

CHAPTER 3

LAW AND THE ECONOMY: 1776-1850

LAISSEZ-FAIRE AND ITS LIMITS

By reputation, the nineteenth century was the high noon of *laissez-faire*. Government, by habit and design, supposedly kept its heavy hands off the economy. But when we actually burrow into the past, what we find is much more complicated. Yes, it is true that, for much of the century, opinion leaders and official policy strongly supported business, growth, and production. In particular, the first half of the century was a period of promotion of enterprise. Policy aimed—in Willard Hurst's phrase—at the release of creative energy, and that meant economic energy, enterprise energy. Government reflected what its constituents wanted. It did what it could to help the economy grow. Where this meant subsidy or intervention, theories and dogmas rarely held government back. This puts the case somewhat negatively. In fact, as William Novak has argued, people in the nineteenth century believed that government had a positive obligation to "further the welfare of the whole people and community."¹

If we talk about government intervention, or government regulation, in the first half of the nineteenth century, we are talking primarily about the states, not the federal government. We are so used to a big central government that we forget that the country was local, fragmented, disjointed, in 1800 or 1830. We forget that the federal government was tiny; we forget how little it actually did. Legal literature never has given the states their due. National events seemed so much more important than what happened in the towns and localities. Dramatic and striking events, acted out on a national stage—the growing storm over slavery and the slave trade; or the delicate relationship between state and federal governments; or the debates over tariff policy, a national banking system, and internal improvements—these captured the attention of most scholars. This left little room for a Vermont statute on the licensing of peddlers. But to draw an accurate picture of law and the economy, we have to look closely at what went on in states and counties and townships and towns.

The federal government was not totally passive. There was some pressure to build big works of internal improvement; this actually bore some fruit in the National Road. The federal effort was not frustrated by a *laissez-faire* philosophy.

¹ William N. Novak, *The People's Welfare: Law and Regulation in Nineteenth-Century America* (1996), p. 9.

the "real issue," rather, was "between national and state action."² Generally speaking, the states carried the day. The federal government owned no railroads and acts of Congress showed little awareness of railroads before the Civil War. But this did not mean that the effort to build railroads was essentially, as in England, private. There was feverish activity in the states. The Pennsylvania Railroad was once quite literally the railroad of the state of Pennsylvania. The state of Georgia built a railroad, too—the Western and Atlantic Railroad. Other states bought stock in railroads, or authorized local governments to do so. Some states gave tax breaks, or exemptions, to railroads.³ State governments, furthermore, turned to railroad building after years of intimate involvement with turnpikes, plank roads, ferries, and bridges.

In the first half of the century, to be sure, laws and doctrines did not, on the whole, try to regulate, meaning monitor and control. The thrust of the law was promotional. The aim was to stimulate and encourage. There were cycles of up and down. The depression of 1837 left states with debts and bad investments. This led to a reaction against direct investment in railroads. The Michigan Constitution of 1850 told the state it could not own stock in any corporation; and most northern states, by 1860, had something similar in their fundamental law.⁴

Public opinion strongly supported the general idea of building railroads and other public improvements. But routes, terms and conditions, and other details were the stuff of intense political battle. And canals, turnpikes, and railroads were often at battle with each other. In each state, pressure groups tried to gain advantages. Harry Scheiber studied the Ohio canal era; he found that strong political forces not only demanded state intervention to provide a general basis for economic growth, but demanded "equal distribution of costs and benefits among all members of the polity as well." This meant, in essence, giving every identifiable interest group (geographical ones included) its cut of the pie—its canal, railroad, turnpike, bank, bridge, patronage, county seat, or whatever.⁵ If there was a golden age of *laissez-faire* at all, in its pure, libertarian sense, it came later in the century; and even then, it was never clean and unadulterated. Government promoted and encouraged the building of the Western railroads, and there was a constant stream of state laws that affected the economy in one way or another.

In the first half of the century, *franchise* was a key legal concept. The franchise was a grant to the private sector, out of the inexhaustible reservoir of

² Carter Goodrich, *Government Promotion of American Canals and Railroads, 1800-1890* (1960), p. 44.

³ See, in general, James W. Ely Jr., *Railroads and American Law* (2001), ch. 1.

⁴ Ely, *op. cit.*, at 20.

⁵ Harry N. Scheiber, *Ohio Canal Era: A Case Study of Government and the Economy, 1820-1861* (1969). See also Scheiber's essay, "The Transportation Revolution and American Law: Constitutionalism and Public Policy," in *Transportation and the Early Nation* (1982), p. 1; on the general question of the relationship between law and the economy, the pioneer work of J. Willard Hurst is still a fundamental starting point, especially *Law and the Conditions of Freedom in the Nineteenth Century United States* (1956); *Law and Economic Growth: The Legal History of the Lumber Industry in Wisconsin, 1836-1915* (1964); and *Law and Markets in United States History: Different Modes of Bargaining among Interests* (1982).

state power. Historically, it meant a freedom, a release from restraint. But it also carried with it the flavor of monopoly. This meant that franchise and franchises were bound to be controversial, either in general, or in particular cases. Before 1850, there was more emphasis on how to unlock the door of enterprise than on whether enterprise should be given exclusive rights. It was not uncommon for railroad charters to confer monopoly status—New Jersey, for example, gave the Camden and Amboy railroad, in 1832, the sole franchise to haul people and goods across the state, between New York City and Philadelphia.⁶

There was a public right—indeed, a public duty—to help foster growth, production, and enterprise. This meant that government must provide public goods, especially transport, but also currency and credit. The monetary system was one of the irritants that led to Shays's Rebellion. This bitter struggle between debtors and creditors raged in the background at the very time that the men in Philadelphia were debating the Constitution of 1787. This background noise profoundly affected the debate. The Constitution itself clearly showed a "strong distrust of allowing state legislatures to set money-supply policy"; rather, control of the money supply had to be "a matter of national policy."⁷ Thus, the Constitution federalized the coinage of money; the states could not "emit Bills of Credit"; they could not "make any Thing but gold and silver Coin a Tender in Payment of Debts."⁸

Banking policy was always a subject of controversy. Early banks, in the 1780s for example, were really clubs of merchants—a kind of credit union for merchants.⁹ But they soon became important sources of notes—of currency, in short. Should the federal government play a role? Twice, the federal government chartered a national bank. President Andrew Jackson was the sworn enemy of the second bank; and he succeeded in killing it. Both before and after this event, there was far more banking activity in the states. The states tried to ensure sound money and credit by creating their own banks or by encouraging private banking.¹⁰ Pennsylvania owned one-third of the capital of the Bank of Pennsylvania, chartered in 1793. The Bank of the State of South Carolina, chartered in 1812, acted as the state's depository and fiscal agent; it was in effect the banking arm of the state itself.¹¹ Later on, it was not so common for states to own an outright share of banks. Instead, they enacted programs of regulation, which on paper were often quite heavy. In either case, the banks, public and private, were deeply enmeshed in politics. The currency and credit problem seemed central to the life of the community. An unsound bank—and there were many of these—threatened its community with financial ruin.

⁶ Ely, *op. cit.*, pp. 11–12.

⁷ J. Willard Hurst, *A Legal History of Money in the United States, 1774–1970* (1973), p. 8.

⁸ U.S. Const., art. I, sec. 10.

⁹ Joseph H. Sommer, "The Birth of the American Business Corporation: Of Banks, Corporate Governance, and Social Responsibility," 49 *Buffalo Law Review* 1011 (2001).

¹⁰ The subject is exhaustively treated in Bray Hammond, *Banks and Politics in America, from the Revolution to the Civil War* (1957); see also J. Willard Hurst, *A Legal History of Money in the United States, 1774–1970* (1973). There is interesting material on bank litigation in Alfred S. Konefsky and Andrew J. King, eds., *The Papers of Daniel Webster: Legal Papers*, vol. 2, *The Boston Practice* (1983), pp. 527–37.

¹¹ Hammond, *op. cit.* p. 168.

States chartered their banks one by one. The chartering process was therefore a rite de passage in the life of every bank; at this crucial point, the state could (in theory) exert critical control over the bank, simply by inserting clauses into the charter. There was a good deal of variation in bank charters; and many of them had provisions designed to tie the hands of the bank in this or that way. For example, a Vermont law of 1833 chartering a bank to be known as The Farmer's Bank, limited interest on loans to 6 percent, required every director to post bond with the state treasurer, and kept for the state of Vermont the option of acquiring 10 percent of the shares.¹²

In practice, the special charter system was not a convenient or effective way to control the behavior of banks. The states began instead to adopt general banking laws—laws that would apply to any and every bank. In 1829, New York passed a safety fund law. Under this law, banks had to contribute a portion of their capital to a general fund, to insure payment of the notes of insolvent banks.¹³ In 1837, Michigan passed the first free banking law. This dispensed with the need for a special charter. Any group of incorporators could start up a bank, so long as they followed the statutory formula. New York passed a similar law in 1838.¹⁴

The banks of New England were, in the period before the Civil War, typically small and closely held. Their customers were local people. In fact, they did a great deal of their business with "insiders," that is, their own directors and stockholders, and their families. A new group of insiders would form its own bank, to give themselves a supply of credit. By 1860, there were 91 banks in little Rhode Island; there were 178 in Massachusetts. Other states followed different patterns. There were branch banks in Pennsylvania and Virginia. In some states, there was more direct government involvement: the Bank of the State of South Carolina was wholly owned by the state, and lent money to planters and farmers, who felt they could not get credit from the other banks. Tennessee and Illinois also chartered banks.¹⁵ Meanwhile, the "free banking" law made a difference, ultimately, in the nature of banking. By 1860, eighteen states had free banking laws; and a few others had variants of the law. As we shall see, corporation law went through the same cycle of development, from special charter to general laws: from narrow, one-at-a-time acts of the legislature, to a general business form, open to all budding entrepreneurs.

Transport, like money, was part of the economic infrastructure, the skeletal frame of economic life. The federal government was clearly not going to play a big role. So the states and cities moved into the vacuum. After 1820, a tremendous amount of statutory law dealt with bridges, roads, ferries, and canals. Much of the work of the legislatures, in the first half of the nineteenth century,

¹² Acts of Vt., 1833, ch. 34, pp. 60–67.

¹³ Ronald E. Seavoy, *The Origins of the American Business Corporation, 1784–1855* (1982), pp. 117–48.

¹⁴ For a study of one such bank, see Howard Bodenhorn, "Free Banking and Financial Entrepreneurship in Nineteenth Century New York: The Black River Bank of Watertown," 27 *Business and Economic History* 102 (1998). See also J. T. W. Hubbard, *For Each, the Strength of All: A History of Banking in the State of New York* (1995), pp. 94–96.

¹⁵ Howard Bodenhorn, *A History of Banking in Antebellum America: Financial Markets and Economic Development in an Era of Nation-Building* (2000), pp. 31–44.

consisted of chartering transport companies, and amending these charters. Taking the Maryland laws of 1835-1836 as an example, we find in the first pages an amendment to "an act for building a bridge over the Little North-East, in Cecil County, near McCauley's mill" (ch. 23), three more bridge laws, and an amendment to "the act incorporating the Annapolis and Potomac Canal Company" (ch. 37), all in January 1836; many other laws in the same session incorporated or amended the charters of road or turnpike companies, or authorized road building, for example, "An Act to lay out and open a road through a part of Frederick and Baltimore Counties," which was passed March 2, 1836 (ch. 121). Chartering, however, was only one of the ways in which the government played a role in stimulating transport, as we have already noted. The states and cities supported internal improvements with money, credits, and favorable laws. They did some of the building work themselves. New York dug the great Erie Canal between 1817 and 1825—363 miles long—at a cost of a little more than \$7 million. It was a tremendous financial success. The tolls surpassed all expectations. Even more important, the canal stimulated commerce and served as a "great channel of westward migration." Its opening "may be regarded as the most decisive single event in the history of American transportation."¹⁶ The success of the Erie Canal invited emulation. In the peak year of 1840, an estimated \$14.19 million was invested in canals in the United States.¹⁷

By this time, the railroad was already moving toward the center of the stage. The full flowering of the railroad era came later. But both the Pennsylvania Railroad and the Baltimore and Ohio (B&O) were founded in this period; and both were supported if not controlled by government. The city of Baltimore supplied the money for the B&O. Other states chose one or the other path of support for their railroads during the early, flush period of enthusiasm. In 1837, Ohio passed a general law—the "Loan Law"—promising support in the form of matching funds, to any internal improvement company (railroad, canal, or turnpike) that met certain standards. The law was repealed in 1842; but more than a hundred special laws, between 1836 and 1850, authorized local aid to the promoters of railroads.¹⁸

The states granted charters; sometimes they contributed money. They also used their lawmaking power to make rules and give instructions to legal institutions, in ways that would help the entrepreneur. For example, the state had the power of eminent domain (the power to seize property for public use). If it did so, the state had to pay fair value for any property it took. This requirement of "just compensation" was written into federal and state constitutions. More often than not, in the first half of the nineteenth century, it was not the state itself that used the power. Rather, the power was rather freely lent to private businesses that served "public" purposes—canal or turnpike companies, very notably. The companies could then take what land they chose. This was itself a

kind of subsidy, but there was more. Judicial doctrine tilted very substantially toward the companies, and not the landowners. In many places, for example, the doctrine of "offsetting" values was in effect. This meant that if a canal company took my land, worth \$5,000, it did not necessarily have to pay me \$5,000. It was entitled to take account of the benefits I would get from the canal. If the canal would raise the value of the rest of my land by \$3,000, this could be subtracted from my compensation. The result was "no doubt a very large involuntary private subsidy" for public undertakings.¹⁹

On the surface, such policies favored business, especially transport business, and disfavored the ordinary farmer and landowner, the backbone of the country. But this is somewhat misleading. These policies were, no doubt, genuinely popular. A few unlucky people suffered; but the great bulk of farmer-settlers had a desperate hunger for transport: bridges, ferries, canals, turnpikes, and later, railroads. They needed these things to carry their goods to market, to bring settlers to their region, to stimulate business, to raise the overall value of their lands. In general, the subsidies were welcomed, and so was the orgy of bond-floating and shaky investment, which the states and cities indulged in like drunken sailors. The national hangover came somewhat later.

Outside of transport and finance, state regulation was rather random and planless. Not that a massive ideology dictated limits. The country was underdeveloped; most Americans no doubt felt that the state should encourage development, though perhaps they also felt that the state, like the Lord, helped those who helped themselves. Economic law was practical and promotional. Trade laws were tailored to specific needs. The states continued colonial programs of quality control over export commodities. Georgia law (1791) required tobacco to be "packed in hogsheads or casks" and "stamped by some inspector legally thereunto appointed";²⁰ unstamped tobacco could not be legally exported. In Connecticut, by a law of 1794, bar iron could not be sold unless "stamped with the name of the manufacturer thereof, and of the town where such iron is manufactured."²¹ In New York, salt was to be packed "in barrels, casks or boxes" and inspected to make sure that the salt was "free from dirt, filth and stones, and from admixtures of lime . . . and fully drained from pickle."²² The New York revised statutes of 1827-1828 included laws to regulate sales by auctioneers, hawkers and peddlers, and provisions for the inspection of flour, meal, beef, pork, "pot and pearl ashes," fish, "fish or liver oil," lumber, staves, flaxseed, sole leather, leaf tobacco, butter, and pressed hay. Not all of these were export commodities. Some were merely staple goods.

It was an established task of government to regulate weights and measures and to provide standard measures for commodities. Massachusetts, for example, prescribed standard measures by statute for potatoes, onions, salt, and

¹⁶ Carter Goodrich, *Government Promotion of American Canals and Railroads, 1800-1890*, pp. 52-55.

¹⁷ Carter Goodrich et al., *Canals and American Economic Development* (1961), p. 209; see also the excellent study by Harry N. Scheiber, *Ohio Canal Era: A Case Study of Government and the Economy, 1820-1861* (1969).

¹⁸ Carter Goodrich, *Government Promotion of American Canals and Railroads*, pp. 136-37; Harry Scheiber, *Ohio Canal Era*, pp. 110-11, 152.

¹⁹ Harry N. Scheiber, "The Road to *Munn*: Eminent Domain and the Concept of Public Purpose in the State Courts," in Donald Fleming and Bernard Bailyn, eds., *Law in American History* (1971), pp. 329, 364. On eminent domain in this period, see also Tony A. Freyer, *Producers versus Capitalists: Constitutional Conflict in Antebellum America* (1994), ch. 4.

²⁰ Oliver H. Prince, comp., *Digest of the Laws of the State of Georgia* (2nd ed., 1837), p. 817 (act of Dec. 23, 1791).

²¹ Stats. Conn. 1808, pp. 421-22 (act of May, 1794).

²² Rev. Stats. N.Y. 1829, vol. I, p. 270.

wood. There were also state laws that aimed at protecting consumers against false labeling and adulteration. In Massachusetts (1833), only "pure spermaceti oil"²³ could be "sold under the names of sperm, spermaceti, lamp, summer, fall, winter and second winter oils." A seller who sold "adulterated" oils under one of these names had to pay double the difference between the value of pure and adulterated oil. No statutory machinery was set up to enforce this law. Perhaps it was hoped that the crude penalties would be enough of an incentive for aggrieved merchants or consumers to enforce the law on their own.

The age of conservation was a long way off; nonetheless, there were some small moves to protect natural resources. Massachusetts in 1819 made it unlawful to take pickerel "with spears, in the night time," or to shoot these fish "at any time." This act attached a money penalty of fifty cents per unlawful fish, payable "to and for the use of the person who shall sue for the same."²⁴ The usual motive for such laws was economic, not the love of Mother Nature. Massachusetts (1818) prohibited indiscriminate killing of birds that were "useful and profitable to the citizens, either as articles of food or as instruments in the hands of Providence to destroy various noxious insects, grubs, and caterpillars."²⁵ New Jersey, in 1789, restricted the picking of cranberries between June 1 and October 10, because "cranberries, if suffered to remain on the vines until sufficiently ripened, would be a valuable article of exportation."²⁶ By a protectionist act of 1822, Massachusetts forbade nonresidents to "take any lobsters, tautog, bass or other fish, within the harbors, streams, or waters of the towns of Fairhaven, New Bedford, Dartmouth, and Westport," and transport the catch "in smacks or vessels" of over fifteen tons, or in those of any size owned outside the Commonwealth.²⁷

Public health was also a matter of some state concern, though the tools were primitive and the scope of regulation rather narrow. Quarantine laws were common, however. New York had an elaborate law in the 1820s directing ships to anchor near "the marine hospital on Staten-Island," dividing ships into classes depending on the perceived danger, and prescribing rules for clearing quarantine, including whitewashing and fumigation "with mineral acid gas" and the washing and airing of clothing and bedding. The rules were especially strict for ships coming from places where "yellow, bilious, malignant, or other pestilential or infectious fever" had existed, or if disease had broken out on board the ship.²⁸ State laws allowed "nuisances" to be "abated" when they were a danger to health. Land-use controls were in their infancy; but Michigan, for example, in the 1830s, authorized township boards, village governments, and the mayors and aldermen of cities to "assign certain places for the exercising of any trade or employment offensive to the inhabitants, or dangerous to the public health." Any such "assignment" could be revoked if the place or building became a "nuisance" because of "offensive smells or exhalations," or was

²³ Laws Mass. 1833, ch. 215.

²⁴ Laws Mass. 1819, ch. 45. A later act subjected the operation of this law to local option.

²⁵ Laws Mass. 1818, ch. 103.

²⁶ Rev. Stats. N.J. 1821, p. 89 (act of Nov. 10, 1789).

²⁷ Laws Mass. 1822, ch. 97.

²⁸ Rev. Stats. N.Y. 1829, vol. I, pp. 425ff. On quarantine laws, see William Novak, *The People's Welfare*, pp. 204-17.

"otherwise hurtful or dangerous."²⁹ Fire was a constant threat to cities; hence, New York City, by 1813, had rather elaborate regulations to prevent and handle fires: bans on fireworks or the shooting of guns in the city, for example; and the mayor had the power, if two aldermen agreed, to destroy buildings when necessary, to prevent a fire from spreading.³⁰

When food products were regulated, the primary goals were usually economic; but sometimes public health or the protection of consumers was at least a secondary goal.³¹ Some states gave local medical societies the power to examine and license prospective doctors. Unlicensed doctors were not allowed to collect fees through regular court process. Other laws made unauthorized practice subject to fines.³² Lastly, laws on gaming, drinking, and gambling aimed to protect public morality. In New York, no "puppet-show . . . wire or rope-dance, or . . . other idle shows" could be exhibited for profit.³³ These regulations of morality were also, in a way, economic; they defined the permissible limits of earning a living. In a way, too, much of the penal code aimed to protect property and the economy—laws against theft, to take the simplest example.

Novak's point about the nature of nineteenth-century government, and its commitment to public welfare, is thus a good one, as these examples show. But we have to remember that nineteenth-century government was certainly in no way a leviathan. Even the bigger states had only a weak hold over the economy. Some programs probably existed only on paper. Many inspection laws, licensing laws, and laws about weights and measures were probably weakly enforced. Two pillars of the modern state were missing: a strong tax base and a trained civil service. Without these, the state could do only so much to master and control. State government depended chiefly on the property tax. This tax was locally assessed and locally collected. It was supplemented by excise taxes—on slaves, on carriages, or on personal property in general. Hard money was scarce, and the voting public was not used to the idea of handing over to the state any appreciable part of their income or wealth. John Marshall, in one of his most famous lines, said that the power to tax was the power to destroy.³⁴ Power to destroy was not given away lightly in the nineteenth century.³⁵ Taxing and spending were, by the standards of later times, laughably small. The state of Massachusetts

²⁹ Rev. Stats. Michigan 1838, p. 171.

³⁰ William Novak, *The People's Welfare*, p. 57.

³¹ Oscar and Mary Handlin, *Commonwealth: A Study of the Role of Government in the American Economy: Massachusetts, 1744-1861* (rev. ed., 1969), p. 206.

³² Laws N.Y. 1806, ch. 138; Laws Mass. 1819, ch. 113; Laws N.Y. 1830, ch. 126; unauthorized doctors were liable to forfeit "a sum not exceeding twenty-five dollars." See, in general, Richard H. Shryock, *Medical Licensing in America, 1650-1965* (1967).

³³ Rev. Stats. N.Y. 1829, vol. 1, p. 660.

³⁴ The case was *McCulloch v. Maryland*, Wheat. 316 (1819).

³⁵ There was some concern about fairness in tax policy. A clause in the Arkansas Constitution of 1836 declared that "no one species of property . . . shall be taxed higher than another species of property, of equal value," excepting taxes on "merchants, hawkers, peddlers, and privileges" (art. VII, Revenue, sec. 2). Citing this clause, the state supreme court declared void a special tax on billiard tables, and a tax on "the privilege of keeping each stallion or jack." The right to own a billiard table or to keep a stallion was a "property right" not a "privilege"; it was unlawful, therefore, to tax these rights specially. *Stevens v. State*, 2 Ark. 291 (1840); *Gibson v. County of Pulaski*, 2 Ark. 309 (1840).

spent \$215,200, all told, in 1794. More than half of this was interest on debt.³⁶ Dollars went a lot further in those days; still, the puniest sewer district today could better that mark.

State action, then, was pinched for pennies. It had to find substitutes for the tax dollars it simply did not have. Hence there was heavy use of the fee system. Wherever possible, the costs of state services were shifted to users. Litigants paid judges for their lawsuits; brides and grooms paid for their marriage licenses. Local users had to pay assessments for local roads; if they were cash-poor themselves, they could pay off this tax in labor or sweat. In Mississippi, under a law of 1831, free adult males who paid less than six dollars of taxes a year had to "perform not exceeding four days labour on the roads in each year," along with "all free persons of colour, male and female, over eighteen and under forty-five years of age." Under some conditions, a man could substitute by providing horses, oxen, and plows.³⁷ Under a Virginia act of 1818, staves could not be exported before an inspector general and "cullers" had inspected them. The inspector general was "entitled to demand and receive" a fee of ten cents "on every thousand merchantable staves"; cullers too had to be paid their fee.³⁸ An elaborate Pennsylvania act of 1835 set up a similar system for meat. For "inspecting, examining and branding each tierce, barrel and half barrel of salted beef or pork," the inspectors could demand eight cents.³⁹

There was no trained civil service in the modern sense. Government was not run by experts, even experts in running a government. Politics was a way to make money or use power. It was sometimes an occupation, less frequently a calling. Many politicians were amateurs, or lawyers who were amateurs except at law. That every man could aspire to high office was part of the democratic faith; as we saw, the principle of rotation was written into some of the early constitutions. Men like Jefferson and Jackson considered high turnover a positive virtue in government. Jackson, especially, felt that government jobs called for basic, fungible skills; any man of intelligence and honor could hold office. In fact, Jefferson and Jackson tended to appoint men of elite background and standing to higher offices, despite their egalitarian ideologies—men who were not experts, but were skilled, and educated. If there was any lack of trained men in government, the lawyers filled the gap. Lawyers had some education, some grasp of the machinery of government, some insight into state ways.⁴⁰

In general, then, administration was weak and limited. Regulation tended to be local, self-sustaining—as in the fee system—and conservative in the use of staff. Often administrative jobs went to existing officeholders. If, for example, a state set up an insurance commission, it might appoint the state treasurer commissioner. Laws often required private citizens to stamp, mark, label, or post, to make for easier oversight. Every ferry keeper in Illinois had to maintain "a post or board, on which shall be written the rates of ferriage . . . by law allowed."⁴¹ Private citizens usually had to enforce what regulation there was. If

no one brought a lawsuit, or complained to the district attorney about some violation, nothing was done.

Some types of social control, which worked better in tight, narrow, sea-bound colonies, were strained to the breaking point in a huge, sprawling country, with a scattered population. In the Western states and territories, there were laws, borrowed from the East, that mentioned public markets and commodity inspection. Probably these were dead words on paper. Weak government, in general, opened a door to the private sector. Traditionally, money and credit were public functions; and the state built and ran highways, ferries, bridges, and canals. In the nineteenth century, farmers and merchants had a great hunger for these improvements. They wanted infrastructure. At a critical point, the state could not meet the demand; and the market took over. *Laissez-faire*, it may turn out, was more powerful as practice than as theory, even in the nineteenth century.

THE BUSINESS CORPORATION

A corporation, in the jargon of law books, is an artificial person. This means that it is a legal entity, which, like a person, can sue and be sued, own property, and transact business. Unlike natural persons, the corporation can dream of immortality. Officers and shareholders die, but the corporation lives on. The life of a corporation begins with a charter; and it ends if and when the charter runs out or is done away with. But the charter can provide for perpetual life; and this, in fact, is the normal case for corporations of the twentieth and twenty-first centuries.

The charter is a grant of authority from the sovereign. It specifies the powers, rights, and duties of the corporation. In an American state in the beginning of the twenty-first century, anybody who fills out a simple form and pays a small fee can get articles of incorporation and embark on corporate life. In the early nineteenth century, however, charters were statutes. They were doled out one by one. Every charter was in theory tailor-made to the case at hand.

In the colonial period, this was a perfectly appropriate system. Corporations were uncommon before 1800. And few of these were business corporations. Almost all of the colonial corporations were churches, charities, or cities or boroughs.⁴² New York City was a chartered corporation.⁴³ In all of the eighteenth century, charters were issued to only 335 businesses. There were only seven in

⁴² In England, only the crown had the right to incorporate. In the colonies, royal governors, proprietors, and in some cases legislative bodies issued charters. Actually, not many colonial cities and towns were technically corporations at all. It did not seem to make much difference in the way these municipalities behaved. In 1778, Governor Livingston of New Jersey tried to issue a charter himself without legislative approval, but that was an isolated incident. It was generally recognized after the Revolution that the legislature was the branch of government that made corporations. John W. Cadman Jr., *The Corporation in New Jersey: Business and Politics, 1791–1875* (1949), p. 4.

On the colonial corporation in general, see Joseph S. Davis, *Essays in the Earlier History of American Corporations* (1917).

⁴³ See, in general, Hendrik Hartog, *Public Property and Private Power: The Corporation of the City of New York in American Law, 1730–1870* (1983).

³⁶ Handlin and Handlin, *op. cit.*, p. 62.

³⁷ Laws Miss. 1831, p. 364 (act of December 16, 1831).

³⁸ Va. Rev. Code 1819, vol. II, pp. 197, 200.

³⁹ Laws Pa. 1834–35, sec. 82, p. 405.

⁴⁰ See, in general, Sidney H. Aronson, *Status and Kinship in the Higher Civil Service* (1964).

⁴¹ Francis S. Philbrick, ed., *Pope's Ill. Digest, 1815*, vol. 1 (1938), p. 264.

the whole colonial period; another 181 were granted between 1796 and 1800.⁴⁴ Banks, insurance companies, water companies, and companies organized to build or run canals, turnpikes, and bridges made up the overwhelming majority of these early corporations. A mere handful, notably the New Jersey Society for Establishing Useful Manufactures (1791), were established for manufacturing purposes.

In the nineteenth century, the situation began to change. In the first place, more and more charters were issued each year. Most charters, in the first half of the century, were still connected with finance and transport. A small but growing minority had more general commercial or industrial purposes. In Pennsylvania, 2,333 special charters were granted to business corporations between 1790 and 1860. Of these about 1,500 were transportation companies; less than two hundred were for manufacturing.⁴⁵ Joseph S. Davis has pointed out that:

The English tradition that corporate powers were to be granted only in rare instances, never deeply entrenched here, was opposed by a strong and growing prejudice in favor of equality—a prejudice which led almost at once to the enactment of general incorporation acts for ecclesiastical, educational, and literary corporations. Partiality in according such powers was to be expected of the English crown, but it was a serious charge to lay at the door of democratic legislatures. . . . Not least important, the physical ease of securing charters was far greater in the new states than in England. . . . Legislatures were not overworked and did business free of charge and with reasonable promptness. . . . Finally, the practice in creating corporations for non-business purposes, though it did not lead promptly to granting freedom of incorporation to business corporations, undoubtedly smoothed the way for special acts incorporating business associations.⁴⁶

Until about the middle of the century, the corporation was by no means the dominant form of business organization. Most commercial enterprises were partnerships. They consisted of two or three partners, often related by blood or marriage. The partnership was "used by all types of business, from the small country storekeepers to the great merchant bankers."⁴⁷ But as the economy developed, entrepreneurs made more and more use of the corporation, especially for transport ventures. The corporate form was a more efficient way to structure and finance their ventures. The special charter system, though, was clumsy and cumbersome. It was a waste of the legislature's time as well—or would have been, if in fact the legislature scrutinized each charter, and cut its clauses to order for the particular case. In fact, except for projects of special importance, charters became stylized, standardized, matters of rote. They were finally replaced, as we shall see, by general incorporation laws.⁴⁸

⁴⁴ Joseph S. Davis, *Essays in the Earlier History of American Corporations*, vol. II (1917), p. 24.

⁴⁵ Louis Hartz, *Economic Policy and Democratic Thought: Pennsylvania, 1776–1860* (1948), p. 38.

⁴⁶ Davis, *op. cit.*, vol. II, pp. 7–8.

⁴⁷ Alfred D. Chandler Jr., *The Visible Hand: The Managerial Revolution in American Business* (1977), pp. 36–37.

⁴⁸ The movement from special charter to general incorporation laws in New York is treated in Ronald E. Seavoy, *The Origins of the American Business Corporation, 1784–1855* (1982).

Early charters had many features that, from the standpoint of the corporation law of recent times, appear odd or idiosyncratic. Eternal life was not the rule. In the early nineteenth century, charter terms of five, twenty, or thirty years' duration were quite common. In New Jersey, every manufacturing company (except one) had a limited term of life before 1823; perpetual duration remained rare before the Civil War.⁴⁹ In Maryland, a general law of 1839 limited corporate life (for mining or manufacturing companies) to a maximum of thirty years.⁵⁰ Early charters also often departed from the principle of one vote for each share of stock. It was not the rule in Maryland, for example, until after 1819. In New Hampshire, under the charter of the Souhegan Nail and Cotton Factory (1812), each of the fifty shares of capital stock was entitled to a vote, but no member was entitled to more than ten votes, no matter how many shares he owned.⁵¹ The 1836 charter of a Maryland company, incorporated to build a turnpike from Hagerstown to the Pennsylvania border, allocated votes as follows: "for every share . . . not exceeding three, one vote each; for any number of shares greater than three and not exceeding ten, five votes; for any number of shares greater than ten, and not exceeding fifty, seven votes; for any number of shares greater than fifty, and not exceeding one hundred, ten votes; and for every additional hundred shares above one hundred, ten votes"; thirty votes was the maximum for any shareholder.⁵² Some charters restricted the number of shares any individual might hold in any one corporation. In Pennsylvania, after 1810, bank charters usually prohibited the transfer of bank stock to "foreigners."⁵³ In 1822, a bank charter in New Jersey required the new corporation to use some of its capital to aid the fisheries at Amboy.⁵⁴ Limited liability is the doctrine that shareholders are liable for corporate debts only up to the value of their shares, but nothing more; once their investment is wiped out, they cannot be made to pay for corporate debts. Limited liability is now considered one of the main reasons to choose the corporate form, and it is one of the basic features of corporation law. Limited liability had been part of English law, but in the United States, there was a reaction against it, in the early years of the century. Bank stock did not possess this great boon in New York, for example. In Connecticut, limited liability was common for manufacturing companies before the 1830s; but in some charters—for example, that of the Mystic Manufacturing Company of 1814—the stockholders were to be "responsible in their private capacity," if the corporation became insolvent. Massachusetts's law briefly provided for unlimited liability. But limited liability, by the 1830s or so, was clearly dominant.⁵⁵

The main line of development in corporation law seems fairly clear. Variations were leveled out, and the practice moved in the direction of a kind of common law of corporations; business custom and the needs of entrepreneurs fixed its basic contours. Between 1800 and 1850, the essential nature of the corporation changed. The corporation was, originally, a kind of monopoly. It

⁴⁹ John W. Cadman, *The Corporation in New Jersey, 1791–1875* (1949), p. 366.

⁵⁰ Joseph G. Blandi, *Maryland Business Corporations, 1783–1852* (1934), p. 56.

⁵¹ Laws N.H., vol. 8, 1811–20 (1920), p. 149.

⁵² Laws Md. 1835–36, ch. 321, sec. 4.

⁵³ Hartz, *op. cit.*, p. 255.

⁵⁴ Cadman, *op. cit.*, p. 68.

⁵⁵ *Resolves and Private Laws, Conn., 1789–1836*, vol. II (1837), p. 851; Herbert Hovenkamp, *Enterprise and American Law, 1836–1937* (1991), pp. 49–55.

was a unique, ad hoc creation; it tended to vest exclusive control over a public asset, a natural resource, or a business opportunity in one group of favorites or investors. This was the essence of a charter to a town, a hospital—or a turnpike, a bank, or a bridge company. As such, it was odious to many people, especially those of the Jeffersonian persuasion. But now the corporation began to become a general form for organizing a business, legally open to all, and with few real restrictions on entry, duration, and management. The law moved, in a sense, to democratize the corporation, to make it available to everybody.⁵⁶ Business practice led the way, in many regards. The living law on proxy voting, general and special meetings, inspection of books, and the transfer of stock, gradually created demands (which were met) for standard clauses in corporate charters; and ultimately these norms found their way into the statute and case law of corporations.

There were many detours along the way before the law arrived at the position that access to the corporate form should be simple and open to everybody. Something must be said about state partnership in corporate affairs, about the anti-corporation movement, and about the fate of rival forms of business organization.

It seemed only natural, in the early nineteenth century, for the state to act in partnership with corporations, for a number of reasons. In the first place, many corporations were chartered to do work that was traditionally public: road building, banking, digging canals, and so on. Secondly, since each franchise was a privilege and favor, the state had the right to exact a price,⁵⁷ which might include strict controls or even profit sharing. Thirdly, state participation was a good way to help out an enterprise. It was a way of priming the pump, a way of supporting enterprise that would in turn enrich the economy. Fourth, public participation increased public control: if the state owned stock, and its men sat on the board, they could make sure the company acted in the public interest. And fifth, state investment could bring money into the treasury. If the dreams of the enterprise came true, big dividends would flow into public coffers. Thus Pennsylvania, for example, not only owned stock in its banks, but, after 1806, invested in turnpikes, bridge companies, canal companies, and finally in railroads. States and cities both engaged in railroad boosting. Initially, there was an orgy of chartering. Ohio granted forty-seven charters for railroads between 1830 and 1859; Illinois in 1857 incorporated fifty-five railroad companies.⁵⁸ Then there was outright aid: Between 1827 and 1878, New York State lent, leased, or donated \$10,308,844.77 for construction of sixteen railroads.⁵⁹ Some of these loans turned very sour in the aftermath of the panic of 1837. The New York constitution of 1846 severely restricted state aid to private corporations. The railroads then turned to the cities and towns with "astonishing success."

⁵⁶ Hovenkamp, *op. cit.*, p. 2. Hovenkamp calls this a "distinctively Jacksonian" development.

⁵⁷ Sometimes quite literally. The charter of the Bank of Philadelphia (1803) required the bank to pay a bonus of \$135,000 to the state. The bonus practice was not abolished in Pennsylvania until 1842. Hartz, *op. cit.*, pp. 54–56.

⁵⁸ James W. Ely Jr., *Railroads and American Law* (2001), p. 18. On financial aid to the railroads, *ibid.*, pp. 19–23.

⁵⁹ Harry H. Pierce, *Railroads of New York: A Study of Government Aid* (1953), p. 15.

Cities and towns were passionately eager to get railroad routes that connected them to the rest of the world. A railroad meant access to markets, rising land values, and general prosperity. Most commonly, the cities bought stock in the railroads. The city of Buffalo, for example, subscribed \$1,000,000 for stock in the Buffalo & Jamestown Railroad. A few towns bought bonds; a few donated money outright; and in 1842, the city of Albany guaranteed, by endorsement, \$100,000 worth of bonds of the Mohawk & Hudson.⁶⁰

Pennsylvania also experimented with mixed public and private enterprises. At one stage in the state's marriage with its railroads, in the 1830s, Pennsylvania furnished locomotives; private companies supplied the other cars. Before 1842, the state of Maryland chose ten of the thirty directors of the B&O; the city of Baltimore chose eight. In New Jersey, the "monopoly bill" of 1832 granted exclusive transport franchises in exchange for gifts of stock to the state. The state's shares carried a higher priority for dividends than other shares—one of the earliest instances of preferred stock. For years, New Jersey profited nicely from its railroad investments; the income helped lower the taxes that New Jersey levied on its residents.

State participation in enterprise, as it turned out, was only a passing phase. There were always people who felt that the state should not go into business. The business cycle made this argument compelling. During periods of crashes, panics, and depressions, states lost money on their investments. The whole idea of state participation turned sour. States and cities, nearly bankrupted in the years after 1837, were tempted to sell off their assets for cash. In 1844, a referendum in Pennsylvania approved sale of the Main Line to private interests. As it happened, the sale was not consummated until 1857. The Pennsylvania Railroad then bought the line for cash and railroad bonds. In exchange, the state gave the railroad all tracks and equipment of the line, and exempted it "forever, from the payment of taxes upon tonnage or freight carried over the said railroads; and . . . on its capital stock, bonds, dividends or property, except for city, borough, county, township, and school purposes." This extraordinary boon was declared unconstitutional one year later, in the great case of *Mott v. Pennsylvania Railroad*.⁶¹ Pennsylvania's Chief Justice Ellis Lewis wrote a strong opinion denying that the state had any right to commit "political suicide" by giving up the power to tax. Legislative authority was not for sale. Lewis also felt that the public had to exert some control over the legislature, to keep it from pawning its sovereignty. Alas, faith in the "fidelity of the legislature" was often misplaced:

Limitations of power, established by written constitutions, have their origin in a distrust of the infirmity of man. That distrust is fully justified by the history of the rise and fall of nations.⁶²

The system of checks and balances fed on this very American fear. It was a fear of unbridled power—mostly, government power, but also the power of large landholders and dynastic wealth. Politically active members of the public

⁶⁰ Pierce, *op. cit.*, pp. 18–19.

⁶¹ 30 Penn. State 9 (1858); see James W. Ely Jr., *Railroads and American Law* (2001), pp. 8–9.

⁶² 30 Penn. State at 28.

were willing to try all sorts of techniques to keep authorities in check, and to offset the corrosive effects of money. Corruption was a problem from the start; legislatures that had power to grant franchises and to charter corporations, could also be bribed with money and stock.

The story of the business corporation is a story of triumph and success. But the process was neither painless nor noiseless. There was much controversy over corporations in the first half of the nineteenth century. People tended to associate them, not illogically, with franchises and monopolies. They were entities the state created, to hold some power or right that no one else could lay claim to. Most corporations were transportation monopolies, banks, insurance companies—aggregations of "capital," representing the "few" against the "many." Unlike farms and industrial enterprise, they did not produce anything real—at least this is what people thought. They were in a sense parasitic, and unduly powerful. The more corporations, the more danger to the body politic. James Sullivan, attorney general of Massachusetts, warned in 1802 that "The creation of a great variety of corporate interests . . . must have a direct tendency to weaken the power of government."⁶³

The word "soulless" constantly recurs in debates over corporations. Everyone knew that corporations were really run by human beings. Yet, the word was not completely inappropriate. Corporations did not die, and there was no real limit to their size, or their greed. Corporations might aggregate the worst urges of whole groups of men. No considerations of family, friendship, or morality, would temper their powers. People hated and distrusted corporations, the way some people came to fear the soulless computer—machines that can join together the wit, skill, power, and malevolence of infinite numbers of minds.

In theory, the special charter system was a good way to control corporations. But the demand for charters, in the end, got to be too heavy. By the 1840s and 1850s, it would have swamped the legislatures, if the process had not become so routine. Even so, state session laws bulged with special charters. Time was wasted in the drudge work of issuing, amending, and extending hundreds of charters. In the rush, there was little time to supervise those charters that perhaps needed supervision.

Legislatures then took the next logical step—they passed general corporation acts. The legislature could save itself time, and could effectively make rules for all corporations, by passing one carefully considered law. They could also turn the corporate form into a right which any person or group could make use of, rather than a privilege of the few.

Even in the late eighteenth century a few general laws were passed, which applied to churches, academies, and library societies. A New York law of 1811, "relative to incorporations for Manufacturing purposes," is usually credited as the first general law for business corporations. Under this law, "any five or more persons who shall be desirous to form a company for the purpose of manufacturing woollen, cotton, or linen goods, or for the purpose of making glass, or for the purpose of making from ore bar-iron, anchors, millirons, steel, nail-rods, hoop-iron and ironmongery, sheet copper, sheet lead, shot, white lead and red lead," and who filed a certificate with some standard information in the office of the secretary of state, became, for "the term of twenty

years next after the day of filing such certificate," a "body corporate and politic, in fact and in name."⁶⁴

Other corporation acts picked up the New York plan. These laws were general in the sense that they applied to all corporations in a particular field—manufacturing, banking, or insurance. Typically, too, the laws did not provide an exclusive method of starting a corporation. They left the door open for private charters, if the incorporators preferred. In fact, the early general laws were not particularly effective. When they imposed rules with any bite at all, the business community ignored them and took the private-charter route. Some entrepreneurs incorporated temporarily under a general law, and then tried to extract a private charter from the legislature. To put teeth into the general laws, the New York Constitution of 1846 took a somewhat more drastic step. It restricted special charters to "cases where in the judgment of the Legislature, the objects of the corporation cannot be attained under general laws."⁶⁵ As it turned out, the legislature was quite accommodating in making such judgments. At the close of the period, then, the special charter was still dominant. But the handwriting was on the wall. The Louisiana Constitution of 1845, a bellwether in many ways, contained a much stronger clause: "Corporations shall not be created in this State by special laws except for political or municipal purposes."⁶⁶

The fight against corruption was one of the reasons for these constitutional revisions. There were unscrupulous incorporators, and there were recurrent bribery scandals. These scandals weakened public confidence in elected officials. To win the war against evil corporations, the legislatures had to be put under restraint. Under the New York Constitution of 1821, the "assent of two-thirds of the members elected to each branch of the legislature" was needed for passage of any bill "creating, continuing, altering, or renewing any body politic or corporate."⁶⁷ A similar provision appeared in the Delaware Constitution of 1831. Delaware would one day be a snug harbor for out-of-state corporations; but this was still far off in 1831. Under the Delaware Constitution, no act of incorporation "shall continue in force for a longer period than twenty years, without the re-enactment of the Legislature, unless it be an incorporation for public improvement."⁶⁸

There were two sides to the debate. When a two-thirds provision, like New York's, was proposed in the New Jersey convention of 1844, one delegate remarked he was "a friend to corporations. They have done more to increase the prosperity of our State than anything else. Let the legislature grant all that may apply, if the object is to benefit the community." The two-third rules was a way for people to "show their teeth at these little monsters, but if they believe them to be such dangerous creatures as they have represented them to be, they had better come manfully up to the work and strangle them at once, than to keep up this continued snapping at their heels."⁶⁹ The proposal was defeated.

⁶⁴ Laws N.Y. 1811, ch. 47.

⁶⁵ New York Const., 1846, art. 8, sec. 1. See Seavoy, *op. cit.*, pp. 177-88.

⁶⁶ Louisiana Const., 1845, art. 123. This provision was copied in Iowa the following year.

⁶⁷ New York Const., 1821, art. 7, sec. 9.

⁶⁸ Delaware Const., 1831, art. 2, sec. 17.

⁶⁹ *Proceedings of the New Jersey State Constitutional Convention of 1844* (1942), pp. 537-38, 539.

⁶³ Quoted in Handlin and Handlin, *op. cit.*, p. 260.

In fact, the anti-corporation movement never succeeded in doing more than snapping at heels; strangulation was simply not in the cards.

But the issue of control over corporations was a persistent one, in the first half of the nineteenth century. It was a period that made distinctions between the productive use of capital, and wasteful, parasitic, nonproductive use. Money-lenders were parasites; and people who played the stock market were little better than gamblers. These attitudes weakened over time, but slowly and somewhat painfully. Some states passed laws against speculation in stocks. A Pennsylvania law of 1841, for example, made contracts for the sale of securities void, if the delivery was to be done more than five days in the future. New York in 1837 prohibited people who bought stock in banks from selling the stock, until three months after all the stock had been paid for. Mississippi in 1840 made it illegal for a bank to deal in "stocks of any kind." Virginia and other states licensed stockbrokers. None of these laws was particularly effective; but they illustrate how queasy many people felt about those who bought, sold, and dealt in corporate securities.⁷⁰

In the famous case of *Dartmouth College v. Woodward* (1819),⁷¹ the U.S. Supreme Court faced squarely the issue of control over corporations. By the terms of the federal Constitution, no state could impair the obligation of a contract. But what was a "contract"? Dartmouth College was a corporation, with a charter from New Hampshire. The state enacted a law changing the terms of that charter. The Supreme Court held that this was beyond the power of the state. A corporate charter was "a contract made on a valuable consideration," a "contract for the security and disposition of property." It followed that the legislature could not change the terms of a charter. To do so would "impair" the charter, that is, the contract between the state and the corporation.⁷²

Dartmouth College was no business corporation; but the court, and the newspaper-reading public, well understood that the decision went beyond any question of a small college and its charter from the state. News of the decision evoked a great howl of protest. Many contemporaries felt that the case was a blow to popular sovereignty; it took away from "the people and their elected representatives" a "large part of the control over social and economic affairs." That was one way of looking at the case. The court and its defenders saw it differently. This decision, and others like it, protected investments and property interests. It shielded them from shifting, temporary winds of public opinion.

⁷⁰ Stuart Banner, *Anglo-American Securities Regulation: Cultural and Political Roots, 1690-1860* (1998), pp. 222-36.

⁷¹ 4 Wheat. 518 (1819). An important precursor was *Fletcher v. Peck*, 6 Cranch 87 (1810). This case came out of the so-called Yazoo land scandals in Georgia. The Georgia legislature entered into a corrupt land-grant deal. The next legislature repealed the grant; but, meanwhile, some of the land had passed into the hands of out-of-state investors who were not part of the original tainted deal. The United States Supreme Court, under John Marshall, sided with the buyers of the land. The grant of land by the legislature, said Marshall, was a "contract"; what one legislature gave, the next could not take back. See C. Peter Magrath, *Yazoo, Law and Politics in the New Republic: The Case of Fletcher v. Peck* (1966).

⁷² On Marshall's opinion in *Dartmouth College*, and the other contract-clause cases, see Charles F. Hobson, *The Great Chief Justice: John Marshall and the Rule of Law* (1996), pp. 78-110.

The doctrine, guaranteed a level of legal stability. In this way, it promoted economic growth. It encouraged risk-taking in business.

Dartmouth College had a far less sweeping effect on the law of corporations than one might have guessed. In a concurring opinion, Justice Joseph Story hinted, perhaps deliberately, at a simple way to get around the new rule. If the legislature, Story said, really wanted to alter corporate charters, it ought to reserve the right to do so when it issued such charters. Then the right to change the terms of the charter would be, legally speaking, part of the "contract" between the state and the corporation; and when the legislature passed a law amending the charter, there would be no "impairment." In later years, it was routine for the legislature to insert in every charter a clause reserving to the state the right to alter, amend, and repeal. This right was also a common feature of general incorporation laws. Finally, the right was inserted in state constitutions. The New York Constitution of 1846 provided that "all general laws and special acts" about corporations "may be altered from time to time or repealed" (art. 8, sec. 1).

Corporations were rare before 1800; hence the case law on corporations was thin before the nineteenth century. As corporations multiplied, so did litigation over rights and duties. For all practical purposes, the courts created a body of corporation law out of next to nothing. Old decisions and doctrines, from the time when most corporations were academies, churches, charities, and cities, had little to say about managers and directors that was germane to the world of business corporations.

At first, the courts treated corporate powers rather gingerly. They adhered to the "general and well settled principle, that a corporation had no other powers than such as are specifically granted; or, such as are necessary for the purpose of carrying into effect the powers expressly granted."⁷³ This "principle" followed from the idea of a corporation as a single venture, or a mass of capital to be used for a single purpose—a bridge, a factory, a bank. Chief Justice Roger Taney built on this principle in the famous case of the *Charles River Bridge* (1837).⁷⁴ Massachusetts had chartered a company to build a bridge over the Charles River, in the late eighteenth century. It was to be a toll bridge. Many years later, the state granted another charter, to a new group of entrepreneurs. The second bridge, to be built very close to the first one, would eventually be entirely free. This would destroy the investment in the original bridge. The owners of this bridge sued, claiming the second charter violated the constitution: it impaired the obligation of a contract (their charter). The Supreme Court held against them. A charter had to be strictly construed. The state had never promised not to charter a competing bridge. The case can be read narrowly, to mean only that the powers of corporations, like those of government, had to be kept within narrow boundaries; and its charter had to be read in that light. But the case also stood for "progress," for impatience with vested rights;

⁷³ Joseph K. Angell and Samuel Ames, *A Treatise on the Law of Private Corporations Aggregate* (2nd ed., 1843), p. 66.

⁷⁴ *Proprietors of the Charles River Bridge v. Proprietors of the Warren Bridge*, 11 Pet. 420 (1837). On the background and meaning of the case, see Stanley I. Kutler, *Privilege and Creative Destruction: The Charles River Bridge Case* (1971).

it stood for the idea that you can't make an economic omelette without breaking eggs. The old bridge, like the old turnpikes, had to give way to what was more dynamic, more modern, and more progressive.

This was the lasting message of the Charles River Bridge. In the long run, the creative draftsmanship of private citizens—the people who actually wrote the texts of the charters—helped to bury the idea of strict construction. Business practice led the way. The charters came to reflect what was fact: enterprise was growing in scope and flexibility. The logic of economic growth, invisible to most contemporaries, was drawing up law for itself. What the draftsmen devised, the courts accepted, and legislatures only weakly resisted. The old controls on corporations, meant to reduce their power or their economic role, either disappeared or became innocuous.

But while one kind of restriction faded, others were beginning to develop. The business corporation was an economic animal. It existed to make profits. It was managed by officers and directors; and it had stockholders, who were in theory the people who owned the company. Then there were the corporation's creditors. What rights and duties did all these people have, with regard to each other? The case-law tried to answer these questions. There was, for example, the so-called trust-fund doctrine, which Joseph Story gets credit for inventing. The leading case was *Wood v. Drummer* (1824).⁷⁵ Stockholders of the Hallowell and Augusta Bank, of Maine, which was winding up its corporate existence, declared dividends amounting to 75 percent of the capital stock of \$200,000. The bank thus became a hollow shell, especially since not all of the capital stock had actually been paid in. The plaintiffs held bank notes that became worthless. Story held that it was wrong for the stockholders to distribute the capital to themselves in such a way as to defraud the bank's creditors, that is, the holders of the bank notes. The capital stock of banks was "to be deemed a pledge or trust fund for the payment of the debts contracted by the bank." Creditors could "follow" the funds "into the hands of any persons, who are not innocent purchasers," and recover it from them. This gave the plaintiffs a right to recover from the stockholders, who had lined their pockets with the money from the bank. Later cases picked up this doctrine, and applied it to other situations. Meanwhile, the courts slowly built up a body of rules about the internal life of corporations, and the relationships between corporations and the outside world.

The triumph of enterprise was probably inevitable; but the corporate form was not the only possibility. A New York statute of 1822, widely copied later on, introduced the limited partnership into American law. This was based, in part, on a French business form, the *société en commandite*. In a limited partnership, some members ("general partners") were fully responsible for partnership debts. Limited (or "special") partners, however, were liable "no further than the fund which he or they have furnished to the partnership stock."⁷⁶ A limited partnership (with its "one or more sleeping partners") was "supposed to be well calculated to bring dormant capital into active and useful employment."⁷⁷ (The words are Chancellor Kent's.) Most commercial

⁷⁵ 3 Mason C.C. Rpts. 308, Fed. Cas. No. 17,944 (1824).

⁷⁶ See Edward H. Warren, *Corporate Advantages without Incorporation* (1929), pp. 302ff.

⁷⁷ James Kent, *Commentaries on American Law* [cited hereafter as Kent, *Commentaries*], vol. III (2nd ed., 1832), p. 35.

enterprises were partnerships of one form or another before the middle of the nineteenth century.

Another kind of business association was the Massachusetts or business trust. This was an unincorporated association, which used the structure of a trust. Managers (trustees) held title to the property of the trust. Instead of stockholders, there were "beneficiaries"; instead of capital stock, the owners held certificates of beneficial interest. A "trust government," something like a charter, spelled out the powers and duties of the managers.

The joint-stock company was another type of business association, in common use. It was something like a partnership; but its capital, unlike that of a partnership, was divided into transferable shares.

It was by no means certain that a corporation, as that term was understood in 1800 or 1820, was the best way to raise and manage money for a new enterprise. Shaw Livermore studied early American land companies. They made use of a broad menu of business forms. Speculative land companies, even before 1800, showed "all the various states of complexity in modern business organization beyond the partnership"; yet they were not incorporated. Livermore has argued that these associations were the "true progenitors of the modern business corporation."⁷⁸ The argument, in other words, is that the modern corporation is not really the direct descendant of the special charter system, but rather an evolution from a rich palette of business practices and business forms.

Words, forms, and slogans did come from the old law of corporations; and these were used, like rubble from which a new bridge is built. The architecture and the plans came from business practice, and from the marketplace. That the final, triumphant form was a "corporation," not some mutation of the partnership or Massachusetts trust might be due to almost random factors, which tipped the balance one way or another. Similarly, in the twentieth century, before the Uniform Commercial Code was adopted by the states, the legal form used for goods sold on the installment plan differed in form from state to state. In some states, the form was called a conditional sale; in some, a chattel mortgage; in Pennsylvania, a bailment lease; in England, a hire-purchase contract. If some annoying or technical case, doctrine, or statute blocked one type of arrangement, the practice flowed freely into another channel, like water when it is dammed. This was the case with the triumph of the corporate form. What the growing market needed was an efficient, trouble-free device to aggregate capital and manage it in business, with limited liability and transferable shares.

The argument over origins—this is often the case—is mostly an argument over words. French law was not the "progenitor" of the limited partnership; charters of towns, colleges, and hospitals were not the "progenitors" of railroad charters; land syndicates were not the "progenitors" of general corporation laws. All these were merely models and occasions. The theory of legal history is that contemporary fact is always the architect of contemporary law. History does not supply decisions—only raw materials and plans.

⁷⁸ Shaw Livermore, *Early American Land Companies: Their Influence on Corporate Development* (1939), p. 216.