

Institutions and U.S. Regional Development:

A Study of Massachusetts and Virginia

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August 2008

I am grateful to Kenneth Sokoloff and Douglass North for the many illuminating conversations which led to this project and to David Konig for his helpful advice on U.S. colonial legal history. I thank the editor Geoffrey Hodgson, Don Nichols, three anonymous referees, and participants at a conference hosted by the St. Louis Initiative, CNISS and an urban conference at UBC hosted by Bob Helsley for their helpful comments.

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Abstract

The development of the American economy was accompanied by significant spatial income inequalities between the northern and southern regions. While many factors contributed to northern industrialization and southern stagnation, an important factor was differences in the region's institutions. In the North, a democratic institution fostered growth whereas in the South, oligarchic institutions favored status quo. To gain insights on the nature and causes of this divergence, this paper examines the development of political and legal institutions in Massachusetts and Virginia, the two leading states in the North and the South.

Introduction

U.S. regional economies diverged between the nineteenth and the early twentieth centuries and then converged over the second half of the twentieth century (Easterlin 1960, Kim and Margo 2004). Evidence suggests that regional divergence occurred sometime between the late eighteenth and the early nineteenth centuries. In 1774, wealth and income per capita were relatively similar across the New England, Middle and Southern colonies for all populations but were significantly higher for free whites in the Southern colonies ((Jones (1980)). However, by 1840, income per capita in the Northeast (New England and Middle Atlantic states) exceeded that of the South Atlantic (Southern colonial states) and East South Central states for all populations as well as for the free white population.¹ Southern incomes finally started to converge toward northern levels in the second half of the twentieth century.

Why did U.S. regional economies diverge and then converge? While factors associated with slavery, capital, labor and resource endowments played significant roles, this paper argues that the divergence of regional political and legal institutions was also a major contributing factor.² In the colonial period, the North emerged with democratic institutions which fostered trade and development whereas the South arose with plutocratic institutions which fostered agrarianism. In the early nineteenth century, the North experienced a shift in its legal institutions to a judge-based, “instrumental” law which promoted industrial development whereas the South held onto its traditional jury-based, common law which defended the agrarian status quo. Even after independence and the formation of the United States, state political and legal institutions in

¹ In 1774, the wealth per capita (in pounds sterling) for New England, Middle and Southern colonies were £36.4, £40.2 and £36.4 respectively. Similar patterns emerge when these wealth estimates are converted to incomes (Walton and Rockoff (2002)). In 1840 income per capita (in 1860 prices) was \$129 in the Northeast as compared to \$66 and \$69 in the South Atlantic and East South Central. By 1880, the North-South gap widened even more significantly. ((Fogel (1989)).

² It is beyond the scope of this paper to summarize the vast literature on the divergence and convergence of U.S. regional economies. For a survey of this literature, we refer the reader to Kim and Margo (2004), Kim (1998), Mitchener and Mclean (1999)), Hughes and Cain (2007) and Walton and Rockoff (2002).

the North and South remained divergent , through the antebellum period due to substantial states' rights under American federalism.³ With the outcome of the Civil War, the South faced a significant assault on its institutions but the convergence of their political and legal institutions toward those of their northern counterparts did not become clearly apparent until the second half of the twentieth century.

In recent years, scholars have proposed a variety of explanations for why institutions diverged across the European colonies around the world. One class of explanation emphasizes the role of initial conditions (North (1990), La Porta et. al (1998), and Glaeser and Shleifer (2002)). In particular, because the Spanish, Dutch, French, and the English colonizers brought with them different sets of institutions, the development of colonial institutions was partly determined by the national identity of their colonizers. In general, these scholars believe that regions colonized by the British were more likely to inherit institutions of democracy and common law whereas those colonized by the Spanish and French were likely to inherit centralized bureaucracies and civil law.⁴

The second class of explanations focuses on the geographic conditions of the colonies. For Engerman and Sokoloff (1997), the decisive factor was colonial factor endowments. In countries and regions where geography favored small scale farming, democratic institutions were likely to arise whereas in regions that favored plantation economies based on African or native slave labor, institutions based on elite-rule were likely to arise. For Acemoglu et. al (2002), colonial climate and native density or productivity were important factors. Since few Europeans settled in places with high settler mortality or high native population density, they had few incentives to develop democratic institutions in these colonies.

³ See Key (1949).

⁴ Berkowitz and Clay (2006) find that legal origins influenced the quality of state courts in the U.S. Also see Michener and McLean (2003).

To better understand the nature and causes of the divergence of U.S. northern and southern institutions, this paper examines the historical developments of political and legal institutions in Massachusetts and Virginia from their early colonial beginnings. Because there were important differences in the development of other colonies, the lessons learned from these two colonies must be interpreted with some caution. Nevertheless, these two major founding colonies served as important models for their respective regions. Over time, because settlers tended to migrate westward along the latitudes, institutions developed in Massachusetts were transplanted into other northern states such as Ohio and Illinois whereas those developed in Virginia found roots in other southern states such as Tennessee and Alabama.⁵

The study of Massachusetts and Virginia suggests that their initial variations in purpose, demographic composition and wealth inequality played significant roles in creating the divergence of political institutions between these two colonies. In Puritan Massachusetts, where the distribution of land, wealth and status was unusually equal, a democratic government arose in a relatively short time; in Cavalier Virginia where the society was highly unequal, a plutocratic polity took root and persisted over time.⁶

After the early founding years, the differences in their climates contributed to the continued divergence in demographic and institutional structures in Virginia and Massachusetts. In Virginia, the extremely high mortality rates created an unsettled community which could only

⁵ See Mathews (1962), Steckel (1983), Meinig (1993) and Kim and Margo (2004).

⁶ Fischer (1989), in his classic work *Albion's Seed*, argued that the British transplanted four distinct "folkways" in colonial America. In Virginia, Fischer (1989) credits the rise of plutocracy in Virginia to the actions of Sir William Berkeley who governed Virginia between 1642-1677. Berkeley, in his desire to re-create the Royal government in England, recruited cavaliers in large numbers and then granted them large estates to create a ruling oligarchy. According to Fischer, a great majority of the ruling elite in Virginia arrived between 1647 to 1660 and that nearly all the ruling families were founded by younger sons of eminent families with no hope of inheriting an estate in England. This period of Cavalier settlement in Virginia was during a period of Parliamentary supremacy and republican government in England. In New England, however, Fischer finds the Puritan immigrants were extremely homogenous, composed of nuclear families, came principally from the middle classes of the eastern counties of Norfolk, Suffolk, Essex and Cambridgeshire. Quakers migrated from the North of England to the Delaware Valley, and Northern British and Scots-Irish to the Appalachian backcountry and beyond. Fischer also identified two other folkways – Quakers of Delaware Valley and the northern British immigrants of the Appalachian backcountry.

be sustained by the continual recruitment of new, poor, young male servants until the death rates stabilized in the eighteenth century. As a stable free white population emerged over time, an important element of democracy was introduced with the election of the Houses of Burgesses; however, many important offices, such as the county justice, continued to be appointed for life. In Massachusetts, a stable community led to a surprisingly quick emergence of a democratic society based on elections on many levels of government.⁷ While important elements of democratic rule were removed by the British government when Massachusetts became a royal colony in 1691, democratic institutions quickly re-emerged after American independence.

Finally, factor endowments contributed to a major divergence in agricultural scale economies in the northern and southern colonies which in turn re-enforced the divergence of political and legal institutions in these colonies. In Massachusetts, poor soil led to small scale agriculture, fishing and commerce; in Virginia, however, climate proved excellent for growing tobacco in large scale, especially with the introduction of slavery.⁸ Because the land laws in Virginia based on headrights, unlike those in Massachusetts, enabled the southern elites to accumulate significant amounts of land, an elite landed gentry with strong common economic and political interests emerged in Virginia. Moreover, the institution of slavery itself also contributed to diverging legal developments between the northern and southern colonies.⁹

Whether the geographic distribution of institutions is determined by historical initial conditions, climate or endowments, the establishment of stable political and legal institutions reflects a self-enforcing equilibrium solution to the fundamental dilemma of the state ((North

⁷ Massachusetts did not possess democracy in the modern form, but it possessed significant early elements of democracy. See Wilentz (2005: xix) for a definition of democracy.

⁸ There has been extensive debate over the economic impact of slavery (Hughes and Cain 2003, Walton and Rockoff 2002). Fogel and Engerman (1974) find that southern agriculture under slavery was more efficient than northern agriculture due to plantation scale economies. Irwin (1988) finds that slave plantation economies extended to wheat production in the Virginia Piedmont. On the other hand, Wright (2006) and other scholars argue that slavery was economically inefficient.

⁹ See Morris (1996), Wahl (1998), Hindus (1980) and Tushnet (1981).

(1981), Acemoglu et. al (2004)). To establish property rights, it is necessary to have a state which has a monopoly on violence; however, if the state has sole military power, then it has the incentive to extract rents from society. For North and Weingast (1989), the rise of Parliamentary rule by oligarchs in Britain in 1688 was associated with a greater commitment by the state to curtail the power of royal prerogatives. For Acemoglu and Johnson (2000), the rise of democratic rule in Britain in 1832 represented a credible commitment by the state to distribute resources toward the masses and was a necessary response to the potential mass rebellion.

In the American colonies, the states' coercive ability to enforce their laws and policies also played an important role in determining the level of democracy. Since the colonies relied on voluntary militia for their armies, the governor, council and elected officials were acutely aware of their limited military authority over the governed. Rebellion by the free masses was a constant threat. Even in Massachusetts, the elites granted greater levels of democracy only after facing severe threats of rebellion. In Virginia, the potential for mass rebellion led to greater access to democracy, but this movement was short-lived when the elites regained an upper hand with royal military support. In Virginia, the potential for rebellion by poor free whites also lessened over time as their incentives became more and more aligned with the elites under the institution of slavery and as the elites relied less on local militias composed of free whites for social control.

The paper is organized as follows. Section II documents the historical development of political institutions in Virginia and Massachusetts; section III documents the development of their legal institutions. Section IV examines the role of states' rights and federalism on the continued divergence of institutions in Virginia and Massachusetts. Section V explores the causes of institutional divergence and section VI concludes with a summary.

The Political Institutions of Virginia and Massachusetts

Virginia and Massachusetts were both founded on the principles of royal corporate charters, but in the New World these colonies by necessity formed governing institutions which resembled commonwealths rather than corporations. Yet, even though both of these colonies were founded by peoples of one European nation with common history, culture and background, they emerged with differing political institutions over time. In the early years of settlement, Virginia struggled to form a working political order but eventually emerged with an oligarchic or plutocratic society. In Massachusetts, however, a more democratic form of government arose in a relatively short time. This section presents a selective historical account of the evolution of political institutions in these two colonies.¹⁰

A. The Development of Political Institutions in Virginia

The founding of Virginia was based on a royal corporate charter drafted in 1606 for the Virginia Company which contained a mixture of private and royal organizational form. For profit making, the private company planned to establish plantations worked by servants and laborers under contract managed by overseers. The company was given the right to transport settlers, supply provisions and trade goods. For governing, however, the task was entrusted to three councils whose members were appointed by the King. The powers of government and ownership of land ultimately rested with the King who used instructions to give judicial powers to the local council and issued patents to grant land.

In 1607, 104 passengers in three vessels reached the Chesapeake and settled in Jamestown. The settlers were all male: a third to half were designated as gentlemen and the rest were artisans and laborers. By the order of the King, the identity of the local governing council was kept secret until arrival when the identity was to be revealed. The members of the council

¹⁰ There are many excellent and comprehensive accounts of the histories of political institutions in Virginia and Massachusetts. For example, see Osgood (1904), Morgan (1975), Sydnor (1952), Wall (1972) and Andrews (1934).

then chose a president. By most accounts, under the trying conditions of famine, disease and threat from Indians, the council form of government proved to be ineffective. In 1608, when many of the council members had died or returned to England, John Smith emerged as the leader who commanded the colony in military style using labor gangs.

In response to the ineffectiveness of the council government, the Virginia Company requested and was granted a new charter by the King in which the company had complete control over the colony. In London, the company took steps to run the colony under a military regime initiated by Smith.¹¹ The new leaders of the colony were old soldiers. Between 1611 and 1618, the company ruled the colony through a governor who exercised absolute powers.¹² The government forged by the first governor, Lord De la Warr, his deputy Sir Thomas Gates, and subsequent deputy Sir Thomas Dale, was a code of military rule known as Dale's Laws. The settlers continued to work in gangs and were deprived of protection under the common law.¹³

When the gang labor system and military rule failed to bear any fruit in the New World, the Virginia Company in 1618 re-organized its governing structure and introduced a charter of grants and liberties. The general assembly, which possessed the powers to make laws, was composed of the governor and council, who were chosen by the company as before, but it now also included two Burgesses from each district who were elected. In June 19, 1619, 22 Burgesses were elected for the first time. While evidence on the workings of the assembly is scant, it is doubtful whether Virginia achieved a fully working form of government during this period. Nevertheless, the election of the Burgesses signaled a significant turning point in Virginia

¹¹ See Shea (1983: 13-15).

¹² A decision was reached near the end of 1609 "to appoint a single head entrusted with exceptionally large powers. The company made up its mind to try a new experiment by sending to America a single and absolute governor, with authority so extensive as to make him almost a dictator for life." Andrews (1934: 107).

¹³ See Morgan (1975: 80).

history. It marked the beginnings of a two-tier plutocratic society where access to political participation was open to the elites but closed for most of the masses.¹⁴

When the financially troubled Virginia Company was dissolved by the King in 1624, Virginia became a royal colony and the King appointed the governor and the council of the general assembly. Given the distance from England and a the lack of a royal standing army, however, the royal governor could not overrule the colonists on important matters. The Virginians made up of the Houses of Burgesses and the council were able to effectively legislate on matters of taxes and law. As the Virginia colony stabilized and grew over the seventeenth century, the government of Virginia evolved into its mature colonial form and formed political boundaries in counties and parishes.

More than the transition to a royal colony, the introduction of tobacco seeds of the Spanish West Indian variety by John Rolfe in 1617 had a major impact on the social organization of Virginians. With the tobacco boom of the 1620s, immigration of male indentured servants and share tenants increased. Under the headrights system introduced in 1618, a settler who came on his own or who paid the transportation of someone else was entitled to 50 acres. In these early years, given the abundance of land, the societal division arose in terms of the accumulation of servants. The growing of tobacco was both intensive in land and labor, but labor was scarce. Evidence show that the elites were able to acquire numerous indentured servants, often by illegal means. The muster of inhabitants in 1625 show that the officers of the Virginia Company each held 10 to 39 servants.¹⁵

The elites were able to accumulate wealth and hold political power, but the basis for their power was precarious since they relied on local militias to enforce their laws. As mortality rates

¹⁴ See Morgan (1975: 124).

¹⁵ See Morgan (1975: 123-124).

stabilized, an increasing share of the population was composed of free single males who once were servants. In the early seventeenth century, election of the Houses of Burgesses were held infrequently at the discretion of the governor; however, as free whites became more numerous and rebellious, Governor Berkeley was forced to hold new elections with greater access to voting.¹⁶ In the election of 1676, the free whites were able to vote into office a large share of their choices. However, this movement toward greater access was short-lived. When the Bacon's rebellion collapsed, the elites re-established their political authority, confiscated the property of those who rebelled, and re-established the status-quo of elites.

The introduction of slavery solidified the elite rule based on the ownership of land and slaves rather than on servants. In this period, a mature, stable, plutocratic society emerged based on planter elites (Kulikoff (1986)). Prior to the eighteenth century, based on the identity of justices in tidewater Maryland, Kulikoff finds that justices were highly varied in background. However, by the mid-eighteenth century, the justices and burgesses were dominated by the planter gentry. In the late seventeenth century, Virginia justices and burgesses, as well councilmen, used their public offices to patent thousands of acres of frontier land. By 1705, three-fifths of Virginians who owned 2,000 or more acres of land were justices or burgesses. By the mid-eighteenth century, strong political dynasties formed. For example, more than a quarter of the 1,600 justices appointed in Virginia between 1757 to 1775 belonged to only 55 patrilineages. The gentry used entail and marriage to consolidate the political ruling class.

The governor usually chose council members from the top families of the planter gentry. Sydnor (1952) finds that a small number of families enjoyed the powers of this office. Only 57 family names appear from 1680 to the Revolution as council members; nine families account for

¹⁶ In order to keep the same men in office in the House of Burgesses, Governor Berkeley did not call for a general election for 15 years between 1661 and 1676 (Andrews (1934: 247)).

almost a third of the councilors during this century. The House of Burgesses was the only elected body in Virginia, but the election was also controlled by the elite gentry.¹⁷ Election dates were chosen by the governor and two members were elected from each county and one each from Jamestown, Williamsburg, and the College of William and Mary.

In Virginia, the county became the most important level of government for most people. Moreover, unlike Massachusetts, where local town officials were elected by freemen, county officials in Virginia were appointed and these officials possessed broad legislative, executive and judicial powers.¹⁸ County justices, who individually settled disputes on small debts and collectively composed the county court, were appointed to serve for life by the governor. In practice the justices provided the governor with a nominee who the governor then commissioned. The county justices not only decided on issues of law but they also set tax rates, allocated county funds, and managed roads and bridges. Just as importantly, the county justices appointed local government officials, such as the sheriff (who enforced laws, managed jails, collected taxes, managed the treasury, and conducted elections), coroner, militia officers below rank of brigadier, and tobacco inspectors.

B. The Development of Political Institutions in Massachusetts

The Massachusetts Bay Company, formed in 1629, was based on a corporate charter, much like those of the earlier Virginia Company except in one important aspect.¹⁹ In all the previous colonies, they were managed chiefly for profit and controlled by proprietors in England and the colonists were not entitled to the right of self-government. For Osgood (1904), the founding of the Massachusetts Bay colony marked a major change where the government of the

¹⁷ See Sydnor (1952), Griffith (1968), and Morgan (1975).

¹⁸ Most scholars believe that the government in Virginia was undemocratic (see Porter (1947), Sydnor (1948, 1952), Morgan (1975)). However, Brown and Brown (1964) contend that Virginia was much more democratic.

¹⁹ The discussion on Massachusetts will concentrate on the more influential Massachusetts Bay colony. Plymouth and Massachusetts Bay colonies joined to form Massachusetts in 1691. See Osgood (1904).

plantation was transferred to those who lived in the colonies. For governing, the general court, prior to their departure in England, elected Winthrop as governor of colony and company, Dudley as deputy governor, and 18 other assistants. For profit making, the company created a temporary trusteeship known as undertakers who assumed control of assets and liabilities of the joint stock. Undertakers were to receive profits from the fur trade, the salt-making monopoly, and the transportation of passengers and goods.

In 1630, approximately 700 individuals in 11 ships sailed for New England. When the settlers arrived in Massachusetts Bay, they intended to work and live as a corporate body in one location where each settler received an allotment of land based on their investments.²⁰ Within months of their arrival, however, these plans were abandoned as settlers dispersed into nearby areas, formed separate towns and claimed land for themselves. These early settlements were established without the explicit authority of the general court. In addition, as the commercial element of the Massachusetts Bay Company quickly disappeared, trade was authorized to take place in private hands and the colony became a de facto commonwealth.

In Massachusetts, unlike Virginia, a democratic government based on regular elections arose in a relatively short period of time. Immediately, Winthrop and his associates were forced to recognize the new towns, fix their boundaries, and give them the rights to grant land. They were also forced to relinquish oligarchic control as large number of colonists applied for admission as freemen. In 1634, the colony declared that the freemen alone had power to admit new freemen, make laws, appoint officers, raise money and grant lands in the commonwealth of Massachusetts. The General Court, composed of two elected deputies from each town, was authorized with legislative powers; the governor and the assistants elected by freemen retained executive and judicial powers.

²⁰ See Rutman (1965: 44).

The General Court also took control over unoccupied lands and claimed the exclusive rights to grant land and create townships (Akagi (1924) and Martin (1991)). Prospective settlers, called proprietors, petitioned the General Court for a grant of land. Although the land was granted freely, starting a town was an expensive and complicated affair (Martin (1991)). Town promoters, often politically connected and experts in Indian affairs, coordinated the founding of towns and received land for their services. The General Court surveyed the land, coordinated its purchase from the local Indians, and then granted it to proprietors who were given exclusive rights to distribute land and admit new town members. The General Court also gave towns a considerable degree of local political control and in 1641, selectmen were officially designated as chief administrators of local affairs.

In Massachusetts, democratic town governments became the most important local institution. Once a year in March, freeholders met to elect local town officials: clerk, selectman, treasurer, constable and many lesser offices. Since the voting procedure was left to the discretion of towns, there was a great deal of variation in electoral practices. Over time, the elections were handled by a moderator, used written but not secret ballots, and became more formal (Cook (1976)). Yet, towns were not free of disputes. Because towns were often ill-equipped to settle and enforce disputes, Konig (1979) argues that the quarterly courts were an indispensable institution for establishing social order throughout the colony.²¹

The continual movement toward a democratic government in Massachusetts occurred under considerable dissension and debate (Breen (1970)). For a colony founded to form a religious community, the political separation of church and state was a major issue, especially in the early years. Related to the idea of the religious and moral authority of the ruler was whether

²¹ The colonists, according to Konig (1979), drew upon their English experience and created a judicial system based on the patterns of English county, the borough justices of peace, and courts of quarter sessions.

political leaders possessed wide discretion or possessed delegated authority. While dissension on the right form of government never dissipated, political debates increasingly became more secular and were on topics of property and liberty rather than of scripture and religion.

With the return to power of the Stuarts in 1660 in England, the Massachusetts colony faced a major challenge to its autonomy. In an abrupt change of policy, the King and the Board of Trade annulled the original charter in 1684 and established royal political authority over the colony. Massachusetts and other northern colonies were consolidated into a single Dominion of New England and placed under the rule of a royally-appointed governor. Representative government and town authority were significantly curtailed. While an elected House of Representatives became the legislative body, and nominated the members of the upper house, the governor, selected the Council from the representatives' list of nominees and his signature was necessary for an enactment to become law.

The period under royal rule between 1684 and 1776 was a period of uneasy compromise. When property rights and representation were significantly undermined as were under the rule of the royal governor Edmund Andros in 1686, the colonists rebelled by arresting Andros thereby setting the boundaries of what they would allow. After the Andros affair, the royal governors learned to work within the limits of their authority, but for colonists who developed their own political institutions based on electoral representation, the royal government never gained full legitimacy. In the eighteenth century, as the interests of England and the American colony continued to diverge, the colonists who without representation on major policies rebelled to recover their democratic institutions developed in their early years of colonial history.

The Legal Institutions of Massachusetts and Virginia

In the colonial period, the legal institutions in Virginia and Massachusetts were local, jury-based, and founded on the common law tradition of England (Nelson (1975)). To the extent that there were divergent trends in these two colonies, they may be accounted for by the fact that early colonists did not bring with them the English common law of the King's court, but rather the customary law of English local courts which varied by region (Groebel (1931), Allen (1981)). Moreover, in Massachusetts, there seems to be some evidence that local colonial circumstances may have led to changes in the application of common law (Konig (1979)). On the other hand, in Virginia, courts were presided by country justices with little education in law for most of the colonial period (Roeber (1981), Konig (1992), Miller (1994)).

Property law in the American colonies, especially in New England, according to Priest (2006), may have diverged significantly from that of English law in its alienability. As the property law in England was designed to protect the devolution of real property, an individual's title to land was protected from the claims of unsecured creditors. In New England, however, the colonial legislatures moved to reject English protection of real property and, in 1732, the Parliament endorsed this movement by enacting a statute known as the Debt Recovery Act. Thus, in Massachusetts and elsewhere, land became equivalent to any other property. While the act was designed to apply in all the American colonies, evidence suggests that Virginia may have remained an important exception. In Virginia, the use of primogeniture, entail and local juries provided an important mechanism for protecting real property from creditors.²²

²² Virginia and the southern colonies adopted the common law of primogeniture widely practiced in England whereas Massachusetts and the other New England colonies (with the exception of Rhode Island and New York) adopted male multigeniture, a practice found in County of Kent (Alston and Shipiro (1984)). Primogeniture and entail significantly reduced the potential devolution of property in Virginia. While Keim (1968) finds that only a small percentage of property in Virginia was subject to entail, Brewer (1997) argues that Keim's estimates are flawed and that a larger share of property may have been subject to entail.

In the first half of the nineteenth century, legal scholars believe that the American legal system went through a more fundamental transformation. In this period, the legal system went from jury-based, common law to judge-based, “instrumental” law (Nelson (1975) and Horwitz (1977)).²³ While the evidence of the geographic divergence of legal systems between Massachusetts (North) and Virginia (South) is relatively scant, a growing number of scholars believe that Massachusetts was a leader in this transformation whereas Virginia remained a laggard (Ely and Bodenhamer (1984), Konig (1992), Miller (1994), among others).²⁴ Cases from Massachusetts (and New York) state supreme courts were cited, but those from Virginia and other southern states were ignored (Friedman (1984)).

A. Colonial Law in Massachusetts and Virginia

For Nelson (1975), pre-revolutionary law in Massachusetts was characterized by a legal system based on the British common law tradition of local communal consensus. One of the most important features of pre-revolutionary law was that the jury ruled both as law and fact.²⁵ Because norms of local communities varied, and since local juries did not provide written commentaries on their decisions, jury-based law did not provide a sound basis for a uniform law over a wide geographic area. Moreover, the common law concept of fair exchange, often determined by the ethical norms of a local community, subjected the enforceability of a contract to local community standards of fairness. Likewise, under common law, corporations were believed to be created by the legislature for public rather than for private purposes and their charters could be amended or abolished for the communal purposes of a community.

²³ To the contrary, Simpson (1979) and Schwartz (1981) argue that the Horowitz thesis is unfounded in the data. Both of these scholars claim that there was no radical change in law between the late eighteenth and the early nineteenth centuries.

²⁴ Campbell (1975) and Huebner (1999) argue that, while Virginia’s legal system was not as advanced as that of Massachusetts, the legal system in Virginia was also moving away from common law to instrumental law.

²⁵ See Nelson (1975: 3-4).

Common law property rights gave the land owner the right to prevent the use of any neighbor's land that conflicted with his own quiet enjoyment. The natural use and prescription doctrines limited the use of a property to natural uses (agriculture) and gave monopoly rights to the first developer of a resource. Horwitz (1977) argues that property rights under common law hindered development. These laws raised the costs of building roads, canals and railroads as well as building mills for water power. For example, the natural use doctrine did not allow the alteration of water flow except in its natural channel and any use of water that conflicted with the interests of other land owners along the stream was an unlawful invasion of property.

Common law principle of contract was based on the fairness doctrine that sought to protect people from unfair exchanges. The fairness standard, however, created uncertainty in contractual transactions. Under the fairness doctrine, if two parties agreed on a contract on the delivery of a good at a specified price, the contract could be nullified by the courts if the contract was deemed to be unfair to one party. Thus, the enforceability of a contract was at the discretion of the courts rather than bounded by the agreement drawn up by individuals.²⁶ Since the standards of fairness may differ between jurors in different communities, the fairness principle raised the costs of transactions across localities. In addition, the fairness standard limited the negotiability of a contract. If individual A gave a promissory note to B, who transferred the note to C, then C could not sue A in the event that the contract was breached.

B. Post-revolutionary Law in Massachusetts

Between the American Revolution and the early nineteenth century, the legal institution in Massachusetts was transformed from one based on preserving status quo and traditional social stability to one based on free will, uniformity and predictability for economic exchange (Nelson

²⁶ See Horwitz (1977: 167).

(1975), Horwitz (1977)). Between 1804 to 1809, reforms were enacted to limit jury power. The law finding function was shifted from the jury to the judge and the jury's task was relegated to fact finding functions such as determining the credibility of the witness or weighing the probability of competing testimonies. Moreover, the common law of contract was replaced by the "will theory" of contract. What mattered was whether individuals agreed on the terms of the bargain rather than whether the agreement was fair, foolish or inequitable to a party. These developments reduced the uncertainty of contractual exchanges and the costs of market transactions.

The will theory of contract affected many areas of economic activity. In the sale of land, individuals were free to devise contracts which were binding in courts. The sentiment for will theory was expressed by Chief Justice John Marshall: "To deny the power of two individuals, capable of acting for themselves, to make a contract for the purchase of land and sale of lands defeasible by the payment of money at a future date, or, in other words, to make a sale with reservation to the vendor a right to repurchase the same land at a fixed price and at a specified time, would be to transfer to the Court of Chancery, in a considerable degree, the guardianship of adults as well as of infants."

In pre-revolutionary law, *caveat emptor* did not apply. For example, if two people bargained over a horse and the horse died subsequent to exchange, the buyer could sue the seller for damages. In post-revolutionary law, the will theory of contract increased the importance of *caveat emptor*. Thus, even if a person purchased a defective good, the buyer was now responsible for his actions. By limiting the buyers' right to sue for decline in the quality of goods after purchase, *caveat emptor* reduced the transactions costs of market exchanges.

Common law viewed corporations as similar to municipalities which were created for public rather than private purposes. In the early nineteenth century, Massachusetts recognized the private nature of corporations, upheld the private contractual nature of the corporate charter, and provided limited liability to managers and shareholders. In *Ellis v. Marshall* (1807), the Massachusetts Supreme Judicial Court made a firm distinction between public and private corporations. In deciding that a private corporation was distinct from a public corporation, the court effectively limited legislative authority over corporations. Likewise, in *Wales v. Stetson*, the Massachusetts Supreme Court ruled that private corporations were closer to contracts than municipal governments.²⁷

In *Gray v. Portland Bank* (1807) the Massachusetts Supreme court established that the officers of a corporation had fiduciary duty to its shareholders. In the early nineteenth century, it was not clear whether a breach of contract or in tort could be brought against a corporation rather than its officers who performed the injury-creating act. In *Gray and Riddle v. Locks and Canals on Merrimack River* (1810), the court ruled that corporations could be sued for damages. However, while the corporation could be sued for damages, the court also gave the officers and shareholders of the firms limited liability. In *Nichols v. Thomas* (1808) the court ruled that owners were not personally liable for the debts of the firm.

In Massachusetts, the state legislature played an important role in eroding the common law vested property rights through enacting mill acts in the early nineteenth century. The foundation of common law was the view that property owners had absolute dominion over their land.²⁸ Because the development of mills, water power or transportation often impacted

²⁷ *Wales* was the primary precedent for *Dartmouth College v. Woodward* (1819).

²⁸ Before the nineteenth century, the common law view of water was a natural flow rule which restricted the uses of water for domestic and agricultural purposes. Beyond the natural use of water for supporting humans and animals, common law ruled that water flows and ought to flow, as it has customarily flowed, and that every man has a right

negatively on adjacent private properties, the hold-up costs associated with vested rights doctrine raised the costs of development. The mill acts lowered the costs of litigation by allowing the owner to flood a neighbor's land and pay an annual compensation specified by the act. Thus, the legislature reversed the common law rule that flooding the land of a neighbor created an injury and nuisance (Hall (1989)).

Under the "common law" rules of contract, the transaction costs of developing roads, canals, and railroads were very high because property owners had absolute dominion over their land. By using its power of eminent domain, the state legislature in Massachusetts was able to reduce the transaction costs associated with the development of roads, canals and railways. Because transportation networks traversed property owned by numerous private individuals, traditional vested rights of property guaranteed under common law significantly raised the costs of infrastructural investments and collided with the public's interest in economic growth. In the antebellum period, state legislatures and courts used eminent domain to take property for public purpose subject to reasonable compensation to land owners.

C. Post-revolutionary Law in Virginia

While the study of laws and legal systems in Virginia is not as developed as that of Massachusetts, scholars generally believe that the legal system in Virginia continued to champion the English common law traditions based on local juries (Miller (1994)). Unlike Massachusetts which transformed its legal system to foster industrial development, Virginia used its legal system to protect the landed interests of the elites. Virginia's legal system inhibited development in a variety of ways: it favored debtors over creditors, favored landlords over

to have the advantage of flow of water in his own land without diminution or alteration. In the early nineteenth century, a new view of water rights emerged. "Under the influence of the mill acts, men had come to regard property as an instrumental value in the service of the paramount goal of promoting economic growth (Horwitz (1977: 47-51)). See Steinberg (1991).

tenants and sharecroppers, was slow to adopt *caveat emptor* or recognize private corporations, and adhered to “vested” rather than legislative rights (Ely and Bodenhamer (1984)).

In Virginia, unlike Massachusetts, Miller (1994) argues that the legal system continued to advance the traditional rights of the jury over the judge. Because a large share of civil suits between 1785-1825 involved British debt cases, the local jury system provided effective means to delay and reduce debt claims. The judges role in Virginia was only to answer a question concerning a specific point of law if requested. A judge instructing the jury was seen as an invasion of the jury’s province; judges in Virginia were not allowed to sum up the evidence at the end of the trial. In a series of cases brought to the appeals court on the relative roles of juries and judges, the Virginia appellate courts consistently upheld the traditional, common law rights of the jury.

Due to the lack of systematic legal studies, it is difficult to determine to what extent Virginia’s contract law was based on the common law fairness doctrine rather than the will theory introduced in Massachusetts. At best, the evidence is mixed. In *Groves v. Groves* (1790), Virginia’s lower court appeared to adopt the will theory of contracts by ruling for expectations damages in connection with a buyer’s action for securities, but the Virginia Court of Appeals subsequently reversed this decision (Horwitz (1977)). In the sale or hiring out of slaves, Wahl (1998) finds continued acceptance of the common law fairness doctrine, but Morris (1996) argues that, except for the Carolinas and Louisiana, southern judges adopted *caveat emptor* by the end of the eighteenth century.²⁹

In Virginia, corporate charters were often seen as a public good and the legislature either reserved the power to amend the charter or, if not, limited the duration of the corporation

²⁹ Because Virginians tried to tie slaves to land, slaves were considered as realty for some purposes for most of the eighteenth century (Morris (1996)).

(Campbell (1975)).³⁰ In the well-known case of *Currie's Administrators v. Mutual Assurance Society* (1809), Justice Spencer Roane ruled that the legislature could amend the original charter of the corporation.³¹ The Mutual Assurance Society, an insurance scheme where members insured each other, was originally chartered by the legislature in 1794. However, in 1805, the legislature amended the charter under interest group pressure. Since country subscribers were subsidizing town subscribers who faced great danger of fire, the legislature separated the subscribers into the two groups. In 1805, Currie, a town dweller, brought a suit against the Society claiming that the 1805 act violated the society's original charter by increasing rates without consent.

Roane upheld the 1805 legislative act and sided against Currie. Roane's verdict is interesting on two important accounts. First, Roane's decision is consistent with the common law theory of contract. Roane's decision was fair in the common law sense because the rural residents should have contributed less than the urban interests and they should have been protected from unfair exchanges. However, under the will theory of contract, the court would have upheld the original contract, even if it turned out to be unfair. Second, Roane did not believe in the sanctity of private corporations. Since corporations were created by legislatures for public rather than private purposes, the Mutual Assurance Charter was not sacred nor inviolate. Thus, the legislature was well within its rights to amend the charter, especially if it served the public.

³⁰ While Ely and Bodenhamer (1986) believe that southern law diverged from northern law, they argue that southern courts enforced *caveat emptor* and accepted the private contractual nature of corporations.

³¹ Spencer Roane served on Virginia's Court of Appeals, the highest appellate court, between 1794 and 1822. "English precedents and principles held a place of particular importance in Roane's decisions... In Roane's view, English authorities stood on equal footing with decisions of Virginia's courts... Harkening back to the great legal tradition of English legal scholarship, Roane cited Blackstone and others in support of adherence to such long-established precedent... Roane's conception of the judicial role combined a belief in strong, independent, authoritative judiciary with a devoting to the wisdom of the ages as expressed through the common law (Huebner (1999: 22))."

In Virginia, the rights of property favored agriculture rather than transportation and manufacturing. The legal system through the use of local juries continued to uphold the traditional common law rights of property which raised the costs of industrialization. Unlike Massachusetts, where the mill acts and eminent domain were used by the legislature and the courts to transfer the rights of land use to transportation companies and manufacturing firms, the opposite remained true in Virginia. Whereas statute laws minimized compensation to affected land owners in Massachusetts, the local juries determined damages to landowners in Virginia.³²

Finally, scholars believe that Virginia and the South promoted a tradition of violence and extra-legal methods of enforcing behavior (Ely and Bodenhamer (1984), Friedman (1984)). In his study of criminal justice in South Carolina and Massachusetts, Hindus (1980) argues that South Carolina promoted extra-legal and informal authority whereas Massachusetts took strong steps to limit extra-legal authority. In Virginia (like South Carolina), extra-legal authority of planters was consistent with localism. In addition, slavery condoned violent behavior of whites such as whipping even though brutality of masters was restricted (Wahl (1998)).

States' Rights and American Federalism

Even after the formation of the United States, the political and legal institutions in Virginia and Massachusetts continued to diverge because the *Constitution* granted significant rights to states ((McDonald (2000)). The sentiment for states' rights was the strongest in Virginia. When John Adams, a pro-nationalist, was elected president, Virginians reacted strongly. In response to the Alien and Seditions Acts, which made it illegal to criticize the federal government, Madison and Jefferson wrote the Virginia and Kentucky Resolutions in 1798. In

³² For example, see Miller (1994) for a discussion of the legal case *Crenshaw and Crenshaw v. Slate River Company* (1828). Also see Majewski (2002) for a similar case involving *Shadwell Mills and Rivanna Navigation Company* and *James River and Kanawha Company* in Albemarle County, Virginia. In antebellum South Carolina, however, Downey (1999) argues that state legislatures passed riparian acts which fostered free navigation and then manufacturing interests at the expense of local property owners.

these resolutions, Madison and Jefferson declared that the Constitution was a federalist compact and that state governments have the right to declare offensive federal laws illegal in their lands. In the early antebellum period, Virginia's call for its state's rights was only muted by the fact that a Virginian controlled the presidency most of these years.

The key institution for maintaining state sovereignty for Virginians was the local judicial system supported by a local militia.³³ The Bill of Rights and the Judiciary Act of 1789 gave broad judicial powers to states. Not surprisingly, the boundaries of federal district courts were based on state boundaries. Most importantly, section 34 of the 1789 act dictated that federal judges rely on state rather than federal decisions on comparable points of law. While the Supreme Court gradually established its rights of jurisdiction over all states, Virginia strongly resisted these attempts through the nineteenth century.³⁴ Just as importantly, despite the perceived superiority of a modern professional army, especially with the rise of the Prussian army, Virginians held steadfast to an army based on a locally based militia system.

The divergence in political institutions between the colonies of Virginia and Massachusetts had a profound impact on the development of the political institution of the United States. Because of the deep differences between the federalists of Massachusetts who desired a more centralized government based on the principles of democracy versus the anti-federalists of Virginia who held deep suspicion of centralized state power, the American *Constitution* was a compromise that yielded significant room for decentralized power. Consequently, state and local governments were much more significant in the U.S. until the rise of a more centralized national government between 1877 and 1920 (Skowronek (1982)).

³³ See Edling (2003).

³⁴ See Miller (1994).

American-style decentralized federalism proved to have lasting legacies for the development of the American economy (Kim (2008)).

Evaluating the Causes of Institutional Divergence in the United States

The review of the political and legal histories of Virginia and Massachusetts suggests that the initial differences in the demographic and wealth distributions of the two colonies, determined in part by the legacy of history, played a profound role in the initial divergence of political institutions between the two colonies. After the early founding years, however, other factors such as climate and factor endowments solidified their road to diverging political institutions. Moreover, the divergence in their political institutions seems to have set the stage for the divergence of their legal institutions in the early nineteenth century.

First, as argued by Fischer (1989), the initial divergence of colonial institutions in Virginia and Massachusetts is partly explained by the different English regions and cultures of the colonists: Massachusetts being founded by Puritans from the East of England and Virginia being populated by Cavaliers and settlers from the less egalitarian culture of the English South-West. The differences in the private goals and strategies of the Virginia and Massachusetts companies led to major differences in their demographic characteristics and their early governing institutions. In Virginia, the goal of using plantation labor for profit led to a stratified demographic structure conducive to military rule. By contrast, in Massachusetts, the goal of establishing religious communities led to a homogenous, egalitarian population structure conducive to the rise of democratic government (Fischer (1989)).

In addition, as noted by Konig (1992), the divergence of early political and legal institutions based on the demographic characteristics found in the colonies of Massachusetts and Virginia had English legal precedence. Whereas the early immigrants to Massachusetts had

generally enjoyed common law rights in England and were familiar with the English county or borough judicial system, the majority of the Virginia immigrants, composed of servants and convicts, was denied these rights in England.

Second, climatic differences of the American colonies contributed to the continued divergence of demographic structures and institutions in Virginia and Massachusetts. In Virginia, due to the extremely high mortality rates until the eighteenth century, there was a constant turnover of young, male servant population.³⁵ The unbalanced sex-ratios and stratified demographic structure were not conducive to the introduction of a full-fledged democratic government in Virginia. As mortality rates stabilized and as increasing numbers of servants survived to form a sizeable population of free whites, an element of democracy was introduced in the form of the election of the Houses of Burgesses. Despite this change, however, as all other important offices were appointed, often for life, the elites were able to effectively control the government of Virginia. In Massachusetts, the low rates of mortality and low rates of immigration contributed the emergence of stable communities. After the early years, no sizeable numbers of new immigrants were introduced. The stable, egalitarian demographic structure fostered the extension of democracy to many levels of government.

Finally, factor endowments contributed to the divergence in economic and landholding structures which influenced the final development of institutional structures in the two colonies. In Massachusetts, a climate conducive to small scale farming contributed to egalitarianism and democracy. In Virginia, a climate conducive to tobacco plantations, led to the rise of plutocracy based on the political power of the landed gentry class. In Massachusetts, there was little economic incentive to accumulate large holdings of land the method of distributing land through town governments raised the costs of land accumulation. In Virginia, the land intensive tobacco

³⁵ See Gemery (2000)).

farming provided significant incentive to acquire land and the headrights system lowered the costs of accumulating large landholdings by elites.

The limits of state military capacity and the possibility of rebellion by the general population also played major roles in determining the structure of American colonial governments. In Massachusetts, democracy did not arise because the elites promoted it as an ideal form of government. Rather, the elites believed that democracy would lead to mob rule. Democracy emerged, in part, as the ruling elites were forced to grant electoral concessions to the general population under a constant threat of rebellion. In 1631, when taxes were imposed on the residents of Watertown to pay for the fortification of Newtown by an elite legislative body of “assistants,” the Watertown residents rebelled against what they believed was taxation without representation. In 1632, fearing outbreaks in other towns, the “assistants” called for the election of two freemen from each town to meet with them and discuss the question of raising funds by taxation.³⁶ As theorized by Acemoglu and Johnson (2002), these electoral concessions served as a credible commitment to a fair allocation of resources by the ruling state and were given to avert a mass rebellion.

In Virginia, the only elected office was the Houses of Burgesses. Because the elections were held at the discretion of the governor and all remaining offices, including important local offices such as sheriffs, were appointed, the elites had far greater control of the governing structure of Virginia. One reason for the political dominance of the landed elites was that, except for few brief episodes like the Bacon’s rebellion, the threat of rebellion by the masses was much lower in Virginia. Because the population in Virginia was much more dispersed and few towns

³⁶ While many scholars attribute the rise of a democratic government in Pennsylvania to William Penn’s enlightened religious and political philosophies (see Fischer (1989) and Osgood (1904)), Keller (1969) finds that the primary impetus toward a more democratic local government in Pennsylvania, as in Massachusetts, came from the concern over “taxation without representation.”

existed, the costs of organizing a rebellion was much higher. More importantly, most free whites who were servants were not qualified for public office and the poor often relied on the landed elites for capital as well as marketing and retail services. With the rise of slavery, the incentives of all whites became much more aligned against African slaves. Finally, the elites were able to develop a better military organization under their control to subdue uprisings.

Legal institutions diverged only slightly between Massachusetts and Virginia during the colonial period since the English common law based on local jury law served both communities relatively well. Common law and the primacy of the local jury were consistent with the system of local militia. Since local juries ruled on law and fact, local juries defined law for their local communities. Given the limited military power of the state, the governing by a militia system dictated a legal system based on local consensus and fairness. Ordering a militia to enforce a legal decision that violated a community's sense of fairness was difficult at best.³⁷

In the early nineteenth century, legal institutions in Virginia and Massachusetts diverged. In Virginia, planter gentry who controlled Virginia had great incentives to keep the legal institution based on common law and local juries as protection from arbitrary powers of a more centralized government. In Massachusetts, however, the argument that local juries ensured protection against the arbitrary use of powers by the state weakened. To the contrary, the full power to establish laws, statutes, and ordinances, provided that they are not repugnant to the Constitution, including the power to modify or repeal common law, was explicitly granted to the jurisdiction of the legislature.³⁸ Because democratic elections limited the arbitrary powers of the government, the people of Massachusetts favored a stronger centralized state government with a strong state military powers to enforce its laws.

³⁷ See Nelson (1975: 34-35).

³⁸ See Nelson (1975: 92).

Conclusion

The economic development of the United States involved the divergence of U.S. regional economies between the eighteenth and the nineteenth centuries. Unlike the previous literature which has emphasized the role of slavery and other economic factors, this paper suggests that the divergence in political and legal institutions may have played a significant role. Although it is beyond the scope of this paper to provide a robust empirical test of this hypothesis, the study of the divergence in the political and legal institutions of Virginia and Massachusetts suggests that the early rise of a democratic government in Massachusetts fostered industrial development, whereas an oligarchic government in Virginia favored the agrarian plantation elites.

While other studies have emphasized the role of slavery in the divergence of U.S. northern and southern institutions (Wright (2006)), this paper argues that the divergence of political institutions between Virginia and Massachusetts arose well before the introduction of slavery in Virginia. The roots of their institutional divergence were sewn by the variations in Albion's seed which determined the initial levels of social inequality of the two colonies. The homogenous, egalitarian Puritan society emerged swiftly with a democratic government whereas a stratified society in Virginia developed with an oligarchic one. Over time, local conditions such as climate and factor endowments sustained the levels of social inequality until mature divergent political systems emerged. Importantly, the lack of a centralized military authority allowed the geographic dispersion of political and legal authority.

In the early years, both colonies adopted the local, jury-based common law tradition of England. However, in the early nineteenth century, as trade and industry developed in Massachusetts, instrumental, uniform state-wide law emerged, whereas in Virginia, traditional

common law and local juries remained the primary basis for ensuring local control of society.³⁹

The political and legal institutions in Massachusetts and Virginia diverged even after their independence as the *Constitution* allowed significant states' rights, but with the aftermath of the Civil War and the rise of the powers of the federal government in the second half of the twentieth century, the institutions of Virginia and other southern states finally began converging toward those of the North.

The founding of American colonies in the seventeenth century provides a valuable historical experiment in the development of political and legal institutions in a new world. Even though the American colonies were established to extend the territory of the British Empire, distance and circumstances forced these colonies to develop their own governing institutions and seek independence over time. While the histories of Massachusetts and Virginia yield important clues as to why institutions diverged between the U.S. North and South, a fuller picture of the causes of institutional developments in the New World will no doubt emerge with additional investigations of the histories of the other eleven colonies.

³⁹ Equally important was the fact that both Virginia and Massachusetts were settled by the English with the Anglo-Saxon common law rather than the Roman civil law tradition. Unlike civil law, a system of positive rules codified in books called codes, the English common law had a two-tier system: the King's court of chancery and the common law courts. Whereas the law of equity from chancery evolved into a complex body of rules understood by trained lawyers and judges, the common law for common people was based on local tradition, custom and precedents (Hall (1989)). In the American colonies, this common law heritage combined with local methods of selecting judges reinforced the development of localism and divergence (Ely and Bodenhamer (1986)). Thus, legal institutions of nations with common law traditions, unlike those of civil law traditions, may vary considerably over time.

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