory behaviour. While 1840s legal reforms were consistent with the classical belief that publicity baffles frauds and facilitates economic decisions (see O’Brien, 2014), the legislation gave no specifications as to the form and substance of balance sheets, asset valuation, and audit principles (Johnson, 2010). By the 1850s, recurrences of banking scandals and falsified statements increasingly led to the belief that legal facilitation had ironically enlarged “the scope of abuse” (Wilson, 2006, p. 1078). With directors continuing to publish “worthless documents” without breaching disclosure rules, the *Bankers’ Magazine* (Jul. 1857, p. 580) changed its stance, attacking the legislation as one of the most “insane enactments” which offered “no security against

frauds". The periodical went on to warn about the tendency in public mind "to credit any report, however vague, when accompanied by assertions of prosperity and promises, however false, of large profit". Evans (1859a, p. 111) complemented that it often appeared in the last moment "there had been either extravagance, ignorance, or mismanagement, in the usual sense of the terms".

Disclosure is supposed "to inform the investing public of actual practice" and encourage expressions of views about "the boundaries of what could be constituted as acceptable" (O'Brien, 2014, p. 218). As it turned out in Victorian banking, there were at least two reasons as to why "frequent publicity did not mean good publicity" at all (Robb, 1992, p. 72). First, demand for "ubiquitous transparency" creates perverse incentives to conduct "more outside meetings" and diverts corporate resources to defensive strategies, stifling open discussions and "serious discussion of options" that might attract negative publicity or depress share prices (O'Neill, 2014, p. 183). Second, reducing corporate reporting to mere "legal permissibility and technical compliance" runs the risk of undermining the "ethical and normative foundation" upon which the architecture of disclosure was once built (O'Brien, 2014, p. 209). This thesis confirmed the findings of contemporary scholars that disclosure is "more than mere transparency" and requires effective communication: information is only meaningful when conveyed intelligibly and adapted to the specific needs or characteristics of different users (O'Neill, 2014, p. 185). Disclosure makes little sense unless information available allows users and regulators to make intelligent judgement on "where to award trust, and to ensure that trust where given is warranted" (Jaffer et al., 2014a, p. 123). By the middle of the nineteenth century, it remained notorious that a "seemingly solid, safe bank" could suddenly turn out to be "a black hole, swallowing wealth, disrupting credit, and destroying trust" (Taylor, 2013a, p. 122). With annual statements continued to be riddled with inaccuracies and fabrications, prevention gradually "fell out of favour" and the government began to take punishment of financial misconduct more seriously (Taylor, 2013a, p. 121).

By wrecking confidence in the investment market which formed the lifeline for industrial capitalism, in the 1850s the wider effects of bank failures became increasingly "harder to ignore" (Wilson, 2014, p. 172), prompting the state to present criminalisation of fraud as "the natural corollary of deregulation" (Taylor, 2013a, p. 121). The *Bankers' Magazine* (Dec. 1856a, p. 792) criticised that existing laws were seemingly "intended more for the benefit of the dishonest man". An unnamed commentator wrote that recurring "moral delinquency and guilt" had penetrated more deeply into the commercial

system than before (Dec. 1856b, p. 786). Another feared that the nation was losing its "banking fraternity" earned through "high character for prudence probity", intimating that the virus was "more widely spread" than the public imagined (May 1857, p. 375). A series of trials of bank directors during the decade illustrated the growing emphasis placed upon the "public dimensions" of financial misconduct and its "perceived capacity for societal destructiveness" (Wilson, 2006, p. 1080). The outcome of the trial of the Royal British Bank directors reinforced the view that their offence had transcended "mere breach of contract" and constituted "great public mischief" (Evans, 1859a, p. 385). The civic verdict passed upon Joshua Dixon of the Liverpool Borough Bank indeed answered to the growing public intolerance of financial misrepresentation. Most notably, tougher legislation and legal sentences reflected the underlying concern about the seriousness of dissipating confidence in commercial dealings, and the resulting disintegration in Britain's reputation as a trading nation (Wilson, 2014; Evans, 1859a).

The passage of the Punishment of Frauds Act (1857) gave a clear signal of political interventions in the corporate economy "to address the need for honesty in representations made in the public domain" by a business organisation – particularly about its financial status (Wilson, 2014, p. 141). In making misrepresentation punishable by law, directors were – "at least in theory" – legally obliged to disclose nothing but the truth (Taylor, 2017, p. 11). The fact that the state proactively enforced the legal requirement signified a departure from the *laissez-faire* approach witnessed in the first half of the century. The shift from prevention to punishment also reflected the growing appreciation of the role of fiduciary agents, stressing their duty to act with honesty, loyalty, and prudence in the best interests of the principals (see Jaffer et al., 2014d, p. 34). By establishing a common understanding among market participants of what comprised the underlying ethics, the law is meant to provide a framework capable of resolving violations and disputes in a manner that is "proportionate, targeted, and ultimately conducive" for the development of a trustworthy banking system (O'Brien, 2014, p. 230). Notwithstanding the reform, the cases detailed in the Consolidated Bank and the Preston Banking Company showed that directors and interested parties preferred to resolve disputes among themselves rather than taking the matters to courts, citing the costs and uncertainties which accompanied prolonged litigation processes. In fact, before the 1870s criminal and civil prosecutions were largely atypical or judged "superfluous", insofar as extra-legal sanctions resulting from negative publicity were capable of regulating the marketplace by inflicting reputational loss and public humiliation upon the transgressors (Taylor, 2017, p. 8).

As to the trustworthiness and reliability of the banking sector, the reforms undertaken by Victorian lawmakers attracted mixed responses. The *Bankers' Magazine* (May 1844, p. 70), for example, complained that "the law is either defective or ambiguous", often passed and hurried through the Parliament with little consideration as to its design and implications. Another article (Dec. 1856a, p. 792) decried that reforms in the company law were "a tinkering and a patching", carried out spasmodically in response to new forms of frauds and deception camouflaged in a flux of financial innovations in the industry. Modern scholars agree that because of their lack of knowledge and resources, regulators struggle to understand the dynamics and incentive structure of the industry (O'Brien, 2010; Jaffer et al., 2014a). Regulatory initiatives are based on "circumstantial and anecdotal evidence", with legal machinery being somewhat inadequate to cope with the density and dynamism behind financial transactions. It would take until the outbreak of the next financial crisis before it could be ascertained whether past reforms had effectively broken the "desultory cycle" (O'Brien, 2014, p. 210). Victorian reforms were incremental and arguably haphazard, revealing the difficulty faced by the state to align the regulatory framework with a rapidly evolving banking industry, in an effort "to promote healthy, wealth-creating risk-taking whilst seeking to stay ahead of innovations for abuse within this culture" (Wilson, 2006, p. 1088). There were obvious tensions between promoting economic freedom in banking activities whilst simultaneously seeking to restrict abuses arising from the new market environment (Wilson, 2014, p. 141). The extension of limited liability to banking firms and criminalisation of frauds, for instance, represented "a symbiotic rather than a contradictory relationship" between freedom of contract and a tougher criminal law (Taylor, 2017, p. 12). This seemingly ideal arrangement was to many parties "the best of both worlds": entrepreneurial freedom was guaranteed but those who abused it would face legal penalties (p. 12).

By the 1870s, the state progressively took upon itself the role of a market watchdog by enforcing laws and directing resources towards commercial matters of public concern (Wilson, 2014). This change also coincided with the emergence of a new era of commerce where formalised transactions increasingly replaced face-to-face dealings between individuals "by virtue of reputation" as witnessed during the first half of the century (Wilson, 2014, p. 149). By repealing "ill-suited" or "outdated" laws and enacting new ones, the question was to what extent the state had effectively restored trustworthiness and credibility to the banking system (Wilson, 2014, p. 149; see also Lobban, 1996). The long-term concern is that intrusive regulations only encouraged weak trustworthiness,

with agents behaving trustworthily simply because they want to avoid legal penalties (Jaffer et al., 2014a). Strong trustworthiness, on the other hand, requires organisational leaders to recognise their fiduciary obligations and express genuine concern for stakeholders' well-being (Jaffer et al., 2014a). Fiduciary duties, in this sense, become "an object of regulation", making clear the terms of liabilities and on whom they would fall (Jaffer et al., 2014c, p. 23). To restore the "faded lustre of responsibility" in the long-term, O'Brien (2014, p. 218) argues the case for establishing a "more granular definition" of the ethical constructs which underline the banking architecture – and challenging the assumptions of the policy options which govern "the worldview of finance" every now and then, if necessary (O'Brien, 2014, p. 218).

8.8 Concluding Comments: Forward to the Past?

This thesis does not seek to deduce and construct any nostalgic "moral" proposals from historical lessons to provide explicit charters for future banking reforms. Rather, by using a contemporary trust repair model to unpack the underlying dynamics of how effectively Victorian joint-stock banks emerged from organisational crises and regained stakeholders' trust, the thesis presents a persuasive case for understanding and (re)connecting with the past through the perspectives of management scholars in the twenty-first century. Simultaneously, contextualised and retrospective case studies of nineteenth-century banking also provide a historical lens for reviewing the applicability of modern trust repair principles and practices, often generated from conceptual and experimental work undertaken in the present day (see Gillespie et al., 2012, p. 211). A study of such nature is fairly uncommon among mainstream economists or management scholars. For this reason, this thesis is characteristically different, as it does not see historical crises as "a homogenous data pool with which to test modern theories" (Dow & Dow, 2014, p. 1341). Rather, given the "open nature of economic processes" through which the source of evidence varied as time rolled on, this study focuses on how institutions and human actions evolved "in non-deterministic ways, and in different ways in different societies and at different times" (Dow & Dow, 2014, p. 1341). In so doing it also demonstrates the value of using different historical and institutional contexts to inform the modern understanding of the connection between banking and trust-related issues.

Two important merits of this study are summarised as follows. The first relates to its use of a multiple-level perspective in analysing the dynamics of trust repair, which went

beyond direct, interpersonal "one-on-one" engagements (Gillespie et al., 2012, p. 193). A person may be scrutinised for his ability and integrity; an organisation for its security, and the system for its stability – and all these facets may either reinforce or undermine each other such that trust repair efforts should be approached across multiple agents and levels (Gillespie et al., 2012, p. 180). This study identifies and views the (un)trustworthiness of individual bankers in relation to the system of training, selection, and socialisation they had experienced, and the wider cultural norms and legal requirements that constrained their behaviour. This principle is important because institutions consist of norms, rules, and procedures that condition and influence social behaviour, implying that the dynamics of trust repair transcended different levels (see Bachmann & Inkpen, 2011). Efforts at both the interpersonal level (e.g. directors' engagements with stakeholders) and institutional level (e.g. organisational and legal reforms) were necessary for re-establishing the basis for trust building between market participants (see Gillespie et al., 2012, p. 192). The approach of this study thus adds richness to the analysis of the sources of trust deficits in the banking industry, and how they may be repaired, and in so doing it validates the importance of robust institutional structures, rules and norms that "mandate and reinforce trustworthy behaviour" (p. 193).

Second, this thesis goes beyond "private dyadic relationships" addressed in past studies and considers the influence of "broader systemic variables" over the trust repair process, and how multiple players operated at different levels accordingly (Gillespie et al., 2012, p. 192). In conjunction, it also applies a multi-stakeholder perspective, in recognition of the heterogeneity of diverse parties whose vested interests were assigned different degrees of moral urgency. This approach presents the case for adapting the strategies and approaches for repairing trust at intervals, in view of possible variations in trust antecedents across different interest groups (Gillespie et al., 2012). A multi-stakeholder perspective also allows this study to explore how different sets of organisational relationships were structured by (unequal) corporate power and control, which in turn had profound impact on the trust repair process (see Gillespie et al., 2012). Because how bank directors assessed and prioritised competing interests was almost certain to invoke different emotions and responses from diverse stakeholders (see Pfarrer et al., 2008), they facilitated trust restoration by actively engaging stakeholders in dialogues, offering reasonable relief and reparation, and tactfully abstaining from exercising corporate power, which could be interpreted as unfairly coercive amidst a heightened sense of vulnerability and resentments. If differences were difficult to

reconcile, then common ground had to be identified. This was especially important when banking crises triggered a breakdown in an intricate network of relationships accompanied by broad and disruptive economic suspensions, often played out in the "full glare of the media" (Gillespie et al., 2012, p. 192). The success in defusing the impact of negative publicity and restoring organisational legitimacy depended critically on the management's effective capitalisation upon the shared perspective and identity between the company and local community.

There are, nonetheless, two limitations which suggest potential areas for future research. First, effective trust repairs require a transparent and holistic diagnosis across different organisational components. However, the evidence inferred and extrapolated from the case studies was arguably mixed. In banking crises for which a wide range of actors and agents were responsible, a transparent diagnosis could sound "more as an ideal to strive towards" (Gillespie et al., 2012, p. 208). Analysis shows that reforms undertaken in response to periodic crises did not necessarily conform to the "principle of congruence", vital for ensuring a consistent and robust system, in which norms and rules were realigned to improve the predictability of banking behaviours (p. 209). Some components of the institutional framework – unequal corporate power relations, financial opacity, and company law, for instance – were somewhat slow or showing little inclination to adapt, thus sending contradictory signals as to the system's trustworthiness as a whole. Further work is therefore required to explore how reform agendas are determined and dictated, in the face of resistance to changes and relative power vested in different interest groups.

Second, the case studies also provide little evidence as to whether the banks had placed themselves under exhaustive and rigorous post-crisis evaluation, in order to erect safeguards and fend off future violations. What comes next after successful trust repair clearly matters. The appearance of reforms may prove deceptive, leaving loopholes for future exploitations. According to Gillespie et al. (2012, p. 208), post-crisis reforms which followed the global recession in 2008, for instance, had witnessed the attempts by some banking firms and hedge funds "to work around rules and hire lobbyists" to manipulate the reform agenda. As the argument goes, "without successive reviews and refinements, it is unclear whether reforms will produce real, enduring change". Will trust return to the pre-crisis level? Will there be "an ambivalent relationship comprising positive and negative perceptions", in which stakeholders' willingness to trust again is accompanied by heightened vigilance and monitoring (Gillespie et al., 2012, p. 212)? Clearly, trust repair efforts must go beyond the immediate term: it requires the offending organisation

to address any "residual of distrust" resulting from frustration and any apparent lack of repentance (Gillespie et al., 2012; Lewicki et al., 1998). Without a rigorous and comprehensive examination of reforms over time, there is every likelihood any appearance of trustworthiness is delusional and speciously be "celebrated as progressive", only to be condemned later for not going far and deep enough (Gillespie et al., 2012, p. 212).

There are numerous significant differences between banking in the nineteenth and twenty-first century. Besides obvious questions of scale and complexity of operations, there are fundamental moral ones. The strong ties between the banks and local stakeholders starkly contrasts with modern banking institutions which Lord Adair Turner, Chairman of the Financial Services Authority, famously castigated as "socially useless" (Lord Turner, cited in Wilson & Wilson, 2013, p. 55). Once largely based on "relationships and moral suasion", the "commoditisation of financial services" has transformed financial institutions into "organisations whose purpose was to look for people from whom they could make money, in contrast to ones who saw their purpose as helping their clients to make money" (Jaffer et al., 2014c, p. 9). Changing business models and financial innovation has resulted in a growing chasm between institutions and stakeholders, thus reducing the importance of relationships conducive for the inculcation of trust, honesty, and reliability (Jaffer et al., 2014d, p. 32). Perhaps as a result, much of the post-2008 literature has focused on the question of state regulation. Though obviously important, there is scope to extend the focus to include other sets of relations. Responsibility extends beyond the duties exacted by legislation under which banking entities were held liable in the event of trust failures. The sense and scope of responsibility vested in Victorian banking institutions were invariably conditioned by the working of the social order, in which banking practices came under constant public scrutiny and appraisal. In an age when banks were not deemed "too big to fail", they could, when faced with crisis, do much to influence narratives, rebuild damaged relationships, and restore trust without turning to the state for help.

Importantly, this thesis approached the development of Victorian banking not so much as a *planned* progression towards a known goal as many contemporary policymakers or economists would understand, but rather as "a process of formation and modification of the human intellect, a process of adaptation and learning", along which *unknown* possibilities are numerous, and human values and objectives are subject to frequent alterations (Hayek, 1960, p. 37). As underlined in the analysis of the historical

narratives, institutional changes and improvements were slow and incremental, and the rise of joint-stock banks was nothing short of a protracted evolutionary course over which new ideas and knowledge were constantly adapted, modified, and developed. As the *Bankers' Magazine* (Oct. 1847, p. 495) put it, there were intermittent setbacks or casualties which left many stakeholders "dead or wounded" but on the whole joint-stock banks had increasingly gained "a solid footing", steadily replacing private banks as the "sole banks" in the nation over time. The path to growth and maturity followed by many joint-stock banks testified to the general progress made possible by the readiness of members of society to experiment with the unknown. It was the willingness to trust, re-trust, and enter into social cooperation in the face of limited knowledge and uncertainties that made market participants wiser by learning what they had not known before.

[Word count inclusive of in-text references: 86,028]

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