

Revisiting American Exceptionalism: Business Organizational Forms and Corporate Governance in Comparative Perspective

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Abstract: The legal rules governing businesses' organizational choices vary across nations along two main dimensions: the number of different forms that businesses can adopt; and the extent to which businesses have the contractual freedom to modify the available forms to suit their needs. During the last quarter of the twentieth century, legal rules in the U.S. have converged on those of other advanced industrial nations along both of these dimensions. Over the preceding century and a half, however, businesses in the U.S. had a narrower range of forms from which to choose than their counterparts in these other countries and also much less ability to modify the basic forms contractually. This chapter argues that the sources of this "American exceptionalism" reside in the interplay between the early achievement of universal (white) manhood suffrage (which fueled "Jacksonian" attacks on corporate privilege) and elites' efforts to safeguard property rights.

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1. Introduction

The idea of American exceptionalism, particularly the notion that American institutions should be held up as a model to the rest of the world, has been out of favor among historians in recent years. The idea had its roots in Massachusetts Puritans' vision of their settlement in the Bay Colony as the "city on the hill" and in early nineteenth-century American's belief in their "manifest destiny" (Murrin 2000; Onuf 2012). "Whig" historians like George Bancroft, writing in the third quarter of the nineteenth century and "Progressive" historians like Frederick Jackson Turner at the century's end transformed it into a story of the growth of democracy and the spread of liberty (Ross 1984; Tyrrell 1991). This version had considerable influence on historical writing through much of the twentieth century, though there was always a counter narrative that emphasized the limits of the achievement and the extent to which progress was the result of bottom-up struggles. More recently, historians have tended to stress the dark side of these trends and in particular the extent to which increases in the rights and status enjoyed by common white men came at the expense of women, blacks, native peoples, and other minority groups. As a result, the notion that we should study U.S. history for lessons that other countries might profitably emulate has largely disappeared from historical writing, despite the strong hold that the idea of American exceptionalism continues to exert on the popular mind (Tyrrell 1991).

Economists are more likely than historians to hold the United States up as a model, but they do not typically use the language of American exceptionalism. Instead, economists usually discuss the American advantage as the product of a set of measurable characteristics that cross-

country regressions have shown to be significantly related to economic performance. These characteristics include geographic factors that are largely outside history (such as climate or topography); institutional or cultural characteristics that, though they are products of history, are very difficult to change (such as a country's ethnic makeup); and institutional or cultural variables that, though they are products of history, could at least in theory be adopted by any country (like a political system with a constrained executive).¹ It is mainly this last category that leads economists to treat the U.S. as a standard to which other countries should aspire.

Cross-country analysis is necessarily crude, however. The need to collect the same types of data for a large set of countries means that the explanations they test are couched in terms of variables that are readily available and easy to gather, but as a consequence very broad and general—such how many degrees of latitude a country is from the equator, whether its lands contain valuable mineral deposits, the number of different linguistic groups it encompasses, or whether it has a civil-law or a common-law legal system. What is lost in these exercises is the particular geographic context, the specific factor endowments, the distinct set of institutions, and the way all these peculiarities interact to give each country its own separate history. Most economic analysis ignores these nuances, relegating them to the error term or attempting to sweep them out collectively by adding various kinds of fixed effects as controls.² Cross-country analysis would be impossible without such techniques, but much of what is unique about a country—much of what drives its specific history—is in those fixed effects.

¹ The literature is voluminous, but see Barro 1997; Barro and McCleary 2003 and 2006; La Porta, Lopez-de-Silanes, Shleifer, and Vishny (hereafter LLSV) 1997 and 1998 and 1999, and the studies summarized in La Porta, Lopez-de-Silanes, and Shleifer 2008; and Roe and Siegel 2009. See also Bloom and Sachs 1998; Gallup, Sachs and Mellinger 1999; and Sachs and Warner 2001.

² Much of the advance in this literature has come from developing novel instrumental variables that stand in for more complex historical processes, such as settler mortality for institutional quality or proportion of the population sold into slavery for social disorganization. These innovations have introduced all kinds of measurement problems that may drive the results. More important, they still force us to relegate most country-specific nuances to the error term or to fixed effects, where they are lost to analysis. See Acemoglu, Johnson, and Robinson (2001), Ablouy (2012), and Acemoglu, Johnson, and Robinson (2012).

Clearly one cannot take on a cross-country study with scores of cases and do a detailed investigation of each one. Not only would such a study be prohibitively expensive, but it would fall apart. It would quickly become apparent that the variables coded so seemingly objectively for the purposes of cross-country regressions often mean very different things in different contexts and so the comparisons are really quite artificial. For some variables, moreover, there would be so much within-country variation, especially for large countries, that picking a single national magnitude obscured more than it revealed. The scholars exploring the nuances of the particular countries would find themselves pulled in different directions and would end up with a set of observations that would be incommensurate in many ways and hence defy generalization.

Case studies are an important alternative to cross-country regressions and are usually justified in one of two ways. The first is the inherent importance of the subject. For example, many economists research only the U.S. economy and do not think of themselves as doing a case study. The U.S. is the largest economy in the world; it drives much of the international economy. Scholars who study it simply see themselves as writing on something that is obviously important. The second justification is analytical leverage. A case may be important to study because it offers a critical test of a hypothesis or opens up the analysis in some way—for example, by suggesting new alternative hypotheses or casting doubt on the conventional scholarly wisdom. A good example is Karen Kupperman's history of the failed English settlement of Providence Island in the early seventeenth century. The colonizers were from the same group of Puritans that promoted the Massachusetts Bay Colony, yet on Providence Island they set up an agricultural system that relied on slave labor and did not give settlers property rights to land. Trivial though the case was in the broader scheme of colonial settlement, it was

worthy of study because it cast doubt on the conventional association between Puritan ideas and the landholding and labor systems of colonial New England (Kupperman 1993).

Although studying the history of business organization forms in the United States could easily be justified on the first grounds, I want to rest my case on the second. The cross-country literature has produced a number of studies debating the advantages for economic development of common law systems versus civil law systems.³ Much of this literature uses a simple one-zero coding scheme that treats all countries with common-law legal systems alike and then accounts for differences by including various kinds of controls and fixed effects. The starting point of this paper is the observation that the legal rules governing corporations in the most successful of all the common-law countries, the United States, historically were fundamentally different from those in Britain, which were themselves more like the rules in civil-law countries. U.S. law was distinctive in that it was both more restrictive about what corporations were allowed to do and more prescriptive about the forms their internal contractual relations could take. This paper will argue that the U.S. difference can largely be explained by the timing of the expansion of the franchise relative to general incorporation. In Britain, and also on the European continent, general incorporation predated universal manhood suffrage by many years. In the U.S. the timing was the reverse. General incorporation laws were passed in the context of mass political partisanship where restrictions on corporations were a way of preventing “the moneyed few” from using their political influence to gain unfair advantages over other economic actors. They were also passed in a context where elites feared that the expansion of the franchise would encourage democratically elected legislators to tamper with property rights.

How these countervailing forces played out varied from one state to the next. There was no archetypal U.S. story in the nineteenth century. Rather there was a Massachusetts story, a

³ ##citations

New York story, a Virginia story, an Ohio story, and so on. This paper focuses in particular on the experience of Pennsylvania in the late nineteenth century, when democratic politics kept the state's general incorporation laws remarkably restrictive and creditor-oriented (pro-property rights) courts hamstrung an early effort to create what Larry Ribstein (2010) has called an "unincorporation," essentially a limited liability company (LLC). The same forces played out in different ways in the different U.S. states, and there was little pressure for uniformity until the very end of the century. Nonetheless, the conflict over privileges versus property rights that the expansion of the franchise propelled was a national phenomenon that, I would argue, drove the legal evolution of business organizational forms in the United States throughout the nineteenth century and would continue to exert an effect in the twentieth, even after the chartermongering competition from New Jersey and then Delaware began to erode the differences among the states. Hence, although this paper tells a story of American exceptionalism in the old fashioned sense, it is a story rooted in conflict. It is a story of how the struggle over economic power in a period of increasing democratization shaped an important set of institutions, giving them characteristics that many scholars have since held up as examples for the rest of the world to emulate.

2. The Distinctive Character of Business Organizational Forms in the U.S.

Virtually everywhere in the world, business people could only form corporations in the early nineteenth century if they had the specific authorization of the state. In other respects, however, there were substantial differences in the menu of business organizational forms available across countries. In Britain, for example, the only alternative to the corporation that multi-owner enterprises could use was the ordinary partnership, a form in which all members of

the firm bore unlimited liability. In France, by contrast, business people had two alternative forms. They could organize ordinary partnerships in which all the members were unlimitedly liable, or they could organize limited partnerships in which one or more partners bore unlimited liability but the rest were liable only for the amount of their investments. Most of the U.S. states passed laws allowing businesses to organize limited partnerships, but the form was never as popular as in France, in part because the courts interpreted the law much more strictly (Guinnane et al. 2007).

In most countries governments chartered very few corporations during the early nineteenth century, and many more businesses wished to form corporations than could obtain charters. In France, business people developed a workaround in the 1820s in the form of the *commandite par action*—that is, the limited partnership with tradable shares. Disgruntled shareholders in failed *commandites* challenged this innovation in 1830 on the grounds that it was not explicitly permitted by the *Code de Commerce*, the body of law that governed forms of business organization. However, both the Commercial Tribunal of Paris and, on appeal, the Royal Court loosely construed the *Code de commerce*. Once the practice was upheld, the number of *commandites* with tradable shares grew rapidly in the middle of the century, and the ability freely to form *commandites par action* reduced the need for corporations. It was only when the government responded to a series of scandals by passing legislation in 1856 that more strictly regulated the issuance of shares that demand for the corporate form increased.⁴ The government finally in 1863 enacted a general incorporation law for firms with a capitalization of

⁴ Demand for the corporate form was also lower in France than in the U.S. and Britain because business people could more easily control their liabilities in partnerships. In both Britain and the U.S. partnership contracts were a private matter and so were not enforceable vis-à-vis third parties that did not have specific notice of their contents. If one partner borrowed on behalf of the firm, all of the partners were liable for the debt, even if their partnership contract had forbidden them from encumbering the firm without the permission of the other parties. In France, by contrast, so long as a partnership registered its governing contract as required by law, the terms of the contract were fully enforceable. Thus members of ordinary partnerships could limit the extent of their exposure by insisting on their right to sign off on all their company's debts (Lamoreaux and Rosenthal 2005).

20 million francs or less and then in 1867 for all firms (Freedeman 1979, Lamoreaux and Rosenthal 2005).

In Britain business people responded to the difficulty of securing a corporate charter from Parliament by developing a very different work around: unincorporated joint stock companies. These were essentially partnerships whose governing contracts allowed them to concentrate managerial authority and function, for the most part, as if they were legal persons. Because they lacked limited liability, however, they were a second-best solution to the problem of pooling capital. Moreover, under the Bubble Act of 1720 they were technically illegal. Although they flourished in a legal grey area for many decades, during the mid-1820s the courts handed down a series of decisions interpreting the Bubble Act in ways that cast doubt on their legality. Worried entrepreneurs responded by deluging Parliament with petitions for corporate charters, and Parliament, overwhelmed by the sheer number of petitions, repealed the Bubble Act in 1825 (Harris 2000; Freeman, Pearson, and Taylor 2012). Not surprisingly, the number of joint-stock companies surged over the next couple of decades, but so did the number of companies that went bust. Entrepreneurs, who wished to form new companies, as well as wealth holders with assets to invest, wanted something done about the situation, and consensus built within the elite for legislation that would regulate the hodge-podge of private companies soliciting investments from the public without killing them off. The composition of Parliament had already shifted in favor of business interests in the wake of the Reform Act of 1832. Finally esponding to the growing demand for action, Parliament passed an act in 1844 granting corporate status, though not limited liability, to any company that registered, met certain minimal requirements, and promised to file regular financial statements. It completed the transition to general incorporation by adding

limited liability in 1855 and 1856 (Harris 2000; Taylor 2006; Freeman, Pearson, and Taylor 2012).

The U.S. from the beginning was an important outlier, with the U.S. states chartering many more corporations than governments in other places, in large measure because they were strapped for funds. The states faced insistent demands during the early nineteenth century to provide their citizens with the infrastructure needed for economic development, from transportation improvements to financial services. Without revenue sources to finance these projects on their own, they granted corporate charters to private groups that would promise to undertake them in their stead. [Here add numbers showing the much greater number of charters granted in the U.S. than in Britain or France.]

Nonetheless, even in the U.S. the demand for corporate charters greatly exceeded supply. In order to convince private investors to finance infrastructural project of uncertain profitability, the states offered additional inducements. Perks granted to incorporators of the Society for Useful Manufactures (SUM), a textile company chartered in New Jersey in 1791, included permission to raise funds through a public lottery and exemptions for the company's employees from taxes and military service, except in the case of invasion (Maier 1993). The most common boon, however, was the grant of market power. Charters for turnpike, bridge, and canal companies typically conveyed the monopoly right to levy tolls on a particular route, as well powers of eminent domain. Perhaps the most famous example was the monopoly granted by the Commonwealth of Massachusetts to the Charles River Bridge Company because it led to an important decision by the U.S. Supreme Court (Kutler 1971). Early bank charters invariably carried with them an implicit promise of monopoly power, as well as the right to issue currency in the form of bank notes (Handlin and Handlin 1969; Lamoreaux 1994). Indeed, bank charters

were so valuable that control of entry into banking became an important way of solidifying political power in the years following the American Revolution. Whichever party dominated the legislature kept tight control of bank charters and only awarded them to prominent supporters (Lamoreaux and Wallis 2012, Lu and Wallis 2013, Bodenhorn 2006).

The monopoly privileges that accompanied corporate charters generated a tremendous amount of resentment, both among the members of the general population who shouldered the burden of higher prices and among other entrepreneurial groups seeking to compete away some of the monopoly rents. In the context of an expanding franchise, mounting discontent led to an erosion of monopoly power. In some places (Massachusetts is a good example), legislatures responded to popular pressure by granting additional charters. In 1828, for instance, the Massachusetts General Court granted a charter of incorporation to a company that proposed to build a bridge over the Charles River right next to one that purportedly had been granted a monopoly. Massachusetts also granted numerous charters for banks in competition with existing financial institutions—so many, in fact, that when the state finally passed a general incorporation law in 1851, almost no banks formed under it (Kutler 1971, Lamoreaux 1994, Lu and Wallis 2013). In most states, however, popular pressure led to the passage of general incorporation laws. When the political turmoil that followed the Panic of 1837 finally dislodged the Albany Regency (New York's Democratic political machine) from power, the legislature passed the first "free banking" act. Other states soon followed, and the act subsequently became the model for the National Banking Acts passed by the U.S. Congress during the Civil War. The first general incorporation act for manufacturing was enacted by the New York legislature as a way of encouraging domestic industry during the run-up to the War of 1812, but few states followed suit until the late 1840s. The Panic of 1837 and the depression that followed a second major

financial crisis in 1839 led a number of states to default on their debts. The political realignments that followed led to major constitutional reforms and also to the spread of general incorporation laws, so that by 1860 the vast majority (27 out of 32) states and territories had enacted them (Hilt 2013, Wallis 2005).

Enacted in a context where there was widespread outrage about corporate privileges, many of the general incorporation laws passed during this period contained severe restrictions on what corporations could do, how big they could grow, and what forms their internal governance could take. The extent of these regulations varied from state to state, but as a general rule they tended to be most restrictive in states that had chartered large numbers of corporations by private act (Harris and Lamoreaux 2010, Hilt 2013). [Discussion of Table 1, which shows some of the variation in restrictiveness among the most important states. Mention that statutes often included additional prescriptions, e.g. for quorums at stockholders' and directors' meetings and for the supermajorities needed to increase or decrease capital or change the business purpose. Mention also that they applied only to limited types of business.]

By contrast, in Britain and on the European continent, where general incorporation laws long preceded the expansion of the franchise, the statutes were much more permissive. The case of Britain is particularly interesting because the law and finance literature lumps it together with the U.S. as a common-law country. However, beyond the requirement that a company could not be formed by less than seven persons, the law imposed none of the kinds of restrictions that one finds in the U.S. statutes. Companies were by default perpetual. They could engage in any lawful business, could be as large or as small as the incorporators desired, could have limited or unlimited liability, and could hold any amount of real estate or other property. Moreover, they had almost complete contractual freedom to organize their internal affairs as they chose.

The original 1844 act had been drafted by a committee chaired by William Gladstone, then president of the Board of Trade under Prime Minister Robert Peel. The early years of Peel's administration were the heyday of free trade and laissez-faire, and the act that came out of Gladstone's committee permitted incorporators to add to the law's very basic governance template any "provisions for such other purposes (not inconsistent with Law) as the parties to such Deed shall think proper."⁵ The 1856 law increased the extent of contractual flexibility by replacing the basic template with a set of default governance rules, included in a table appended to the act. This table was formalized in the 1862 act as Table A. If a company did not supply its own articles of association, the detailed governance rules in Table A applied. But a company could reject any or all of the provisions of the table and write its own rules from scratch. About the only provisions the law required was that the company hold a general meeting each year and that the articles of association be amendable by a three-quarters vote of the shareholders (Guinnane, Harris, and Lamoreaux 2013).⁶

[Discuss how in the U.S. how popular attacks on corporate privileges were perceived by elites as attacks on property rights and how led to pro-creditor bias in the courts and strict construction of statutes granting limited liability.]

3. A Tale of Two Statutes: The Case of Pennsylvania in the Late Nineteenth Century

Pennsylvania's general incorporation acts for business were particularly restrictive in the early nineteenth century. The first act, passed in 1836, applied only to companies manufacturing

⁵ Companies Act 1844 7&8 Vict. C. 110 Section VII. For the historical background see Harris (2000) 278-286 and the references therein.

⁶ There was no requirement that directors be elected at the annual meeting, and indeed quite a few companies entrenched at least some of their directors for life. See Guinnane, Harris, and Lamoreaux 2013.

iron using processes fueled by coke or mineral coal.⁷ This limitation was so strict that not even other kinds of iron companies could avail themselves of the act; as Section 7 emphatically reiterated, “nothing herein contained shall be construed to empower such corporation to manufacture iron which has not been manufactured from the ore, with coke or mineral coal.” Not until 1852 was the act extended to companies manufacturing iron with charcoal.⁸ Companies organized under the 1836 act were limited to twenty-five years duration. They had to have a capital of at least \$100,000 but not more than \$500,000 and would forfeit their charter if at any time they contracted “debts to a greater amount than that of the capital subscribed.” They could not hold more than 2,000 acres of land divided into not more than three parcels, all of which had to be in the same county or in “two counties which shall adjoin each other” (Sections 1, 3 and 6). Companies were to be managed by a board of directors elected by the stockholders according to a proportional voting rule that limited the number of votes large shareholders could cast (Section 3).

Pennsylvania’s first general law “To encourage manufacturing operations in this commonwealth,” enacted in 1849 still applied only to a limited set of companies formed “for the purpose of carrying on the manufacture of woolen, cotton flax, or silk goods, or of iron, paper, lumber or salt.”⁹ It was gradually extended over the next couple of decades to “the manufacture of glass” (1850), “articles made from salt, except in Philadelphia” (1851), “printing and publishing” (1851), “manufacture of enamelled and vitrified iron, and articles made of cast or wrought iron, coated with glass or enamel, within the County of Allegheny” (1852), “oil and other products of rosin” (1852), “mining and manufacturing of mineral paints and artificial slates

⁷ “An Act to encourage the manufacture of Iron with Coke or Mineral Coal ...,” *Laws of the General Assembly of the Commonwealth of Pennsylvania, Passed at the Session of 1835-36* (Harrisburgh: Teo Ferk, 1836), 799-803.

⁸ It was extended to companies that made steel as well as iron in 1864. See Eastman 1908, Vol. 1, p. 6.

⁹ ##citation to statute

and other articles made by the use of said painting materials except in Philadelphia” (1852), “manufacture of artificial manures, and of articles made out of iron and other metals, or out of wood, iron and other metals” (1853), “mining coal, mining, quarrying and preparing for market lime, marl, soda, hydraulic cement, or other minerals, smelting copper, lead, tin or zinc ores, quarrying marble, stone or slate, and manufacturing lumber” (1853), “manufacture of flour in Philadelphia and Beaver counties” (1853), “quarrying, preparing for market and vending marble, sandstone and other stone used for building purposes” (1853), “common carriers, without the capacity to hold real estate” (1854), “manufacture of leather in certain counties” (1859), “manufacture of oils, hydro-carbon fluids and all other products resulting from subjecting coal of any kind to the action of heat or the process of distillation” (1856), “manufacture of oil from mineral coal in Beaver County” (1859), “the mining, manufacturing and refining of carbon oil” (1860), “manufacture of fuel” (1860), “manufacture and preparation of lubricating oil and material, out of and from mineral oils, and other oils or fatty substances, whether mineral animal or vegetable” (1863), and the “manufacture of leather in the county of Elk” (1865) (Eastman 1908, 8-9).

Moreover, even given their restricted application, the laws imposed substantial limitations on companies’ activities and internal governance structures. Although the 1849 “general” law was expansive in some ways (companies faced no ceiling on capital and could have liabilities up to three times the amount of capital paid in), they could not hold more than 2,000 acres in real estate and their duration was limited to twenty years. They were to be managed by a board of 5 to 13 directors, the majority of whom must be citizens of the United States. The president had to be a director, but the secretary and treasurer could not be. Stockholders had one vote per share, but no individual stockholder could cast votes amounting to

more than one-third of issued shares (see Table 1). Directors had the power to make bylaws “subject however to the revision and approval of the stockholders.” There were elaborate rules governing voting by proxy (for example, “no stockholder, females excepted, residing within ten miles of the place appointed for such general meeting or election, shall vote by proxy”), the powers of directors (they could not use the company’s funds “for any banking purposes whatever, nor in the purchase of any stock in any other corporation,” nor to make loans to any stockholder or officer on the security of the company’s own stock), and for calling special meetings or holding meetings and votes to increase or decrease capital.¹⁰

These detailed regulations were not the result of any fundamental antipathy to general incorporation laws. Pennsylvania was one of the first states to pass a general statute “for the incorporation of religious, charitable and literary associations (1791) had early passed a general incorporation act for churches.¹¹ Rather they stemmed from conflict economic power (Hartz 1948). [Discuss how main disputes were about banking but how they carried over to other sectors. Use the debates at the 1837 Constitutional Convention to show that the issues were framed as corrupt privileges versus demagogic attacks on property rights.]

[Discuss how the restrictive general incorporation legislation led companies to seek special charters. Give sense of the large numbers of special charters and the relatively few companies chartered under the general laws. Show how legislature’s willingness to grant special charters fueled further antipathy to both corporations and the legislature. The main reform impulse became getting the legislature out of the business of passing “local or special” laws, including corporate charters, that might give some person or persons opportunities that others did

¹⁰ Citation to statute.

¹¹ That act was extended to beneficial societies and associations and to fire-engine and hose companies in 1832 and to Odd Fellow’s, Free Masons’, and town and city hall associations in 1855. Eastman 1908, 5.

not possess and that might, therefore, be a source of corruption. The issue came to a head during at Pennsylvania's 1872-73 constitutional convention.]

3.1. The 1872-73 Constitutional Convention

If businesses were no longer going to be able to secure special charters that met their needs, then the restrictive character of the state's general incorporation laws posed serious problems. Worried businessmen found a champion among the delegates in the person of Henry C. Carey, the well-known writer on political economy. Carey was a Republican delegate at large and chaired the Committee on Industrial Interests and Labor. He thought there should be a constitutional provision embodying the principle that Douglass North, John Wallis, and Barry Weingast have called "open access." In Carey's words, the constitution should guarantee "the right of the people of the State to associate together for all lawful purposes, and for trading on principles of limited or unlimited liability" (*Debates*, Vol. 5, 481). Carey's recommendation was embedded in a report he presented to the convention on June 12, 1873 under the title "Capital and Labor" (*Debates*, Vol. 5, 470-81). The report complained that in Pennsylvania, in contrast to Great Britain and a few of the U.S. states, "the right of association, for any purposes of trade or profit, has never been admitted" (*Debates*, Vol. 5, 479). To the contrary, Pennsylvania's laws imposed such liabilities and taxes on members of corporations that "the general law has remained almost, if not absolutely, a dead letter" and businesses of necessity sought special acts (*Debates*, Vol. 5, 480). As late as the previous year, he pointed out, the legislature had passed general incorporation acts for iron and steel and other manufacturing enterprises that gave companies the choice of organizing with either limited or unlimited liability but imposed significant disadvantages on firms that chose to be limited. Not only did the latter have to pay a

higher “bonus” to the state at the time of their formation than firms choosing unlimited liability, but their members were still unlimitedly liable “for debts due for labor or services” from the preceding six months (*Debates*, Vol. 5, 480).

Carey’s committee did not have jurisdiction over the parts of the constitution that concerned corporations, so it overstepped its authority in making this recommendation. There was no similar statement in the article initially drafted by the committee that did have jurisdiction, the “Committee on Private Corporations,” but on the article’s second reading the committee’s chair, George W. Woodward (Chief Justice of the Pennsylvania Supreme Court and a Democratic delegate at large), proposed an amendment that Carey accepted as a close substitute: “It shall be the duty of the Legislature to provide by general enactment that any five or more persons, citizens of this Commonwealth, associated for the prosecution of any lawful business, may, by subscribing to articles of association and complying with all requirements of law, form themselves into an incorporated company, with or without limited liability, as may be expressed in the articles of association, and such publicity be provided for as shall enable all who trade with such corporations as adopt the limited liability to know that no liability exists beyond that of the joint capital which may have been subscribed” (*Debates*, Vol. 6, 17). After an extensive discussion, the convention agreed provisionally to a revised version of the amendment that was closer to Carey’s original assertion of a right of association: “Any two or more persons, citizens of this Commonwealth, associated for the prosecution of any lawful business, may, by subscribing to articles of association and complying with all the requirements of the law, form themselves into an incorporated company with or without limited liability as may be expressed in the articles of association, and such publicity shall be provided for as shall enable all who trade with such corporations as adopt the limited liability to know that no liability exists beyond that of

the joint capital which may have been invested or subscribed” (*Debates*, Vol. 6, 27). The amendment, however, was stricken from the draft constitution on the third reading. Despite Woodward’s support, it had been added to the article mainly with Republican votes. Republicans had overwhelmingly supported the measure on second reading, with 40 in favor and only 11 opposed, whereas the Democratic delegates had been evenly divided, with 23 for and 25 against (*Debates*, Vol. 6, 27). After the debate heated up on the third reading, Democrats voted to strike the amendment by a three to one margin, 33 to 11. The Republican vote was closer, but also in favor of striking the amendment by a vote of 27 to 23 (*Debates*, Vol. 7, 779).

When the amendment had been originally proposed, a few Democratic delegates had spoken against it on the grounds that it was “class legislation in favor of capitalists” (*Debates*, Vol. 6, 23). When the section came up again on the third reading, these opponents moved beyond their general antipathy to corporations to expound on the dangers to creditors of making limited liability so broadly accessible. Thus S. C. T. Dodd warned that “we shall have no more partnerships; individuals cannot do business; it will all be done by corporations ... and every one knows that the moment men form themselves into a corporation they lose their moral responsibility in their business” (*Debates*, Vol. 7, 765).¹² These expressions of concern for creditors were somewhat disingenuous. The very next year, as we will see, the legislature would pass overwhelming and with virtually no discussion a law that freely granted limited liability to “any three or more persons who may desire to form a partnership association,” an early type of limited liability company (LLC), at the same time as they continued to impose significant restrictions on corporations.¹³ As the convention’s, and the legislature’s, subsequent actions

¹² Ironically, about a decade later, Dodd would, as lawyer for Standard Oil, engineer the formation of the Standard Oil Trust.

¹³ See “AN ACT Authorizing the formation of partnership associations, in which the capital subscribed shall alone be responsible for the debts of the association, except under certain circumstances,” enacted 2 June 1874, in

make clear, the positions many of the Democratic representatives were driven by fears about the economic power of large-scale business or about the economic power of wealthy individuals within large-scale businesses. Their warnings about the dangers of limited liability did, however, resonate with a certain type of Republican worried about protecting creditors. As one Republican delegate who had originally supported the amendment fretted, the clause would enable any two persons to “set up a grocery on the corner in any town, advertise that they have put in a thousand dollars, spend it all, and leave their creditors minus” (Vol. 7, 763). As a consequence, the vote on striking the amendment was much less along party lines than other votes on corporations.

Not only did Democrats in the convention oppose embodying a right freely to form corporations in the constitution, but they went further and imbedded in that document rules restricting what corporations could do and how they could be governed—rules that one normally might expect to be a matter of statute and that in Britain were left for the articles of association to determine. For example, the 1873 constitution specified that a corporation could not hold real estate beyond what was “necessary and proper for its legitimate business” (Article XVI, Section 5), that “no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received” (Article XVI, Section 7), and that increases in capital within the ceilings allowed by law required “the consent of the persons holding the larger amount in value of the stock” obtained at a meeting “held after sixty days notice” (Article XVI, Section 7). The constitution even imposed a uniform voting rule for “all elections for directors or managers of a corporation,” mandating that “each member or shareholder may cast the whole number of his votes for one candidate, or distribute them upon two or more candidates, as he may prefer” (in other words, cumulative voting) (Article XVI, Section 4).

The most vocal supporters of including these restrictions in the constitution spoke about the evils of corporate privileges and their corrupting influence on the legislature. Thus Charles R. Buckalew, a Democratic delegate from a largely rural part of the state, countered an objection that the imposition of cumulative voting would bypass the legislature and strip it of its regulatory powers by claiming that legislators had been so corrupted by large corporations that they could not be trusted to use their powers for the public good:

Yes, sir, it does take away the power from the Legislature to give undue power to dominating men or cliques who undertake to run corporations in their own special interests and to the disadvantage of the stockholders. It is a check upon the Fisks and the Vanderbilts of the country in manipulating Legislatures to the injury of the general stockholders of a company; and that is all the effect that it has. The Legislature ought not to have this subject in charge. It ought to be settled as one of the fundamental arrangements concerning these corporate bodies. (Vol. 5, 759)

Rallying to this kind of Jacksonian rhetoric, Democratic delegates voting overwhelmingly (37 to 7) in favor of inserting into the constitution a requirement that corporations adopt cumulative voting. A large majority of Republican delegates opposed the measure (the Republican vote was 14 to 27), but that was not sufficient to prevent its passage on second reading (Vol. 5, 768). The provision easily withstood a motion to delete it on the third reading of the bill (Vol. 7, 760-61).

The 1873 constitution stripped the Pennsylvania legislature of much more than the right to regulate voting procedures in corporations. The revulsion that Delegate Buckalew expressed about the corrupt use of legislative power permeated the entire convention. As a result Article III, Section 7 contained a long list of categories of special legislation that the legislature was prohibited from enacting, ranging from the political (laws “locating or changing county seats,

erecting new counties or changing county lines,” “creating offices, or prescribing the powers and duties of officers in counties, cities, boroughs, townships, election or school districts,” “fixing or changing the place of voting, laws changing the venue of civil or criminal cases”) to the judicial (laws “changing the venue in civil or criminal cases” or “regulating the practice or jurisdiction of, or changing the rules of evidence in any judicial proceeding”) to the personal (laws “changing the names of persons or places,” “authorizing the adoption or legitimation of children,” or “granting divorces.”) Prominent on the list was the prohibition against special charters of incorporation: “The General Assembly shall not pass any local or special law ... Creating corporations, or amending, renewing or extending the charters thereof [or] Granting to any corporation, association or individual any special or exclusive privilege or immunity ...”¹⁴

3.2. Pennsylvania’s 1874 General Incorporation Law

As we have already seen, business people had long sought special charters to escape the restrictive features of the general laws. Now that there was no longer any escape hatch, the content of general law became all the more important. The legislature immediately got to work on a revision of the state’s general incorporation law, but the statute that was finally passed on April 29, 1874 fell dramatically short of what Carey and his allies in the constitutional convention had wanted.¹⁵ Rather than a liberal statement of the right of association, the statute limited the right to incorporate to a list of types of enterprises specifically enumerated in Section

¹⁴ Many states enacted similar constitutional prohibitions around the same time. See Hennessey and Wallis 2013.

¹⁵ See “AN ACT To provide for the incorporation and regulation of certain corporations,” enacted 29 April 1874, in Pennsylvania, *Laws of the General Assembly, Passed at the Session of 1874* (Harrisburg: Benjamin Singerly, State Printer, 1874), 73-107.

2.¹⁶ Rather than simply granting members of corporations limited liability, it continued to burden them with additional liabilities. Rather than a statute that granted incorporators a great deal of contractual flexibility, like the British statute Carey admired, the law specified important aspects of the governance structure that corporations had to adopt. In addition, the law placed strict limitations on the size of many types of corporations, as well as the extent of their real estate holdings and indebtedness.¹⁷

More specifically, the statute directed that the business of any manufacturing, mining or quarrying companies must “be confined exclusively to the purposes ... specified in its charter, and no such company shall manufacture or sell any commodity or articles of merchandise other than those therein specified” (section 43).¹⁸ Shareholders were subject to double liability. That is, in addition to their investment, they were individually liable “to the amount of stock held by each of them, for all work or labor done, or materials furnished, to carry on the operations” of their company (Section 14). Stockholders in iron and steel companies were individually liable for “debts due to the laborers, mechanics, or clerks, for services” provided in the past six months (Section 38). Shareholders in manufacturing companies were jointly and severally liable for the company’s debts “if any part of the capital stock ...[was] withdrawn and refunded to the stockholders.” Directors were personally liable for dividends declared when the company was insolvent or if they encumbered the enterprise beyond the statutory ceiling (Section 39).

¹⁶ Section 2 listed the types of “Corporations Not for Profit” that could be formed under the act and also the types of “Corporations for Profit.” The latter included narrow categories such as “the supply of ice to the public,” or “the construction and maintenance of a bridge over streams within this state,” but also broad categories, such as “the carrying on of any mechanical, mining, quarrying or manufacturing business.” “The manufacture of iron or steel,” was listed separately from other manufacturing activities and the statute imposed some different rules on corporations in this category, as it did for other separately listed types of corporations.

¹⁷ See “AN ACT To provide for the incorporation and regulation of certain corporations,” enacted 29 April 1874, in Pennsylvania, *Laws of the General Assembly, Passed at the Session of 1874* (Harrisburg: Benjamin Singerly, State Printer, 1874), 73-107.

¹⁸ Legislators were especially concerned to prevent corporations from establishing company stores, and the section went on to restrict buying and selling on company premises and to prohibited companies from withholding of employees’ wages in payment for goods.

Corporations could enact bylaws for their governance, but the latter were subordinate to the statute, as well as to the laws and constitution of the state and the U.S. constitution (Section 5). The statute specified that the business of every corporation “shall be managed and conducted by a president, a board of directors or trustees, a clear, a treasurer,” and such other officers as the corporation authorizes. Directors or trustees were to be chosen annually by the stockholders. There must be at least three, and a majority was a quorum for the board to act (Section 5). As mandated by the state constitution, stockholders had the right to cumulate their votes for specific directors or trustees (Section 10). Corporations could borrow money but, except as otherwise provided by the act, only to an amount “not exceeding one-half of the capital stock ... paid in, and at a rate of interest not exceeding six per centum” (Section 13). Corporations could issue preferred stock with the “consent of a majority in interest of its stockholders, obtained at a meeting to be called for that purpose” (Section 16). The law required a similar majority vote of the stockholders to increase or decrease a corporation’s capital, but specified in elaborate detail the method of conducting such a ballot (Sections 19-21).

With a few exceptions, corporations chartered under the act were limited to \$1 million in capital (Section 11). Iron and steel companies could have a capital of up to \$5 million and could issue bonds amounting to three times paid-in capital (“bearing interest not exceeding six per centum”), but they could not hold more than 10,000 acres of land within the state, “including leased lands” (Section 38). As a general rule, it was not lawful for corporations to use their funds to purchase stock in any other corporation “or to hold the same, except as collateral security for a prior indebtedness” (Section 11), but iron and steel companies were specifically exempted from this prohibition (Section 38). “Mechanical, mining, quarrying, manufacturing” and other corporations included in that separate category also faced a capital ceiling of \$5

million dollars, but these companies, upon the vote of three quarters of their stockholders, issue a second kind of stock called “special stock” up to two-fifths of their total capital. Special stock was more like bonds in that it was “subject to redemption at par, after a fixed time to be stated in the certificates.” It also bore a fixed rate of dividend, “not exceeding four percent.” Holders of special stock bore no personal liability beyond their investment. A corporation in this category could hold real estate, but only so much as was “necessary for the purpose of its organization,” and it could borrow up to the amount of its paid-in capital (Section 39).

The prescriptive features were present in the bill from its first introduction in the Senate (as Senate Bill No. 44) on February 11, and they survived the amendment process large intact. [Discussion of the debate. Key point to emphasize is how still about market power. Restrictions in the bill now explicitly justified as ways of guaranteeing corporations a level playing field with each other—true open access.¹⁹]

3.3. Pennsylvania’s 1874 Statute for Partnership Associations

A few days after the legislature passed the new general incorporation law, it began consideration of an enabling statute for something very much like a modern LLC. Senate Bill No. 295, “An act authorizing the formation of partnership associations in which the capital subscribed shall alone be responsible for the debts of the association, except under certain circumstances,” was introduced in the Senate on May 4 and became law on June 2.²⁰ The legislation passed with bipartisan support and generated little debate in either house.²¹ In many

¹⁹ Pennsylvania, Legislature, *Journal for the Session of 1874*.

²⁰ See “AN ACT Authorizing the formation of partnership associations.”

²¹ In the senate, Republicans voted 14 to 1 in favor and Democrats, 6 to 2 in favor. In the House, Republicans voted overwhelmingly in support of the bill (74 to 2), but Democrats also voted strongly in favor (23 to 13). For the roll

respects the bill was completely opposite in spirit to the general incorporation act. It was only three pages long, as opposed to thirty-five pages for the corporation bill, and the business form it enabled was remarkably flexible.

The bill's simple language allowing "any three or more persons ... to form a partnership association, for the purpose of conducting any lawful business or occupation within the United States or elsewhere" was similar to Carey's original proposal to the constitutional convention.²² Although the term of a partnership association was limited to a maximum of twenty years, there were no ceilings on capital or on the amount of real estate that could be owned and no restrictions on the types of business in which the firm could engage, the state of citizenship of the incorporators, or where the company could conduct its business (so long as it maintained a headquarters in Pennsylvania). Any three people could form a partnership association simply by registering with a local county official (Section 1).

Despite the absence of limits on capital, legislators seem to have written the bill with small, closely held companies in mind. Section 4 provided that interests in a partnership association were to be considered "personal estate" and hence transferrable, but it also specified that "no transferee of any interest ... shall be entitled thereafter to any participation in the subsequent business of said association, unless he or she be elected thereto by a vote of a majority of the members in number and value of their interests" The statute thus explicitly allowed (indeed, required) members of partnership associations to do something that members of corporations could not easily do at this time—control the identity of their associates.²³

call votes, see Pennsylvania, Legislature, *Journal for the Session of 1874* (11 February 1874), p. 1982. Party affiliations are from Smull 1874.

²² As Edward H. Warren later cynically commented, "it would seem to be probably that those who favored the principle of liability limited to the capital subscribed thought that the legislature would be more likely to pass a law sanctioning such a limitation if the term 'corporations' were avoided in framing the law." See Warren 1929, 512.

²³ Pennsylvania's 1874 general incorporation law followed standard practice in making shares transferable "on the books of the company, in person or by attorney, subject to such regulations as the by-laws may prescribe." In

Otherwise, aside for specifying procedures for winding up the company, the act contained only the most minimal governance prescriptions: There must be at least one general meeting each year at which the membership would elect three to five managers, including a chairman, a secretary, and a treasurer (or a chairman and a secretary-treasurer) (Section 5); and the association could not “loan its credit, its name or its capital” to any of its members and could only loan it to others with “the consent in writing of a majority in number and value of interest” (Section 7). The rest was up to the members.

Section 4, of course, reduced the liquidity of a company’s shares, and so one would expect large firms aiming to raise capital externally to have shunned the partnership-association form. Unfortunately, there are no general estimates of the numbers and types of firms that adopted the form.²⁴ To begin to remedy this lack, I collected registrations for all partnership associations filed in the county of Philadelphia in every fifth year beginning in 1877. As Table 2 shows, most of the firms adopting the new form had the statutory minimum number of partners and relatively small capitalizations, but especially early on there were a significant number of larger enterprises that apparently found the contractual flexibility of the partnership-association form appealing. Through the 1880s, approximately a fifth of the registrants in 1877 had capitalizations of \$100,000 or more, and several had capitalization of \$1,000,000 or more.²⁵

Pennsylvania, as elsewhere, courts did not permit by-laws that impeded the transferability of shares until the second quarter of the twentieth century. For nineteenth-century cases recognizing that the rule for partnership associations was different than for corporations, see *Eliot v. Himrod*, 108 Pa. 569 (1885); and *Carter v. Producers’ Oil Co., Ltd.*, 182 Pa. 551 (1897).

²⁴ There are tax ledgers in the state archives beginning in 1880 that include partnership associations, but most of the partnership associations that I know existed are not found in them. See State Treasurer, Capital Stock Tax Ledgers, 1876-1900. These records were indexed in two volumes mislabeled as Corporate Endorsement Index, Nos. 7-8, 1909-13. For later years, see Bonus Ledgers for Limited Partnerships and Associations, No. 1, 1914-16. These volumes are all in Record Group 28, Records of Treasury Department, Pennsylvania State Archives, Harrisburg, Pennsylvania.

²⁵ After 1879 the tax treatment of corporations and partnership associations was the same, so from that point on taxes did not affect the choice between the two forms. See Freedley 1883.

An important example of a large partnership association (though not one registered in Philadelphia) was the Carnegie Steel Company, Limited, capitalized at \$25 million. At the time of its organization in 1892, the company included four major steel plants, several iron furnaces and mills, two coke works, and an assortment of other properties. The appeal of form resulted from Andrew Carnegie's dominant position in the company. A few years earlier Carnegie had been so seriously ill that it appeared he would die, and his partners in the company's predecessor firms (all partnerships) had faced the dire possibility that the firms would be bankrupted by the cost of settling his estate. Although they could have protected themselves by organizing their enterprise as a corporation, Carnegie was not willing to go along. He wanted to be able to control who could be a member of the firm, reward talented managers with ownership shares, and rid the firm of partners who did not share his strategic vision. The solution, the so-called "Iron Clad" agreement, was possible under the flexible partnership association statute but not under the Pennsylvania's general incorporation law. In the event of Carnegie's death, his partners got the right to buy out his interest at book value over an extended period of time (fifteen years). In exchange, Carnegie got a clause that enabled him (upon the vote of three-quarters of the members in number and value of shares) to force a partner to sell out his interest in the company at book value.²⁶

Another important partnership association, the Bessemer Steel Company, Limited, was registered in Philadelphia in 1877 with a capital of \$825,000. This partnership association gave form to the patent pool that controlled the process of making Bessemer steel in the United States. Its membership consisted of five individuals (the association's managers) and eleven major steel

²⁶ The partners all had an interest in keeping the company's book value below market value, so the agreement had considerable bite. The details of the agreement became public when Carnegie tried to force Henry Clay Frick out, and Frick sued to get the company revalued. See Wall 1970, 491-93; Livesay 1975, 171-72; and Bridge 1991, 336-38.

companies. Members of the association had the right to use the patents held by the pool at the cost of a specified royalty per ton of steel produced. Profits from the royalties were then divided among the members in the form of dividends. The partnership association form allowed members of the pool to develop a set of enforceable rules to control access to steel technology. Members that did not adhere to the rules, that failed to give a proper accounting of their production, or that refused pay royalties due could be expelled by a two-thirds vote of the “members present at a meeting called for the purpose ... and shall thereafter have no rights in the Association or in the property which it owns and controls.”²⁷

The ability to control access to valuable property also explains the attractiveness of the partnership association form for the Producers’ Oil Company, a firm created by an organization of oil producers (the Producers’ Protective Association) with the aim of liberating well owners from dependence on the Standard Oil Trust. The whole purpose of the enterprise was to prevent Standard from gaining access to the oil supplies it controlled. If the company had been organized as a corporation, the producers would never have been able to prevent some of their number from selling out to Standard; they had suffered such defections before. The partnership-association form gave them the necessary means, however, because the simple purchase of shares did convey membership in the company (Tarbell 1904, II, Ch. 15). Transferees had to be voted in. In fact, parties associated with Standard managed to buy up a huge block of the shares in the Producers’ Oil Company, but they were not admitted to the company. John J. Carter, a member of the company who then took possession of these shares on behalf of the Standard interests, sued to be allowed to the vote the additional shares, but he was not successful. On appeal, the Supreme Court of Pennsylvania ruled in favor of the partnership association. “We

²⁷ Articles of Association of the Bessemer Steel Company, Limited, 1 March 1877, Limited Partnership, F. T. W., 1873-1879 (LP4), Partnership Books, 1836-1955, RG 5.23, City Archives, City of Philadelphia, Department of Records.

cannot assent,” the justices declared, “to the plaintiff’s claim that the defendant company is a corporation restricted, in the adoption of by-laws, rules and regulations for its government, to such as it is within the power of the latter to prescribe. It may be conceded that the defendant company has some of the qualities of a corporation, but it is nevertheless a partnership association, governed by the statutes and articles under which it was organized.”²⁸ Under Pennsylvania law corporations had to adhere to governance rules imposed by the state and could not restrict the transferability or voting rights of shares. But partnership associations had much more contractual flexibility, and by means of carefully worded bylaws the Producers’ Oil Company was able to prevent Standard Oil from buying control.²⁹

The courts’ willingness to see partnership associations as different from corporations could also be a disadvantage, however. In an 1885 debt case involving the Keystone Boot and Shoe Company, Limited, the Pennsylvania Supreme Court used this same feature of partnership associations to justify piercing the veil of limited liability and holding the members unlimitedly liable as general partners. Although for convenience partnership associations were “clothed with many of the features and powers of a corporation,” in a partnership association, unlike a corporation, “no man can purchase the interest of a member and participate in the subsequent business, unless by a vote of a majority of the members in number and value of their interests.” They were thus in a fundamental way different from corporations. Moreover, the state did not grant a charter to a partnership association; its privileges rested entirely on the statement submitted at the time of registration. Because a corporation was a chartered entity, its “existence

²⁸ *Carter v. Producers’ Oil Co., Ltd.*, 182 Pa. 551 (1897) at 573-74.

²⁹ The company had adopted a bylaw prohibiting any member from selling or transferring “any interest in capital or shares of stock to any person not a member in good standing of the Producers’ Protective Association, unless with the approval in writing of a member of the board of managers.” The bylaw also specified that “no transferee of any interest in capital or shares of stock shall be entitled to participate in the subsequent business or profits of the association, or to vote on such interest or shares so transferred, unless elected to membership therein by a vote of a majority of the members in number and value of their interests.” *Carter v. Producers’ Oil Co., Ltd.*, 182 Pa. 551 (1897), “Prior History.”

and ability to contract [could not] be questioned” in a suit brought against a corporation for payment of a debt. But the legitimacy of a partnership association rested on the truthfulness of its filing. As a result, it was “competent” for a plaintiff suing for payment of a debt “either to point to a fatal defect” in the statement “or to prove that an essential requisite, though formally stated, is falsely stated.”³⁰

This type of judicial reasoning had earlier curtailed the appeal of the limited-partnership form, and the lower court judge who first heard the case had made a valiant attempt to prevent the partnership-association form from suffering the same fate. Counsel for the plaintiffs had cited the extensive case law on limited partnerships in support of their claim that the members of Keystone Boot and Shoe Company, Limited should be considered general partners who were individually liable for the company’s debts. But the judge did not accept this line of reasoning, instead ruling that the 1836 enabling act for limited partnerships was so different from the 1874 act for partnership associations, “that the decisions under the former are not to be taken as conclusive of the rights and liability of the parties under the latter Act.” For example, the 1836 act explicitly listed a set of circumstances in which failure to conform to the terms of the statute would cause limited partners to be held fully liable, but the 1874 statute included no similar provisions. “We must presume,” the judge declared, “that the Act of 1836 and the decisions under it were well known to the law-makers at the time the Act of 1874 as passed,” so the omission of similar penalties “is good reason for concluding that no such liability was intended.” The 1874 act authorized the formation of partnership associations in which the capital subscribed “shall alone be liable for the debts of the association except under certain circumstances,” and

³⁰ *Eliot v. Himrod*, 108 Pa. 569 (1885) at 580.

the judge pointed out, “in no instance do the excepted circumstances impose a liability as general partners on the members of the association.”³¹

As already noted, however, the Pennsylvania Supreme Court reversed the judge’s decision. The justices acknowledged that the Act of 1874 bore “little resemblance to the Act of 1836” and was far less stringent in its terms. Rushing to the defense of creditors, however, they insisted “that the statute demands a true statement of capital” at the time of registration, because the filing is what informs the public “of the strength of the association.”³² This idea that creditors could rely on the initial statement of capital for information about the credit worthiness of companies that potentially lasted twenty years is dubious to say the least and certainly formed no part of the jurisprudence on corporations, even though their capital could also be paid in real or personal estate.³³ Nonetheless, the Pennsylvania Supreme Court enforced this principal increasingly stringently by the late 1880s, assessing registration filings to determine whether creditors looking at a statement of capital could “form any estimate of its quantity, character or value,”³⁴ and holding members of partnership associations unlimitedly liable as general partners in cases where the statements of real or personal estate paid in were insufficiently detailed.³⁵ Above all, the justices emphasized, property put into an association as capital had to be accurately described. That was more important than valuing it precisely because if the valuation “is excessive, the creditor can decline to give the company credit.” By contrast, “if the

³¹ *Eliot v. Himrod*, 108 Pa. 569 (1885).

³² *Eliot v. Himrod*, 108 Pa. 569 (1885) at 579.

³³ See, for example, Section 17 of Pennsylvania’s 1874 general incorporation act.

³⁴ *Vanhorn v. Corcoran*, 127 Pa. 255 (1889) at 266.

³⁵ Most of the opinions were written by James P. Starrett, an upright Republican justice from Alleghany County, who first joined the court in 1877. The composition of the court seems to have shifted in his favor during the late 1880s with four new justices (three Republicans and one Democrat) elected in 1887 and 1888. There were seven justices in total. Two of the justices leaving the court had dissented in the first case holding members of a partnership association to be unlimitedly liable because of a defective filing. See *Maloney v. Bruce*, 94 Pa. 249 (1880). Cases subsequent to *Eliot v. Himrod* include *Hill, Keiser & Co. v. Stetler*, 127 Pa. 145 (1888); *Vanhorn v. Corcoran*, 127 Pa. 255 (1889); *Sheble v. Strong*, 128 Pa. 315 (1889); *Gearing v. Carroll*, 151 Pa. 79 (1892); *Haslet v. Kent*, 160 Pa. 85 (1894); *First National Bank of Danville v. Creveling*, 177 Pa. 270 (1896); and *Lee & Bacchus v. Burnley*, 195 Pa. 58 (1900).

description be so defective or inaccurate that the creditor may be misled, he has no means of forming an accurate judgment.”³⁶

As a result of this emphasis on an accurate description of personal estate paid in as capital, the registration documents filed for both limited partnerships and partnership associations grew longer and longer in the early 1890s. The most extreme example was the filing for Wanamaker’s department store, a limited partnership, which took up an entire ledger volume and part of a second and seems to have included a complete inventory of the store’s goods, but other registrations went on for scores of pages.³⁷ Even the most painstaking filing was no guarantee against creditors’ attempts to pierce the veil, however, as members of the National Electric Company, Limited, found to their chagrin. At the time of its registration in 1890 it had a capital of \$8,500, most of it paid in as items of personal estate. Although it filed a long inventory that included such detail as 109 8” Flat Porcelain Shades valued at 13 cents each, and 34 boxes of no. 8 screws valued at 35 cents each, the trial judge did not find the inventory sufficiently detailed and ruled in favor of the creditors suing the members personally to recover a debt. This time, however, the Pennsylvania Supreme Court reversed. Justice J. Brewster McCollum wrote the opinion for the Court. Noting that company’s filing “consisted of a hundred and fifty-one items, the integrity and valuation of which were not questioned,” he ruled that “this schedule was sufficient to enable parties dealing with the company to readily ascertain the kind, amount and value of the property contributed to its capital” and that “the defendants in forming the National Electric Company, Limited, honestly sought to comply with the statutes.”³⁸

³⁶ *Cock v. Bailey*, 146 Pa. 328 (1892) at 340. See also *Rehruss v. Moore*, 134 Pa. 462 (1890).

³⁷ The Wanamaker’s filing was in Limited Partnership, Vols. 10-11 (LP10-LP11), Partnership Books, 1836-1955, RG 5.23, Philadelphia City Archives. I examined all registrations of limited partnerships and partnership associations filed during every fifth year and found no long inventories before the 1890s.

³⁸ Interestingly, McCollum was a Democrat. See *Robbins Electric Co. v. Weber*, 172 Pa. 635 (1896) at 644-45.

In fact, the justices had begun to back away from their extreme position in 1892, declaring that “it was never intended” that the filing requirements “should be used as a trap to catch persons who have honestly complied with their substantial requisites, and impale them upon a meaningless technicality.”³⁹ But the damage was done. As the cost of filing mounted along with the length of the required descriptions, the popularity of the partnership-association form declined.⁴⁰ As Table 1 shows, in Philadelphia use of the form peaked during the 1890s and then declined precipitously, so that by the 1920s hardly any partnership associations were registered. The problem was likely not with the form itself. When similar types of entities were introduced in Germany, Britain, and France, they quickly established themselves. Within two decades of the passage of enabling legislation in Germany more than one third of all new firms registered as private limited liability companies, in Britain more than ninety percent, and in France more than seventy-five percent (Guinnane et al. 2007 and 2008). Moreover, in the U.S. today, LLCs are quickly becoming the form of choice for the majority of new enterprises, even though the corporate form is much more flexible than it was in Pennsylvania in the late nineteenth century.⁴¹

3.4. Pennsylvania and the Nation

[This section will discuss how the interstate context began to matter by 1) looking at the how partnership associations were treated when their business crossed state line (only a few states had statutes similar to Pennsylvania’s, so elsewhere the companies risked being treated as

³⁹ *Cock v. Bailey*, 146 Pa. 328 (1892) at 342. See also *Laflin & Rand Co. v. Steytler*, 146 Pa. 434 (1892).

⁴⁰ 53 percent of the partnership associations registered in Philadelphia registrations during the 1892 and 1897 had capital paid in the form of personal or real estate. The proportion fell to 36 percent in 1902 and 1907. None of the few partnerships registered in the 1920s had capital in this form.

⁴¹ For the number of registrations of LLCs relative to corporations in each state, see the International Association of Commercial Administrators, *Annual Report of Jurisdictions*.

ordinary partnerships), and 2) the effect of the chartermongering competition that began in 1889 on differences in corporate law across states. There was convergence, but it was slow and incomplete.]

Conclusion and Epilogue

[Political conflict played out in Pennsylvania differently than it did in other states. Emphasize the heterogeneity of experiences. Nonetheless, the early spread of universal (white) manhood suffrage conditioned the evolution of corporate governance rules in ways that differentiated the U.S. from other countries. To give one example, much easier to disenfranchise stockholders in Britain and Europe (and even entrench specific individuals as directors) than in U.S. Although many ways in which U.S. practice has converged on Europe, spread of franchise has changed things in those nations. Increase in shareholders' rights in Britain with labor government in 1948; labor representation on boards in Germany, etc. Perhaps also discuss limitations of way political conflict played out in the U.S.]

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Table 1. Restrictions on Manufacturing Corporations in Early General Incorporation Statutes

State	Year of Statute	Restrictions on capital stock	Restrictions on borrowing or assets	Restrictions on duration	Governance Structure	Voting Rule	Shareholders' Liability
Massachusetts	1851	Must be at least \$5,000 but not more than \$200,000	Debts cannot exceed paid-in capital	None	Managed at least 3 directors, one of whom is president; must also elect clerk and treasurer	None	Stockholders jointly liable for all debts until capital is fully paid in; then for debts to workers
New York	1848	None	Debts cannot exceed amount of capital stock	50 years	Managed by 3 to 9 trustees, one of whom is president	One vote per share	Stockholders individually liable for debts up to amount of subscription until capital is fully paid in; jointly liable for debts to workers
New Jersey	1849	Must be at least \$10,000	Debts cannot exceed paid-in capital	50 years	Managed by at least 3 directors who must be stockholders;	None	Stockholders liabilities limited to amount of subscription

					majority must be residents of state; president must be a director and resident of state		
Pennsylvania	1849	Must be at least \$20,000	Liabilities cannot exceed three times paid-in capital; can't own more than 2000 acres of land	20 years	Managed by 5 to 13 directors; majority must be citizens of state; president must be a director; treasurer and secretary elected by stockholders but cannot be directors	One vote per share, but no shareholder can vote more than one third of total	Stockholders jointly liable for amount of for debts up to amount of subscription until capital is fully paid in
Ohio	1846	Must be at least \$5,000 but not more than \$200,000	None	40 years	Managed by 3 to 7 directors; president chosen by directors	One vote per share	Stockholders liability limited to amount of subscription except are fully liable for debts to

							workers
Illinois	1857	Must be at least \$10,000 but not more than \$500,000	Debts cannot exceed the amount of capital stock.	50 years	Managed by 3 to 7 directors who must be stockholders; directors choose other officers	One vote per share	Stockholders liable for debts up to amount of subscription until capital is fully paid in
California	1850	None	Debts cannot exceed amount of paid-in capital	50 years	Managed by 3 to 9 trustees, one of whom chosen president	One vote per share	Unlimited individual proportional liability, also jointly liable for debts to workers

Sources: ##list of statutes.

Table 2. Number and Size of Partnership Associations Registered in Philadelphia County, 1877-1927

Year	Number of Firms	Percent with 3 Owners	Percent with 4-9 Owners	Percent with 10+ Owners	Average Capital in \$\$	Percent with Capital \leq \$10,000	Percent with \$10,000 < Capital < \$100,000	Percent with Capital \geq \$100,000
1877	31	45.2	45.2	9.7	113,300	35.4	38.7	25.8
1882	47	59.6	36.1	4.3	43,700	46.8	38.3	14.9
1887	59	57.6	37.3	5.1	69,600	45.8	32.2	22.0
1892	69	69.6	29.0	1.4	111,800	56.5	37.7	5.8
1897	65	69.2	27.7	3.1	48,400	67.7	18.5	13.8
1902	30	83.3	13.3	3.3	6,400	80.0	20.0	0.0
1907	12	75.0	16.7	8.3	8,000	83.3	16.7	0.0
1912	5	80.0	20.0	0.0	6,000	100.0	0.0	0.0
1917	0	na	na	na	0	na	na	na
1922	1	0.0	100.0	0.0	10,000	100.0	0.0	0.0
1927	2	50.0	50.0	0.0	2,700	100.0	0.0	0.0

Source: Partnership Books, 1836-1955, RG 5.23, City Archives, City of Philadelphia, Department of Records.