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The Modern State and the Rise of the Business Corporation

ABSTRACT. This Article argues that the rise of the modern state was a necessary condition for the rise of the business corporation. A typical business corporation pools together a large number of strangers to share ownership of residual claims in a single enterprise with guarantees of asset partitioning. We show that this arrangement requires the support of a powerful state with the geographical reach, coercive force, administrative power, and legal capacity necessary to enforce the law uniformly among the corporation's various owners. Strangers cannot cooperate on the scale and with the legal complexity of a typical business corporation without a modern state and the legal apparatus it supplies to enforce the terms of their bargain. Other historical forms of rule enforcement, such as customary law among closely knit communities and commercial networks like the Law Merchant, are theoretically able to support many forms of property rights and contractual relations but not the business corporation.

We show that this hypothesis is consistent with the experiences of six historical societies: late imperial China, the nineteenth-century Ottoman Empire, the early United States, early modern England, the late medieval Italian city-states, and ancient Rome. We focus especially on the experience of late imperial China, which adopted a modern corporation statute but failed to see much growth in the use of the corporate form until the state developed the capacity and institutions necessary to uniformly enforce the new law. Our thesis complicates existing historical accounts of the rise of the corporation, which often emphasize the importance of economic factors over political and legal factors and view the state as a source of expropriation and threat rather than support. Our thesis has extensive implications for the way we understand corporations, private law, states, and the nature of modernity.

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INTRODUCTION

The two great institutions of modernity are the business corporation and the state. They dominate, respectively, the private and public sectors of modern societies. The goal of this Article is to understand the historical connection between these two institutions. We focus on the genesis of the corporation to argue that the rise of the modern state was a necessary condition for the rise of the modern corporation.

As a large academic literature has shown, modern states were the product of intensive state-building that began in Western Europe in the seventeenth century, spreading to the rest of the world over the next two to three centuries.[1] The central feature of a modern state is its comparative strength in achieving its objectives: in terms of fiscal, administrative, and legal capacity, nearly all modern states are qualitatively stronger than nearly all premodern states.[2] The business corporation emerged at around the same time, originating in Northwestern Europe in the seventeenth century and institutionally maturing in the later eighteenth century.[3] A central feature of a modern corporation is its comparative success in combining the ownership interests of many shareholders who are socially disconnected from one another. Together, these two institutions embody the bureaucratic socioeconomic ordering that defines modern private and public life.

Unlike preexisting theories that view the relationship between the two as a predominantly negative one—that the state's primary role in the rise of the corporation was to credibly constrain its own use of coercive power[4]—we argue that

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1. *See, e.g.*, MARK DINCECCO, STATE CAPACITY AND ECONOMIC DEVELOPMENT: PRESENT AND PAST (2018); RICHARD BONNEY, THE RISE OF THE FISCAL STATE IN EUROPE C. 1200-1815 (1999); Thomas Brambor, Agustín Goenaga, Johannes Lindvall & Jan Teorell, *The Lay of the Land: Information Capacity and the Modern State*, 53 COMPAR. POL. STUD. 175, 175-213 (2020); Hendrik Spruyt, *The Origins, Development, and Possible Decline of the Modern State*, 5 ANN. REV. POL. SCI. 127, 127-49 (2002). On debates over the definition of state capacity, see, for example, Elissa Berwick & Fotini Christia, *State Capacity Redux: Integrating Classical and Experimental Contributions to an Enduring Debate*, 21 ANN. REV. POL. SCI. 71, 71-91 (2018).

2. *See, e.g.*, Jørgen Møller, *Medieval Roots of the Modern State: The Conditional Effects of Geopolitical Pressure on Early Modern State Building*, 42 SOC. SCI. HIST. 295, 295-316 (2018); Spruyt, *supra* note 1, at 131-35.

3. *See, e.g.*, RON HARRIS, GOING THE DISTANCE: EURASIAN TRADE AND THE RISE OF THE BUSINESS CORPORATION, 1400-1700, at 4-6 (2020).

4. *See, e.g.*, *id.* at 4; Timur Kuran, *The Absence of the Corporation in Islamic Law: Origins and Persistence*, 53 AM. J. COMPAR. L. 785, 792-93 (2005); Douglass C. North, *Institutions and Credible Commitment*, 149 J. INST. & THEORETICAL ECON. 11, 11-12 (1993); Douglass C. North & Barry R. Weingast, *Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England*, 49 J. ECON. HIST. 803 (1989); Yingyi Qian & Barry R. Weingast, *Federalism as a Commitment to Reserving Market Incentives*, 11 J. ECON. PERSPS. 83,

the state also contributed to the corporation's emergence positively. In fact, the modern state's positive contributions were so significant that they were likely *indispensable*. It is no coincidence that the business corporation did not become socioeconomically prominent until after the ascendancy of modern state-building. As we argue below, the state played a central role in the rise of corporations in numerous major economies.

Our thesis has two parts. The first is theoretical and consists of two primary arguments. First, we argue that there can be significant demand for the modern corporate form only after complex, long-duration business collaboration between strangers becomes economically prominent. Business activities within closely knit communities—the dominant form of collaboration prior to the rise of modern states—was unlikely to produce enough demand for corporate legal technologies like asset partitioning and tradable shares. Instead, these technologies emerged only in response to business relationships that breached traditional communal boundaries, of which the paradigmatic early modern example was interregional Eurasian and transatlantic trade.

Second, we argue that, within the context of transcommunal business relationships, the business corporation can only emerge with robust institutional support from a sufficiently modern state, in the form of legal enforcement, dispute resolution, and information sharing. In particular, we argue that modern state-building is necessary to the success of the modern corporation because the legal arrangements that enable corporations require uniform enforcement among strangers.

The essence of a corporation is the collective ownership of a pool of resources by a large number of people who are mostly unknown to one another. As we argue, there is, in theory, much less need for corporate legal technologies outside of those conditions. Under them, the possibility that a corporation's many owners might be treated differently from one another poses grave risks. Since the owners of a corporation all share a residual claim on the same pool of resources, any deviations from uniformity tend to be zero-sum: more resources for one owner means less for the others. Deviations from uniformity thus undermine trust and discourage investment. A modern state—that is, one with strong coer-

83-84 (1997). *See generally* Giuseppe Dari-Mattiacci, Oscar Gelderblom, Joost Jonker & Enrico C. Perotti, *The Emergence of the Corporate Form*, 33 J.L. ECON. & ORG. 193 (2017) (discussing the historical interaction between states and corporations); Aldo Musacchio & John D. Turner, *Does the Law and Finance Hypothesis Pass the Test of History?*, 55 BUS. HIST. 524 (2013) (summarizing business-history scholarship); Timothy Frye, *Credible Commitment and Property Rights: Evidence from Russia*, 98 AM. POL. SCI. REV. 453 (2004) (arguing that constraining state agents is crucial to increasing the security of property).

cive power, centralized lawmaking, extensive geographical reach, and commitment to formal equality before the law—can solve this problem because of its unique capacity to ensure uniformity.

The second part of our thesis is descriptive. We survey six case studies—twentieth-century China,[5] the nineteenth-century Ottoman Empire,[6] early seventeenth-century England,[7] the nineteenth-century United States,[8] early modern Italian city-states,[9] and ancient Rome[10]—and show that in none of these historical places have the formal legal technologies that enable corporations been used successfully at a large scale without the enforcement power of a functionally modern state. Rarely does anything resembling corporate law appear on the books of a premodern state. And when such law was recorded in a premodern state, it was rarely, if ever, used widely among business enterprises and, thus, rarely accomplished its intended purposes.

5. *See infra* Section II.A.

6. *See infra* Section II.B.

7. *See, e.g.*, John D. Turner, *The Development of English Company Law Before 1900*, at 2-3 (Queen's Univ. Ctr. for Econ. Hist., Working Paper No. 2017-01, 2017), https://www.econstor.eu/bitstream/10419/149911/1/877815712.pdf [https://perma.cc/7EJ4-T5BN]; Graeme G. Acheson, Gareth Campbell, John D. Turner & Nadia Vanteeva, *Corporate Ownership and Control in Victorian Britain*, 68 ECON. HIST. REV. 911, 911-13 (2015); HARRIS, *supra* note 3, at 251-330; Dari-Mattiacci et al., *supra* note 4; JAMES TAYLOR, CREATING CAPITALISM: JOINT-STOCK ENTERPRISE IN BRITISH POLITICS AND CULTURE, 1800-1870 (2006) (chronicling the emergency of the joint-stock corporation in nineteenth-century Britain). For more detailed discussion, see *infra* Section II.C.

8. On American corporations, see, for example, Timothy Guinnane, Ron Harris, Naomi R. Lamoreaux & Jean-Laurent Rosenthal, *Putting the Corporation in Its Place*, 8 ENTER. & SOC'Y 687 (2007); David McBride, *General Corporation Laws: History and Economics*, 74 LAW & CONTEMP. PROBS. 1 (2011); Naomi R. Lamoreaux, *Partnerships, Corporations, and the Limits on Contractual Freedom in U.S. History: An Essay in Economics, Law and Culture*, *in* CONSTRUCTING CORPORATE AMERICA: HISTORY, POLITICS, AND CULTURE 29 (Kenneth Lipartito & David B. Sicilia eds., 2004); and John J. Wallis, *Constitutions, Corporations, and Corruption: American States and Constitutional Change, 1842-1852*, 65 J. ECON. HIST. 211 (2005). For more detailed discussion, see *infra* Section II.D.

9. *See, e.g.*, Ron Harris, *The Institutional Dynamics of Early Modern Eurasian Trade: The* Commenda *and the Corporation*, 71 J. ECON. BEHAV. & ORG. 606, 606-22 (2009); John H. Pryor, *The Origins of the* Commenda *Contract*, 52 SPECULUM 5, 8 (1977); Abraham L. Udovitch, *At the Origins of the Western* Commenda*: Islam, Israel, Byzantium?*, 37 SPECULUM 198, 198 (1962). For more detailed discussion, see *infra* Section II.E.1.

10. *See, e.g.*, Geoffrey Poitras & Frederick Willeboordse, *The* Societas Publicanorum *and Corporate Personality in Roman Private Law*, 2019 BUS. HIST. 1; Ulrike Malmendier, *Law and Finance "at the Origin,"* 47 J. ECON. LITERATURE 1076 (2009); Robert W. Hillman, *New Forms and New Balances: Organizing the External Relations of the Unincorporated Firm*, 54 WASH. & LEE L. REV. 613 (1997); Barbara Abatino, Giuseppe Dari-Mattiacci & Enrico C. Perotti, *Depersonalization of Business in Ancient Rome*, 31 OXFORD J. LEGAL STUD. 365 (2011). For more detailed discussion, see *infra* Section II.E.2.

This thesis significantly enriches our understanding of the rise of the corporate form. To date, economic historians have tended to attribute the rise of the corporate form either to the growth of economic activities that demanded the corporate form or to the achievement of limits on state power that encouraged private investment by securing it against state-sponsored expropriation. We do not deny the necessity of these forces as conditions for the rise of the corporation. But we add to them by showing that the strong legal and administrative capacities of a modern state represent another, heretofore unrecognized, necessary condition in the process of modern corporate development. We show that economic demand alone cannot compel the rise of the modern corporation and that the influence of the state on the corporation was positive as well as negative.

The power of our thesis is perhaps most evident in our study of twentieth-century China.[11] China enacted a modern corporate-law statute as early as 1904, but almost no businesses actually used the corporate form until decades later. The reason was not that economic activity in China remained insufficiently developed. By 1904, interregional trade and other complex and long-lasting activities had thrived in China for centuries. Nor was the reason that the state threatened to expropriate the value created by private corporations. The early twentieth-century Chinese state was too weak to enforce even modest forms of taxation, let alone to expropriate large shares of the value created by corporate enterprise.[12] Rather, the main issue was that the Chinese state was simply not strong enough—not *modern* enough—to make its corporate law meaningful. Few firms with large numbers of owners trusted the Chinese state to enforce its corporate laws with the uniformity and vigor required to sustain the cooperation among large groups of strangers that characterizes modern corporate ownership. The corporation was not widely used by businesses in China until much later in the twentieth century, after the state had become powerful enough to make it meaningful.

While this Article is primarily interested in theories of the corporation, its thesis has broader implications for private-law theory. It suggests, in particular, that private legal institutions—that is, legal institutions that order relationships between private parties—can be separated into two groups: those that can socioeconomically proliferate without state support and those that cannot. As much scholarship has demonstrated, many segments of private law, especially those in the realm of contract and property, have long existed in human communities

11. *See infra* Section II.A.

12. *See id.*

even when institutional support from the state was meager or absent.[13] In fact, numerous full-liability partnerships also fall into this category.[14] But what differentiates these institutions from state-dependent legal forms like corporations? We suggest here that the differentiating factor is the existence, or lack thereof, of private demand: many private legal institutions are indispensable even within closely knit communities, but others, like the corporation, become significantly useful only in the context of cooperation between strangers.

Our thesis comes with at least two caveats and limitations. First, we acknowledge that the relationship between the corporation and the state has more facets than we have identified here.[15] The modern state might have been necessary to the rise of the modern corporation for any number of reasons; the value of uniform and strong law enforcement may have been just one of them. The threads of possible connection between the state and the corporation are as innumerable as the forces that pushed the world into modernity more generally.[16] In arguing for the plausibility of our legal and economic thesis about uniformity, we mean not to deny the importance of these other connections between the state and corporation but merely to supplement them. We identify *some* of the many connections between the state and the corporation without claiming to have identified *all* of them.

A second caveat is that we cannot guarantee the representativeness of our case studies. We chose our case studies based on the depth of existing historical scholarship about them and the idiosyncratic reach of our own expertise. These studies are incapable of proving our thesis definitively, but we think the thesis stands on its own as a matter of theory and hope that our case studies will illustrate its appeal.

This Article proceeds first by explaining our thesis in general theoretical terms in Part I and then by illustrating it with case studies in Part II.

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13. *See, e.g.*, ROBERT C. ELLICKSON, ORDER WITHOUT LAW: HOW NEIGHBORS SETTLE DISPUTES 167-83 (1991); ERIC A. POSNER, LAW AND SOCIAL NORMS (2000) [hereinafter POSNER, LAW AND SOCIAL NORMS]; Eric A. Posner, *Law, Economics, and Inefficient Norms*, 144 U. PA. L. REV. 1697 (1996); Richard H. McAdams, *The Origin, Development, and Regulation of Norms*, 96 MICH. L. REV. 338 (1997); Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 J. LEGAL STUD. 115 (1992).

14. Partnerships have a very long history, reaching back into Roman times, and also saw significant use during the medieval period. *See, e.g.*, MAX WEBER, THE HISTORY OF COMMERCIAL PARTNERSHIPS IN THE MIDDLE AGES (Lutz Kaelber trans., Rowman & Littlefield Publishers 2003) (1889); John F. Padgett & Paul D. McLean, *Organizational Invention and Elite Transformation: The Birth of Partnership Systems in Renaissance Florence*, 111 AM. J. SOCIO. 1463 (2006).

15. Many would even argue that the growing power of the state was harmful to the rise of the corporation. *See, e.g.*, ARTHUR S. MILLER, THE MODERN CORPORATE STATE: PRIVATE GOVERNMENTS AND THE AMERICAN CONSTITUTION (1976).

16. *See* Eugene Kamenka, *Gemeinschaft and Gesellschaft*, 17 POL. SCI. 3, 4 (1965).

I. THEORY

A. Definitions

Our first task is to define what we mean by the terms "business corporation," "modern state," and "state capacity." Like many others, we use the term "business corporation" to mean a business enterprise that possesses a particular set of legal features: most importantly, centralized management,[17] independent legal personality,[18] capital lock-in,[19] tradable shares,[20] and asset partitioning—including both strong entity shielding,[21] which prevents the personal creditors of firm investors from forcing the liquidation of firm assets, and, somewhat less importantly, limited liability.[22] However, when we speak of "the rise of the corporation," we do not refer to the mere legal existence of these technologies but rather to their *socioeconomic proliferation*, especially among private economic actors. Legal technologies can be created but not widely used if lawmakers misjudge the level of socioeconomic demand for them or if their effective use in actual business requires more robust institutional support than just nominal legal creation.

As argued below, we think that such proliferation requires the business corporation to combine the interests of a large number of owners who are socially disconnected from one another in the sense that they are not kin or members of the same closely knit communities. In many ways, these socioeconomic conditions come closer to our core interests: we are more interested in the emergence

17. In other words, the day-to-day operation of the corporation is run by a centralized group of directors or managers, wielding powers delegated to them by shareholders.

18. That is, the corporation is an artificial entity that is legally distinct from its shareholders and officers.

19. This term means that shareholders cannot withdraw their investments in the corporation for either a term of years or until formal dissolution.

20. There are different levels of "tradability" in corporate shares: a share can be traded without dissolution of the corporation but only with the express consent of other shareholders, or it can be traded without dissolution and without the consent of other shareholders. In the modern era, the latter arrangement tends to differentiate limited-liability firms from full-liability ones. *See* Henry Hansmann, Reinier Kraakman & Richard Squire, *The New Business Entities in Evolutionary Perspective*, 2005 U. ILL. L. REV. 5, 11-12.

21. *See* Henry Hansmann, Reinier Kraakman & Richard Squire, *Law and the Rise of the Firm*, 119 HARV. L. REV. 1335, 1337-38 (2006).

22. *See, e.g.*, HARRIS, *supra* note 3, at 253; John Armour, Henry Hansmann & Reinier Kraakman, *What is Corporate Law?*, *in* REINIER KRAAKMAN, JOHN ARMOUR, PAUL DAVIES, LUCA ENRIQUES, HENRY HANSMANN, GERARD HERTIG, KLAUS HOPT, HIDEKI KANDA & EDWARD ROCK, THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 1, 9 (2d ed. 2009). *See generally* Hansmann et al., *supra* note 21 (arguing that "entity shielding," rather than legal liability, is the key distinguishing characteristic of corporations).

of large-scale, capital-intensive business collaboration than in the appearance of specific legal technologies—although the latter is functionally tied to the former.

To be clear, our use of the term "corporation" is broader than the term in ordinary usage, but the way we study "the rise of the corporation" may be narrower than what is immediately intuitive. Our use is broader because it is not restricted to entities that specifically carry the label "corporation." In our usage, any enterprise that possesses the legal and socioeconomic characteristics we identify can be a "corporation," even if it may be known commonly by some other name, such as a "joint-stock company," "limited-liability company," "partnership," or even "trust." Our discussion of "the rise of the corporation" is also narrower because it insists on the widespread socioeconomic use of these characteristics, not just on their existence.[23]

We also note that these concepts are more of a continuum than a binary category. The resemblance between an enterprise and a corporation can be greater or lesser depending on the extent to which the enterprise carries the key legal features, whereas the extent to which the corporation has "risen" in any specific economy is a quantitative judgment, not a qualitative one.

To date, historical scholarship on the corporate form has focused more on the legal aspects of the corporate form than its socioeconomic aspects.[24] Scholars have focused on dating the appearance of entity shielding, for instance, rather than dating the appearance of the enterprises with large numbers of unfamiliar owners that might have made entity shielding valuable.[25] This focus on legal technologies reflects both the intellectual priorities of legal scholars and the dearth of documentary evidence on the activity of businesses prior to the appearance of corporate law.

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23. For other examples of how the use of corporate legal technologies can diverge from their nominal creation in law, see James Ang, Rebel Cole & Daniel Lawson, *The Role of Owner in Capital Structure Decisions: An Analysis of Single-Owner Corporations*, 14 J. ENTREPRENEURIAL FIN. 1 (2010), which evaluates the effects of managerial decision-making on firm behavior and performance.

24. Ron Harris focuses on the socioeconomic phenomenon of long-distance trade but also anchors his argument in the emergence of the legal corporate form. *See generally* HARRIS, *supra* note 3 (exploring the relationship between long-distance trade and corporate forms). Other works are likewise focused on one or more corporate legal technologies. *See generally* Kuran, *supra* note 4 (exploring the root of the absence of the corporate form in Islamic law); Dari-Mattiacci et al., *supra* note 4 (analyzing the emergence of the permanent commitment of capital as a critical step in the emergence of the corporate form); Hansmann et al., *supra* note 21 (arguing that "entity shielding" is a key distinguishing characteristic of corporations); Guinnane et al., *supra* note 8 (comparing corporate forms in the United States with European alternatives).

25. *See, e.g.*, HARRIS, *supra* note 3.

We define the "modern state" functionally, rather than chronologically.[26] A modern state is one that exhibits a combination of legal, administrative, economic, and coercive capacities. First, a modern state is one that monopolizes the legitimate use of force.[27] It exerts enough control over social and economic activity that the primary rules in everyday life are the laws it creates rather than the norms and customs of the community. Second, the state is strong enough to enforce its laws, regulations, and orders reliably and predictably, to the point where private parties can reasonably rely upon the prospect of successful state enforcement.[28] Needless to say, no state in human history has completely monopolized, in actual social perception, the legitimate use of force, and no state is capable of perfect law enforcement. Nonetheless, we can intelligibly speak of more or less "modern" states, and when a state possesses enough of these institutional features and capacities, most scholars would have little difficulty recognizing it as "modern."

This raises the question of why we use the term "modern state" rather than simply "strong state." There are two reasons. First, modern states are distinguished not merely by their brute coercive power but also by the rationalization of that power: by the predictable ways in which that power is exercised, which, in turn, can enhance the state's administrative and legal power to levels unattainable through sheer coercion.[29] Specifically, such states tend to construct legal systems that offer high levels of uniform and standardized rule enforcement that disregards external sociopolitical status differences between private parties—

26. Chronologically, most historians would date the beginning of the "modern era" in continental European history to 1789 (the French Revolution), in English history to perhaps 1688 (the Glorious Revolution), in Chinese history to 1840 (the Opium War), in Japanese history to 1868 (the Meiji Restoration), and so on. The wide variation in these starting dates clearly indicates that the underlying logic behind this periodization is substantive, rather than purely chronological. The debate over what constitutes "modernity" is, of course, a massive and inconclusive one, although there seems to be more consensus around what constitutes a "modern state," with most scholars coalescing around functional definitions similar to the one that we have given here.

27. *See* MAX WEBER, ECONOMY AND SOCIETY: AN OUTLINE OF INTERPRETATIVE SOCIETY 941-48 (Guenther Roth & Claus Wittich eds., Ephraim Fischoff et al. trans., Univ. of Cal. Press 1978); Dieter Grimm, *The State Monopoly of Force*, *in* INTERNATIONAL HANDBOOK OF VIOLENCE RESEARCH 1043, 1043 (Wilhelm Heitmeyer & John Hagan eds., 2003).

28. *See, e.g.*, CHRISTOPHER PIERSON, THE MODERN STATE 15-16, 67-68 (3d ed. 2011).

29. *See* BERNARD S. SILBERMAN, CAGES OF REASON: THE RISE OF THE RATIONAL STATE IN FRANCE, JAPAN, THE UNITED STATES, AND GREAT BRITAIN 1-6 (1993); GIANFRANCO POGGI, THE DEVELOPMENT OF THE MODERN STATE: A SOCIOLOGICAL INTRODUCTION 101-03 (1978).

"*Contract*," rather than "*Status*," to quote Henry Maine.[30] Second, the term "modern" reflects that states with the features of modernity are almost exclusively clustered in the past three to four centuries of human history. If we employ fiscal capacity as a crude measure of broader state capacity, then prior to 1650 or so, even the most fiscally robust states on Earth only extracted some fifteen to twenty percent of annual economic output as government revenue, and their less robust peers only extracted at most five to ten percent.[31] In contrast, many modern states manage to tax upwards of a third of annual gross domestic product (GDP).[32] For better or worse, the powerful, professionalized state and legal apparatuses to which we are accustomed are a very recent phenomenon.

Because our definition of "modern state" is more functional than chronological, the historical evolution of "state modernity" is not a linear one. Some classical era states—Roman, Qin, or Tang—were likely more "modern" than some of their late medieval, early modern, or even modern era successors.[33] There are many chronologically recent states that were not, and perhaps still are not, functionally "modern."

Our functional definition of "modern state" also identifies, by logical extension, the specific kinds of "state capacity" that this Article focuses on. State capacity, as conventionally understood, refers to the state's ability to "implement official goals, especially over the actual or potential opposition of powerful social

30. HENRY SUMNER MAINE, ANCIENT LAW 100 (J.M. Dent & Sons 1917) (1861); *see also* Katharina Isabel Schmidt, *Henry Maine's "Modern Law": From Status to Contract and Back Again*?, 65 AM. J. COMPAR. L. 145, 145-86 (2017) (reassessing Henry Sumner Maine's thesis and its place in modern scholarship).

31. *See* TAISU ZHANG, THE IDEOLOGICAL FOUNDATIONS OF QING TAXATION: BELIEF SYSTEMS, POLITICS, AND INSTITUTIONS 4 (2022). For more detailed discussion, see KENT DENG, CHINA'S POLITICAL ECONOMY IN MODERN TIMES: CHANGES AND ECONOMIC CONSEQUENCES, 1800-2000, at 36 (2012); THOMAS C. SMITH, NATIVE SOURCES OF JAPANESE INDUSTRIALIZATION, 1750-1920, at 50-70 (1989); Peer Vries, *Public Finance in China and Britain in the Long Eighteenth Century* 7-8 (London Sch. of Econ., Working Paper No. 167/12, 2012), https://eprints.lse.ac.uk/45563/1/WP167.pdf [https://perma.cc/JFH5-KK25]; Mark Dincecco, *Fiscal Centralization, Limited Government, and Public Revenues in Europe, 1650-1913*, 69 J. ECON. HIST. 48 (2009); and Kivanç K. Karaman & Şevket Pamuk, *Ottoman State Finances in European Perspective, 1500-1914*, 70 J. ECON. HIST. 593, 608 (2010).

32. *See Revenue Statistics 2022: The Impact of COVID-19 on OECD Tax Revenues*, ORG. FOR ECON. COOP. & DEV. 1 (2022), https://www.oecd.org/tax/tax-policy/revenue-statistics-highlights-brochure.pdf [https://perma.cc/69VE-T58H].

33. *See* Michael Mann, *States, Ancient and Modern*, 18 EUR. J. SOCIO. 262, 270-73 (2009). Historians largely agree that Chinese state capacity declined over the course of the second millennium. *See* ZHANG, *supra* note 31, at 125-210.

groups or in the face of recalcitrant socioeconomic circumstances."[34] Needless to say, this leaves open an enormous range of possibilities on what constitutes "official goals," and therefore incorporates a very large number of functional possibilities: the ability to conduct wars, the ability to tax, the ability to enforce laws and maintain social order, the ability to control local agents and limit corruption, and the ability to provide fiscal or monetary stimulus to the economy, just to list a few.

Given that we define the core characteristics of a modern state to be the monopolization of the legitimate use of force, combined with the reliable, systematic, and rational enforcement of legal rules, we focus on the kinds of state capacity that can functionally produce those characteristics. First and foremost, we are concerned with the state's legal capacity: whether it possesses a professionalized legal apparatus of adequate size and sophistication, large and strong enough to dominate public and private dispute resolution yet rational and professional enough to enforce legal rules consistently and predictably.

The production of such legal capacity is usually expensive, in terms of both money and labor, and therefore requires a substantial amount of fiscal capacity—an institutional apparatus capable of reliably generating high levels of revenue without causing widespread rebellion. High fiscal capacity might not be a *sufficient* condition for high legal capacity, but it is almost certainly a *necessary* one. Effective law enforcement also requires high levels of coercive capacity, both to subjugate competing systems of regulation and rule enforcement such as religious or kinship organizations and to enforce the legal system's own decisions. Such coercive capacity tends to be symbiotic with the state's fiscal capacity. Other kinds of state capacity, such as educational or military capacity, will often functionally synergize with the state's legal, fiscal, and coercive capacities, but they do not always do so—and they matter for our present purposes only insofar as they do.[35]

B. Literature Review

Preexisting accounts about the emergence of the modern business corporation come in two varieties: demand-side accounts that emphasize interregional trade and commercialization, and supply-side accounts that emphasize the state's ability to make credible commitments against its own expropriation of corporate

34. Theda Skocpol, *Bringing the State Back In: Strategies of Analysis in Current Research*, *in* BRINGING THE STATE BACK IN 3, 9 (Peter B. Evans, Dietrich Rueschemeyer & Theda Skocpol eds., 1985).

35. Such synergy does not always exist; private education may or may not be an adequate substitute for the state's educational capacity, and a state with strong coercive capacities may or may not be one with strong military capacity.

assets.[36] These two accounts are not mutually exclusive. In recent scholarship, they have often merged into a single coherent theoretical framework.[37] Nonetheless, they are conceptually and logically distinct. Demand-side accounts focus on interregional trade and commercialization to argue that modern corporations were not needed in most premodern societies because family firms or forms of partnership were able to meet capital-investment needs.[38] It was only after socioeconomic demand for large-scale, long-distance, and long-term business investment ramped up in the early modern era, specifically through international maritime trade, that the modern corporate form truly became attractive to investors. Theories of state commitment argue, on the other hand, that modern corporations could not emerge without credible commitments from the state to refrain from expropriating corporate assets for its own purposes.[39] No matter how large the economic incentives created by long-distance trade, investors would not make use of the corporate form if they felt their assets were vulnerable to state expropriation.

While we do not deny that these demand- and supply-side conditions were essential for the emergence of the modern corporation, we argue that they are incomplete in two ways. First, the demand-side conditions must be laid out in more theoretically general terms to capture the modern corporation's continued appeal in activities that have little to do with long-distance trade. Whereas recent scholarship has persuasively identified long-distance trade sustained over long

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36. Guiseppe Dari-Mattiacci et al. and Ron Harris place heavy emphasis on long-distance trading as the crucial demand-side force. *See* Dari-Mattiacci et al., *supra* note 4; HARRIS, *supra* note 3. Harris also emphasizes the state's ability to make credible commitments as a necessary supply-side condition. *See* HARRIS, *supra* note 3, at 313-15. Timothy Guinnane et al. argue that the appeal of the corporation was, in its early history, largely limited to large-scale business operations. *See* Guinnane et al., *supra* note 8, at 688-90. Avner Greif and Guido Tabellini argue that the corporation emerged in commercial settings where business was largely conducted among strangers, of which long-distance movement of persons and goods was one of the most important examples. *See* Avner Greif & Guido Tabellini, *The Clan and the Corporation: Sustaining Cooperation in China and Europe*, 45 J. COMPAR. ECON. 1, 3, 27-28 (2017). A more comprehensive and theoretical demand-side analysis of one particular institutional feature—entity shielding—can be found in Hansmann et al., *supra* note 21. That article does not, however, go deeply into the supply-side politics and institution-building surrounding entity shielding. The large literature on law and finance, which takes much of its theoretical framework from Douglass North's New Institutional Economics, focuses on credible commitments. *See, e.g.*, Musacchio & Turner, *supra* note 4, at 529; Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert W. Vishny, *Law and Finance*, 106 J. POL. ECON. 1113 (1998); Douglass C. North, *The Evolution of Efficient Markets in History*, *in* CAPITALISM IN CONTEXT: ESSAYS ON ECONOMIC DEVELOPMENT AND CULTURAL CHANGE IN HONOR OF R.M. HARTWELL 257, 258 (John A. James & Mark Thomas eds., 1994).

37. *See, e.g.*, HARRIS, *supra* note 3; Dari-Mattiacci et al., *supra* note 4.

38. *See* HARRIS, *supra* note 3, at 1-2.

39. *See* North, *supra* note 36, at 258.

periods of time as the primary driver of corporate development in the early modern world,[40] modern firms make regular use of the corporate form even if they are not engaged in international or interregional trade. This implies that, even in the early modern context, long-distance trade was only one of many settings in which demand for the corporation became common. While existing scholarship has made some progress in identifying in general terms what these settings were,[41] it has yet to produce a systematic theoretical framework.

Second, and more importantly, preexisting accounts overlook the *positive* contributions of modern state-building to the corporate form. Their supply-side conditions generally portray the state as something to be safeguarded against—as a potentially predatory expropriator that needs to be institutionally chained. But this is only part of the story, and not necessarily the most important part. Modern states also contributed positively to corporate development by supplying the legal and administrative infrastructure necessary to enforce incorporation and investment agreements, so much so that the rise of modern corporations *depended*—and *continues* to depend—on modern state-building. In particular, it depended on the creation of professionalized judicial systems with strong informational and enforcement capacities.

As many studies have shown, there are virtually no significant examples of modern business corporations or their functional equivalents in premodern legal systems.[42] Instead, their emergence tended to follow the rise of modern states and the great expansion of formal administrative and judicial capacity those states engineered. But why?

Preexisting accounts, demand-side and supply-side alike, fail to answer this question fully. Demand-side accounts fall short because of the existence of clear and robust functional demand for modern corporate forms in several major premodern societies—demand that could not be met by the otherwise highly sophisticated customary legal systems that existed in those countries. Late imperial China is perhaps the best and most significant example of this: significant socioeconomic demand for modern corporate forms likely existed there centuries before the advent of modern state-building, but that demand was not substantively met until the state-building had begun in earnest.[43] Clearly, demand-side conditions alone cannot explain these bottlenecks.

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40. *See, e.g.*, Dari-Mattiacci et al., *supra* note 4; HARRIS, *supra* note 3.

41. *See, e.g.*, HARRIS, *supra* note 3, at 4 (characterizing the conditions as a "large-scale, multilateral, impersonal cooperation"); Dari-Mattiacci et al., *supra* note 4, at 195 (describing the conditions as the "permanent commitment of capital"); Greif & Tabellini, *supra* note 36, at 4 (arguing that corporations proliferated in situations where individuals were not connected through kinship ties).

42. *See, e.g.*, HARRIS, *supra* note 3, at 253 fig.9.1.

43. For further discussion, see *infra* Section II.A.

Supply-side accounts that are limited to credible-commitment theories likewise fall short for the straightforward reason that premodern regimes, by their very nature, generally *could* make fully credible commitments not to expropriate. This was again true in the case of China: the late imperial Chinese state that existed prior to 1912 was extremely weak in terms of fiscal capacity and administrative muscle and, as a result, had feeble coercive capabilities.[44] Private investors rarely had any reason to fear that the state would expropriate their business assets because the state simply lacked the administrative means to do so. In other words, the late Qing dynasty was both an era in which high levels of commercialization and growing integration within the global market created significant demand for modern corporate forms[45] *and* an era in which the state was generally too weak to expropriate private business assets. Despite the existence of both conventional demand- *and* supply-side conditions, the modern corporate form never became popular, even as the state seriously attempted to introduce the features of corporate law that should theoretically have enabled it.[46]

In its dependence on the power of a modern state, corporate law differs from other bodies of private law. As generations of law-and-economics scholars and sociologists have argued, much of private law, including core components of contract, tort, and property law, can be adequately sustained under many circumstances without significant state intervention and existed for centuries before the emergence of strong state apparatuses.[47] In many premodern societies, customary law has largely been up to the task of supplying these institutions. In contrast, the business corporation is a distinctly modern phenomenon.[48]

A chain of highly influential articles authored by Henry Hansmann, Reinier Kraakman, and others in the early 2000s, for example, identify entity shielding

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44. *See* ZHANG, *supra* note 31, at 5; Loren Brandt, Debin Ma & Thomas G. Rawski, *From Divergence to Convergence: Reevaluating the History Behind China's Economic Boom*, 52 J. ECON. LITERATURE 45, 66-70 (2014).

45. *See* William C. Kirby, *China Unincorporated: Company Law and Business Enterprise in Twentieth-Century China*, 54 J. ASIAN STUD. 43, 44 (1995).

46. *See id.* at 47. Greif and Tabellini argue that the success of clan-based businesses reduced demand for corporations throughout much of Chinese history. *See* Greif & Tabellini, *supra* note 36, at 34-35. This may have been true for certain periods, but it clearly did not apply to the late nineteenth and early twentieth centuries, when the capital-accumulation demands of industrialization had outpaced the ability of family firms to supply them.

47. *See, e.g.*, ELLICKSON, *supra* note 13, at 148-49. *See generally* POSNER, LAW AND SOCIAL NORMS, *supra* note 13, at 3 (examining the interaction between law and social norms); McAdams, *supra* note 13 (same); Bernstein, *supra* note 13 (same).

48. *See* HARRIS, *supra* note 3, at 251-55, 253 fig.9.1.

as a central feature of modern firms, and argue that entity shielding, unlike limited liability, cannot be created through contract but instead requires *law*.[49] The crux of their argument is that entity shielding, in order to be economically viable, must impose costs on the creditors of individual shareholders without first obtaining their consent. Such an arrangement is therefore more similar to property rights than contractual rights in that it requires external legal enforcement rather than internalized bargaining between interested parties.[50]

As compelling as this argument is, it does not explain why, historically, such external legal enforcement of asset-partitioning arrangements has almost exclusively come from formal state institutions as opposed to communal customs or social norms. As we argue below, customs and social norms are, in theory, fully capable of enforcing entity-shielding arrangements within certain social boundaries—and yet entity shielding only became a widespread institutional and economic phenomenon under the auspices of modern state-building in the eighteenth and nineteenth centuries.

In response to these gaps, we construct a theoretical framework that recognizes a more positive role for the state while also giving a more systemic account of demand-side conditions. Applying this framework to several major historical legal systems, we argue that it does a better job of explaining the general chronology of corporate institutions in early modern and modern history than preexisting theories. The demand- and supply-side conditions identified in those theories are not discarded but are instead folded into this model in a more theoretically distilled form.

C. *The Conditions of Demand for the Corporate Form*

1. *Economic Conditions*

The first step to building this theoretical framework is to understand when people begin to demand the corporate form. What sort of economic conditions must be in place before the corporate form becomes useful? Theorists of organization, including Ronald H. Coase and Oliver E. Williamson, argue that businesspeople are likely to organize their activities through a single business firm rather than a series of individual contracts whenever transacting inside of the

49. *See, e.g.*, Hansmann et al., *supra* note 21, at 1340-43; Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 390 (2000).

50. *See* Hansmann & Kraakman, *supra* note 49, at 390.

firm is cheaper than transacting outside of it.[51] That is, people are likely to use a business firm whenever it is easier to deploy resources through the hierarchical process of coordinated decision-making that characterizes corporations rather than through the market-based competition and negotiation that characterize individual contracting.

Williamson identifies three problems that often push people into firms over individual contracts.[52] "Asset specificity" forces business partners into a closed relationship in which one or more of them cannot end the relationship easily and move her resources elsewhere.[53] "Bounded rationality" prevents the parties from perfectly foreseeing the future and planning or contracting for it from the outset.[54] And "opportunism" motivates the parties to exploit these other problems for individual gain.[55] If one party cannot leave the relationship in response to future misconduct or foresee the future well enough to contract to prevent the misconduct, then the other party will be free to act selfishly in the future and to take more of the relationship's economic value. This risk of future misconduct will deter parties from entering long-term contracts in the first place.

Economic theory depicts the business corporation as a solution to these problems.[56] It provides a mechanism by which people can commit to each other over a long period of time and construct a framework of governance. Rather than writing a contract to address all future possibilities, the parties commit to a process for making decisions about future circumstances as they arise.

The legal technologies of the corporate form are part of this solution. Asset partitioning keeps resources committed, tradable shares reduce the cost of this commitment by making it possible to sell an interest in a firm while keeping the

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51. *See* R.H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 390-92 (1937); Oliver E. Williamson, *The Vertical Integration of Production: Market Failure Considerations*, 61 AM. ECON. REV. (PAPERS & PROC.) 112, 113-14 (1971). Many classic articles are collected in THE NATURE OF THE FIRM: ORIGINS, EVOLUTION, AND DEVELOPMENT (Oliver E. Williamson & Sidney G. Winter eds., 1991). For a summary of more recent literature, see Oliver Hart, *Thinking About the Firm*, 49 J. ECON. LITERATURE 101 (2011), which reviews DANIEL F. SPULBER, THE THEORY OF THE FIRM: MICROECONOMICS WITH ENDOGENOUS ENTREPRENEURS, FIRMS, MARKETS, AND ORGANIZATIONS (2009).

52. *See* OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM 30 (1985).

53. *Id.*

54. *Id.*

55. *Id.*

56. *See id.* at 273.

resources committed to the firm, and centralized management creates a process for resolving disputes and coordinating action.[57]

What kind of real-world economic conditions tend to produce high and durable levels of asset specificity, unforeseeability, and opportunism? The answer, in our view, is long-term collaboration between large numbers of strangers who share residual-claimant status over a business that engages in complex economic activity.[58]

To be clear, we define "strangers" as people who are socially distant from each other in the sense that they do not belong to the same closely knit social circles and therefore cannot rely on the interpersonal relations and informal social capital available to their members.[59] Greater social distances tend to produce higher levels of distrust between collaborators and greater levels of uncertainty, thereby exacerbating the problems of both opportunism and unforeseeability. These challenges of coordinating among strangers grow as the number of strangers increases.

"Residual claims," which are also known as "equity" or "profits interests," refer to claims that are unfixed and equal only to the value of an enterprise in excess of the value of all fixed claims against it. Residual claims are uniquely vulnerable to risk because of their unfixed and residual character, and they exist in all manners of joint-stock firms, from partnerships to corporations.[60]

"Complexity" refers to the density and difficulty of decision-making about the firm's business operations. Factors that make a business more complex include its duration, the physical distances across which it operates, and the num-

57. *See, e.g.*, HARRIS, *supra* note 3, at 251-55; STEPHEN M. BAINBRIDGE & M. TODD HENDERSON, LIMITED LIABILITY: A LEGAL AND ECONOMIC ANALYSIS 9-15 (2016); Dari-Mattiacci et al., *supra* note 4, at 199-200; Hansmann et al., *supra* note 21, at 1336; Thomas S. Ulen, *The Coasean Firm in Law and Economics*, 18 J. CORP. L. 301, 307-10 (1993); Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416 (1989); Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89 (1985). Notably, these "theories of the corporation" are closely tied with theories of incomplete contracting. *See, e.g.*, Ian Ayres, *Making a Difference: The Contractual Contributions of Easterbrook and Fischel*, 59 U. CHI. L. REV. 1391, 1395-97 (1992) (reviewing FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991)).

58. Several of these patterns, most notably distance and numerosity, have been identified in HARRIS, *supra* note 3, at 251-55; and Dari-Mattiacci et al., *supra* note 4, at 195.

59. On social proximity—and, by extension, social distance—and the idea of closely knit groups, see, for example, ELLICKSON, *supra* note 13, at 177-82; Lior Jacob Strahilevitz, *Social Norms from Close-Knit Groups to Loose-Knit Groups*, 70 U. CHI. L. REV. 359, 360-61 (2003); and Richard D. Alba & Charles Kadushin, *The Intersection of Social Circles: A New Measure of Social Proximity in Networks*, 5 SOCIO. METHODS & RSCH. 77, 85-98 (1976).

60. *See* Eugene F. Fama & Michael C. Jensen, *Agency Problems and Residual Claims*, 26 J.L. & ECON. 327, 329-31 (1983).

ber of different transactions and decisions it involves. Complexity is a major determinant of unforeseeability: shipping food over a thousand miles is a less foreseeable task than shipping it over ten miles, and manufacturing goods with a complicated supply chain can be even less foreseeable.

Long-distance trading sustained over long periods of time—the demand-side context that has drawn the lion's share of attention in recent scholarship—is a paradigmatic example of a situation that presents these conditions: the amount of capital needed to power long-distance trade, coupled with the physical distance, often required collaboration between large numbers of strangers who held residual-claimant status over firm assets.[61] Moreover, sustained long-distance trade naturally involved a great amount of financial and logistical complexity, both because of the time it took and because of the density of decision-making it required—it was, in other words, an inherently complex activity. That said, long-distance trade is not the only situation in which demand for the corporation might grow. This is clear from the experience of modern economies, which use the corporate form for myriad uses well beyond long-distance trade.

2. *The Inadequacy of Communal Institutions*

Our argument that the business corporation relied and still relies on the modern state must be understood within the context of these demand-side conditions. It is precisely because the business corporation was designed to coordinate economic activity under conditions of high unforeseeability that modern state-building was required to sustain it. There is no obvious supply-side theoretical reason why a modern business corporation composed of mutually acquainted investors within a closely knit community cannot function properly, even in the absence of a functionally modern state or a modern court system, but the point is that mutually acquainted investors within a closely knit community would likely neither need nor want to structure their collaboration within a modern business corporation. Significant socioeconomic demand for the corporate form tends to emerge only in conditions where large numbers of strangers are attempting to collaborate on long-term, complex economic activities. Under such conditions, robust state-driven rule enforcement and information sharing are theoretically necessary, which, in turn, necessitates effective state-building.

The business corporation has never been popular where the activities and owners of businesses are confined to small, closely knit communities, as they were in much of the premodern world. This is not because closely knit communities are incapable of creating and sustaining complex law-like institutions and

61. *See* HARRIS, *supra* note 3, at 263-67; Dari-Mattiacci et al., *supra* note 4, at 201-03.

rights within their own social and geographical boundaries. As a rich interdisciplinary literature on social norms has exhaustively argued, closely knit communities across the world have created these institutions in contracting, property rights, and torts since ancient times.[62] In particular, closely knit merchant or entrepreneur communities across the premodern and early modern world sustained business entities that modern legal scholars would recognize as variations of partnerships: firms with clear governance structures and joint-stock equity finance, and sometimes with separate legal personalities and investment lock-in.[63] What these entities tended to lack were asset-partitioning institutions—strong entity shielding for the firm and limited liability for investors—and the free transferability of shares.[64]

This does not mean, however, that community institutions were functionally *incapable* of recognizing and enforcing asset partitioning. As a kind of in rem right akin to a property rule, asset partitioning is not intuitively any more difficult to recognize and enforce than, for example, real covenants that run with the land: both are enforceable against unspecified third parties that were not privy to the original agreement. Covenants that run with the land are enforceable against unenumerated future landowners who had no say in the initial negotiation of the covenant, whereas entity-shielding agreements are enforceable against unenumerated future creditors who had no say in the initial partitioning of firm and shareholder assets. The core functional challenges of either arrangement—most importantly, the need to give reasonable notice to uninformed third parties—are broadly similar. A large academic literature has demonstrated that premodern communal customs and social norms across the globe had no visible difficulty enforcing covenants that run with the land or nearly any other form of property right in land, and indeed did so with great sophistication.[65] It therefore seems rather likely that these institutional entities also possessed the capacity to enforce asset-partitioning agreements within their own territorial jurisdiction.[66]

62. Quite a bit of this history is distilled and summarized in ELINOR OSTROM, GOVERNING THE COMMONS: THE EVOLUTION OF INSTITUTIONS FOR COLLECTIVE ACTION (1990). For specific applications to private law, most notable to property law, see sources cited *supra* note 47.

63. *See* HARRIS, *supra* note 3, at 253 (summarizing the chronology).

64. *See id.*

65. For examples of complex property rights, including multilayered covenants that ran with the land, being enforced in premodern customary law, see TAISU ZHANG, THE LAWS AND ECONOMICS OF CONFUCIANISM: KINSHIP AND PROPERTY IN PREINDUSTRIAL CHINA AND ENGLAND 12-13 (2017); and ERIC KERRIDGE, AGRARIAN PROBLEMS IN THE SIXTEENTH CENTURY AND AFTER 81-85 (1969).

66. The functional similarities between asset partitioning and covenants that run with the land can be observed in the analysis applied by Hansmann et al., *supra* note 21, at 1356-1402, on the

This suggests that the general absence of asset-partitioning arrangements in premodern customary law likely stemmed from the *lack of demand* within closely knit communities rather than from a lack of rule-enforcement capacity. There are strong theoretical reasons to believe this. Asset partitioning, in both its entity-shielding and investor-shielding forms, is essentially a mechanism that shifts risk from investors to creditors, including both voluntary contractual creditors and involuntary tort creditors,[67] and therefore comes with the downsides of both higher borrowing costs and potentially significant third-party social externalities.[68] Within closely knit communities, the financial risks of business collaboration are typically much lower than what they would be in stranger-oriented societies because collaborators tend to be well informed about each other's economic circumstances.[69] The benefits of shifting risk onto third parties—either contract creditors or potential tort creditors from society at large—are, therefore, substantially lower.

Moreover, under such conditions, engaging in asset partitioning despite the lower benefits sends a more negative signal to potential creditors, especially to institutionalized lenders from outside the community, about discord and distrust among investors than it would in a stranger-dominated market, potentially leading to even higher borrowing costs.[70] In other words, firms may well face higher costs for pursuing asset partitioning in closely knit communities than they would in stranger-oriented ones. This combination of substantially lesser benefits with potentially higher costs makes it quite unlikely that asset partitioning would have been strongly attractive to groups of joint-stock investors within the same closely knit community.

Note that the previous paragraph does not claim that there should be *no* demand for asset partitioning in closely knit communities. The fact that many modern corporations are closely held indicates that there can be such demand.[71] Business owners can face many idiosyncratic circumstances—social schisms,

former, and Henry Hansmann & Reinier Kraakman, *Property, Contract, and Verification: The* Numerus Clausus *Problem and the Divisibility of Rights*, 31 J. LEGAL STUD. 373, 374, 405-06 (2002), on the latter.

67. "Tort creditors" refers to third parties who are legally entitled to damages due to the firm's conduct. That is, they are people the firm commits a tort against.

68. *See* Hansmann et al., *supra* note 21, at 1351-54; BAINBRIDGE & HENDERSON, *supra* note 57, at 48-51.

69. On cooperation in closely knit communities, see sources cited *supra* note 41.

70. Essentially, it would send a signal that investors expect relatively large amounts of unpredictability and risk in the business's foreseeable future, significantly beyond what normal closely held firms in closely knit communities would experience.

71. *See* ROBERT A. RAGAZZO & DOUGLAS K. MOLL, CLOSELY HELD BUSINESS ORGANIZATIONS: CASES, MATERIALS, AND PROBLEMS 1-2 (2006); George D. Hornstein, *Stockholders' Agreements in the Closely Held Corporation*, 59 YALE L.J. 1040, 1040-41 (1950).

personal uncertainties, and so on—that make asset partitioning *somewhat attractive* even when the firm is held and operated within a limited socioeconomic circle. The question is whether it is *attractive enough* to warrant the kind of societal investment needed to make asset partitioning work as a publicly available institution.

Our claim here is, strictly speaking, a comparative one: in theory, there is significantly *less* demand within closely knit communities than there is beyond or between them. Given that, first, scholars have found little evidence of asset partitioning in premodern closely knit communities, and, second, there is no good supply-side reason why those communities could not have enforced such institutional arrangements, even a weaker, relative claim goes a very long way toward explaining why the widespread adoption of this legal technology was a modern phenomenon that first emerged in business collaboration that extended well beyond the geographical and social boundaries of closely knit communities.

Of course, one might wonder why the business owners who do desire some form of asset partitioning do not simply draw up their own limited-liability and entity-shielding agreements, with or without the institutionalized consent of the broader community. The problem here is that, as Hansmann and others have argued, entity shielding in particular cannot be established through contract but instead requires the functional equivalent of "law."[72] More precisely, it requires a top-down institutional guarantee from an authorized rule maker that the future creditors of shareholders will not be able to force the company to liquidate its assets for debt payment.[73] Given the indeterminate number of such future creditors, entity shielding functionally resembles property rights of exclusion, and it requires the same level of coordinated rights protection as property ownership.

Therefore, entity shielding can emerge not simply whenever a few business owners find it moderately desirable but only when *aggregate* socioeconomic demand for it becomes powerful enough to persuade the entire community—or whatever entity has authority and power to recognize and enforce property rights in that part of the world—that it is needed. Specifically, the community must be persuaded that, societally, the potential benefits to risk-averse investors are substantially more valuable than the socioeconomic externalities imposed on contract and tort creditors. This is a far higher demand-side burden that is much less likely to be satisfied within most closely knit communities.[74]

72. *See* Hansmann et al., *supra* note 21, at 1340-43; Dari-Mattiacci et al., *supra* note 4, at 200.

73. *See* Hansmann et al., *supra* note 21, at 1338, 1340.

74. Given the functional similarities between entity shielding and property rights discussed in these paragraphs, one might wonder why, as a matter of theory, we should expect there to be demand for property rights in closely knit communities, even when we do not expect there to

Limited liability is a different story. Technically, it can be created simply through a contract between the firm and its investors, although the willingness of states or communities to enforce such contracts is hardly guaranteed.[75] In practice, owner shield provisions are, of course, far more effective when rule makers affirmatively agree to recognize and enforce them. As discussed in a few of the case studies below, we do see evidence that weak limited-liability arrangements were irregularly used in some premodern businesses, but we find virtually no evidence of strong entity-shielding arrangements prior to the advent of modern state-building.[76]

The situation is very different in stranger-oriented business relationships, where business partners do not belong to the same closely knit, information-sharing community. There, the information barriers between partners are often much higher and the risks correspondingly larger. This greatly enhances the incentive to shift financial risk onto third-party creditors, who may have stronger institutional tools to price and digest risk because of their ability to charge inter-

be demand for entity shielding. This question is probably best reserved for a future article, but the most obvious explanation, which we find compelling, is that the nature of risk is different in a standard property relation than in a standard entity-shielding relation. Property rights, whether a standard right of exclusion or a covenant that runs with the land, safeguard rights against completely unforeseeable third parties—potential trespassers or future owners of the land. That is their primary and often sole purpose. While entity shielding is also enforceable against unforeseen third parties—namely, future creditors or shareholders—those third parties are only made relevant by future actions of the shareholders, who are parties to the initial investment agreement that created the entity-shielding arrangement in the first place. In other words, the true substantive purpose of an entity-shielding agreement is to safeguard against future behavior by *parties to the transaction* instead of *unforeseeable third parties*. As a result, the level of risk that conventional property rights deal with is, in this theoretical formulation, inherently higher than the level of risk that entity-shielding relations deal with. There may, therefore, be robust social demand for the former even when there is only limited demand for the latter, and we suspect that most closely knit communities fit this description. Even the most closely knit of community members cannot always predict what future generations or outside trespassers might want to do with their property holdings, which creates institutional demand for conventional property rights. In contrast, as long as a business firm is only constituted within the community, shareholders may well feel no particularly strong need to safeguard against future behavior by fellow communal shareholders through entity shielding. This is, of course, a line of argument that needs to be fleshed out much more carefully in future work, and for now it serves only as an intellectual stopgap. On the kinds of risk and information costs inherent in property relations, see Henry E. Smith, *Exclusion Versus Governance: Two Strategies for Delineating Property Rights*, 31 J. LEGAL STUD. 453, 464-67 (2002); and Taisu Zhang, *Beyond Information Costs: Preference Formation and the Architecture of Property Law*, 12 J. LEGAL ANALYSIS 1, 14-19 (2020).

75. *See* Hansmann et al., *supra* note 21, at 1340-43.

76. These are found in the Chinese and Ottoman case studies. *See infra* Sections II.A & II.B; *see also* HARRIS, *supra* note 3, at 251-74 (summarizing the relevant history).

est. As a result, we should expect significantly greater demand for asset-partitioning legal technologies in business relationships that cover greater social and geographical distances. Because such relations generally extend beyond the boundaries of any single closely knit community, their rule-enforcement and dispute-resolution needs likewise extend beyond the institutional capacities of communal customs and social norms.

As discussed in greater detail below, this was indeed broadly true in the premodern world: contractual agreements that resembled asset partitioning were familiar to long-distance traders as early as the Roman Republic and, following the fall of the Western Roman Empire, again from the eighth century onward. They were generally employed in many investment agreements between suppliers of goods and the merchants who shipped and sold them.[77] These early asset-partitioning-like arrangements, however, should not be confused with modern corporations. They lacked the socioeconomic features such as numerosity, long duration, and complexity that are functionally central to corporations. The medieval *commenda* employed in Mediterranean commerce, for example, involved agreements between a limited set of merchants and goods suppliers that were limited to only one voyage and dissolved upon the voyage's conclusion.[78] In terms of the complexity of the underlying economic relationship, they were closer to employment contracts than to modern firms. Modern business corporations, in contrast, are designed to last for the long term and incorporate large numbers of investors.

In summary, as a matter of theory, business relations within closely knit communities are unlikely to produce robust *demand* for asset-partitioning technologies. Closely knit communities are quite capable of *supplying* those technologies within their own boundaries, but they tend to lack strong incentives to do so. The tables are flipped in socially or physically distant business relations. There, business partners have ample incentives to demand these technologies, but they can no longer rely on communal custom as their primary source of rule enforcement. They must, instead, seek out entities capable of enforcing rules and contracts *between strangers*. The very limited application of asset partitioning in premodern interregional commerce suggests that they did not have much success in doing so. The next Section explains why.

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77. *See* sources cited *supra* note 10.

78. *See* Yadira González de Lara, *Business Organization and Organizational Innovation in Late Medieval Italy*, *in* RESEARCH HANDBOOK ON THE HISTORY OF CORPORATE AND COMPANY LAW 65, 71-77 (Harwell Wells ed., 2018); Yadira González de Lara, The Impact of Formal Monitoring on Financial Innovation from Debt to Equity in Late Medieval Venice 9-12 (Oct. 2017) (unpublished manuscript), https://www.unige.ch/sciences-societe/dehes/files/8615/0713/5354/sar_fall_2017_gonzalez_monitoring_financial_innovation_venice.pdf [https://perma.cc/R88H-2433].

Before moving on, we should note that asset partitioning is not the only corporate legal technology that is, in theory, primarily limited to stranger-oriented relationships. That description also applies to share transferability—which, in its stronger forms, allows investors to transfer their shares to third parties without the consent of their fellow investors. We do not develop the share-transferability argument in great detail simply because, as many have observed, share transferability is functionally reliant on asset partitioning: without asset partitioning, free share transferability would impose too much risk on existing shareholders.[79]

D. The Role of State Institutions

Once we are in the realm of stranger-oriented economic activity, the potential sources of legal or quasi-legal regulation become much more limited. When business partners are recruited from beyond a single community, a larger, more expansive lawmaking and law-enforcement entity is required, one that crosses communal and regional boundaries. Early modern human history contains two prominent examples of such entities: the state, as it was beginning to expand its administrative and legal capacity, and self-regulatory interregional commercial networks, such as the Law Merchant.[80] The contrast between the two represents the modern ideological clash between a top-down regulatory state and bottom-up self-regulation by economic actors—bureaucracy versus the market, to some extent.

This Section argues that, of these two options, only the former could adequately provide institutional support for the business corporation. We make this argument in three steps. First, we identify some of the specific institutional demands that the corporation makes of legal systems, focusing primarily on legal uniformity. Second, we give some theoretical reasons why interregional regula-

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79. *See* Hansmann et al., *supra* note 21, at 1350.

80. *See, e.g.*, Emily Kadens, *The Medieval Law Merchant: The Tyranny of a Construct*, 7 J. LEGAL ANALYSIS 251, 253-71 (2015) [hereinafter Kadens, *The Medieval Law Merchant*]; Emily Kadens, *The Myth of the Customary Law Merchant*, 90 TEX. L. REV. 1153, 1153-61 (2012) [hereinafter Kadens, *The Myth of the Customary Law Merchant*]; HAROLD J. BERMAN, LAW AND REVOLUTION: THE FORMATION OF THE WESTERN LEGAL TRADITION 341-44 (1983); A. CLAIRE CUTLER, *Medieval* Lex Mercatoria, *in* PRIVATE POWER AND GLOBAL AUTHORITY: TRANSNATIONAL MERCHANT LAW IN THE GLOBAL POLITICAL ECONOMY 108-40 (2003); ANA M. LÓPEZ RODRÍGUEZ, LEX MERCATORIA AND HARMONIZATION OF CONTRACT LAW IN THE EU 87 (2003); RUDOLF B. SCHLESINGER, HANS W. BAADE, PETER E. HERZOG & EDWARD M. WISE, COMPARATIVE LAW: CASES, TEXT, MATERIALS 278 (6th ed. 1998); Robert D. Cooter, *Decentralized Law for a Complex Economy: The Structural Approach to Adjudicating the New Law Merchant*, 144 U. PA. L. REV. 1643, 1647 (1996).

tory networks like the medieval Law Merchant were unable to meet those demands. Finally, we explain why modern states could succeed where decentralized, network-based regulation failed.

1. The Value of Uniformity

The regulation of business relations between strangers across communities and regions requires a few basic capacities. First, given the assumption of social and physical distance, the regulator must cover a relatively large geographical territory. Second, it must be able to impose some measure of rules-based standardization within that territory and to reliably enforce the law against most private parties, regardless of communal affiliation. In other words, it must be able to implement some degree of legality.[81] Third, it must be capable of extracting necessary information from groups of socially unconnected business actors and sharing it within that group, so that there can be some informational basis of mutual trust and collaboration between strangers—think, for example, of disclosure rules and centralized recordkeeping institutions in securities law[82] or in real-estate transactions.[83] The functional necessity of these capacities is fairly obvious and is not limited to the corporate context. Without them, it is hard to imagine how *any* intercommunal regulation of private economic activity, whether in contract, property, or tort, is possible.

Beyond these three capacities, we identify a fourth institutional capacity that is somewhat more specific to the corporate context: the intercommunal regulatory entity must be able to provide relatively strong and credible guarantees to potential investors that they will be treated *uniformly* by the law-enforcement apparatus regardless of their social affiliations. The legal technologies of the corporate form mean little if they are not reliably enforced against every owner and the people with whom they might contract.

A corporation is unique among modern economic arrangements in its tendency to bring large numbers of people together into shared residual claims on a common pool of resources. Under these conditions of highly multilateral cooperation, uniformity is immensely important. To be clear, by uniformity, we do not mean the uniformity of corporate law across geographical regions, nor do we mean the completely identical treatment of corporate shareholders. The claims

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81. When scholars have argued for the possibility of "order without law," they do so almost exclusively in closely knit societies. *See* ELLICKSON, *supra* note 13, at 123, 284.

82. For a general discussion of social disclosure laws, see Barnali Choudury, *Social Disclosure*, 13 BERKELEY BUS. L.J. 183 (2016).

83. *See* Benito Arruñada & Nuno Garoupa, *The Choice of Titling System in Land*, 48 J.L. & ECON. 709, 712-25 (2005).

that owners have on a corporation can vary widely. Some owners may have larger stakes than others; others may have stronger control rights than others, and so on.

What we mean by "uniformity" is therefore less about perfectly identical treatment than about the sort of fairness that is known in the Anglo-American common law of trusts as "impartiality."[84] The duty of a trustee to treat beneficiaries impartially requires the trustee to treat each beneficiary in accordance with the terms of the trust and with due regard for his or her legal interests. In a trust, a beneficial interest can take a limitless variety of forms. The duty of a trustee, therefore, is not to treat all beneficiaries identically but to treat them all fairly and consistently within the terms of the trust. Similarly, a corporation must treat its shareholders fairly and consistently *within the terms of its incorporation documents*.

Nonuniformity can occur in a variety of ways. It can occur when a patron is allowed either to give too little or to take too much. And it can result from underenforcement against a patron or overenforcement against another. It can also result from differences in the substance of the law. One patron might be subject to one law and another to a different law, and if these differences are not predictable and consistent enough to be the subject of advance bargaining, they can end up treating owners nonuniformly.

A lack of uniformity can be a problem for any commercial relationship, but it is especially problematic for a corporation.[85] The owners of a corporation are more numerous than the parties to a conventional bilateral contract. A corporation involves large-scale multilateral dealing by large numbers of people unknown to one another, making the risk of nonuniform treatment more serious than if the business had only a small number of owners. Though a bilateral contract also requires uniformity among the parties, the smaller number of parties involved reduces the risk of nonuniformity.

Additionally, in a corporation, the people we call owners all have a claim on the same pool of assets. They share in common rather than being granted specific interests in specific items of property. Moreover, the claims they share do not carry fixed values, such as the wage paid to a worker or the price paid to a supplier. Instead, owners take a mere portion of what is left over after other claimants have been paid. The claim of an owner is thus uniquely sensitive to inequities of treatment. Claims among owners are zero-sum, and they can be

84. RESTATEMENT (THIRD) OF TRUSTS § 79 (AM. L. INST. 2007).

85. This concept of uniformity is closely related to the work of Henry Hansmann, who has identified the immense costs associated with heterogeneity among a corporation's owners. *See* HENRY HANSMANN, THE OWNERSHIP OF ENTERPRISE 40, 98, 140, 144 (1996).

immediately diminished by nonuniform treatment. More money for one owner automatically means less for each of the others.

To see why uniformity is so important, consider how it underpins most of the key legal technologies that make up the corporate form. Centralized management involves the consolidation of authority to make commitments for a firm to a small group of designated managers. In a twenty-first-century American corporation, this group is the board of directors.[86] Centralized management is important because it prevents the firm from being pulled into pieces by a scattering of unpredictable owners who make commitments and incur liabilities inconsistently with a common plan. Centralized management presupposes uniformity almost as a matter of definition. If inconsistent enforcement of the law allows some owners to make commitments arbitrarily against the wishes of the central managers, then management is not truly centralized.

Uniformity is also important to entity shielding. Entity shielding must be uniform to be effective because, as Hansmann and Kraakman have shown, it operates as a kind of property right.[87] It affects the rights not merely of a corporation's owners but also of all those creditors who might have claims against them. The contract that limits the claims of a shareholder over the assets of, say, General Motors must bind not only that shareholder but also his credit-card lenders, mortgage lender, and tort claimants. Such far-reaching legal effects require far-reaching legal enforcement capacity and equally expansive legal uniformity, lest information costs grow overwhelmingly large.

The tradability of shares, too, depends on uniformity. It is not essential that every owner uniformly be able to trade her shares. But it is important that when an owner does trade, the law can be counted upon to hold anyone who might buy the shares to the terms of the existing corporate bargain. Existing shareholders cannot allow shares to be sold if the bargain of the corporation will not remain intact or will be enforced unevenly against potential buyers. Uniformity is essential because the technology of tradable shares presupposes equal treatment of all shareholders, regardless of whether they purchase, sell, or hold.

2. *The Limitations of Network-Based Alternatives*

Achieving uniformity without top-down state regulation is extremely difficult. For quite some time, scholars believed that the existence of an interregional Law Merchant made interjurisdictional commerce possible in medieval and early

86. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141 (2022) (granting the power to manage a corporation's business and affairs to the board of directors).

87. *See* Hansmann & Kraakman, *supra* note 49, at 391-93.

modern Europe,[88] as it provided a set of uniform rules for commercial activity that transcended regional differences and was enforced by legal tribunals capable of adjudicating disputes between geographically distant parties. This Law Merchant was purportedly the achievement of a bottom-up synthesis of communal customs and norms.

Recent scholarship has, however, debunked much of this traditional view, demonstrating that what we call the Law Merchant was instead a decentralized network of brokers, middlemen, and local laws and norms that lacked both substantive and adjudicative uniformity.[89] More precisely, it was a collection of local legal authorities – a patchwork of formal legal systems with limited geographical and social reach and local commercial communities enforcing their own rules and norms – tied together through networks of brokers, agents, and arbitrators who played the triple role of introducing outsiders to local rules, negotiating terms between them, and helping local authorities to enforce the ensuing contract.[90] Through these legal networks, merchants from different regions and jurisdictions could reliably enter into and enforce contracts, generally by placing them within a single, mutually agreed-upon jurisdiction and applying the substantive and procedural rules of that jurisdiction.[91]

While such networks were capable of sustaining fairly robust interregional commerce, they had some obvious limitations. First, the reliance on intermediaries limited both the scale and the complexity of interregional collaboration. Interregional collaboration between strangers depended on the parties being able to establish a baseline of mutual trust through local agents and brokers. The height of this baseline, however, depended on what kind of collaboration was being negotiated. Contractual arrangements involving short-term, single-transaction exchanges with simple and easily predictable outcomes and straightforward enforcement mechanisms required much lower levels of trust than complex and long-lasting activities that potentially involved large uncertainties. Moreover, the larger the number of outsiders involved and the more diverse their geographical distribution, the more difficult it would have been for them to find a collection of mutually trusted intermediaries.

For each of these reasons, although interregional merchant law networks were reasonably competent at enforcing *contracts* between limited numbers of strangers, including those that created single-voyage joint ventures such as the

88. *See* sources cited *supra* note 80.

89. *See* Kadens, *The Medieval Law Merchant*, *supra* note 80, at 274-75; Kadens, *The Myth of the Customary Law Merchant*, *supra* note 80, at 1160.

90. *See* Kadens, *The Medieval Law Merchant*, *supra* note 80, at 274; Kadens, *The Myth of the Customary Law Merchant*, *supra* note 80, at 1154.

91. *See* Kadens, *The Medieval Law Merchant*, *supra* note 80, at 278-81.

commenda,[92] they were largely incapable of supporting the formation of *firms* between strangers, let alone something as complicated as a long-lasting business corporation with many unfamiliar owners.

Moreover, interregional networks, anchored in collections of self-regulating communities, almost certainly had great difficulty making credible commitments to treating all investors in a business firm the same. Closely knit communities cannot, in general, make this kind of credible commitment. When the foundation of governance and rule enforcement is mutual trust built through complex social interaction, it is very difficult to treat outsiders and insiders the same. In addition, even when a community internally commits to equal treatment, it will inevitably struggle to convince outsiders that this commitment is trustworthy. Outsiders, by definition, have no social basis for trusting insiders, or vice versa, which makes it difficult to persuade outsiders that they will be guaranteed equal and uniform treatment by a regulatory community to which they are socially unconnected.[93]

Merchant law networks were able to solve this problem for relatively simple economic transactions by linking outsiders and insiders via brokers and other middlemen, but they were unable to do so for business corporations with complicated, long-lasting activities and numerous unfamiliar owners. As Emily Kadens notes, "Medieval merchants needed more protection than private ordering could afford them, and they looked for it in government intervention."[94] The solution to the trust deficit that interregional, stranger-oriented commerce inherently carried was not the Law Merchant but rather state-building.

3. *The Capacity of Modern States to Achieve Uniformity*

Modern states were much more capable of treating strangers uniformly. A modern state is more capable than a premodern state of forcing people subject to its power to conform to its dictates. This power could encourage uniformity by stopping a corporation's many owners from avoiding the terms of the corporate bargain by refusing to comply. A modern state's administrative capacity ensured that owners would not be forced to contribute too much or allowed to contribute too little by virtue of the state's excesses or blunders.

92. *See* Kadens, *The Myth of the Customary Law Merchant*, *supra* note 80, at 1167. *See generally* Pryor, *supra* note 9 (describing the development of the *commenda* as a pragmatic system of borrowing contract features from other proven contracts).

93. *See generally* Robert K. Merton, *Insiders and Outsiders: A Chapter in the Sociology of Knowledge*, 78 AM. J. SOCIO. 9 (1972) (describing ideological differentiation between socially connected insiders and unconnected outsiders, along with the mutual distrust this creates).

94. Kadens, *The Medieval Law Merchant*, *supra* note 80, at 278.

A modern state also has a geographical reach that extends across many social communities and a land area large enough to encompass complex economic activities of long duration and enterprises with many unfamiliar owners. This geographical reach assured uniformity even among owners who may not have been part of the same small communities of trust.

A modern state also has a formalized and institutionalized organization. A modern state tends to be impersonal—in sociological terms, it leans more toward *gesellschaft* (a society of unconnected or loosely connected individuals) than *gemeinschaft* (a community of closely connected persons).[95] It is usually centered around the monopolization of violence and coercive power by a single political entity, which then wields its authority in relatively institutionalized ways simply due to the size and reach of the state.[96] This gives it certain qualities—formalization, institutional predictability, and transparency—that help it make credible commitments to both political insiders and outsiders. In particular, under the right institutional circumstances, it can credibly commit through legislation and rulemaking to treating business investors, including noncitizens, equally and professionally before the law, regardless of their sociopolitical status.

These kinds of commitments are not the same kinds of credible commitments commonly seen in the preexisting academic literature. The latter commitments, as noted above, tend to be purely negative in nature: the state credibly commits to not arbitrarily expropriating firm assets, either through taxation or outright seizure.[97] The credible commitments we discuss here, in contrast, are positive ones: credible commitments to supply certain services—specifically, equal and effective enforcement of shareholder rights and obligations—to firm investors.

That said, both kinds of credible commitments rely on the likelihood that the public, or some portion of it, can hold the state to its promises. As an enormous scholarly literature has argued, the state can increase this likelihood

95. For a discussion of these classic concepts, which were core to the early development of modern sociology, see Kamenka, *supra* note 16. Basically, the concepts posit the existence of two ideal types of social organization: "societies" versus "communities." The former refers, more or less, to modern societies in which individuals are not organized into tightly knit, self-regulating communities. The latter refers primarily to a premodern world in which such communities account for the bulk of interpersonal interaction.

96. *See generally* WEBER, *supra* note 27 (characterizing the state as holding a monopoly of coercive power over actors in its territory); Grimm, *supra* note 27 (similar).

97. *See, e.g.*, La Porta et al., *supra* note 36, at 1140; North, *supra* note 4, at 19-21.

through institutionally constraining itself: separation of powers, constitutionalism, democracy, legislative transparency, and so on.[98]

However, such mechanisms are unable to produce fully credible commitments by themselves. They require high levels of professionalization and rationalization within the state apparatus, especially in its legal components.[99] This is something that is at least as important to modern states as, say, separation of powers or democratic accountability: compared to their early modern or medieval predecessors, successful modern states exercise considerably stronger control over their lower-level agents and invest greater resources in training those agents to behave professionally and predictably.[100] Once these conditions are in place, as long as high-level lawmakers and policymakers can credibly commit to equal treatment of shareholders, then the entire law-enforcement apparatus can credibly claim to faithfully carry out those commitments. Combined, credible commitment at the top and faithful implementation at the bottom are theoretically capable of producing a legal system that treats all shareholders equally regardless of their sociopolitical connections and, just as importantly, can persuade potential investors of that fact.

The two kinds of commitments discussed here – negative and positive – not only coexist as necessary conditions for the corporate form but can also mutually reinforce. The state's ability to make negative credible commitments depends on the central leadership's ability to control its local agents: a commitment by high-level officials to not expropriate, however genuine, is not economically significant if local government offices can still expropriate through their own administrative decisions. Positive state-building enhances the state's ability to make negative commitments by strengthening its ability to control local agents.

On the other hand, negative state commitments also enhance the state's positive capacities by boosting the willingness of private parties to cooperate. A state that can only rule through coercion is almost certainly a very limited one, capable

98. *See, e.g.*, Frye, *supra* note 4, at 453-66; North & Weingast, *supra* note 4, at 804. *See generally, e.g.*, DARON ACEMOGLU & JAMES A. ROBINSON, WHY NATIONS FAIL: THE ORIGINS OF POWER, PROSPERITY, AND POVERTY (2012) (connecting national poverty and discontent to a lack of mechanisms for popular control of the state).

99. *See* NIKLAS LUHMANN, A SOCIOLOGICAL THEORY OF LAW 73-83 (Martin Albrow ed., Elizabeth King-Utz & Martin Albrow trans., 2d ed. 2014); Max Weber, *The Three Types of Legitimate Rule*, 4 BERKELEY PUBL'NS SOC'Y & INSTS. 1, 1-11 (Hans Gerth trans., 1958).

100. Weber, for example, argues that "rational" control of agents through law is a hallmark of modern states. Weber, *supra* note 99, at 2. *See, e.g.*, MATTHEW FLINDERS, THE POLITICS OF ACCOUNTABILITY IN THE MODERN STATE 1-27 (2001); ERIKA CUDWORTH, TIM HALL & JOHN MCGOVERN, THE MODERN STATE: THEORIES AND IDEOLOGIES 20-34 (2007) (identifying professionalization as one theory of modern state development); 2 MICHAEL MANN, THE SOURCES OF SOCIAL POWER 44-91 (2d ed. 2012).

of enforcing only a small range of commands.[101] Truly competent state apparatuses govern through a much larger range of institutional tools, most of which require some level of cooperation from private actors, which in turn depends on their willingness to trust the state's expressed commitments. In the context of business corporations, the willingness of owners to accept state arbitration and enforcement—critical components of the state's ability to support corporate organization—depends significantly on the owners' belief in the state's legal and economic neutrality, including their confidence that the state will not attempt to expropriate corporate assets. Positive empowerment and negative constraining of state capacity are deeply symbiotic.

This is not to say that the state's abilities to commit positively and negatively are always synchronized. For example, a state could conceivably make fully credible negative commitments simply by depriving itself of coercive power—this was, in fact, more or less what happened in nineteenth-century China.[102] This would also demolish its local law-enforcement capabilities and thereby render it unable to make positive commitments of uniform legal treatment, but it would at least remove any socioeconomically salient threat of arbitrary state expropriation. Nonetheless, insofar as the state wishes to preserve its coercive power and make credible negative commitments *at the same time*, then positive modern state-building becomes a significant asset: institutionalized and formalized power poses less threat to private investment than discretionary and arbitrary power.

All in all, the modern state's ability to credibly commit to equal legal treatment of investors, combined with its substantial informational and enforcement advantages across large, socially unconnected territories, allows it to support the formation and operation of business corporations by large groups of strangers. This is something that premodern legal or customary systems generally could not provide. Therefore, the rise of modern states should, in theory, precede and facilitate the widespread use of modern business corporations.

It is important to emphasize again that the rise of a modern state and the uniform administration of the law were by no means the *only* conditions necessary for the rise of the modern corporation. The corporation depended on many other developments as well. Indeed, the conditions for the rise of the corporation

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101. Although this claim is intuitive, there have been several recent attempts to empirically lay out its finer mechanisms. *See, e.g.*, Hanne Fjelde & Indra De Soysa, *Coercion, Co-optation, or Cooperation?: State Capacity and the Risk of Civil War, 1961-2004*, 26 CONFLICT MGMT. & PEACE SCI. 5, 5-25 (2009); Jan Nederveen Pieterse, *Metamorphoses of Power: From Coercion to Cooperation?*, 33 ASIAN J. SOC. SCI. 4, 4-22 (2005); Peter J. May & Raymond J. Burby, *Coercive Versus Cooperative Policies: Comparing Intergovernmental Mandate Performance*, 15 J. POL'Y ANALYSIS & MGMT. 171, 171-201 (1996).

102. *See infra* Section II.A.

are almost certainly innumerable. They range from cultural values to technological innovations, political stability, and the accumulation of capital. They include both the demand-side economic conditions and the negative credible commitments discussed above. Our goal in this Article is not to downplay these other conditions but merely to add to them. We simply aim to show that a list of the many conditions necessary for the rise of the corporate form ought to include the formalized power of a modern state.

II. HISTORICAL CASE STUDIES

The basic historical contours of the corporation's legal creation and socioeconomic rise are well known to legal scholars and historians alike[103]: it was pioneered by state-chartered trading companies like the English and Dutch East India Companies in the early seventeenth century, institutionally matured over the next century, and then became widely available—and used—in European commerce and enterprise during the later eighteenth and nineteenth centuries. Globally, it spread as European economic and legal influence penetrated other regions of the world, eventually becoming one of the most important vessels of capital investment by the twentieth century. These developments chronologically followed, with a few decades' delay, the advent of modern state-building, which also began in Western Europe in the seventeenth century and was later pursued by Asian and Middle Eastern powers in the later nineteenth century.[104] The construction of centralized, professional, and socioeconomically powerful legal systems to replace decentralized regional self-governance and self-regulation—the replacement, that is, of custom with law—was a centerpiece of this process in nearly all countries.[105]

Our contribution here is the argument that this timing was not a coincidence. The modern corporation could rise to prominence only after the modern state had developed the legal and administrative capacity to support it. In this Part, we apply this thesis to a series of historical case studies. We separate these case studies into three categories. In the first, we illustrate the necessity of state power to the emergence of the business corporation by studying early twentieth-century China. There, the state attempted to introduce the corporation into its business sector without first engaging in modern state-building. This effort

103. For a summary, see HARRIS, *supra* note 3, at 251-74.

104. For a summary of the large academic literature on the corporation's creation and rise, see Spruyt, *supra* note 1.

105. For discussions of this trend, see BERMAN, *supra* note 80, at 77, 83; and POGGI, *supra* note 29, at 60-85.

failed, and it was not until the advent of a modern state in the 1930s that the corporate form finally began to gain real economic traction.

In the second category of case studies, we further demonstrate our framework's plausibility by examining the rise of the business corporation in three major nineteenth-century economies: the Ottoman Empire, England, and the United States. Because these countries attempted to introduce the corporation only after engaging in significant state-building, their corporate histories do not showcase the necessity of the framework quite as powerfully as the Chinese case does. Nonetheless, they are fully compatible with the framework and illustrate several of its main components.

Finally, we quickly survey two premodern legal systems, Rome and late medieval Italian city-states, that have played major roles in conventional academic narratives of corporate history. We simply argue that the corporate prototypes found in those systems pose no significant challenge to our thesis.

A. Late Imperial China

The history of business firms in China is, in many ways, the strongest case study for our core theoretical claims. It powerfully demonstrates that the rise of the business corporation may not occur even when conventional demand-side conditions—long-distance, long-duration trade and economic collaboration—*and* supply-side conditions—credible commitments by the state to not arbitrarily expropriate firm assets—are both robustly present. Moreover, it points to the lack of state-building in late imperial and early Republican China as the primary limiting factor that held back the economic proliferation of business corporations even after the legal technology had been nominally introduced through state legislation.

1. Commerce and Business in Late Imperial China

The history of large-scale, privatized, interregional commerce in China extends at least as far back as the tenth or eleventh centuries. Beginning in the later Tang dynasty (618-907), and through the first half of the Song dynasty (960-1279), the traditional North China-based ruling aristocracy was gradually overtaken, politically and economically, by a new class of gentry from the Yangtze River regions and South China who relied more heavily on the Imperial Examination System, rather than hereditary privilege, for entrance into officialdom.[106]

106. *See* HILARY J. BEATTIE, LAND AND LINEAGE IN CHINA: A STUDY OF T'UNG-CH'ENG COUNTY, ANHWEI, IN THE MING AND CH'ING DYNASTIES 1-51 (1979); ROBERT P. HYMES, STATESMEN AND

The decline of the traditional aristocracy dovetailed with a decisive southern shift in the country's socioeconomic center of gravity: the extensive network of waterways that connected the southern regions stimulated commercial activity, as did the wave of economic privatization that accompanied aristocratic decline.[107]

International trade, too, moved away from a land-based, northwestern-oriented pattern that relied primarily on caravan trade through Central Asia, toward higher-volume maritime trade with India and the Middle East via the southeastern coastline.[108] Over the next six centuries, dynasties and their political and economic institutions rose and fell, but the Chinese economy remained predominantly privatized and significantly commercialized, with interregional and international trade retaining prominent roles in resource allocation, regional economic specialization, and wealth generation.[109]

By most measures, these commercial trends only accelerated over the course of China's final imperial dynasty, the Qing (1644-1912). Relatively stable domestic political conditions, coupled with some technological innovations and more intensive land use, led to a tripling of both the population and the economy from the late seventeenth century to the early twentieth century.[110] Much of this

GENTLEMEN: THE ELITE OF FU-CHOU, CHIANG-HIS, IN NORTHERN AND SOUTHERN SUNG 1-61 (1986); BEVERLY J. BOSSLER, POWERFUL RELATIONS: KINSHIP, STATUS, AND STATE IN SUNG CHINA (960-1279), at 134-39 (1998); Hisayuki Miyakawa, *An Outline of the Naito Hypothesis and Its Effects on Japanese Studies of China*, 14 FAR E.Q. 533, 538-39 (1955); Robert M. Hartwell, *Demographic, Political, and Social Transformations of China, 750-1550*, 42 HARV. J. ASIATIC STUD. 365, 405-20 (1982); Joseph P. McDermott, *Charting Blank Spaces and Disputed Regions: The Problem of Sung Land Tenure*, 44 J. ASIAN STUD. 13, 32 (1984) (discussing the Song transition from manor-centric landownership to more privatized and fragmented landownership).

107. *See* RICHARD VON GLAHN, THE ECONOMIC HISTORY OF CHINA: FROM ANTIQUITY TO THE NINETEENTH CENTURY 208-25, 242-49 (2016).

108. *See id.* at 216-17; TANSEN SEN, BUDDHISM, DIPLOMACY AND TRADE: THE REALIGNMENT OF SINO-INDIAN RELATIONS, 600-1400, at 142-96 (2003); Shiba Yoshinobu, *Sung Foreign Trade: Its Scope and Organization*, *in* CHINA AMONG EQUALS: THE MIDDLE KINGDOM AND ITS NEIGHBORS, 10TH-14TH CENTURIES 89-115 (Morris Rossabi ed., 1983).

109. *See* VON GLAHN, *supra* note 107, at 255-347 (summarizing general developments from the twelfth century to the eighteenth century); WILLIAM GUANGLIN LIU, THE CHINESE MARKET ECONOMY: 1000-1500, at 77-95 (2015); Martin Heijdra, *The Socio-Economic Development of Rural China During the Ming*, *in* 8 THE CAMBRIDGE HISTORY OF CHINA 417 (Dennis C. Twitchett & Frederick W. Mote eds., 1998).

110. For estimates of population growth and economic expansion respectively, see Brandt et al., *supra* note 44, at 45; and Stephen Broadberry, Hanhui Guan & David Daokui Li, *China, Europe, and the Great Divergence: A Study in Historical National Accounting, 980-1850*, 78 J. ECON. HIST. 955, 956 (2018).

growth was achieved on the back of regional economic specialization, which itself relied on the continued expansion of interregional trade.[111] The economy relied heavily on long-distance trade even though much of the trade was technically contained within a single country: the distance between Beijing and Guangzhou is comparable to the distance between Paris and Istanbul. International trade, too, continued to flourish in South China.[112] In fact, tariff income through foreign trade became one of the state's most important sources of revenue after 1840.[113]

Over this same multicentury period, however, the late imperial Chinese state became progressively weaker until, by the nineteenth century, it no longer wielded significant coercive power across large swathes of the country. Much of this decay in state capacity can be observed through the decline of government income: formal government taxation as a share of estimated GDP declined from a high point of around fifteen percent in the eleventh century to some three to four percent in the eighteenth, and then to between one-and-a-half and two percent in the nineteenth.[114] The causes of this decline are complex and far surpass the scope of this Article, but the accompanying decline in the state's administrative and coercive capacity was unmistakable. The eleventh-century state wielded strong regulatory power over large sectors of the private economy while also managing large amounts of economic assets.[115] In contrast, by the later eighteenth century, the state was so resource constrained that it was effectively forced to farm out large portions of its basic administrative and law-enforcement duties to local communities, leading to an empire-wide rise in lineage, village, and

111. *See* VON GLAHN, *supra* note 107, at 329-36; ROBERT B. MARKS, TIGERS, RICE, SILK, & SILT: ENVIRONMENT AND ECONOMY IN LATE IMPERIAL SOUTH CHINA 284 (Donald Worster & Alfred W. Crosby eds., 2d ed. 2004); Carol H. Shiue & Wolfgang Keller, *Markets in China and Europe on the Eve of the Industrial Revolution*, 97 AM. ECON. REV. 1189, 1190 (2007).

112. *See* Wolfgang Keller, Ben Li & Carol H. Shiue, *China's Foreign Trade: Perspectives from the Past 150 Years*, 34 WORLD ECON. 853, 854 (2011). On illegal trade and smuggling, see PHILIP THAI, CHINA'S WAR ON SMUGGLING: LAW, ECONOMIC LIFE, AND THE MAKING OF THE MODERN STATE, 1842-1965, at 12-13 (2018).

113. *See* ZHANG, *supra* note 31, at 63.

114. *See id.* at 3-4; Yuhua Wang, *Blood Is Thicker Than Water: Elite Kinship Networks and State Building in Imperial China*, 116 AM. POL. SCI. REV. 896, 908 (2022).

115. A particularly vivid illustration of Song state capacity is the government's ability to push through sweeping economic regulatory reform during the Shenzong era. *See* Paul J. Smith, *Shen-tsung's Reign and the New Policies of Wang An-shih, 1067-1085*, *in* 5 THE CAMBRIDGE HISTORY OF CHINA pt. 1, at 347, 408-14, 427-29 (Dennis Twichett & P.J. Smith eds., 2009).

guild self-governance powers.[116] In particular, the considerable majority of commercial disputes were handled and resolved according to communally enforced local customs and social norms, to which official courts and magistrates increasingly deferred.[117]

The key takeaway here is that by the eighteenth century at the latest, the Chinese state was fully capable of making credible commitments not to expropriate private assets because it lacked the ability to do so on any significant scale. There is very little, if any, evidence of serious government encroachment, either in the form of direct seizure or arbitrary tax increases. Although a series of severe fiscal crises forced the Qing state to raise commercial taxes after 1850, such increases were both limited in scale and implemented with the informed cooperation of local business communities.[118] When the state decided, after 1860, that it needed to stimulate military industrial investment, it did so by providing incentives for private businesses rather than by seizing their assets and building its own factories.[119] To a considerable extent, the late imperial Chinese state was the very definition of laissez-faire.

In other words, the late imperial Chinese economy met all of the primary conditions that scholars have previously identified as necessary for the rise of the business corporation: there was robust long-distance trade both within the empire and with foreign parties, and there was ample credible commitment from the state not to expropriate. Despite these favorable conditions, the legal technologies of asset partitioning and share transferability did not emerge in any significant way. As one recent study demonstrates, although there was some documented use of a weak form of limited liability in late imperial Chinese firms, they "did not exhibit a feature comparable to entity shielding vis-à-vis their European counterparts."[120] In fact, other studies would even argue that the use of limited liability was economically insignificant.[121] Instead, Chinese firms, through the

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116. *See* ZHANG, *supra* note 31, at 227-28; SEUNGHYUN HAN, AFTER THE PROSPEROUS AGE: STATE AND ELITES IN EARLY NINETEENTH-CENTURY SUZHOU 14-15 (2016); William T. Rowe, *Introduction: The Significance of the Qianlong-Jiaqing Transition in Qing History*, 32 LATE IMPERIAL CHINA 74, 80 (2011). While delegation of power is not always a sign of weakness in state capacity, it undeniably was in the later Qing, as explained in ZHANG, *supra* note 31, at 369-70.

117. *See* ZHANG, *supra* note 65, at 57-59. The literature on land law in late imperial China is summarized in Taisu Zhang, *Land Law in Chinese History*, *in* ROUTLEDGE COMPANION TO CHINESE LEGAL HISTORY (forthcoming), https://ssrn.com/abstract=3547494 [https://perma.cc/HM7R-NELW].

118. *See* ZHANG, *supra* note 31, at 100-01.

119. *See id.* at 70-75.

120. Lin Lin, *The Evolution of Partnerships in China from the Perspective of Asset Partitioning*, 18 STAN. J.L. BUS. & FIN. 216, 216-17 (2013).

121. *See, e.g.*, Madeleine Zelin, *Informal Law and the Firm in Early Modern China* 16 (IERC Conference Working Paper, 2007) (on file with authors).

end of the nineteenth century, tended to be full-liability partnerships with no robust asset partitioning in either direction and, therefore, very little free transferability of shares.[122]

Why was this the case? One possibility might be that Chinese firms were so well capitalized that there was no substantial need for collaboration among strangers even when conducting long-distance trade. But this was almost certainly not the case. As many studies have concluded, businesses regularly had to collaborate with entities outside of their immediate circles. This was the case even for something as simple as selling salt produced in Sichuan Province in other macroregions.[123] For more complex operations, such as textiles production or protoindustrial manufacturing, entrepreneurs often had to build large and complex networks of suppliers, producers, shippers, and commercial agents, many of whom operated well beyond the entrepreneur's usual socioeconomic circles.[124] The use of sophisticated business contracts and partnerships to facilitate these collaborative projects was widespread—and yet these collaborations fell apart very easily whenever there was socially salient economic and political turbulence.[125]

The lack of risk alleviation seems to have been a major reason for this lack of institutional durability: fully liable but still risk-averse business partners tended to pull their investments at any notable sign of financial weakness, whether in the firm itself or in its other investors.[126] By the last few years of the Qing dynasty, the constant sociopolitical turmoil made investors even more nervous than usual and produced serious instability in the commercial sector, even as economic demand for long-distance trade remained strong. By all indications, the lack of asset partitioning had become a real institutional constraint on Chinese commercial development.

One might also wonder whether the kinship networks, guilds, and other social groups that supplied the lion's share of economic regulation and rule enforcement in the late imperial Chinese economy were simply unable to enforce

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122. *See supra* notes 120-121; Teemu Ruskola, *Conceptualizing Corporations and Kinship: Comparative Law and Development Theory in a Chinese Perspective*, 52 STAN. L. REV. 1599, 1654-56 (2000).

123. *See* Madeleine Zelin, *Managing Multiple Ownership at the Zigong Salt Yard*, *in* CONTRACT AND PROPERTY IN EARLY MODERN CHINA 230, 231-32 (Madeleine Zelin, Jonathan K. Ocko & Robert Gardella eds., 2004).

124. *See* LINDA GROVE, A CHINESE ECONOMIC REVOLUTION: RURAL ENTREPRENEURSHIP IN THE TWENTIETH CENTURY (2006); ALBERT FEUERWERKER, CHINA'S EARLY INDUSTRIALIZATION: SHENG HSUAN-HUAI (1844-1916) AND MANDARIN ENTERPRISE (1958); Robert Brenner & Christopher Isett, *England's Divergence from China's Yangzi Delta: Property Relations, Microeconomics, and Patterns of Development*, 61 J. ASIAN STUD. 609 (2002).

125. *See* Zelin, *supra* note 123, at 263-65.

126. *See id.* at 252-56.

something as institutionally complex as asset partitioning—especially entity shielding, with its considerable third-party externalities. This explanation, too, seems unlikely. There is copious evidence that such communal entities and networks were capable of enforcing highly complex institutional arrangements within their own membership: family-division rules, governance rules for communally held property, and so on.[127] In particular, they were able to provide, functionally speaking, something akin to fully secure private property rights over land—not merely against top-down, state-driven expropriation but also against horizontal encroachment by other private parties—which, in theory, involved the regulation of as many third-party externalities as entity shielding would have.[128] Moreover, the basic idea of entity shielding was familiar enough in customary law: many forms of land mortgages employed, for example, a form of functional asset shielding that protected a piece of land under mortgage from both the original owner/debtor and his other creditors.[129] The conceptual foundations of asset partitioning qualitatively existed but were generally not applied to the business-firm setting.

Kinship networks and guilds were, of course, limited in the scope of their customary jurisdiction, both in terms of geography and social reach. They exercised control only over relatively small areas, such as a village, a town, or parts of cities, and they could not enforce rules over large distances.[130] In countries where state capacity was more robust, formal law courts could have stepped in to fill this regulatory void or even prevented its emergence in the first place. But late imperial Chinese court systems, especially in the eighteenth and nineteenth centuries, were quite limited in their enforcement powers and interregional reach.[131] This appeared to limit, in the eyes of contemporaries, the kinds of legal technologies that could be widely employed in long-distance trade or other intercommunal activities,[132] forcing collaborators to rely on simpler business forms, predominantly partnerships. The problem with these business forms, as noted above, was their durability and reliability. As foreign trade came to occupy an ever-more prominent position in the nineteenth-century Chinese economy,

127. *See* Zhang, *supra* note 117.

128. *See id.*

129. *See* ZHANG, *supra* note 65, at 35-63.

130. The ceiling for informal social self-governance seemed to be guild regulation of economic activity in major commercial hubs like Hankou. *See* Christine Moll-Murata, *Chinese Guilds from the Seventeenth to the Twentieth Centuries: An Overview*, 53 INT'L REV. SOC. HIST. 213, 238 (2008).

131. *See* ZHANG, *supra* note 31, at 58-59.

132. *See* QICHENG LI (李启成), ZIZHENGYUAN YICHANG HUIYI SUJILU:WANQING YUBEI GUOHUI LUNBIAN SHILU (资政院议场会议速记录：晚清预备国会论辩实录) 499 (2011).

pressure on the Qing state to provide stronger institutional alternatives mounted.

2. *Early Twentieth-Century Legislation and Its Economic Impact*

By the early twentieth century, the growth of long-distance commerce and the political elite's desire for stronger legal institutions to support it finally forced the state to act. As the first component of a broader push to modernize Chinese law, especially those portions related to economic activity, the Qing government issued a new Commercial Code in 1904, based largely on Japanese, German, and English models.[133] As legislators expressly laid out during the preratification debates, the new code specifically sought to support and stimulate capital-intensive business projects that required collaboration between numerous parties—something that they believed to be beyond the capacity of customary law and norms.[134] Toward these ends, the new Commercial Code formally introduced, for the first time in Chinese history, the joint-stock limited-liability corporation (*gufen youxian gongsi*) as a legally sanctioned organizational form, complete with all the core legal technologies we have focused on in this Article: asset partitioning, tradable shares, capital lock-in, centralized management, and independent legal personhood.[135] Asset partitioning and tradable shares, in particular, distinguished the business corporation from virtually all other organizational forms that had traditionally been employed in Chinese economic activity and, therefore, drew the lion's share of political attention.

Despite the government's stated hope that the passage of the Commercial Code would provide an immediate boost to capital-intensive development, the actual economic history of the law and its legal successors during the first half of the twentieth century proved otherwise. In the eight years between the law's passage and the Qing dynasty's formal end in 1912, the Code's economic footprint was meager. As historians have noted, very few firms actually made use of the new corporate form: from 1904 to 1908, only 227 companies had registered under it, and of these, only twenty-two held significant amounts of capital.[136] This accounted for a vanishingly small portion of business activity nationwide, especially when most of the registered companies were simply traditional financial

133. The most accessible survey of this episode and its subsequent history remains Kirby's, *supra* note 45.

134. *See* LI, *supra* note 132.

135. QINDING DA QING SHANGLÜ (钦定大清商律) (Guangxu 29th Year, 12th Month/January 1904).

136. *See* FEUERWERKER, *supra* note 124, at 4; Zou Jinwen (邹进文), *Jindai Zhongguo de Gufenzhi* (近代中国的股份制), *in* LISHI DANG'AN (历史档案) 100 (1995).

entities like pawnshops that had little connection to the capital-intensive industrial sector that the state was hoping to stimulate.[137] By all accounts, "the law was not a success."[138]

The primary problem was that firms simply did not trust the state, weak and generally ineffective as it was, to properly interpret and enforce the laws. The court system was not yet prepared for litigation related to the new corporate forms. This meant that dispute resolution was handled by the Ministry of Commerce, which had very little legal expertise and no institutionalized apparatus to enforce its decisions.[139] Accusations of favoritism, corruption, and selective enforcement were commonplace.[140] There was, as a result, little confidence in the Ministry to apply laws in a fair and uniform manner. But while the failures of the court system likely made things worse, the business community's confidence level would likely have been low even if dispute resolution was handled by the courts: the Chinese court system was at that time neither professional—litigation was handled by local administrative officials who doubled as judges—nor adequately vested with enforcement powers.[141]

Furthermore, the transplanted nature of much of the new law created substantial translation and interpretation problems for the business community,[142] which the state was unable to address adequately given its lack of legal and administrative resources. By 1911, lawmakers already recognized that the law had failed to produce the intended effect and had begun drafting a more precisely worded replacement that could be directly applied by the courts.[143] Before much progress could be made, however, the dynasty ended when a wave of provincial elite-led uprisings forced the imperial family to abdicate on January 1, 1912. A revised set of corporate rules were issued by the successor Republican regime in 1914 under the form of "Corporations Regulations" (*Gongsi Tiaoli*), but this document kept the basic structure and functionality of the Qing law.[144]

For the next decade and a half, the business corporation played a slowly expanding but ultimately minimal role in China's commercial and economic boom of the 1910s and 1920s. State capacity remained low throughout these years due to constant military conflict between warlord factions. As a result, the number

137. *See* FEUERWERKER, *supra* note 124, at 3.

138. Kirby, *supra* note 45, at 48.

139. *See* Chun Li, *The Kung-ssu-lü of 1904 and the Modernization of Chinese Company Law*, 11 CHENGCHI U. L. REV. 163, 198-207 (1974).

140. *See id.*

141. *See* ZHANG, *supra* note 31, at 37-70.

142. *See id.*

143. *See* Kirby, *supra* note 45, at 48-49.

144. *See id.* at 49.

of corporations registered each year only exceeded 100 in 1919 and did not exceed 200 until reunification under the Nationalist government in 1927.[145] A significant number of these registered corporations quickly fell apart, leaving, according to estimates, only about 700 to 2,000 active corporations in the entire country in 1929.[146] Scholars have yet to produce reliable estimates of the total number of Chinese firms for that point in time, but we do know that the corresponding number for 1949—after eight years of devastating war with Japan, and another four years of all-out civil war—came to around 1.3 million.[147] Between 1929 and 1949, conventional estimates of the scale of industrial and commercial growth in the Chinese economy often come to around fifty percent.[148] If we assume (very crudely) that the number of firms also broadly tracked this growth rate, then we would be looking at around 800,000 to 900,000 firms in 1929. This calculation implies that the share of total firms that chose to incorporate fell well below one percent and may have been less than 0.1 percent. Some of these corporations may have held greater amounts of capital than the average firm, but even taking that into account, the Chinese economy had, for the most part, "reject[ed] . . . the corporate model."[149]

The pace of incorporation picked up considerably after 1929, when the Nationalist government issued a new Corporations Law (*Gongsi Fa*).[150] By 1949, there were some 11,000 corporations operating across the country, over forty percent of which were in capital-intensive industries.[151] While this was still slightly short of one percent of all registered firms, it nonetheless represented a rate of incorporation that was some four-to-five times higher than the pre-1929 rate. In Shanghai, arguably the single most heavily incorporated regional econ-

145. *See* 1 ZHONGGUO JINDAI GONGYESHI ZILIAO (中国近代工业史资料) 10 (Zhen Chen & Luo Yao eds., 1957); Zongpei Wang (王宗培), *Zhongguo Gongsi Qiye Ziben Jiegou de Fenxi* (中国公司企业资本结构的分析) *[Capital Structure Analysis of Chinese Corporations]*, *in* 4 ZHONGGUO JINDAI GONGYESHI ZILIAO (中国近代工业史资料) 57 (Zhen Chen ed., 1961); ZHONGMIN ZHANG (张忠民), JIANNAN DE BIANQIAN: JINDAI ZHONGGUO GONGSI ZHIDU YANJIU (艰难的变迁：近代中国公司制度研究) 254-66 (2002).

146. *See* Wang, *supra* note 145 (giving an estimate of 716); ZHANG, *supra* note 31, at 260 (placing the estimate at around 2,000). Zhang's higher estimates would still mean that corporations only accounted for perhaps 0.2-0.3 percent of all firms in the country.

147. *See* ZHANG, *supra* note 31, at 266.

148. *See, e.g.*, TA-CHUNG LIU & KUNG-CHIA YEH, THE ECONOMY OF THE CHINESE MAINLAND: NATIONAL INCOME AND ECONOMIC DEVELOPMENT, 1933-1959, at 66 tbl.8 (1965).

149. Kirby, *supra* note 45, at 51.

150. *Gongsi Fa* (公司法), WEIJI WENKU (维基文库) (Dec. 7, 1929), https://zh.m.wikisource.org/zh/%E5%85%AC%E5%8F%B8%E6%B3%95_(%E6%B0%91%E5%9C%8B18%E5%B9%B4) [https://perma.cc/T5Q9-ZSNT].

151. *See* ZHANG, *supra* note 31, at 266, 271.

omy in the country, only about eighteen percent of industrial firms were incorporated in 1931.[152] A few years later, the corresponding number nationwide reached around twenty-five percent.[153]

What changed? The issuance of a new Corporations Law may have had some impact on investor confidence, but much more importantly, the new regime also embarked on a series of state-building projects that significantly enhanced its socioeconomic control. In other words, the state strengthened its ability to enforce corporation law. If we look at the crudest but nonetheless reasonably effective measure of state capacity—fiscal power—the Nationalist government, by the early 1930s, was extracting at least five-to-seven times more revenue in real terms than the Qing state in 1900.[154] This funded a significantly more expansive bureaucracy that could sometimes effectively penetrate, for the first time in centuries, below the county level.[155]

The tide of state-building also extended to the judicial system, which tended to enjoy better legal training, more personnel, and stronger powers of enforcement across the country.[156] The Nationalist government invested heavily in legal professionalism and made serious efforts to construct a well-trained judiciary that could provide fast, reliable, and uniform law enforcement. While these efforts were uneven in the rural countryside, they did have a considerable effect on the quality of adjudication in urban centers. These efforts, combined with the continued growth of the Chinese industrial and commercial sectors, generated a relatively large wave of investor interest in incorporation—relative, at least, to pre-1929 trends—prior to the Japanese invasion in 1937.

If we take a closer look, the state's role in these developments becomes even more prominent. Many of the largest and most important industrial corporations were created with direct state involvement, ranging from capital ownership to active brokerage of investor negotiations.[157] During the Sino-Japanese war, state-owned corporations accounted for over two-thirds of industrial capital in Nationalist government-controlled regions.[158] Many of these took the form of public-private collaborations, with the state's National Resources Committee

152. *See* Kirby, *supra* note 45, at 52.

153. *See id.*

154. *See* ZHANG, *supra* note 31, at 310.

155. On state-building at the local level, see HUAIYIN LI, VILLAGE GOVERNANCE IN NORTH CHINA, 1875-1936 (2005); and PRASENJIT DUARA, CULTURE, POWER, AND THE STATE: RURAL NORTH CHINA, 1900-1942 (1988).

156. *See* XIAOQUN XU, TRIAL OF MODERNITY: JUDICIAL REFORM IN EARLY TWENTIETH-CENTURY CHINA, 1901-1937, at 3 (2008).

157. *See* Kirby, *supra* note 45, at 52-53.

158. *See* William C. Kirby, *The Chinese War Economy*, *in* CHINA'S BITTER VICTORY: THE WAR WITH JAPAN, 1937-1945, at 185, 185 (James C. Hsiung & Steven I. Levine eds., 1992).

holding at least fifty-one percent of a corporation, and then allowing the remainder to be held by and traded among private investors who occasionally were large in number.[159]

Whatever progress had been made toward the growth of the corporation came to a halt in 1949, as the Communist Party-state moved to convert the still largely privatized Chinese economy into a planned economy.[160] This went on for nearly three decades under various models of state planning, none of which left much room for private enterprise. State capacity, however, continued its rapid upward trajectory during this era, both in terms of administrative sophistication and fiscal muscle.[161]

Once the economy began to open up again after Deng Xiaoping's ascension to power in the late 1970s, the corporate form would regain a position of importance and, eventually, prominence within the economy in the 1990s and 2000s. A new Corporations Law, passed in 1993, once again allowed the formation of private limited-liability corporations.[162] And by 2017, publicly traded private corporations accounted for some fifty percent of total private capitalization.[163] Although no one would describe the Chinese legal system as perfectly professionalized during this period, the large amounts of administrative, institutional, and fiscal capacity the Party-state had accumulated during the Mao era did allow it to build up quickly a basically functional judiciary and empower it with investigatory and enforcement powers that likely far exceeded what Republican courts could muster before 1949.[164] As a result, once the institutional commitment to supporting private enterprise had been made, the business sector

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159. *See* ZHANG, *supra* note 145, at 213-41.

160. *See* DWIGHT H. PERKINS, MARKET CONTROL AND PLANNING IN COMMUNIST CHINA 9 (1966).

161. *See* Julia Strauss, *Morality, Coercion and State Building by Campaign in the Early PRC: Regime Consolidation and After, 1949-1956*, 2006 CHINA Q. 891, 891-92. On fiscal capacity, see ZHANG, *supra* note 31, at 267-318. *See generally* A. DOAK BARNETT, COMMUNIST CHINA: THE EARLY YEARS, 1949-55 (1964) (providing a contemporary account of Communist consolidation).

162. Gongsi Fa [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993, effective July 1, 1994), LAWINFOCHINA, http://www.lawinfochina.com/Display.aspx?lib=law&ID=641 [https://perma.cc/2MWF-P7FR]. The business-corporation form authorized in this law is largely based on the Anglo-American model.

163. *See Zhongguo Shangshi Gongsi Shuliang Ju Quanqiu Disan* (中国上市公司数量居全球第三), DONGFANG CAIFU WANG (东方财富网) (Nov. 30, 2020, 4:50 AM CST), http://finance.eastmoney.com/a/202011301719423884.html [https://perma.cc/NX7F-USXU].

164. For accounts of pre-1949 legal institutions and the basic tenor of post-1978 legal reforms, see RANDALL PEERENBOOM, CHINA'S LONG MARCH TOWARD RULE OF LAW 27-54, 137-74 (2009). While Chinese court reform remains a work in progress, few would doubt the basic ability of courts to uniformly enforce private agreements by the early 2000s, even as many continue to doubt their ability to check certain kinds of government power. *See* Taisu Zhang & Tom Ginsburg, *China's Turn Toward Law*, 59 VA. J. INT'L L. 306, 311, 330 (2019).

likely faced fewer supply-side institutional constraints than it had in the 1930s, leading to a far more rapid pace of incorporation and capital accumulation.

3. *Takeaways*

Out of all the country-level case studies we present in this Article, the Chinese one showcases most vividly the limitations of preexisting explanations for the institutional emergence and economic rise of the corporate form. By the later nineteenth century, China possessed in some abundance the conditions that scholars have previously identified for the rise of the corporation, both on the demand side (large-scale, long-distance commercial activity that necessarily crossed the boundaries of closely knit communities) *and* supply side (credible commitments by the state to not expropriate firm assets).[165] However, not only did the corporate form fail to emerge organically from within the late imperial Chinese economy, but even after the state attempted to formally introduce it through legal transplantation in 1904, the legislation was, by and large, an economic failure.

What China lacked was not the nominal existence of the corporate form in a legal statute but rather a state with sufficient power to administratively manage and legally enforce the economic relationships provided for by the form. In particular, the lack of an adequately professional and powerful judiciary that could handle commercial disputes uniformly and effectively seemed to deter private use of the corporate form. Private sources of economic regulation—guilds, lineages, and so on—were capable of considerable regulatory sophistication within their respective sociolegal boundaries. But, as contemporaries observed, these private sources lacked a reliable way to enforce something as complex as a corporate charter *beyond* those boundaries.[166] This was an area in which robust state regulation and enforcement were necessary, and yet China had nothing that functionally resembled an administratively and legally powerful modern state before the 1930s and arguably did not develop such a state until the 1950s and 1960s.

It is unsurprising, then, that the spread of the corporate form in China closely tracked the escalation of state capacity: a first round of serious state-building after 1929 produced a significant escalation in the pace of incorporation; and a second, more robust round after 1949 facilitated the emergence of truly

165. This assessment is different from the description of Chinese business history given in HARRIS, *supra* note 3, at 354-62, which significantly overstates, we believe, the ability of the state to expropriate. For a fuller explanation of why Harris's account is mistaken here, see Taisu Zhang, *Going the Distance: Eurasian Trade and the Rise of the Business Corporation, 1400-1700*, 81 J. ECON. HIST. 318, 318-20 (2021), which reviews HARRIS, *supra* note 3.

166. *See* LI, *supra* note 132.

significant, economically dominant corporations in the Chinese economy after it "opened up" once again in the 1980s. It seems, therefore, that the principal constraint on the introduction and use of the corporate form in the nineteenth and early twentieth centuries was neither a lack of economic demand nor the lack of credible commitments against government expropriation but rather a fundamental lack of state capacity. When this constraint was loosened, robust waves of incorporation almost immediately followed.

B. Nineteenth-Century Ottoman Empire

Up until the sixteenth century, the Ottoman Empire was arguably more economically developed and powerful than any major European economy and was a key player in Eurasian interregional commerce.[167] Although the empire gradually lost its economic edge in the ensuing centuries, it continued to play a highly important role in trade and commerce right up until its collapse in 1922.[168] Despite its commercial significance, the corporate form was effectively nonexistent among Islamic business enterprises until the mid-nineteenth century, when the Ottoman state, as part of a massive drive toward political and institutional modernization—largely in the image of its Western European competitors—gradually introduced and promoted the form over several decades.[169] Recent publications have identified a number of possible causes for the corporation's late emergence in the Ottoman economy, ranging from path dependency to Islamic religious beliefs.[170]

Drawing upon this literature, this Section teases out three specific historical arguments. First, throughout early modern Ottoman history, there appeared to have been little socioeconomic appetite at the local level to recognize corporate legal technologies: the benefits seemed limited, while the potential sociopolitical costs seemed high. Interregional commerce likely would have benefitted from these technologies, but they would have required centralized state sponsorship and institutional support. Second, while not quite as weak as the early modern

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167. *See* Halil İnalcık & Donald Quataert, *General Introduction*, *in* 2 AN ECONOMIC AND SOCIAL HISTORY OF THE OTTOMAN EMPIRE, 1600-1914, at xxxix-xl (Halil İnalcık & Donald Quataert eds., 1994); TIMUR KURAN, THE LONG DIVERGENCE: HOW ISLAMIC LAW HELD BACK THE MIDDLE EAST 3 (2012).

168. *See* Inalcık & Quataert, *supra* note 167, at xl.

169. *See* Kuran, *supra* note 4, at 785-86.

170. *See, e.g.*, KURAN, *supra* note 167, at 32-42; Kuran, *supra* note 4, at 799; Cihan Artunç, *The Price of Legal Institutions: The Beratlı Merchants in the Eighteenth-Century Ottoman Empire*, 75 J. ECON. HIST. 720, 745-46 (2015); Jack A. Goldstone, *Is Islam Bad for Business?*, 10 PERSPS. ON POL. 97, 100-01 (2012) (reviewing KURAN, *supra* note 167); HARRIS, *supra* note 3, at 338-50; MURAT ÇIZAKÇA, ISLAMIC CAPITALISM AND FINANCE, at xiv-xxvi (2011).

Chinese state, the Ottoman state was limited in its administrative and legal capacities, which could have contributed to repressing the emergence of the corporate form. Third, the form's eventual emergence relied heavily on state sponsorship and occurred only after state capacity had significantly increased because of nineteenth-century reforms.

1. *The Dearth of Corporations*

Business in the premodern Islamic world was, as Timur Kuran and others have argued, largely conducted without the aid of the corporate form—specifically, without firms that enjoyed independent legal personhood, entity shielding, and tradable shares. In general, traditional Islamic joint-stock entities were partnerships that became "null and void at the withdrawal, incapacitation, or death of even a single partner."[171] The lack of personhood also meant that these partnerships could not benefit from entity shielding or allow the free trading of shares. These conditions persisted for centuries, despite the development of robust networks of interregional commerce across Europe and the Middle East.[172]

Even after the business corporation emerged in Western Europe in the early seventeenth century and began to play a significant role in interregional commerce, it made virtually no inroads among Islamic business communities.[173] It was not until later in the nineteenth century—with direct state support and investment—that joint-stock companies with tradable shares and, eventually, legal personhood and entity shielding began to proliferate among Muslim investors.[174] Throughout this two-century-long gap, Islamic partnerships interacted regularly with European corporations and were almost certainly aware of their legal characteristics.[175] These interactions indicate, at the very least, that the emergence of the business corporation in the Middle East was not delayed by a lack of knowledge among Muslims of the legal technology.

In fact, many of the core legal technologies of the corporation—including limited liability and entity shielding—*were* employed in Islamic economic activities, just not in for-profit business activities. The most prominent example is the *waqf*, a "type of unincorporated trust" that could be created to pursue, in perpetuity, "any function deemed legitimate under Islamic law" and enjoyed a

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171. Kuran, *supra* note 4, at 786.

172. *See id.* at 787.

173. *See id.* at 788.

174. *See id.* at 831-33.

175. *See* HARRIS, *supra* note 3, at 350.

significant measure of financial and legal independence from its original creator.[176] Funds invested in a *waqf* were deemed separate from the personal wealth of the creator and therefore offered both capital lock-in and "a degree of entity shielding."[177] Despite these features, the *waqf* lacked many of the key functional characteristics of a business corporation: its purpose and rules of operation, once established, could not be changed, and it did not allow for the entrance of new investors.[178] As a result, *waqfs* lacked the institutional flexibility that for-profit business activities generally required and were instead employed primarily to provide long-duration, nonprofit social services that did not need flexible governance or active collaboration between multiple investors, such as schools, roads, waterworks, assistance to travelers, and places of worship.[179]

2. *Possible Explanations*

Scholars have offered a wide range of possible explanations for the "absence of the corporation"[180] in the Islamic world, which fall on both sides of the demand-and-supply typology we developed above. On the demand side, the existence of the *waqf* might, as Kuran has argued, have alleviated some of the socioeconomic need for business corporations, given that many long-term public goods requiring capital lock-in and some measure of entity shielding could be effectively supplied through *waqfs*.[181] Even so, by the eighteenth century, long-distance Eurasian trade had grown to the point that Kuran himself describes the lack of corporations as a major constraint on Islamic commercial development and an institutional disadvantage relative to European corporations,[182] which implies that the basic economic incentives for legal incorporation did exist to some extent.

On the supply side, explanations range from more conventional claims about credible commitment to context-specific arguments about Islamic law and religion. The former posits that the Ottoman state was prone to irregular expropri-

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176. Kuran, *supra* note 4, at 799; 3 MARSHALL G. S. HODGSON, THE VENTURE OF ISLAM: CONSCIENCE AND HISTORY IN A WORLD CIVILIZATION 108 (1974).

177. HARRIS, *supra* note 3, at 345.

178. *See* Kuran, *supra* note 4, at 800.

179. *See id.* at 799.

180. *Id.* at 788.

181. *See id.* at 785, 799-802.

182. *See id.* at 811-15.

ation of Muslim businesses, whereas Christian businesses enjoyed stronger protections provided by overlapping European legal systems.[183] The latter points to the reluctance of Islamic jurists to allow sociopolitical self-governance by substate entities, especially by private, for-profit enterprises, due to religious doctrines that discouraged such activity and out of a concern for potential socioeconomic conflict.[184]

All these observations make a good deal of sense within the theoretical framework we developed in Part I: unlike *waqfs*, which were limited to narrowly tailored purposes and specific operational procedures, a business corporation with independent legal personhood and full asset partitioning could have created substantial costs for third parties and was therefore reasonably considered a potentially significant source of social tension and dispute. Insofar as partnerships and *waqfs* could adequately support most forms of local economic activity, the institutional appetite to take on these costs must have been limited.

Interregional commerce, in comparison, operated under a very different cost-benefit calculus.[185] *Waqfs* and partnerships could no longer substitute for the corporation when for-profit businesses operated over long distances and with larger numbers of socially unconnected investors: *waqfs* could not offer the institutional agility to deal with the unforeseeable contingencies that were necessarily part of such business operations, and partnerships lacked the risk-alleviation technologies that were often desired by socially and physically distant business collaborators. Third-party externalities still might have existed, but they were spread out over a larger range of potential tort and contract creditors, many of whom were socially unconnected to the business owners.

The problem lay on the supply side: as in other early modern economies, the state was likely the only actor capable of enforcing the structure of a long-distance business corporation, but the Ottoman state supplied little initiative in this direction.

3. *The Role of Limited State Capacity*

Relative to the extreme scarcity of state capacity in Qing China, the early modern Ottoman state enjoyed a relatively larger revenue base and, consequently, a stronger administrative and legal presence in everyday life, especially

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183. *See, e.g.*, Yasin Arslantaş, Antoine Pietri & Mehrdad Vahabi, *State Predation in Historical Perspective: The Case of Ottoman Müsadere Practice During 1695-1839*, 182 PUB. CHOICE 417, 419, 421-24 (2020).

184. *See, e.g.*, Kuran, *supra* note 4, at 794-99.

185. *See generally* HARRIS, *supra* note 3 (describing Eurasian trade from 1400-1700 and the factors that allowed it to thrive).

in major cities. Nonetheless, relative to its Western European peers—and certainly to any modern state apparatus—it was still a very limited outfit. By 1800, state revenue accounted for some five percent of estimated annual economic production,[186] which seems much more robust than the one-to-two percent in the Chinese case but much weaker than the eight-to-ten percent that the pre-revolutionary French state collected and dramatically weaker than the fifteen-or-so percent that the eighteenth-century English state took in.[187] Governance at the local level was highly decentralized, and the state relied heavily on tax farmers for revenue collection.[188] In fact, over the course of the seventeenth and eighteenth centuries, Ottoman fiscal institutions actually seemed to move toward even greater decentralization, allowing tax farmers to negotiate rates and collection procedures with local communities without substantial formal oversight.[189]

The legal system, too, was significantly decentralized.[190] Formal state law coexisted with both Islamic law (*sharia*) and a large collection of local customs and rules. In the context of economic regulation, including the regulation of landed assets, the local customs and rules seemed to shoulder the lion's share of functional responsibility. As scholars have argued, property ownership, transactions, and relevant tax obligations were generally regulated and enforced at the village level[191] rather than through high-level institutions, and the state, while retaining a formal claim to final legal authority, tended to incorporate local practices into its legal apparatus whenever sociopolitically possible.[192]

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186. *See* Karaman & Pamuk, *supra* note 31, at 615; Şevket Pamuk, *The Evolution of Fiscal Institutions in the Ottoman Empire, 1500-1914*, *in* THE RISE OF FISCAL STATES: A GLOBAL HISTORY 304, 321 fig.13.1 (Bartolomé Yun-Casalilla, Patrick K. O'Brien & Francisco Comín Comín eds., 2012).

187. *See* sources cited *supra* note 31.

188. *See* Nadir Özbek, *Tax Farming in the Nineteenth-Century Ottoman Empire: Institutional Backwardness or the Emergence of Modern Public Finance?*, 49 J. INTERDISC. HIST. 219, 219 (2018). However, scholars have begun to debate whether a state's reliance on tax farming indicates a lack of centralization. *See id.* at 220-21.

189. *See* Eliana Balla & Noel D. Johnson, *Fiscal Crisis and Institutional Change in the Ottoman Empire and France*, 69 J. ECON. HIST. 809, 824-25 (2009).

190. *See generally* LAW AND LEGALITY IN THE OTTOMAN EMPIRE AND REPUBLIC OF TURKEY 43-91 (Kent F. Schull, M. Safa Saraçoğlu & Robert Zens eds., 2016) (explaining how legal entitlements and obligations were enforced at the local level). One could again argue that decentralization was not necessarily a sign of weak coercive capacity, but if the nineteenth-century state-building exercises, *infra* note 198, are any indication, even Ottoman contemporaries recognized the need to beef up formal state capacity before economic modernization could begin in earnest.

191. *See id.* at 26-91.

192. *See* Gülnihal Bozkurt, *Review of the Ottoman Legal System*, *in* 3 OSMANLI TARIHI ARAŞTIRMA VE UYGULAMA MERKEZI DERGISI 115, 117 (1992).

Systemic pluralism was also a prominent feature of urban legal activity. In major trading centers, Ottoman courts coexisted with consular courts established by European powers, which gave some merchants, particularly those who belonged to minority religious groups, access to French, British, and Dutch law.[193] This access allowed merchants to engage in legal forum shopping, which significantly diluted the Ottoman state's regulatory control over interregional commerce and made regulatory uniformity almost impossible to achieve. The very existence of these overlapping jurisdictions demonstrates the limits on the state's limited capacity. Some historians have argued that merchants even sought out European jurisdiction precisely because of systemic weaknesses in Ottoman legal regulation and enforcement.[194]

Scholars have yet to draw an explicit connection between the Ottoman state's administrative, fiscal, and legal limitations and its reluctance to support business incorporation prior to the later nineteenth century, but it is easy to see how that connection could be made within the confines of the existing literature. A state that lacked the ability to enforce legal and administrative uniformity within its own borders likely would not have been eager to authorize and support the creation of self-governing business corporations that enjoyed independent legal personhood and asset partitioning. Uniformly enforcing these rights and obligations across a set of socially distant investors and creditors—especially tort creditors—may have seemed prohibitively difficult in such a decentralized and pluralistic legal structure. Moreover, the state may have seen these private entities as potential competitors in terms of socioeconomic governance, coordination, and revenue extraction.

The plausibility of this argument is further enhanced by the business corporation's institutional and economic trajectory in the later nineteenth century. Its introduction into the Ottoman economy came in two phases. In the first, which ran from around 1850 to the early twentieth century, the state actively chartered and sponsored a few larger firms, primarily in the maritime-trade sector, with some but not all of the legal features of a business corporation.[195] The first of these, a marine-transportation company founded in 1851, was formed directly

193. *See* Artunç, *supra* note 170, at 723.

194. *See, e.g.*, Asli Cansunar & Timur Kuran, *Economic Harbingers of Political Modernization: Peaceful Explosion of Rights in Ottoman Istanbul* 10-11 (Econ. Rsch. Initiatives at Duke, Working Paper No. 288, 2020), https://ssrn.com/abstract=3434656 [https://perma.cc/KY68-U4WP]; Artunç, *supra* note 170, at 722, 725-26.

195. *See* Kuran, *supra* note 4, at 785; Seven Ağır & Cihan Artunç, *The Wealth Tax of 1942 and the Disappearance of Non-Muslim Enterprises in Turkey*, 79 J. ECON. HIST. 201, 208 (2019).

under the patronage of the sultan and several high-ranking officials.[196] In the second phase, which followed the passage of the first Ottoman law of corporations in 1908, incorporation was offered to private entrepreneurs more generally.[197]

Both phases were closely preceded by significant investments in state-building. Ottoman political and institutional modernization is widely thought to have begun in 1839 with the Edict of Gülhane, which, among other actions, moved to abolish tax farming, formalize state revenue, and rationalize the bureaucracy.[198] Over the next few decades, the Ottoman state would not only experience significant administrative expansion but also undertake a major overhaul of the legal system, adopting Western-style commercial and penal codes in the 1850s, followed by commercial-procedure and maritime codes in the 1860s and a new civil code in the 1870s.[199] Interregional commerce was clearly one of the most important motivating forces behind these changes, which dovetailed with the first phase of corporation-building described above. While these measures ultimately did not manage to generate legal modernization or economic industrialization up to European standards, they produced a substantial increase in the state's governance and legal capacities. By the early twentieth century, with extraterritoriality—under which European powers sought to impose some of their own laws on Ottoman territory[200]—increasingly a source of political tension, the state took further steps to expand its own legal capacity and offer domestic Muslim firms a fully viable alternative to European legal infrastructure.[201]

The basic outlines of Ottoman business history are, therefore, consistent with our theory: only within the context of interregional commerce was there significant local interest in the business corporation. Moreover, nineteenth-century Ottoman state-building and legal reform clearly played a powerful role in the emergence and proliferation of the business corporation, which reinforces the idea that the lack of state support was a major reason why corporate technology failed to emerge in earlier eras. The fact that the government's proincorporation activity in the later nineteenth and early twentieth centuries was systematically preceded by major state-building programs strongly suggests that the

196. *See* Dilara Dal, The Modernization of the Ottoman Navy During the Reign of Sultan Abdülaziz (1861-1876), at 44 & n.70 (Apr. 2015) (Ph.D. dissertation, University of Birmingham), https://etheses.bham.ac.uk/id/eprint/6339/1/Dal15PhD.pdf [https://perma.cc/LY78-GZ2Y].

197. *See* Ağır & Artunç, *supra* note 195, at 233.

198. *See* Cansunar & Kuran, *supra* note 194, at 1-2.

199. *See* Bozkurt, *supra* note 192, at 123.

200. *See* John P. Spagnolo, *Portents of Empire in Britain's Ottoman Extraterritorial Jurisdiction*, 27 MIDDLE E. STUD. 256, 256 (1991).

201. *See* Ağır & Artunç, *supra* note 195, at 216-19.

government's inaction prior to 1851 was due not merely to a lack of interest but also to a lack of state capacity. Unlike in the Chinese case, we do not have the conceptual experiment of a weak state legally recognizing the business corporation without first substantially strengthening its legal and administrative institutions. But everything else largely follows the predictions of our theoretical framework.

C. *Early Modern England*

We now move from two of the most prominent latecomers to corporate law to one of its most important early arrivals: England. In the Middle Ages, England, like other nations in Europe, was filled with private and quasi-public associations that claimed independent legal existences. But it was not until the early modern period, when the administrative and legal capacities of the English state had grown substantially, that anything resembling a modern corporation became viable.

1. *Early Modern English Business Organizations*

Medieval forms of association included religious orders, municipal corporations, and guilds. Each of these, at times, claimed existences as associations, independent of their various members.[202] Religious orders often achieved independent existences in a uniquely English way by titling their property in the names of cotrustees who ensured continuity by holding the property across generations as new members entered the orders and old ones died or left.[203] Guilds likewise held property in trust on occasion as well as in the names of the guilds themselves as quasi-corporate entities with charters from the Crown or local noblemen.[204]

None of these enterprises had the features we ascribe to a modern corporation, however, because none of them were operated for profit. They did not divide their profits across a common pool and issued no capital stock. Entity shielding was not an issue for these associations because they had no residual

202. *See* SUSAN REYNOLDS, KINGDOMS AND COMMUNITIES IN WESTERN EUROPE, 900-1300, at 77 (2d ed. 1997); Edward Cavanagh, *Corporations and Business Associations from the Commercial Revolution to the Age of Discovery: Trade, Jurisdiction and the State, 1200-1600*, 14 HIST. COMPASS 493, 494 (2016).

203. *See* J.M.W. BEAN, THE DECLINE OF ENGLISH FEUDALISM, 1215-1540, at 129 (1968); 2 FREDERICK POLLOCK & FREDERIC W. MAITLAND, THE HISTORY OF ENGLISH LAW BEFORE THE TIME OF EDWARD I, at 231, 237-38 (2d ed. 1898).

204. *See* SHAW LIVERMORE, EARLY AMERICAN LAND COMPANIES: THEIR INFLUENCE ON CORPORATE DEVELOPMENT 17 (1939).

claimants whose debts might plausibly have been satisfied from the assets of the associations.

Guilds warrant particular notice. Prior to the fourteenth century, guilds in England were fraternal organizations concerned primarily with social activities.[205] But in the fourteenth century, they evolved into commercial associations of craftsmen and merchants in specific trades.[206] The guilds established standards for the quality of new goods and for the training of new practitioners. The members of a guild, however, sold their goods as individuals or small partnerships, with no participation in a common pool of profits and no issuance of capital stock.[207]

By the late fourteenth and early fifteenth centuries, the Crown began chartering what are now known as "regulated companies."[208] These were groups of traders who united to buy and sell goods on their own accounts.[209] These companies were empowered to make statutes and ordinances for the governance of their internal affairs as well as the conduct of trade.[210] The governor of each company was further permitted to punish any English subject who disobeyed the rules governing the conduct of trade.[211] These companies accumulated modest pools of capital owing to the fees that they charged members who wished to join.[212] But participation in these pools was never available to persons who were not merchants in the governed areas and was never a principal attraction of joining.[213]

England took the next step toward the creation of corporations with the chartering of regulated companies in the mid-sixteenth century.[214] In 1553, the

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205. *See* Cavanagh, *supra* note 202, at 497.

206. *See id.* at 498.

207. *See* Alfred Kieser, *Organizational, Institutional, and Societal Evolution: Medieval Craft Guilds and the Genesis of Formal Organizations*, 34 ADMIN. SCI. Q. 540, 540 (1989).

208. For a discussion of regulated companies as an intermediate point between guilds and joint-stock companies, see Thomas Leng, *Interlopers and Disorderly Brethren at the Stade Mart: Commercial Regulations and Practices Amongst the Merchant Adventurers of England in the Late Elizabethan Period*, 69 ECON. HIST. REV. 823 (2016).

209. *See id.* at 824.

210. *See id.* at 824, 831.

211. *See id.* at 831.

212. *See* Jelle C. Riemersma, *Government Influence on Company Organization in Holland and England (1550-1650)*, 10 J. ECON. HIST. 31, 34 (1950).

213. *See id.* at 37.

214. Something like a joint-stock company was established for operating mines in 1485. Some noblemen and gentlemen were granted rights over mining in specific areas of the country and

Crown granted charters to the Russia Company and the Africa Company.[215] The Russia Company bore the closest resemblance to a modern corporation. Its charter specifically noted that its members formed "one body" with "one common stocke of the company."[216] The members subscribed £6,000 at £25 per share, and profits from the common enterprise were divided accordingly.[217] It had centralized management, eventually settling upon two governors to be supervised by a 28-member governing committee elected by the company's stockholders.[218] Unlike the Africa Company, which leased its ships and liquidated its capital after each voyage, the Russia Company owned its ships and made its capital somewhat permanent, liquidating and renewing its capital stock only a few times between 1553 and 1620.[219]

The early seventeenth century saw a great profusion of joint-stock companies, many of them organized for overseas trading. First, and most famously, there was the East India Company in 1600.[220] And then, in the two decades following, the Bermuda Company, the Irish Society, the Guinea Company, and the New River Company[221] as well as the Mineral and Battery Works and Mines Royal Societies.[222] Each of these companies issued stock in a common pool and had a centralized set of officers to manage its business and affairs. Shareholders were not craftspeople or merchants who participated in the work of the companies but rather financial speculators who contributed capital passively. Some of these companies reconstituted their capital after each voyage, but eventually, some of them became permanent. The East India Company, for example, made its capital permanent in the mid-seventeenth century, at which point its members probably gained the right to sell their shares without the consent of other owners.[223] Some of these companies also had limited liability as granted by the terms of their charters.[224]

were constituted "governors of the Mines Royal." 1 WILLIAM ROBERT SCOTT, THE CONSTITUTION AND FINANCE OF ENGLISH, SCOTTISH AND IRISH JOINT-STOCK COMPANIES TO 1720, at 18 (1912). "A somewhat similar grant was made for Scotland to a group of foreigners in 1526." *Id.* However, these companies left little record of their internal governance. *See id.*

215. *See id.* at 17.

216. *Id.* at 18-19.

217. *See id.* at 18.

218. *See id.* at 20.

219. *See id.* at 153.

220. *See id.* at 150-51.

221. *See id.*

222. *See id.* at 44-45.

223. *See* SUSAN WATSON, THE MAKING OF THE MODERN COMPANY 44-50 (2022).

224. *See* Philip J. Stern, *The English East India Company and the Modern Corporation: Legacies, Lessons, and Limitations*, 39 SEATTLE U. L. REV. 423, 428 (2016).

Joint-stock companies then declined in popularity throughout much of the latter half of the seventeenth century, until they witnessed another boom in the 1680s and 1690s.[225] It was at this time that trading in common stock first became somewhat widespread.[226] Many of these companies had royal charters, but the bulk operated by titling their property in the names of trustees. The trust ensured entity shielding and even limited liability in the companies that used it, as well as centralized management and tradable shares.[227]

2. *The Role of the State*

One reason to think the rise of joint-stock companies depended on the power of the state is that incorporation required a close association with the state. Prior to the late seventeenth century, nearly all charters for incorporation came directly from the sovereign and promoted the interests of the Crown.[228] As power shifted to Parliament after the Revolution of 1688, incorporation tended to come instead from Parliament.[229]

As the market for shares in joint-stock companies began to boom in the 1690s, it also became common to organize businesses in trust by titling the assets of a business in the names of trustees and causing them to issue beneficial interests in the form of stock to investors.[230] The common-law trust circumvented both Parliament and the Crown by allowing any person to form a business without official action. Such trusts had been available since late medieval times as a matter of right to every English subject, without any need for official permission or even public filing, but they were applied to the business-firm context only in the late seventeenth century.[231]

The process of development from royal chartering to Parliamentary chartering and free formation by trust is consistent with our hypothesis. Prior to the

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225. *See* RON HARRIS, INDUSTRIALIZING ENGLISH LAW: ENTREPRENEURSHIP AND BUSINESS ORGANIZATION, 1720-1844, at 50-57 (2000); SCOTT, *supra* note 214, at 326.

226. *See* HARRIS, *supra* note 225, at 57.

227. *See* MARK FREEMAN, ROBIN PEARSON & JAMES TAYLOR, SHAREHOLDER DEMOCRACIES?: CORPORATE GOVERNANCE IN BRITAIN AND IRELAND BEFORE 1850, at 45-46 (2012); John D. Morley, *The Common Law Corporation: The Power of the Trust in Anglo-American Business History*, 116 COLUM. L. REV. 2145, 2191 (2016).

228. *See* FREEMAN ET AL., *supra* note 227, at 45-46.

229. *See id.*

230. *See* Morley, *supra* note 227, at 2157-58; *see also* FREEMAN ET AL., *supra* note 227, at 15 tbl.1.1 (listing the number of unincorporated companies in the eighteenth and nineteenth centuries alongside the number of businesses organized as corporations).

231. *See* Morley, *supra* note 227, 2156-58.

late seventeenth century, the power of the English state and its judicial institutions was sufficiently weak that the only way to achieve the necessary state support for a corporation was to form the corporation in close partnership with the state.[232] As many have argued, the late medieval and early modern English legal system was both socioeconomically stratified and structurally decentralized: common-law courts coexisted and competed with a large array of other court systems, especially at the local level, ranging from manor and borough courts to ecclesiastical courts, each of which followed a different set of substantive legal rules.[233] While the existence of jurisdictional competition between different courts may have had a positive impact on certain aspects of legal development, it did mean that, until the seventeenth century, the functional finality of any court decision was significantly diluted.[234] Moreover, only a small, highly elite portion of the population had reliable access to royal courts,[235] which further aggravated these courts' unreliability.

Under such circumstances, relying on courts for robust, uniform enforcement of complex business arrangements among large numbers of strangers was a risky proposition. Instead, corporations utilized the direct support of the Crown—and later Parliament—to ensure capital lock-in, asset partitioning, and orderly share transfers. The Crown was interested in promoting corporations to facilitate mercantilist national development and taxation and to enhance the private wealth of royal officials who invested in incorporated business enterprises. After 1688, Parliament may have promoted incorporation for similar reasons.

The emergence of a functionally modern state in the later seventeenth century changed much of this institutional calculus. As much scholarship has demonstrated, the Stuart Restoration in 1660 ushered in an era of robust government investment in fiscal, administrative, and military capacity, which led to a significant expansion and formalization of government institutions.[236] Corre-

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232. On the relatively weak fiscal and administrative capacity of the English state prior to the seventeenth century, see Michael Braddick, *State Formation and Social Change in Early Modern England: A Problem Stated and Approaches Suggested*, 16 SOC. HIST. 1, 2-3 (1991).

233. *See, e.g.*, THEODORE F. T. PLUCKNETT, A CONCISE HISTORY OF THE COMMON LAW 83-100, 176-98 (5th ed. 1956); J. H. BAKER, AN INTRODUCTION TO ENGLISH LEGAL HISTORY 40-47, 127-29 (4th ed. 2002).

234. Nonetheless, as Daniel Klerman observes, "By the seventeenth century, nonroyal courts were of relatively little importance." Daniel Klerman, *Jurisdictional Competition and the Evolution of the Common Law*, 74 U. CHI. L. REV. 1179, 1186 (2007).

235. *See* Richard J. Ross, *The Commoning of the Common Law: The Renaissance Debate over Printing English Law, 1520-1640*, 146 U. PA. L. REV. 323, 335, 378 (1998).

236. *See, e.g.*, STEVE PINCUS, 1688: THE FIRST MODERN REVOLUTION 480-81 (2009); MICHAEL J. BRADDICK, STATE FORMATION IN EARLY MODERN ENGLAND C. 1550-1700, at 253-57 (2000).

spondingly, socioeconomic use of the legal system—both common law and equity—grew significantly, especially after 1688.[237] These developments provided a more hospitable institutional environment for the business corporation and its specific need for legal uniformity. Unsurprisingly, the business corporation did indeed become more generally available to private investors over the same period and even more so in the eighteenth century.[238] Nonetheless, it was not until the mid-nineteenth century that Parliament, through a series of statutes issued between 1844 and 1856, fully relinquished its power to issue business charters, instead allowing free incorporation to any private firm that met a predetermined list of legal requirements.[239]

The growth of business trusts is particularly illustrative because the trust only became widespread in the formation of businesses in the late 1600s, even though the trust had been freely available for the formation of businesses and widely used in the formation of charitable enterprises before then.[240] The late seventeenth century saw several modernizing developments in the operation of the state that may have encouraged the use of trusts. One, of course, was the Revolution of 1688, which not only limited the power of the state to expropriate wealth for itself but also made the state more willing to use its resources in the promotion of private wealth.[241] A closely connected development was the regularization of chancery doctrine. The trust had always been central to the Chancery.[242] But the chancellorship of Lord Nottingham from 1675-1682 regularized all aspects of chancery doctrine and procedure, transforming it from a set of vague, often ad hoc tendencies into a more modern system of clear and definite principles.[243] Lord Nottingham cleared up doubt about whether interests in trust were freely transferable and assured that all forms of property held in trust were not reachable by a trustee's unsecured personal creditors.[244]

237. *See* STEVE HINDLE, THE STATE AND SOCIAL CHANGE IN EARLY MODERN ENGLAND, 1550-1640, at 13-15 (2000).

238. For a summary of the development of English company law during the eighteenth and nineteenth centuries, see generally Turner, *supra* note 7.

239. *See* Henry N. Butler, *General Incorporation in Nineteenth Century England: Interaction of Common Law and Legislative Processes*, 6 INT'L REV. L. & ECON. 169, 179-82 (1986).

240. *See* GARETH JONES, HISTORY OF THE LAW OF CHARITY, 1532-1827, at 6 (1969) (stating that the bulk of charitable endowment in late medieval and early modern England was held in trust).

241. *See* North & Weingast, *supra* note 4, at 820-28.

242. It is possible that the first recorded example of the Chancery enforcing a trust took place in 1446 in *Myrfyn v. Fallan* (1446) 2 Cal. Ch., xxi. *See* JAMES BARR AMES, LECTURES ON LEGAL HISTORY AND MISCELLANEOUS LEGAL ESSAYS 237 n.3 (1913).

243. *See* Dennis R. Klinck, *Lord Nottingham and the Conscience of Equity*, 67 J. HIST. IDEAS 123, 124 (2006).

244. *See* Morley, *supra* note 227, at 2154 n.45, 2169 n.163.

It is possible to see in the development of English state institutions in the early seventeenth century a set of developments that enhanced the appeal of joint-stock companies by modernizing the state and thereby increasing the odds of uniformity in the management of corporate affairs. Among these were the increasing centralization and systematization of the courts. In 1616, King James decreed the supremacy of the Court of Chancery over the common-law courts.[245] The Court of Chancery had long had a close association with the Crown and with the law of trusts. It thus had jurisdiction in matters involving contracts, trusts, and corporations.[246] Though hostility to Chancery persisted through the Interregnum (1649-1660) and the restoration of the monarchy in 1660, the Chancery's authority and jurisdiction remained unchanged.[247]

The strength of the Chancery was important because it offered assurance of reliable law enforcement. Chancery often allowed witnesses to be compelled to testify.[248] It also offered specific enforcement as a remedy.[249] Specific enforcement was valuable because it increased the strength of entity shielding, allowing property taken by an owner or his creditor to be taken back directly without needing to rely on the owner's or creditor's solvency for damages.

The transformation from regulated companies to joint-stock companies is evidence of the growing power of the state. The regulated companies of the sixteenth century existed largely to supplement the deficiencies in the state's capacity to enforce the law. The principal function of the regulated companies was to develop rules and enforce them against members. They operated as quasi-public legal institutions, with authority delegated by the state. The state's willingness to delegate in this way was a tacit acknowledgment of its own limitations. The limitation of membership in the regulated companies to practitioners of a particular craft or merchant trade is further evidence that community-based norm enforcement was challenging to sustain as the community grew too large and the connections among its members became too weak. Members of the regulated companies could be reached by legal as well as extralegal forms of pressure because they all worked in a common social space. The mix of noblemen and wealthy investors who became members of the seventeenth-century joint-stock

245. *See* The King's Order and Decree in Chancery (1616), 21 Eng. Rep. 65, Cary 133.

246. *See id.*; JOHN H. LANGBEIN, RENEE LETTOW LERNER & BRUCE P. SMITH, HISTORY OF THE COMMON LAW: THE DEVELOPMENT OF ANGLO-AMERICAN LEGAL INSTITUTIONS 329-35 (2009).

247. *See* LANGBEIN ET AL., *supra* note 246, at 349.

248. *See* John H. Langbein, *The Disappearance of Civil Trial in the United States*, 122 YALE L.J. 522, 540 (2012) (describing the procedural innovations of the Chancery).

249. *See generally* Joshua Getzler & Mike Macnair, *The Firm as an Entity Before the Companies Acts*, *in* ADVENTURES OF THE LAW: PROCEEDINGS OF THE SIXTEENTH BRITISH LEGAL HISTORY CONFERENCE, DUBLIN, 2003, at 267, 272-74 (Paul Brand, Kevin Costello & W.N. Osborough eds., 2005) (exploring the historical origins and application of this remedy).

companies was more diverse, less connected, and less amenable to extralegal pressure, thereby placing greater pressure on the enforcement capacities of the state.

D. Early United States

The rise of the corporation in the United States in the eighteenth and nineteenth centuries shared a number of characteristics with the corporation's rise in England: it began with a transition phase in which the state's administrative and legal capacities were relatively limited and in which business corporations could only come into existence through individual charters. By the 1830s and 1840s, however, decades of state-building enabled many American court systems to reliably enforce corporate laws and encouraged state legislatures to pass general incorporation acts allowing businesspeople to form corporations freely. Unlike the late nineteenth-century Chinese case, American corporate history does not offer a counterfactual in which a legal system attempted and failed to introduce business corporations prior to modern state-building. Nonetheless, it is consistent with our primary argument that the corporation could not become widespread without robust state-building.

1. Corporations and Individual Charters

Until the early nineteenth century, corporations in the United States could only be created through express acts of government authorization. During the Colonial Era and the first several decades of the Republic, nearly all corporations in the United States were created through individual charters issued by legislatures.[250] There was often doubt regarding the authority and legitimacy of colony-issued charters, however, with many colonial governors unsure of their authority to issue charters.[251] Sometimes, in an attempt to avoid judicial scrutiny, colonial legislatures crafted charters as memorials to the Crown, conditioning the effectiveness of an act of incorporation on royal approval.[252] Nonetheless, incorporations were occasionally invalidated by judges who concluded that the legislature lacked the requisite authority.[253]

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250. *See* JAMES WILLARD HURST, THE LEGITIMACY OF THE BUSINESS CORPORATION IN THE LAW OF THE UNITED STATES, 1780-1970, at 14 (1970).

251. *See* JOSEPH STANCLIFFE DAVIS, *Essay I: Corporations in the American Colonies*, *in* 1 ESSAYS IN THE EARLIER HISTORY OF AMERICAN CORPORATIONS 3, 10-13 (1917) [hereinafter DAVIS, ESSAY I].

252. *See id.* at 19-20.

253. *See id.* at 22.

Prior to 1780, there were few, if any, for-profit business corporations, which further clarifies the state-driven nature of early American incorporation.[254] Corporations were either municipal, ecclesiastical, charitable, or educational organizations.[255] Public corporations were not sharply differentiated in law from private corporations.[256] In the mid to late 1700s, a number of corporations concerned with public works were chartered, including wharf-building and water-supply companies.[257] While these organizations bore a resemblance to business corporations, they may have been more akin to community-funded public-works projects, as it is unclear whether their owners expected or realized any profits.[258]

From the 1780s through the early 1800s, almost all corporations were "chartered for activities of some community interest."[259] The earliest charters can be sorted into three groups: "internal improvement companies (turnpikes, toll bridges, canals, water supply); monied corporations (banks, insurance); and manufacturing companies (textiles, iron and steel, glass, earthenware)."[260] Although these corporations were operated for private gain, they clearly contributed to local community welfare and were recognized as such by contemporaries.[261]

These early American corporations eventually came to possess nearly the full range of legal technologies that we associate with the modern corporation. By the early 1800s, common-law doctrine provided that chartered corporations had limited liability unless otherwise specified in the charter.[262] Some legislatures did

254. *See* Simeon E. Baldwin, *American Business Corporations Before 1789*, 8 AM. HIST. REV. 255, 257 (1903); JOSEPH STANCLIFFE DAVIS, *Essay IV: Eighteenth Century Business Corporations*, *in* 2 ESSAYS IN THE EARLIER HISTORY OF AMERICAN CORPORATIONS 3, 32 fig.5 (1917) [hereinafter DAVIS, ESSAY IV].

255. *See* DAVIS, ESSAY IV, *supra* note 254, at 329.

256. *See id.* at 4.

257. *See id.*

258. *See id.* at 19.

259. HURST, *supra* note 250, at 15.

260. RONALD E. SEAVOY, THE ORIGINS OF THE AMERICAN BUSINESS CORPORATION, 1784-1855: BROADENING THE CONCEPT OF PUBLIC SERVICE DURING INDUSTRIALIZATION 50 (1982). According to James Willard Hurst, corporate charters granted between 1780-1801 featured the following industry breakdown: 66% transportation, 20% banks and insurance, 10% local public services, and 4% "general business corporations." HURST, *supra* note 250, at 17. The "general business corporations" category likely refers primarily to manufacturing enterprises. *See id.*

261. *See* SEAVOY, *supra* note 260, at 48-49.

262. *See* Howard Bodenhorn, Extended Liability at Early American Banks 2 (Aug. 2014) (unpublished manuscript), https://www.atlantafed.org/-/media/documents/news/conferences/2015/0511-workshop-on-monetary-and-financial-history/papers/extended-liability-at-early

seem to harbor some discomfort with this new technology. For example, Massachusetts and Pennsylvania imposed unlimited liability on owners of manufacturing firms.[263] Additionally, legislatures often imposed double liability, a form of limited liability where stockholders' liability extended to twice the value of their invested capital.[264] Despite these variations, by 1832 limited liability was the default rule in most states and was seen as "one of the primary motivating factors encouraging the use of the corporate form."[265]

Corporate charters and common law also established a degree of entity shielding. Charters typically specified that shareholders could not withdraw capital unless the corporation was dissolved, and they provided that dividends could only be paid out of the "clear profits and income" of the firm.[266] Entity shielding was also present from the early 1800s in the form of the "trust fund" doctrine, which held that "in an insolvent corporation, the directors have fiduciary duties running to creditors because corporate assets are held in trust to satisfy creditors first."[267]

Legal recognition of asset partitioning provided the institutional foundation for free share transfers. Judicial decisions from the 1810s-1820s suggest that shares of corporate stock were generally freely transferrable. Though corporate charters or bylaws typically required share transfers to be recorded on a company's books, courts often disregarded this rule, ratifying off-book transfers in many cases.[268] However, in situations where there was no asset partitioning, courts ruled that shareholders could not evade personal liability for corporate

-american-banks.pdf [https://perma.cc/JA75-BADJ]; *see also id.* at 1 ("[L]imited liability appears to have been the default rule for corporations in the United States very nearly from the foundation of the Republic."); Richard Sylla, *Early American Banking: The Significance of the Corporate Form*, 14 BUS. & ECON. HIST. 105, 111 (1985) ("Limited liability of corporations quickly became 'a matter to be taken for granted' in Massachusetts law." (quoting OSCAR HANDLIN & MARY FLUG HANDLIN, COMMONWEALTH: A STUDY OF THE ROLE OF GOVERNMENT IN THE AMERICAN ECONOMY: MASSACHUSETTS, 1774-1861, at 147 (rev. ed. 1969))).

263. *See* Howard Bodenhorn, *Double Liability at Early American Banks* 3-4 (Nat'l Bureau of Econ. Rsch., Working Paper No. 21494, 2015), https://www.nber.org/system/files/working_papers/w21494/w21494.pdf [https://perma.cc/3KEU-MXLS].

264. Double liability was commonly imposed on chartered commercial banks in the early 1800s. *See id.* at 4-5.

265. Margaret M. Blair, *Locking-in Capital: What Corporate Law Achieved for Business Organizations in the Nineteenth Century*, 51 UCLA L. REV. 387, 439 (2003).

266. *Id.* at 430.

267. *Id.* at 432.

268. *See* EDWIN MERRICK DODD, AMERICAN BUSINESS CORPORATIONS UNTIL 1860: WITH SPECIAL REFERENCE TO MASSACHUSETTS 115-18 (1954) (first citing United States v. Vaughn, 3 Binn. 394 (Pa. 1811); then citing Quiner v. Marblehead Soc. Ins., 10 Mass. (9 Tyng) 476 (1813); and then citing Bank of Utica v. Smalley, 2 Cow. 770 (N.Y. Sup. Ct. 1824)).

debts through strategically timed transfers of shares, such as to buyers lacking personal assets.[269]

At this early stage of American history, the legal and administrative capacities of the state were still relatively weak, which ironically seemed to strengthen the institutional reliance of corporations on state support. The authority of colonial governments to engage in certain acts of regulation and governance—including, as noted above, the power to issue corporate charters—was sometimes in doubt.[270] Early state governments were hampered by "limited administrative capacity"—and, as a result, inconsistent judicial capacity—in the 1780s and 1790s.[271] Companies appear to have frequently ignored or circumvented the terms of their charters without legal penalty.[272] What nonetheless made these chartered corporations economically viable was the direct injection of state support: the "semi-public" nature of the corporations,[273] coupled with state sponsorship, provided the institutional credibility for sophisticated asset-partitioning arrangements and, as a result, meaningful capital accumulation. The close relationship between governments and corporations created ample opportunities—as it did in the English case discussed above—for rent-seeking and monopolistic behavior, but this was impossible to eradicate without further expansion of the state's formal legal power. Fortunately, such an expansion was rapidly materializing in the early nineteenth century.

2. *State-Building and General Incorporation Acts*

As a growing body of recent scholarship has demonstrated—and contrary to what some have called the "myth of the 'weak' American state"[274]—American governments, both federal and state, significantly ramped up their administrative and legal capacities between 1783 and 1860.[275] Government fiscal income,

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269. *See, e.g.*, Marcy v. Clark, 17 Mass. (17 Tyng) 330, 335 (1821); DODD, *supra* note 268, at 119-20.

270. *See* DAVIS, ESSAY I, *supra* note 251, at 20-22.

271. Eric Hilt, *Early American Corporations and the State*, *in* CORPORATIONS AND AMERICAN DEMOCRACY 37, 52 (Naomi R. Lamoreaux & William J. Novak eds., 2017).

272. *See id.* at 52-53.

273. Eric Hilt, General Incorporation and the Shift Toward Open Access in the Nineteenth-Century United States 1 (2014) (unpublished manuscript), http://conference.nber.org/confer/2014/CSf14/Hilt.pdf [https://perma.cc/U4CD-GFC8].

274. William J. Novak, *The Myth of the "Weak" American State*, 113 AM. HIST. REV. 752, 754 (2008).

275. *See, e.g.*, GARY GERSTLE, LIBERTY AND COERCION: THE PARADOX OF AMERICAN GOVERNMENT FROM THE FOUNDING TO THE PRESENT 17-86 (2015); MAX M. EDLING: A HERCULES IN THE CRADLE: WAR, MONEY, AND THE AMERICAN STATE, 1783-1867, at 32-38 (2014); Gautham Rao, *The New Historiography of the Early Federal Government: Institutions, Contexts, and the Imperial* both state and federal, experienced substantial growth in the early nineteenth century and then escalated even more quickly after 1830.[276] The growth of fiscal capacity directly supported the robust expansion of state institutions, particularly legal ones. Much of this early state-building occurred at the county level, where local populations invested significant resources into the construction of viable county governments and courts throughout the first five decades of the Republic. The county-court system, in particular, quickly became the locus of early American legal-infrastructural investment. The number of counties tripled between the 1790s and 1830s, bringing with it the creation of new courts across most of the country, upon which additional layers of appellate courts were established during the early nineteenth century.[277] The Mid-Atlantic and Southern states experienced rapid growth in their number of county courts.[278] New England, with its older and more established network of courts, was the exception to this quantitative expansion but nonetheless made significant institutional investments to further formalize, entrench, and empower its county-court system.[279] Much of the American state—and its legal apparatus—was being constructed from the bottom up rather than from the top down. But, at around the same time, there was a significant expansion of federal power, including legal power, much of it driven by the westward expansion of settlers and ensuing legal conflicts with Native American land and territorial claims.[280]

For our purposes, the most salient consequence of early American state-building was the enhanced ability of courts to enforce corporate charters and resolve disputes. From the 1830s onward, the rapidly growing use of courts suggested a growth in trust in the judiciary. The 1832 version of Joseph K. Angell and Samuel Ames's *A Treatise on the Law of Private Corporations Aggregate* already documents a swiftly increasing caseload in state courts on matters of corporate

State, 77 WM. & MARY Q. 97, 107-13 (2020); Jerry L. Mashaw, *Recovering American Administrative Law: Federalist Foundations, 1787-1801*, 115 YALE L.J. 1256, 1277-82 (2006); Jerry L. Mashaw, *Reluctant Nationalists: Federal Administration and Administrative Law in the Republican Era, 1801-1829*, 116 YALE L.J. 1636, 1647-55 (2007).

276. *See* John Joseph Wallis, *American Government Finance in the Long Run: 1790-1990*, 14 J. ECON. PERSPS. 61, 65 tbl.1 (2000).

277. *See* Patrick Peel, Building Judicial Capacity in the Early American State: Legal Populism, County Courts, and Credit, 1645-1860, at 64 fig.3.6 (Aug. 2009) (Ph.D. dissertation, Johns Hopkins University) (ProQuest).

278. *See id.* at 86 fig.3.15, 104 fig.3.17.

279. *See id.* at 75-85.

280. *See generally* GREGORY ABLAVSKY, FEDERAL GROUND: GOVERNING PROPERTY AND VIOLENCE IN THE FIRST U.S. TERRITORIES (2021) (describing the construction of federal power in the territories during the eighteenth century).

governance and liability,[281] but the second edition of the *Treatise*, published in 1861, cites to five times the number of cases.[282] Even in 1830, lawyers

> who had occasion to deal with corporate matters could find answers in American decisions to many more questions relating to business corporations than an English lawyer of the same period could have found in the English cases . . . despite the fact that American case law on [corporate law] had been practically nonexistent at the beginning of the century.[283]

Most importantly, courts had broadly accepted the separate-entity theory of corporate personality.[284]

These legal developments provided the institutional foundation for a wave of general incorporation acts that became mainstream in the 1830s and 1840s.[285] Initial experimentation with general incorporation, which allowed private firms that met certain predetermined criteria to register as corporations without any legislative charter, began in the 1810s. New York passed a general incorporation act in 1811 that covered only manufacturing businesses,[286] which had unusually high capital needs compared to other firms. This was quickly followed by similar statutes in Ohio, New Jersey, and Illinois.[287] These early legal prototypes generally exhibited a certain level of unease with private incorporation and imposed fairly strict limitations on its use. New York, for example, "precisely enumerated the industries in which the firms created could operate; limited the size of the board of directors to nine persons, who were required to be stockholders; limited the capital stock to a maximum of $100,000 and limited the duration of the firms' existence to twenty years."[288] Within several years of their initial passage,

281. *See* JOSEPH K. ANGELL & SAMUEL AMES, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS AGGREGATE, at xxiii-xxxv (Boston, Hilliard, Gray, Little & Wilkins 1832).

282. *See* DODD, *supra* note 268, at 124.

283. *Id.* at 120.

284. *See id.* at 121.

285. For general or regional narratives of this process, see Eric Hilt, *Corporation Law and the Shift Toward Open Access in the Antebellum United States*, *in* ORGANIZATIONS, CIVIL SOCIETY, AND THE ROOTS OF DEVELOPMENT 147, 147-77 (Naomi R. Lamoreaux & John Joseph Wallis eds., 2017); Douglas Arner, *Development of the American Law of Corporations to 1832*, 55 SMU L. REV. 23, 44-53 (2002); and William C. Kessler, *Incorporation in New England: A Statistical Study, 1800-1875*, 8 J. ECON. HIST. 43, 43-48 (1948).

286. *See* Hilt, *supra* note 285, at 152.

287. *See id.*

288. *Id.*

the general incorporation acts of Ohio, New Jersey, and Illinois were actually repealed.[289]

A second, more robust wave of general incorporation acts began to emerge in the late 1830s, on the back of robust state-building and economic growth. Beginning with Pennsylvania's 1836 general incorporation act for iron manufacturers and over the course of the 1840s and 1850s, most states, starting with the Mid-Atlantic and Northwestern states and eventually spreading to the South, passed statutes that allowed general incorporation for at least some segment of their business community.[290] Some of these statutes – the earliest example being Connecticut's 1837 statute – even took the additional step of allowing general incorporation for all industries.[291] By 1860, "twenty-seven of thirty-two states and organized territories had adopted general incorporation acts."[292]

The specific timing of these statutes depended on many factors, ranging from the political strength of vested interests held by previously chartered corporations, which often were not eager to see new competitors emerge, to the economic structure of each individual state – for example, manufacturing-heavy states moved substantially more quickly than agriculture-heavy ones.[293] Nonetheless, the fact that nearly all general incorporation acts came after a nationwide wave of significant state-building from the 1790s to the 1830s strongly suggests that the administrative and legal capacity of the state was an important factor in the rise of general incorporation.

All in all, the antebellum history of the American corporation largely unfolded along the trajectory predicted by our theoretical framework: prior to robust state-building in the early Republic, incorporation generally required direct government authorization and institutional reinforcement. Without such direct injections of state support, the ability of courts to reliably enforce corporate charters was widely held in doubt. Following a few decades of robust state-building, however, states gained the ability to recognize and enforce general incorporation acts, laying the institutional foundation for the modern American corporate economy.

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289. *See id.* at 151 tbl.5.1.

290. *See id.* at 151 tbl.5.1, 153-54.

291. *See id.* at 154.

292. *Id.* at 156.

293. *See id.* at 159-61.

E. Premodern Mediterranean Prototypes

Unlike the previous four cases, our final two historical case studies, medieval Italian city-states and Ancient Rome, are situated in societies that developed neither the business corporation nor a functionally modern state. We include them here only because they have played an outsized role in academic study and contain what some scholars consider prototype corporate forms, that is, forms of premodern business organization that utilized core legal technologies, such as asset partitioning, associated with the corporation.[294] Given that our primary argument is that the rise of the corporation relies on the rise of the modern state, it is, of course, vulnerable to any demonstration that "society *A* had the corporate form but did not have a functionally modern state." A survey of the corporate literature indicates that the most written-about candidates for "society *A*" are medieval Italian city-states and ancient Rome, due to the existence of asset partitioning in at least some of their business forms. The goal here, then, is to demonstrate that, on that literature's own terms,[295] those prototype business forms are not functional equivalents of the business corporation and, therefore, pose no threat to our thesis.

1. Medieval Italian City-States

Italian city-states of the tenth and eleventh centuries produced the *commenda*, a trading venture that involved a passive capital investor and a maritime trader who actively managed venture assets while traveling among major economic centers.[296] In most cases, the trader did not supply capital beyond the

294. Other legal technologies employed by the business corporation have a long history too. Collective governance and separate legal personality are found, for example, in some medieval Catholic Church institutions and municipal governments. *See* HARRIS, *supra* note 3, at 255-62. However, asset partitioning and tradable shares, which, as we explained in Section I.C.2, are critical for the business corporation's ability to scale capital beyond closely knit communities, emerged later. *See id.* at 269-74.

295. In other words, we describe these prototype forms only as they are commonly described in the existing literature and do not seek to revise the history using primary sources. Our posture here is purely defensive: without challenging the historical descriptions offered by corporate-law scholars, we argue that their accounts pose no significant threat to our thesis.

296. *See generally* HARRIS, *supra* note 3, at 130-70 (describing the origin and evolution of the *commenda*); QUENTIN VAN DOOSSELAERE, COMMERCIAL AGREEMENTS AND SOCIAL DYNAMICS IN MEDIEVAL GENOA 62-77 (2009) (describing the history of *commendae* and detailing their structures and restrictions); Harris, *supra* note 9, at 609-12 (detailing the characteristics and debated origins of the *commenda*); Hansmann et al., *supra* note 21, at 1372-74 (discussing the *commenda* structure and its spread); FREDERIC C. LANE, VENICE: A MARITIME REPUBLIC 52 (1973) (describing the rise of the Venetian *commenda*). The *commenda* has drawn academic attention as far back as the late nineteenth century. *See* WEBER, *supra* note 14, at 63-85.

means of transportation, but in some cases he might supply some monetary capital. Once the trader returned to the capital investor's hometown (upon the completion of a single voyage), each party received his share of the assets, including base capital and accumulated profits, and the *commenda* was dissolved.[297]

Although collaboration between wealthy capital holders and traveling merchants had long been a fixture in Mediterranean economic life, the *commenda* has drawn outsized academic attention due to its use of both limited liability and strong entity shielding: the passive investor's liability was limited to his investment.[298] The traveling merchant bore full responsibility for the *commenda*'s third-party liabilities but was liable to the passive investor for losses only if the merchant had breached his fiduciary duties.[299] Moreover, the joint venture enjoyed strong entity shielding from either partner's personal creditors, who could not force the liquidation of its assets prior to dissolution.[300] Generally speaking, the demand-side conditions for the formation of the *commenda* were similar to those seen in previous case studies, namely, long-distance interregional trade that exceeded the geographical and regulatory boundaries of any single closely knit community.[301] On the supply side, however, the *commenda* operated without the advent of any government entity that was functionally comparable to a modern state. Medieval Italian city-states were among the most powerful administrative and legal entities of their time, but compared to later nineteenth-century Eurasian or American legal systems, the city-states were less able to police and enforce their laws over large geographical and social distances.[302]

Why, then, should we not consider the *commenda* a counterexample to our thesis? In terms of legal functionality, there are several major differences between the *commenda* and a business corporation. First, the *commenda* only provided limited liability to a subset of business collaborators—the capital investors and not the merchant. More importantly, it was very limited in both scale and duration. The standard *commenda* was between a single capital investor and a single traveling merchant, and if the merchant wished to carry additional goods on this

297. On the basic institutional structure of the *commenda*, see HARRIS, *supra* note 3, at 131-36; Hansmann et al., *supra* note 21, at 1372-74; and Harris, *supra* note 9, at 609-11.

298. *See* HARRIS, *supra* note 3, at 132-33.

299. *See id.* at 133.

300. *See* Hansmann et al., *supra* note 21, at 1372-73.

301. *See* HARRIS, *supra* note 3, at 132-33.

302. On state-building in medieval Italian city-states, see THOMAS ERTMAN, BIRTH OF THE LEVIATHAN: BUILDING STATES AND REGIMES IN MEDIEVAL AND EARLY MODERN EUROPE 35-89 (1997); and Avner Greif, *Self-Enforcing Political Systems and Economic Growth: Late Medieval Genoa*, *in* ANALYTIC NARRATIVES 23 (Robert H. Bates, Avner Greif, Margaret Levi, Jean-Laurent Rosenthal & Barry R. Weingast eds., 1998).

trip, he would generally have to assemble multiple *commendae*.[303] In addition, the duration of a *commenda* was typically limited to one voyage, and dissolution was automatic upon the ship's return to the original harbor.[304] These features significantly limited the economic value and complexity of *commenda* agreements, constraining them to a specific kind of economic transaction with fairly narrow uses. In other words, the socioeconomic component of our definition of "rise of the corporation"[305] simply did not exist.

For more complex, longer-duration commercial activities, or for any kind of agricultural or manufacturing activity, business collaborations in medieval and Renaissance Italy generally took the form of a *compagnia*, which was functionally similar to a modern partnership. The *compagnia* provided only weak entity shielding to firm assets – that is, it gave firm creditors priority over the personal creditors of individual investors but did not prevent the personal creditors from forcing liquidation – and offered no limited liability to investors.[306] The *commenda* form thus limited itself across many of the dimensions we associate with "modernity" in a corporation: number of collaborators, duration of collaboration, and complexity of activity.

The limitations of the *commenda* are intuitive once we consider the constrained legal and administrative capacity of Italian city-states. Their information-collection and rule-enforcement abilities were confined to a relatively small geographical region, beyond which they had to rely on cooperation from sometimes adversarial political entities.[307] Therefore, it seems unlikely that the city-states could have supplied adequate institutional support for complex, long-duration collaboration between large numbers of socially unconnected investors.

These dynamics become even more apparent when we consider the geographical and economic reach – or rather, limitations – of the *commenda*. Despite the outsized academic attention it has drawn, the *commenda* was not necessarily the dominant way of funding and supplying maritime trade in medieval Venice or Genoa. Instead, it coexisted with at least one other major form of maritime financing: the sea loan, an older and less complicated financial transaction in which the merchant trader simply took out loans prior to a journey and repaid them with interest upon its completion.[308] What made the sea loan somewhat

303. *See* HARRIS, *supra* note 3, at 131-36; Hansmann et al., *supra* note 21, at 1372.

304. *See* Hansmann et al., *supra* note 21, at 1372.

305. *See supra* Section I.A.

306. *See* Hansmann et al., *supra* note 21, at 1365-67; HARRIS, *supra* note 3, at 134.

307. *See* sources cited *supra* note 296.

308. *See generally* Yadira González de Lara, *Enforceability and Risk-Sharing in Financial Contracts: From the Sea Loan to the Commenda in Late Medieval Venice*, 61 J. ECON. HIST. 500 (2001) (explaining the coexistence of the two methods of funding).

distinctive was the assumption of greater risk by creditors, whose right to demand repayment was conditional upon the ship's safe return to harbor.[309] Nonetheless, compared to a *commenda*, the sea loan was both less risky for capital contributors and easier to enforce, given that their financial returns were not pegged to the voyage's actual profits.

The choice between a *commenda* and a sea loan, as several scholars have argued, essentially came down to proximity and predictability: "The further away a node was in a mercantile network . . . the younger the network and the newer the destination, and the lower the frequency of voyages to that destination, the more likely it was that [the] sea loan would be selected rather than a commenda."[310] Furthermore, "[w]ars, the Black Death, and other such large-scale interruptions" increased the use of sea loans while suppressing the use of the *commenda*.[311]

Commenda-like maritime-trade institutions were thus a relatively common fixture in late medieval Eurasian trade, appearing in the Islamic world, where it likely originated, as well as in Northern Europe, the Indian subcontinent, Central Asia, and China.[312] And yet, until the advent of modern state-building, nowhere did it develop into an economically scalable and durable functional equivalent of the modern business corporation.

2. *Ancient Rome*

The other major set of "prototype corporations" that scholars often speak of comes from Ancient Rome, which is less counterintuitive than it seems when one considers the mainstream historical belief that Europe did not regain the economic and legal sophistication of Ancient Rome until perhaps a millennium after the collapse of the Western Roman Empire in 476 AD. Two institutions in particular have received the lion's share of academic attention[313]: the *peculium*, a device through which slaveowners could invest financial assets into slave-owned

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309. *See* Jonathan R. Ziskind, *Sea Loans at Ugarit*, 94 J. AM. ORIENTAL SOC. 134, 134 (1974).

310. HARRIS, *supra* note 3, at 165 (summarizing Yadira González de Lara, *The Secret of Venetian Success: A Public-Order, Reputation-Based Institution*, 12 EUR. REV. ECON. HIST. 247 (2008); and Dean V. Williamson, *Transparency and Contract Selection: Evidence from the Financing of Trade in Venetian Crete, 1303-1351*, 63 J. ECON. HIST. 555 (2003)).

311. *Id.*

312. *See id.* at 136-63.

313. We make no claim here that these were necessarily the best analogies to modern corporations in the Roman world. The reason we focus on them is that others have highlighted them as possible corporate prototypes. As noted earlier, our posture here is purely defensive: we simply aim to rebut the idea that they were corporate prototypes. If other scholars nonetheless wish to identify other corporate prototypes in ancient law, the burden of proof is on them.

businesses;[314] and the *societas publicanorum*, a vessel for private Roman citizens to collaborate in the provision of public services.[315] Both emerged during the heyday of the Roman Republic, and while the *peculium* persisted into the Roman Empire, the *societas publicanorum* phased out of existence earlier.[316] Both have been described as protocorporations that allowed for some form of asset partitioning, and the *societas publicanorum* in particular has been called "the earliest predecessor of the modern business corporation."[317] The argument here, however, is that, in the way they are commonly described in the corporate-law literature, they did not come close to providing the institutional functionality of the modern corporation.

The *peculium* referred to investments made by slaveowners to businesses managed by their slaves.[318] Under such arrangements, the slaveowner enjoyed limited liability so long as he remained a passive investor, even though he was the full owner of both the business and the slave-manager. The business did not, however, enjoy strong entity shielding—and, according to some scholars, may not even have enjoyed weak entity shielding—against the slaveowner's personal creditors.[319] Occasionally, a *peculium* could be created between father and son, in which the former invested in the latter's business, despite the latter's formal legal subjugation to the former: all Roman property was nominally owned by heads of family (*patresfamilias*), whose relationship with their offspring was, in many ways, as hierarchical as that between slaveowner and slave.[320]

Unlike the medieval *commenda*, the Roman *peculium* offered at least the possibility of long-term business relationships between investors and managers. Nonetheless, the *peculium* lacked the core functionalities of modern corporations. First, it lacked strong entity shielding and possibly weak entity shielding

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314. *See* Hansmann et al., *supra* note 21, at 1358-60; Abatino et al., *supra* note 10, at 370-81; HARRIS, *supra* note 3, at 255.

315. *See* Hansmann et al., *supra* note 21, at 1360-61; Malmendier, *supra* note 10, at 1078; HARRIS, *supra* note 3, at 255.

316. *See* Malmendier, *supra* note 10, at 1087-88.

317. *Id.* at 1077; *see also* HARRIS, *supra* note 3, at 255 (surveying the literature that "views the corporation as a Roman jurists' invention").

318. *See* Richard Gamauf, *Slaves Doing Business: The Role of Roman Law in the Economy of a Roman Household*, 16 EUR. REV. HIST. 331, 332 (2009).

319. *Compare* Hansmann et al., *supra* note 21, at 1359-60 (arguing that the *peculium* enjoyed no entity shielding), *with* Abatino et al., *supra* note 10, at 379-81 (contending that "there was a weak form of entity shielding within the *peculium*").

320. *See* Gamauf, *supra* note 318, at 331; Kate Cooper, *Closely Watched Households: Visibility, Exposure and Private Power in the Roman* Domus, 197 PAST & PRESENT 3, 5, 8 (2007).

as well.[321] This alone removes a critical corporate feature that underlies the operation of modern equity trading. Second, and just as importantly, the *peculium* offered little capacity for capital accumulation beyond what the slaveowner or *paterfamilias* already owned. If the primary economic function of a corporation is the ability to draw capital investments from a large number of socially unconnected investors, then the *peculium* offered virtually none of it. The fact that it was limited to slaveowner-slave or father-son relations meant that it had almost no financial scalability. The only possibility for scaling was if multiple slaveowners agreed to shared ownership of a slave and merged their assets into his business,[322] but co-ownership of slaves could not materialize between strangers, given the near-absolute personal control and strong economic control that slaveowners held over their slaves.[323] More commonly, *peculium* businesses were single-ownership entities.[324]

The primary function of the *peculium* was, therefore, not to accumulate capital or facilitate cross-household collaboration but rather to give slaves with business expertise the necessary legal status and functional separation to independently manage their owner's financial assets.[325] The nearly absolute sociolegal control that slaveowners possessed over slaves, or fathers over sons, allowed these businesses to function without much institutional support from the state, but this came at the near-complete loss of financial scalability.

Given the *peculium*'s socioeconomic limitations, scholars have pointed to another legal institution, the *societas publicanorum*, as the true Roman prototype of the business corporation.[326] Private Roman business collaborations sometimes took the form of a *societas*, which was functionally similar to a partnership and did not offer asset partitioning.[327] A *societas publicanorum* was an exception to this, offering limited liability to passive investors and strong entity shielding to the firm.[328] Consistent with mainstream theoretical predictions, these features allowed the *societas publicanorum* to accumulate capital on a fairly large scale: it

321. *See* sources cited *supra* note 319.

322. *See* Abatino et al., *supra* note 10, at 370-71, 377.

323. *See* Peter Birks, *The Roman Law Concept of Dominium and the Idea of Absolute Ownership*, 1985 ACTA JURIDICA 1, 11, 18.

324. *See* Hansmann et al., *supra* note 21, at 1360. *But see* Abatino et al., *supra* note 10, at 371 n.28 (suggesting that it is unclear how common co-owned slave businesses were).

325. *See* Morris Silver, *At the Base of Rome's* Peculium *Economy*, 22 FUNDAMINA 67, 68-69, 76 (2016).

326. *See* Malmendier, *supra* note 10, at 1077; Hansmann et al., *supra* note 21, at 1360-61.

327. *See* Hansmann et al., *supra* note 21, at 1356-57.

328. *See id.* at 1360-61; Malmendier, *supra* note 10, at 1077.

could sometimes attract hundreds of investors, whereas the standard *societas* typically only had a few.[329] As a matter of institutional structure, the *societas publicanorum* did indeed bear a substantial resemblance to the business corporation.

The catch, however, was that it was not generally available to private enterprises. Instead, the *societas publicanorum* "evidently provided services only to the state and not to private parties."[330] Its primary function was to provide certain public services: the construction of public works, the production of military supplies, or tax collection.[331] Such services were supplied on the basis of contracts between the joint venture and the Roman state, which also monitored and sometimes intervened in the venture's activities.[332] To a large extent, the *societas publicanorum* was treated as a functional extension of the Roman state, providing services that were too expensive for the state to supply itself but were nonetheless backed directly by state authority. Upon the expansion of the professional Roman bureaucracy in the early Empire, the state's administrative need for external contractors began to decline, causing the *societas publicanorum* to fall into disuse by the second century.[333] Its most distinctive institutional features—limited liability and strong entity shielding—were never adopted by private *societas* ventures.[334]

These historical developments fit easily within our theoretical framework. Between the state-adjacent *societas publicanorum* and the private *societas*, only the former allowed for asset partitioning, but it also lost its economic significance as soon as the state withdrew its institutional support. Despite the fact that Roman business actors clearly knew of asset partitioning, they consistently refused to, or perhaps were unable to, utilize it in private-business organizational activities outside of the limited and idiosyncratic circumstances of the *peculium*. This suggests, therefore, that the existence of direct government involvement made all the difference to the institutional and economic viability of asset partitioning in Roman business relations. However, given the legal and administrative limitations of premodern states, even the Roman state, direct government involvement could only be found in a fairly limited set of socioeconomic activities, which meant that there was no true functional equivalent of the business corporation in Roman law. All in all, not only is the Roman case *not*, as corporate scholars

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329. *See* Hansmann et al., *supra* note 21, at 1356, 1361.

330. *Id.* at 1361.

331. *See id.* at 1360.

332. *See id.* at 1360-61.

333. *See* Malmendier, *supra* note 10, at 1090-92.

334. *See* Hansmann et al., *supra* note 21, at 1356.

have conventionally described it, an instance of the business corporation emerging without relying on state-building; the Roman case actually seems to positively support our thesis.

CONCLUSION

Histories of economic development have a tendency to see the state and the corporation as competitors, perhaps even antagonists. If the corporation is the central institution of modern capitalism,[335] and if capitalism thrives on laissez-faire economic policies, then it is not difficult to see why, up to this point, scholars have mainly portrayed a negative relationship between the state and the corporation. On that account, the best thing the state can do for the corporation is to get out of the way—to credibly commit against expropriating corporate assets, whether through taxation or direct takeover.[336]

This Article argues, however, that the state also has a more affirmative role to play in promoting the corporate form. The legal technologies used by the corporation, particularly asset partitioning and tradable shares, are not socioeconomically viable without robust institutional support by a modern state. This is not because other sources of economic regulation, such as those supplied by closely knit communities, are necessarily *incapable* of recognizing and enforcing rules for asset partitioning, but rather because those legal technologies lack the geographical and social reach and the systematic devotion to fairness and uniformity that are necessary to promote collaboration among large groups of strangers.

Beyond explaining the rise of the modern business corporation, the theoretical framework that we have built here also identifies several functional differences between corporate law and other subfields of private law. Much more so than contract law, tort law, or even property law, corporate law deals with complex and not-fully-foreseeable interactions between large numbers of strangers who share interests in a common pool of resources. These attributes render corporate law unusually reliant on state institutions, as opposed to private contractual arrangements or communal self-governance, for legal enforcement.

Corporate law even points the way to a more general theory of the kinds of legal relationships that are in greatest need of institutional reinforcement by modern states: those that connect strangers; those that connect numerous parties; those that last for a long time; and those that involve complex interactions. On all these dimensions, modern business corporations exist predominantly at

335. *See* ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 1 (1932).

336. *See* sources cited *supra* note 4.

one end of the spectrum—strangers, numerous parties, long-lasting, and complex.

In other words, our theoretical framework points to the possibility of separating private-law institutions into two functional categories: those that are only significantly attractive in *gesellschaft* (stranger-oriented) contexts, and those that are also useful in *gemeinschaft* (closely knit communal) contexts.[337] In the latter category reside most subfields of private law, including most kinds of contracts, torts, and property as well as some business organizations, such as the partnership. These institutions are routinely found in premodern customary law, enforced by villages, manors, kinship networks, religious groups, and guilds across most of human history, often without significant reliance on the state's legal institutions.[338]

In the former category is a much narrower range of institutions, of which the corporation is the most prominent, but probably not the sole, example. Many aspects of trust law, modern business-bankruptcy law, and negotiable-instruments law are probably not very useful within the boundaries of closely knit communities.[339] Given their reliance on modern state-building, most of these institutions emerged very late in human history—only in the past two or three centuries—but their ability to accumulate capital and facilitate trade far beyond the limits of *gemeinschaft* institutions has given them an outsized role in the modern global economy. Much more work is needed before we can clarify all the core

337. *See* Kamenka, *supra* note 16, at 3-4. To some extent, this distinction bears a resemblance to the information-cost theory of private law championed by Henry E. Smith in a series of articles, including Smith, *supra* note 74; Henry E. Smith, *Property and Property Rules*, 79 N.Y.U. L. REV. 1719 (2004); and Henry E. Smith, *Property as the Law of Things*, 125 HARV. L. REV. 1691 (2012), in that both emphasize the importance of information conveyance between strangers to the economic functionality of private law. That said, Smith's theories apply primarily to relatively simple interactions in the context of property and contract law. It would be impossible to coordinate complex interactions in the corporate context through the kinds of exclusion-based strategies that Smith champions in property law.

338. On the communal enforcement of complex property, contract, and tort rules in premodern and early modern societies, see ZHANG, *supra* note 65, at 12-13; and Taisu Zhang, *Moral Economies in Early Modern Land Markets: History and Theory*, 80 LAW & CONTEMP. PROBS. 107, 129-33 (2017).

339. Insofar as business trusts used many of the same legal technologies, including asset partitioning, as the business corporation, they are another example of a *gesellschaft* institution, and their late emergence in England in the late seventeenth and eighteenth centuries, largely parallel to the emergence of the corporation, seems to support this contention. *See generally* Morley, *supra* note 227 (explaining how the common-law trust wielded corporation-like powers). On the emergence of business bankruptcy over the same period, see Louis Edward Levinthal, *The Early History of Bankruptcy Law*, 66 U. PA. L. REV. 223 (1918). On the history of negotiable-instruments law, see William S. Holdsworth, *The Origins and Early History of Negotiable Instruments I*, 31 LAW Q. REV. 12 (1915).

institutional and functional features of these "*gesellschaft* institutions." But hopefully, this Article has made a strong enough case for their basic existence.