Business and Economic History
On-Line
Vol. 6 2008

Management and Networks: To What Extent Were Free-Standing Companies Controlled from the Home Country? Four Scottish Examples, 1865-1885

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Although the free-standing company was an important form of foreign investment before 1914, its implications for economic development in home and host countries remain unclear. Scotland was home to at least four hundred free-standing companies between 1862 and 1900. A core debate concerns the level to which these were entrepreneurial firms or purely devices for speculation. I examine four companies to analyze the role of their Scottish head offices: two agricultural companies operating in Australia and New Zealand and two U.S.-hosted firms. The two firms operating in Australasia were more effective in establishing control over their operations by devising clear command structures. The Australasian-hosted companies were more adept than the U.S.-based firms at using the head office presence to establish marketing links in the United Kingdom. I conclude that the role of the head office is important for establishing competitive advantage for the free-standing company in its operations in the host country.

In the mid- to late nineteenth century, one of the main vehicles of foreign investment was the free- standing company (FSC). A fascinating concept in business history, FSCs are companies in the legal sense with headquarters located in one country while almost all operations are situated in another.[1]

[1] Mira Wilkins, the influential U.S. international business historian, first applied the label "free-standing company" in "The Free-Standing Company, 1870-1914: An Important Type of British Direct Foreign Investment," *Economic History Review*, 2nd ser., 41 (May 1988): 259-82. This prompted further study by a variety of historians, particularly Geoffrey Jones, Jean-François Hennart, Mark Casson, T. A. B. Corley, Stanley Chapman, Rory Miller, and Keetie E. Sluyterman. Others who looked at FSCs before Wilkins defined them as such include Clark C. Spence, *British Investments and the American Mining Frontier, 1860-1901* (New York, 1958); W. Turrentine Jackson, *The Enterprising Scot: Investors in the American West after 1873* (Edinburgh, 1968); and perhaps most influentially, Charles A. Jones, *Inter-*

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URL: http://www.thebhc.org/publications/BEHonline/2008/tennent.pdf.

Scotland was home to about four hundred such companies between 1862 and 1900.[2] Of these numerous firms, I focus on the structure of four FSCs for which a reasonable body of archival data remains, emphasizing the level of managerial control actually held in Scotland by the FSCs' home offices. Wilkins proposes that many FSCs failed because they did not develop a suitable system of management, particularly when the United States was the host nation.[3] I investigate the level of managerial control that the Scotland home offices had over operations in the host country and its role in the firms' fortunes.

Michael Porter has argued that the home country of a multinational is crucial to the development of its subsidiaries abroad, particularly in regard to the importance of conditions in the domestic market for a firm's products.[4] Firms developed their competitive advantage according to institutions or demand patterns at home, which forced them to become "world class" before extending that competitive advantage abroad on favorable terms. In the case of the FSC, a firm could not develop such a competitive advantage before it moved abroad. The firm instead had to adapt to the market and institutional conditions of the host country to develop its competitive advantage. This is easier for companies involved in extractive industries, where product development costs are lower. However, there remains the challenge of resource allocation, for which efficient managerial control is important.

We can consider managerial control in this case in the context of executive and organizational decisions made across distance, by those on the principal side rather than the agents. FSCs by nature have internal markets in information as well as finance, and I examine the frameworks used to control these internal markets. The four firms of interest are those highlighted in Table 1.

The Canterbury & Otago Association and the New Zealand & Australian Land Company

Figures 1-4 are organization charts for the four companies I examined in detail. They are as complete as possible and show the complexity of the organizations. Vertical relationships represent principals and agents, while

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national Business in the Nineteenth Century: The Rise and Fall of a Cosmopolitan Bourgeoisie (Brighton, U.K., 1987). In this case, we consider Empire countries such as Australia or New Zealand as separate from the United Kingdom.

[2] See the National Archives of Scotland's (NAS) BT2 series, which is the repository for company registrations made before 1985 at Companies House in Edinburgh. In this paper, we take "Scottish" to mean companies registered in Edinburgh, as those simply seeking a U.K. registration would most likely have registered in London.

[3] Wilkins, "The Free-Standing Company, 1870-1914," 275.

[4] Michael Porter, *The Competitive Advantage of Nations* (Basingstoke, U.K., 1990).

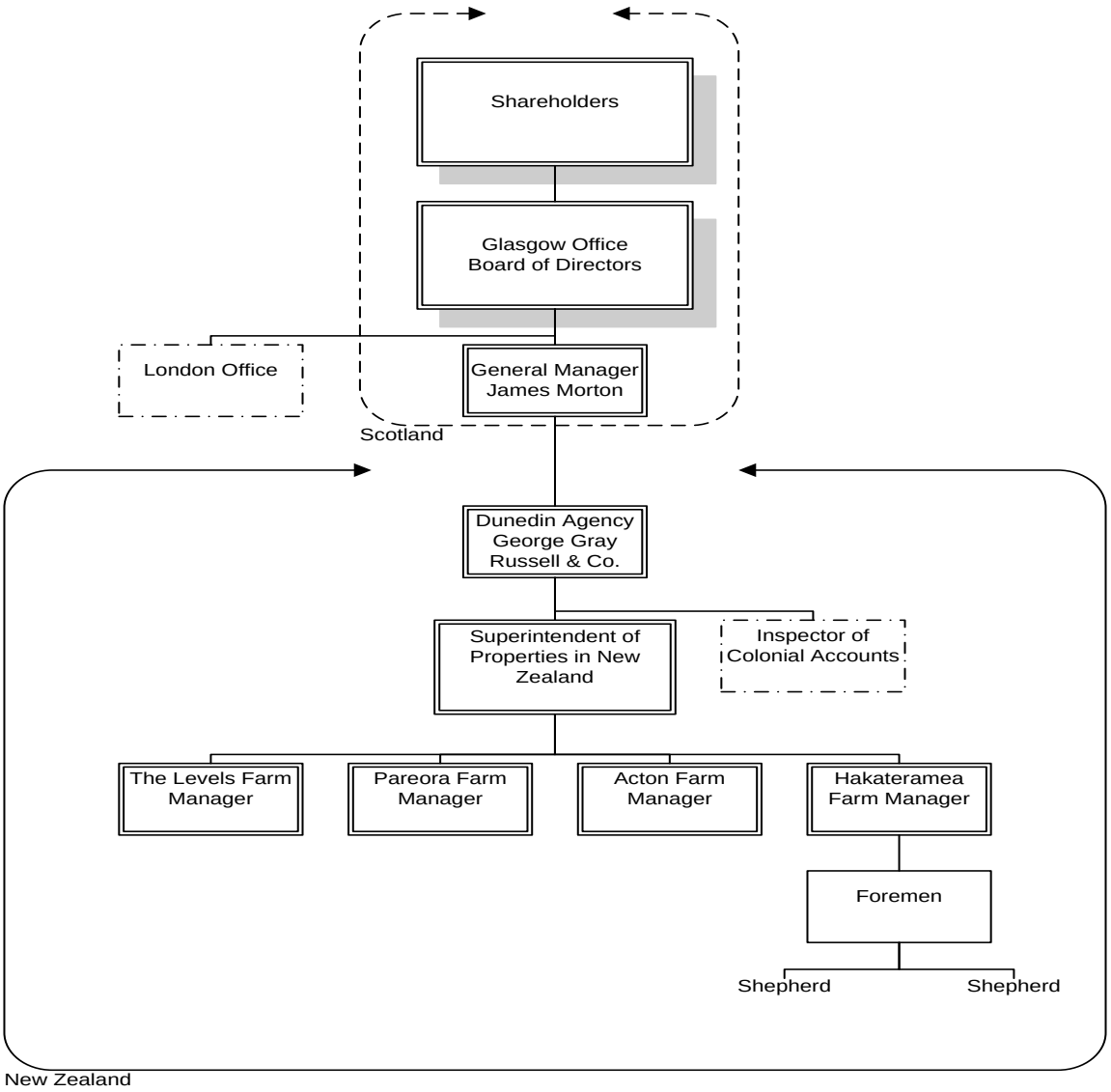
Table 1
The Top Ten Scottish FSCs, 1862-1886, by nominal capital

Rank	Name	Nominal Capital (£,000s)	Paid Capital (£,000s)	Year Registered	Lifetime	Industrial Classification	Host(s)
1	**New Zealand and Australian Land Company, Ltd.**	**2,000**	**1,500**	**1866**	**11**	**Ag Production-Livestock**	**NZ, Australia**
1	**New Zealand and Australian Land Company, Ltd. [2]**	**2,000**	**2,000**	**1877**	**91**	**Ag Production-Livestock**	**NZ, Australia**
3	La Platense Flotilla Company, Ltd.	1,000	519	1886	15	Water Transportation	Argentina, Uruguay
4	**California Redwood Company, Ltd.**	**900**	**468**	**1883**	**7**	**Forestry**	**USA**
5	**Arizona Copper Company, Ltd.**	**875**	**700**	**1882**	**10**	**Metal Mining**	**USA**
5	**Arizona Copper Company, Ltd. [2]**	**875**	**791**	**1884**	**35**	**Metal Mining**	**USA**
7	Carpio Copper and Sulphur Company, Ltd.	600	97	1872	9	Metal Mining	Spain
7	Canadian Copper Pyrites and Chemical Company, Ltd.	600	295	1872	8	Metal Mining	Canada
7	Swan Land and Cattle Company, Ltd.	600	600	1883	42	Ag Production-Livestock	USA
10	**Canterbury and Otago Association, Ltd.**	**500**	**500**	**1865**	**12**	**Ag Production-Livestock**	**NZ**
10	Irrawaddy Flotilla Co., Ltd.	500	400	1875	73	Water Transportation	Burmah
10	American Land and Colonisation Company of Scotland, Ltd.	500	59	1881	25	Real Estate	USA
10	Scottish American Accident Insurance Company, Ltd.	500	0	1881	0	Accident & Health Insurance	USA

Source and notes: Taken from the NAS series BT2 files for these companies; see BT2/197, 229, 415, 441, 637, 1022, 1025, 1144, 1225, 1261, 1375, and 1502. Companies that failed are included to give an indication of the sort of companies promoted. Nominal capital as of the company's initial registration; this may have been increased or decreased later. Paid capital is taken from the highest level of paid capital reported while the company remained with its initial level of nominal capital. Companies in bold are those discussed here.

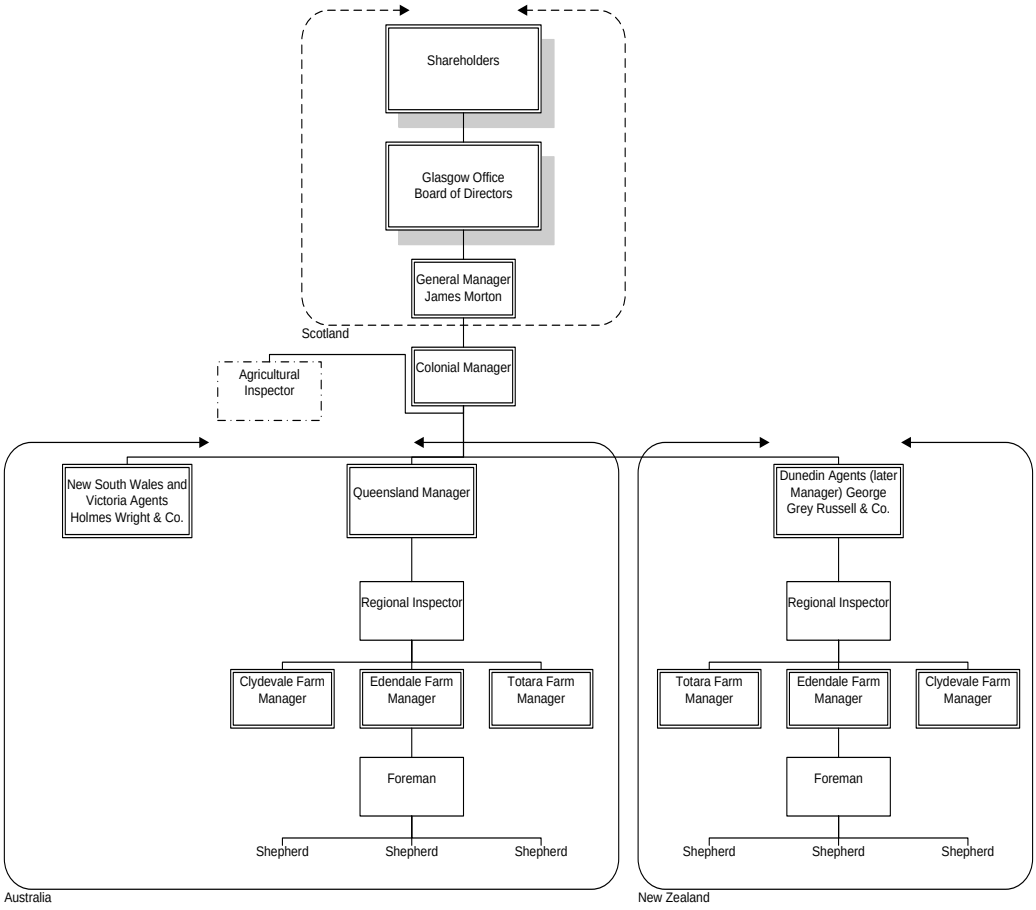
horizontal ones represent officials or organizational units with an advisory/ consultative or a representative role—for instance, the Canterbury & Otago's (C&O) London Office in Figure 1.

FIGURE 1
Canterbury & Otago Association Company Structure, 1866-1877



Source and Notes: I developed this chart mostly from the minutes of the C&O board meetings (which the general manager also attended); see NAS GD435/1 and 2. In addition, the autobiography of William Soltau Davidson, who was recruited in Scotland and spent the early part of his career with the C&O working in New Zealand, was invaluable in filling in the gaps; see William Soltau Davidson, *William Soltau Davidson, 1846-1924* (Edinburgh, 1930).

FIGURE 2
New Zealand and Australian Land Company Structure, 1866-1877



Source: I based this chart on the minutes of the board meetings of the NZ&A; see NAS GD435/7 and 8.

In both of these companies—Glasgow-based, but with their core business in sheep farming in New Zealand--a Scottish-based general manager made most key decisions with reference to the board. At the New Zealand & Australian Land Company (NZ&A) important investment decisions were theoretically supposed to be relayed by the Dunedin, Melbourne, or Brisbane agents back to the board for evaluation; these agents wrote to the board every month, sending an accounting summary and information about important developments. Using the information given, the board made decisions to send back to Australasia. Established very early in the company's development, cash control was not developed as strongly in this system as it might have been, with many decisions made by local managers before a reply giving

permission (taking a minimum of four months) was obtained.[5] The Dunedin, Melbourne, and Brisbane agents had a pivotal role in this, as they were responsible for the allocation of funds sent out to the colonies as share capital in the late 1860s. The company invested huge sums, first in purchasing properties and then in improving them. Although in late 1867 the NZ&A strategically decided to spend just £3,750 per month, this proved difficult to enforce; numerous stories of managerial extravagance surfaced.

The C&O was more fortunate in New Zealand, in that its runs were situated farther north in a more temperate location, better suited to the introduction of English grass for grazing; the NZ&A was less fortunate in its choice of colder land in southern South Island. Over a ten-year period, the C&O attained better results, while investing only 25 percent of the money per acre spent by the NZ&A.[6]

In addition to overseeing spending on this improvement process, the Head Office played an important procurement role in obtaining the resources used for improvement. The Head Office paid for machinery, grass seed, rams for breeding purposes, thoroughbred horses, and even oversaw the purchase of stoats and weasels to attempt to control the rabbit population in the colonies.[7] The Head Office also recruited career staff for all levels of the company in Scotland. The regional inspectors and supervisors mentioned in Figures 1 and 2 trained in a cadet system where they served time as shepherds; farm hands educated them about the workings of a sheep run.[8] As necessary, they recruited laborers from the local populace.[9]

There was also a role for the Head Office in marketing; in the early years both companies relied on wool exports and forged close links with London-based woolen merchants. Later in the 1880s, the Head Office organized a sales network in the London area to oversee the distribution of frozen meat when the company diversified into that market, the demand in the already densely populated London area for meat imports being much higher than in Scotland.[10] The Head Offices in both companies had numerous roles, and

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[5] We know it took this long because letters were frequently reproduced in the minute books along with the date they were sent from New Zealand/Australia, and sometimes even the route that the post took (via Brindlisi or San Francisco). See NAS GD435/1-7 (the copyright status of these books is uncertain; no infringement is intended).

[6] The C&O had managed to support 113,000 sheep on its 28,000-acre Levels estate in Canterbury province by 1878, while spending only £2 1s per acre; the NZ&A supported a similar number of sheep at Edendale in Southland province only after spending £8 2s per acre; see Davidson, *William Soltau Davidson, 1846-1924*, 93.

[7] Ibid., 48.

[8] Ibid. Davidson's description of his recruitment and early life as a farm hand in New Zealand provides the best account of a career with the C&O.

[9] Colin Williscroft, ed., *A Lasting Legacy—William Davidson 125* (Auckland, New Zealand, 2007), 29.

[10] See James Belich, *Paradise Reforged: A History of the New Zealanders from the 1880s to the Year 2000* (Honolulu, Hawaii, 2001), 85: "In 1907 80 per cent of the

there were economies in managing two similar companies. Both firms shared a common general manager in James Morton, and both companies used his office, with a small staff, for the Head Office and boardroom.[11] Although the 1878 merger of the two companies to form a larger NZ&A is not surprising, the two had a partly separate shareholder base and distinct structures and personnel in New Zealand prior to merger, particularly after the NZ&A replaced George Grey Russell & Co. with a more permanent Dunedin management staff. For these companies, then, Morton's joint Head Office played a vital role as it procured scarce resources inaccessible in the colonies for their activities and was not considered an unnecessary burden, as its role was essential to generating revenue, even if indirectly.

The California Redwood Company and the Arizona Copper Company

Figures 3 and 4 show the structures of the two U.S. FSCs studied here, the California Redwood Company (CRC) and the Arizona Copper Company (ACC). An Edinburgh syndicate (which already was heavily involved in cattle FSCs) formed the CRC in 1883, in response to a pitch by James D. Walker, who was seeking capital to exploit two large lumber estates in California.[12] The syndicate agreed to raise as much as £732,000 in cash and shares to purchase this property and made an outlay of at least another £200,000 in all on apparent improvements to both sawmills and railways.[13] The CRC did not last long, being wound up in 1885 amid allegations of illegal land grabbing.[14] In reality, however, the failure of the Edinburgh syndicate to establish an effective framework for management seems to have been more costly.

In Figure 3, it is clear that everyone below the Edinburgh office worked in California, and the office of the agents in San Francisco was some 200 miles distant from the company's main center of operations at Eureka, where David Evans was the U.S. general manager. Evans was responsible for both sites and associated activities, including shipping and the company's two railways.

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meat sold in London was imported, mostly frozen, while 80 per cent of the meat sold in Dundee was home-produced."

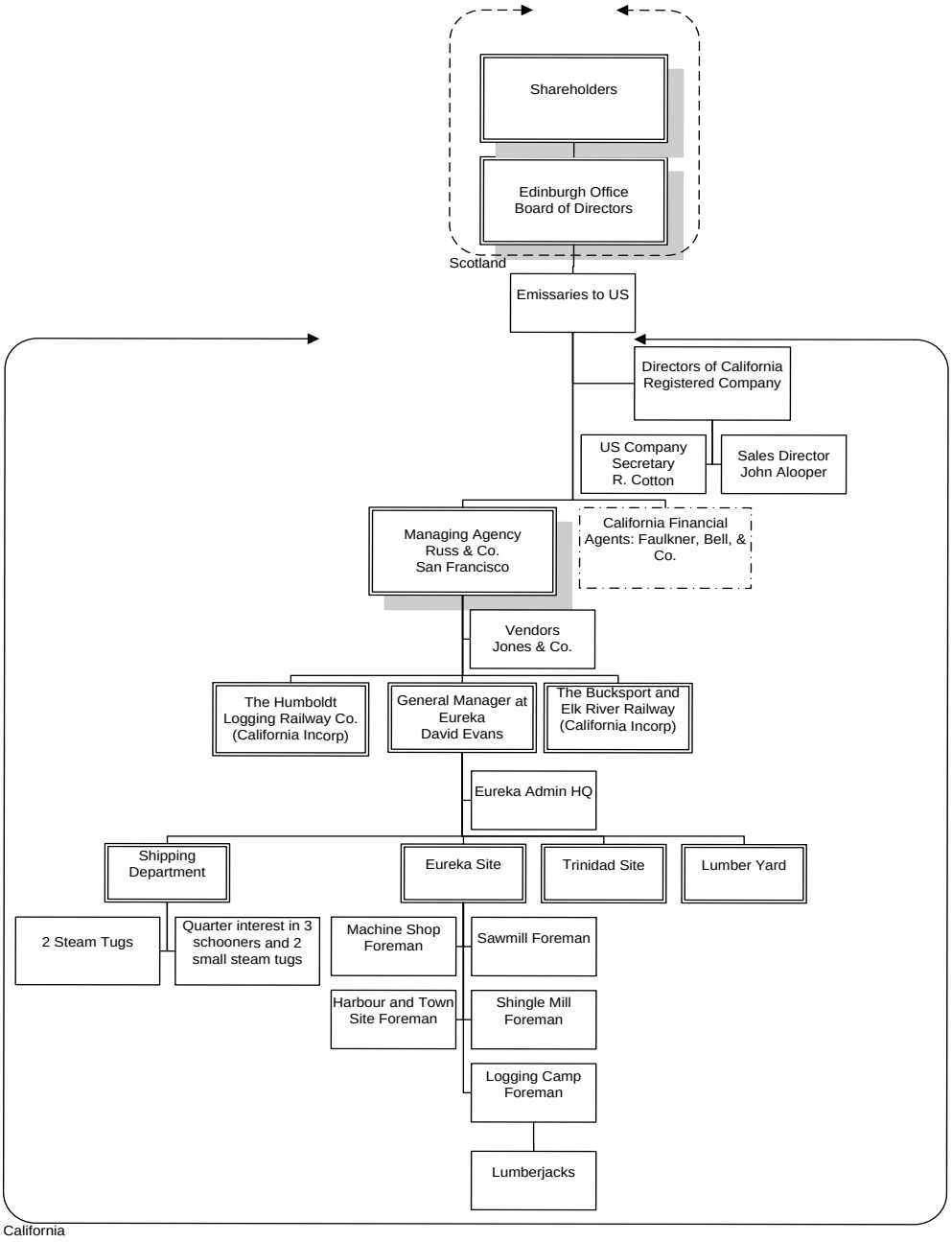
[11] See the minutes of both companies; NAS GD435/2, minute 30 April 1872, tells us that Morton's remuneration was set at £1,250 per annum, but that he was expected to pay his own office expenses such as staffing, rent, and utility costs.

[12] See minute of shareholder EGM, 28 April 1885, NAS GD282/13/142.

[13] Jackson, *The Enterprising Scot*, 222.

[14] NAS GD282/13/125 provides a good summary. Jackson blames this scandal for the CRC's failure, a view picked up by Wilkins in Mira Wilkins, *The History of Foreign Investment in the United States to 1914* (Cambridge, Mass., 1989), 234.

FIGURE 3
California Redwood Company Structure, 1883-1885



Source and Notes: I have extrapolated this from a collection of company documents held at NAS in GD282/13, particularly the reports and correspondence file GD282/13/123 and the scrapbook GD282/13/143. NAS GD282/13 is part of a larger collection under NAS GD282 from the Edinburgh law firm Messrs Davidson & Syme W.S., 1468-1977. Their successor, Dundas & Wilson CS LLP kindly granted access to the collection and permission to publish the information regarding the ACC and CRC in this essay.

Evans later became the target for allegations of extravagance and mismanagement from shareholders back in Scotland, with the San Francisco agents, Russ & Co., accused of not overseeing Evans's activities closely enough. Although the company apparently did have significant lumber resources at its disposal, it never produced the volumes of timber required to break even, and relations between the Scottish principals and Californian agents broke down within a year of the company's founding; the Scots, not seeing any returns, were reluctant to release more funds to California.[15]

The ACC (see Figure 4), formed in 1882, had similar origins as a pitched promotion, in this case by Frank Underwood of Kansas City, who also pitched several ranching schemes to Scottish investors.[16] This company had the highest nominal capital of any Scottish mining FSC at £875,000; it was second in the United Kingdom only to the infamous Emma Silver Mining Company of 1872.[17] Unlike the Emma Company, the ACC managed to survive in the long term, after the American Phelps Dodge Corporation bought it in 1921 for $50 million worth of Phelps Dodge stock.[18] It survived beyond 1884, however, only thanks to a re-registration that allowed a financial reconstruction. A trust company formed in Edinburgh alongside the ACC acted as an in-house financier.[19]

The ACC's early difficulty stemmed, as was often the case with mining FSCs, from the founders' initial failure to consider the cost of smelting the ore to extract the copper onsite and the need to invest further in rail transport to link the mine site with the rail network. As with the CRC, the ACC required investment to make the assets reflect the initial sale value. Further, the new owners had to remove the manager inherited from the previous owners, when an emissary sent from Edinburgh reported that he was overspending on improving the smelters and had lost the confidence of his mining captains.[20] After the removal of Underwood from his initial position as agent, a new managing board made up of the mining captains and railway manager reporting to the Edinburgh board ran the firm more directly. In the ACC's case, once the mines were well established, the close geographical proximity

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[15] See NAS GD282/13/143; a small booklet titled "The California Redwood Company Limited: Report Submitted to the Shareholders by Messrs Blyth and Menzies on Their Return from California" mentions that the hope had been to produce 50 million feet per annum of timber, but it was found that the sawmill capacity was not up to this level in reality; 10.

[16] See Jackson, *The Enterprising Scot*, chaps. 3 and 5, for a good summary of these companies' fortunes.

[17] For a good history of the Emma debacle, see Spence, *British Investments and the American Mining Frontier,* 139-90.

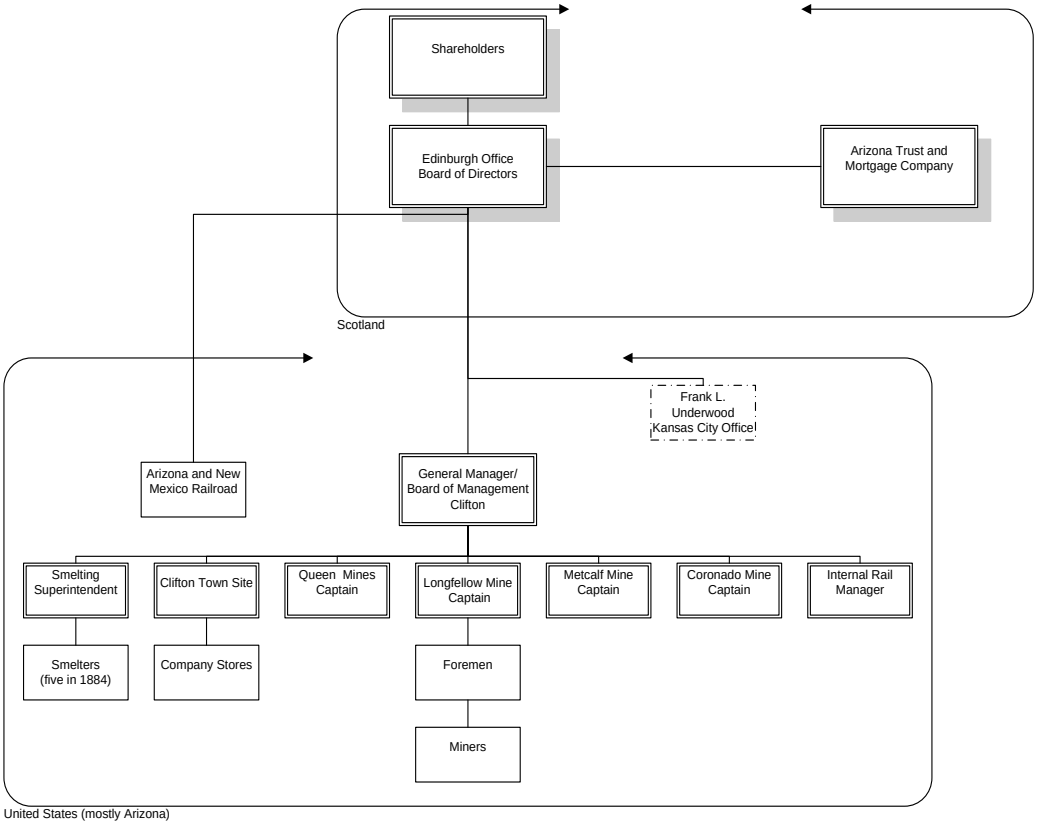
[18] Charles K. Hyde, *Copper for America: The United States Copper Industry from Colonial Times to the 1990s* (Tucson, Ariz., 1998).

[19] See the NAS file GD282/13/154 for various documents concerning the relationship between ACC and the Arizona Trust and Mortgage Company, Ltd.

[20] See NAS GD282/13, report from J. A. Robertson's trip to Arizona, June 1884.

to the company's administration center at Clifton Arizona simplified management.

FIGURE 4
Arizona Copper Company Structure, c. 1884



Source and Notes: I extrapolated this from an examination of a collection of documents on this company held at NAS in GD282/13; particularly of use in doing this was the report of Mr. Robertson's visit to the mines; see NAS GD282/13/154.

Conclusion

The experience of these four companies tells us that FSCs were difficult organizations to manage. Managing assets on a different continent (and in the cases of the C&O, NZ&A, and CRC, multiple sites) presented a considerable challenge to capitalists who had experience mostly with managing single-site businesses. The two Australasian firms, and, to a limited extent, the ACC, overcame these disadvantages by setting up clear monitoring procedures to prevent misallocated resources (a key element was monthly reporting from operational centers back to the Head Office) and to ensure that Scottish-based board members and management had information for decision making. The ACC relied on American smelting technology (it

purchased its hardware from firms based in San Francisco and Chicago).[23] The ACC did manage to recruit some Scottish personnel to send to Arizona; the C&O and NZ&A relied to a large degree on Scottish recruited personnel, raw material inputs, farming knowledge, and distribution networks back at home.[24]

As seen in Table 2, the NZ&A and C&O were more effective in internalizing the trade in information in both directions between their head offices and their operational bases. Although agency problems persisted, they both found an effective solution to run the necessary internal market in

TABLE 2
Casson's Four Types of Free-Standing Company

Does the FSC Internalize:	Technology	Not Technology
Information	A	B
Not Information	C	D

Sources and notes: I have devised the diagrammatic format, but the original idea comes from Mark Casson, "An Economic Theory of the Free-Standing Company," in *The Free-Standing Company in the World Economy, 1830-1996*, ed. Mira Wilkins and Harm Schröter (New York, 1998), 99-128.

Type A: NZ&A after 1877, importation of refrigeration and other technology to New Zealand. Arguably, also NZ&A pre-1877, due to grass and animal imports (terraforming).

Type B: C&O and pre-1877 NZ&A, which imported husbandry knowledge and specialized techniques to Australia and New Zealand.

Type C: None of these firms. This may most frequently apply in cases where a domestic company wants to protect a patent in the host country so sets up an FSC to reduce the risk.

Type D: CRC and ACC. Both companies appear to have been happy to rely on the assets that they purchased and received U.S. knowledge about their industries. This makes them more typical of the speculative style of FSC, which represented more of a portfolio investment, because home office control did not fully expand to the host country.

[23] Hyde, *Copper for America*, 118.

[24] James Colquhoun, the superintendent of smelting after 1884, (1857-1954), and later general manager after 1892, was Scottish. Mr Gibb, a Scotsman who had "large experience" of smelting in England and America, joined him; see J. A. Robertson's report, NAS GD282/13/154.

information flows from principal to agent and back again. Further, the head office had a vital role in capturing technological knowledge and exporting it to Australia and New Zealand without any external cost. In addition, via recruitment the principals were able to pick agents who were likely to be reliable. The Glasgow office also handled relations with wool dealers in London. After moving to Edinburgh in 1879, it would handle the marketing of frozen mutton and dairy products imported from New Zealand. Meanwhile, the ACC marketed its copper outputs mostly in the United States, and while the CRC did attempt to penetrate the home market by sending samples of redwood to trade shows, it never successfully produced enough redwood to sell in volume in the U.K. market.

The experience of these four companies suggests, therefore, that the level of control from the home office in FSCs matters in terms of their success in developing as businesses. Control did not successfully extend in all cases, and when it did not, FSCs were essentially vulnerable to schism into two firms with conflicting aims. Scottish control successfully extended across borders, but seems to have been more effective with a blank institutional canvas, as in Australia and New Zealand. In effect, the C&O and the NZ&A were able to treat Australasia as an extension of the home operating environment, despite being 10,000 miles away. The C&O and NZ&A were able to gain a competitive advantage, based on the knowledge communicated from agent to principal of agricultural conditions in both countries, and to use this to add value to their products for marketing back in Britain. The CRC and ACC were not successful in adding value to their products in this sense. The CRC relied on its U.S. agents for their knowledge of the timber industry, while the ACC relied entirely on U.S.-based mining engineers and chemists of uncertain background to exploit its copper reserves. The CRC and ACC, like many other extractive FSCs, failed to develop a strategy to engage their U.S. agents in exploiting the value creation opportunities open to them, and rapidly ran into financial difficulty as a result.