Law and Finance at the Origin

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[Almost full text of introduction; abbreviated subsequent sections.]

1 Introduction

Understanding the causes of financial development and economic growth is central to the research agenda in economics. The law and finance literature has provided us with theoretical arguments and empirical evidence that a country's legal system affects finance and growth (La Porta, Lopez-de-Silanes, Shleifer, and Vishny, 1997 and 1998).

More recently, researchers have started to re-evaluate the role of legal institutions relative to political institutions (Rajan and Zingales, 2003; Acemoglu and Johnson; 2005; Pagano and Volpin, 2005). These researchers argue that different political environments prompt different degrees of economic and financial development. The effectiveness of institutions might vary considerably with the political support they receive.

One insight emerging from this debate is that it is hard to get definitive answers on the empirical determinants of growth. Given the rarity of perfect natural experiments, careful and detailed analyses of individual cases are particularly valuable and an important part of the literature, even if they stop short of proving causality. In fact, much of the literature revolves around specific examples, mostly referring to the last two centuries.[1]

This paper extends the current evidence to a much earlier time period, two thousand years ago in the Roman Republic and the Roman Empire. We propose that, contrary to widespread belief, the first predecessor of the modern business corporation was not the English East India Company nor the medieval *commenda*,[2] but the Roman *societas publicanorum*, i.e. the "society of government leaseholders." We provide details about the functioning of the Roman corporation and about its rise and fall in the light of a drastically changing political environment.

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[1] See, for example, Engerman and Sokoloff, (1997) and (2002); Berkowitz, Pistor, and Richard (2002); Lamoreaux and Rosenthal (2005); and Haber, Razo and Maurer (2003).

[2] See, for example, Ekelund and Tollison (1980) and Gower (1969), p. 22. Kindleberger (1984) characterizes, more generally, alterations of the "true" partnership as the earliest forms of business organization but views the medieval *commenda* as the starting point (p. 195). Baskin and Miranti (1997) explicitly assess the development of the business organization under Greco-Roman law as restricted to partnerships.

The history of the Roman shareholder company sheds light on the nexus of law, finance, and growth from three angles. First, the historical development of the Roman corporation allows us to disentangle the roles of legal versus political institutions more clearly since the two evolved into opposite directions. Namely, when Roman law was still far from a complete body of civil law, during the "pre-classics" of the Republic, political interests demanded stable business organizations that could raise large-scale financing. During the Roman Empire, when Roman legal science reached its height ("classics"), political interests reversed. The political change induced a regression in financial contracting despite the legal advancement. Our findings suggest that economic development requires little legal underpinning when it is in the government's interest. And, without the government's support, it may wither despite a pre-existing legal framework.

Second, the rise of the Roman corporation suggests that legal systems may be less of a technological constraint for growth than previously thought. Much of the current literature views Roman law as too rigid to foster financial development and classifies it as a growth-hostile. We find, however, that Roman law provided a flexible and nurturing legal environment during the Republic. It accommodated such radical advancements in financial development as the enforcement of a corporate business format. In fact, the case-based evolution of Roman law resembled closely today's common-law systems.[3]

Third, the case of the *societas publicanorum* emphasizes the role of business "formats," in particular the corporation. The organizational format of a business affects access to external finance, the stability (or "longevity") of a firm, the ease of representation by individual managers, and the rights and obligations firms can assume. Each of these implications, in turn, affects the transaction costs of economic interaction with the firm. The case of the *societas publicanorum* illustrates how an advanced (corporate) format facilitates business operation. At the same time, it also shows that the available menu of organizational formats evolves independently of company laws. Any analysis focusing on formal company law risks misconstruing the actual state of organizational development and its implications for finance and growth.[4]

The remainder of the article is structured as follows. Section 2 provides an overview of the literature on the determinants of financial development and growth. The overview contrasts the literature in law and finance with the political economy perspec-

[3] At the same time, we also find that these economic advancements were reversed later, when political interests changed during the Roman Empire. It is possible that other legal systems would have prevented such a reversal. For example, a common law system might have provided better protection against the State, consistent with the view that civil-law systems are weaker in their protection of property rights.

[4] Lamoreaux and Rosenthal (2005) come to a similar conclusion for 19th century business organizations in France and the United States.

tive, stressing the role of governments' interests for financial development and growth. In Section 3, we turn to the specific case of the Roman shareholder company. After some general background on the Roman economy and on the Roman legal system, we present details of the characteristics of the *societas publicanorum* and its rise and fall. We discuss the corporate character of the *societas publicanorum* during the Republic and the likely causes for its demise. In particular, we point out how changed political interests may have triggered the demise of such an advanced business organization at a time when the legal framework was, if anything, better able to support it than when it emerged. Section 4 discusses the implications of the case of the *publicani* and concludes.

2 Determinants of Financial Development and Growth

A burgeoning literature analyzes the nexus of law, finance, and growth. Excellent recent surveys of this literature are provided by Levine (2005) and Beck and Levin (2005). The literature overview in this Section focuses on the debate about legal versus political institutions. We pay special attention to a specific aspect of financial development, access to external finance, and to the role of firms' organizational format.

The literature on the institutional determinants of financial development and growth builds on earlier analyses of the interplay between these two outcome variables. While there is little doubt about the positive correlation between finance and growth (see e.g. Levine and Zervos, 1998), the basic question in this earlier literature is: Does financial development induce economic growth? Or is it economic growth that triggers the development of better financial systems? Or are both outcome variables correlated with a third, unobserved factor?

The literature on this topic is extensively reviewed in Levine (1997) and (2005). A few basic findings merit mention also in the context of this article. First, the vast majority of recent papers argue that the directional impact goes from finance to growth: financial systems strongly affect long-term economic growth (e.g. King and Levine, 1993a and 1993b; Jayaratne and Strahan, 1996; Demirgüç-Kunt and Maksimovic, 1998). Second, an important channel for the impact of finance on growth is the mitigation of informational asymmetries and transaction costs (Levin, 1997). For example, lower informational hurdles facilitate funding by outside investors. The availability and cost of external finance, in turn, is a key determinant of economic growth (Rajan and Zingales, 1998). A large literature in macroeconomics also identifies access to external finance as an important determinant of long-term growth (see Barro, 1997). Aghion, Howitt, and Mayer-Foulkes (2005), for example, argue that the lack of financial development can impede access to external finance and thereby prevent a country using technology transfer to

converge to the growth rate of the world technology frontier. Thus, financial constraints prevent poor countries from fully benefiting from technology transfer. A number of papers explore the role of financial intermediation on growth in AK-style models (building on the assumption of non-diminishing returns to capital). This literature includes Greenwood and Jovanovic (1990), Levine (1991), Bencivenga and Smith (1991, 1993), Saint-Paul (1992), Sussman (1993), Harrison, Sussman, and Zeira (1999) and Kahn (2001). Other papers use innovation-based growth models to explore the relationship between finance and growth, such as King and Levine (1993b), de la Fuente and Marin (1996), Galetovic (1996), Blackburn and Hung (1998) and Morales (2003).

Given the impact of financial development on economic growth, the next step is to understand what triggers the development of a financial system.

The law and finance literature argues that legal institutions are a key determinant. Starting with La Porta et al. (1997) and (1998), researchers have related financial development to private property rights, contract enforcement, and investor protection. This literature has used the legal tradition of a country, or its "legal origin", to instrument for the current legal environment. Building on the classification of commercial legal systems in David and Brierley (1985), and in line with Dawson (1960) and Merryman (1985), they distinguish four legal systems: British common law, French civil law, German civil law, and Scandinavian civil law. Through colonization, and later also through imitation, these legal traditions spread beyond Europe and allow cross-country comparisons around the world. As proxies for financial development, La Porta et al. use market capitalization, initial public offerings, and bank financing.

Civil-law systems and, in particular, French civil law emerge as most detrimental to financial development. The literature proposes several reasons why that may be the case. La Porta et al. relate legal origin directly to the protection of investor rights. (We will discuss the construction of their proxies for shareholder rights protection and for creditor rights protection.) Other work relates investor protection laws and private property rights to firm valuation (Claessens, Djankov, Fan, and Lang, 2002; La Porta et al. 2002; Caprio, Laeven, and Levine, 2003), to dividends (La Porta et al., 2000), and reinvestment of earnings (Johnson, McMillan, and Woodruff, 2002). La Porta, Lopez-de-Silanes, and Shleifer (2006) showcase weak liability rules and insufficient information disclosure rules in French legal origin countries, consistent with weaker enforcement of private contracts. Levine (1998, 1999, 2003) and Beck, Levine, and Loayza (2000) bridge legal-origin induced investor protection to the development of stock markets and financial intermediation, and ultimately to cross-country differences in growth.

One aspect of the legal environment that has received less attention in this context is company law and, in particular, the menu of "company formats." For example, does it matter whether firms can incorporate? The main literature on finance and growth does not discuss organizational formats in the context of financial development. A number of economic and legal historians, however, have studied the role of limited liability and incorporation, most importantly Lamoreaux and Rosenthal (2005) and related papers by Forbes (1986) and Weinstein (2001). These researchers express skepticism about the role of company law. For different time periods and regions, these authors find that the adoption of limited liability had little impact on firms and shareholders. The example of the Roman corporation in the next Section will, on the one hand, confirm this view: whether company law formally allows for private corporations does not seem to matter. Roman businessmen achieved a corporation-type organization in practice, even without the formal legal implementation. On the other hand, it *does* matter whether quasi-corporations were enforced in practice. In the Roman case, the large businesses withered when government interests opposed them and prevented their corporate organization.[5]

Among other implications, the company format is likely to affect the access of the company to external financing. For example, access to external investment is likely to be easier if the liability of investors for company debt can be limited and if the existence of a company does not depend on the presence of its members (partners). Access to external financing, in turn, is likely to affect economic growth. From the law and finance perspective, the legal environment affects the ability of firms to raise external financing and thus to relax financial constraints.

The role of access to external finance has been discussed extensively in the law and finance literature. La Porta et al. (1998) argue that Civil Law systems, in particular, constrain firm financing with low investor protection. Recent empirical literature confirms this argument. Rajan and Zingales (1998) and Beck and Levine (2002) show that legal institutions affect the availability of financing and firm creation. Using the size of firms as a simple proxy for financial constraints, Beck, Demirgüç-Kunt and Maksimovic (2005), in a survey of over 4,000 firms in 54 countries, show that countries with less effective legal protection of property rights have more constrained, i. e. smaller, firms.

[5] The importance of enforcement is more general. As Easterbrook and Fischel (1991) argue, the explanatory power of legal rules is limited if firms can opt out of the default regulation. From this point of view, it is puzzling that legal rules have *any* significant impact on economic outcomes. Gennaioli (2006), however, points out that "opting out" is a true option only if the alternative private contracts are permitted and enforced by courts. He develops a model illustrating the role of the "contractual channel" via which law can affect economic development..

Claessens and Laeven (2003) go one step further and show that the lack of investor protection affects, in particular, firms with little collateral.

Relatedly, Wurgler (2000) and Beck and Levine (2002) show that legal institutions affect not only the volume but also the allocation of external finance across firms and industries. They argue that strong investor protection induces a more efficient allocation of capital to growing firms. Similarly, Demirgüç-Kunt and Maksimovic (1998) show that countries with strong legal investor protection also have better financial systems and, in particular, channel financing to high-growth firms.

The law and finance research, surveyed above, has also triggered some intense criticism. Much of the criticism is rooted in different interpretations of legal rules, legal systems, and legal evolution. Is civil law really more rigid than common law? Are private property rights really less well protected in civil-law countries? How informative and useful is the classification by legal origin? And, even if such a classification *is* useful, how relevant is it for financial development?

These questions are certainly of methodological and juridical interest. It is less clear how important the criticism is on substance. After all, even if law and finance researchers misinterpreted the historical evolution or some characteristics of the law, the empirical relation between certain legal systems and certain economic outcomes is still important. Beck and Levine (2005) present a broad discussion of these issues.

Another recent string of literature re-evaluates the role of legal institutions relative to political institutions. The "political economy view" follows two main lines of arguments. The first argument starts, again, from questioning the exogeneity of legal systems. Legal institutions are viewed as the outcome of political decision-making. This literature posits that the political elites shape legal institutions to maximize their power and ensure that they stay in power (Pagano and Volpin, 2001; Rajan and Zingales, 2003). From that perspective, legal and economic institutions are endogenous to the political environment.

This view does not necessarily contradict that the legal environment has a causal impact on finance and growth. The political economy view merely points out that the finance- and growth-friendliness of a legal system depends on the interest of the political elites. If their interests coincide with financial and economic development, the elites will choose to implement legal and other institutions that foster the development. If their interests and desire to cement their political power demand institutions that are unfavorable to growth and development, they will implement those (North, 1981). Pagano and Volpin (2005) apply this view to company law and relate it to differences in cross-country differ-

ences. A similar discussion of property rights protection and the underlying political economy is in Roe (1994) and Haber, Razo, and Maurer (2003).

The second line of arguments takes the role of politics one step further. Rather than analyzing the interaction of politics and law, some researchers ask directly whether politics determines long-term growth – with or without law. One starting point is the research by Engerman and Sokoloff (1997) and (2002). They identify inequality in political power (as well as in wealth and human capital) as a key determinant of economic growth, in a comparison of the US and Canada, on the one hand, and other New World economies, on the other hand. Similarly, they identify the impact of inequality over time (rather than cross-sectionally), using the example of the Americas. They also discuss the tendencies of government policies to maintain these conditions along the respective economy's path of development.

The role of political institutions is also the theme of Acemoglu and Johnson (2005). They distinguish between political, or "property rights" institutions, which regulate the relationship between the State and citizens, and legal, or "contracting" institutions, which regulated contractual relationships between citizens. The authors compare the two types of institutional determinants and ask how central "contracting institutions," including corporate and business-related laws, are to the economic and financial development of a country. They provide empirical evidence for the primary importance of property rights institutions for financial development and long-run growth, exploiting variation in both types of institutions due to colonial history (building on Acemoglu, Johnson, Robinson (2001)) and legal origin (based on La Porta et al. (1997) and (1998)). They use constraints on the executive, protection against government expropriation, and private property protection as proxies for good political institutions. After controlling for the quality of property rights institutions, the find no effect of contracting institutions on per-capita income, investment over GDP, and private credit over GDP. Thus, they argue, contracting institutions that are not backed up by political power will not have a big impact. And, vice versa, even dysfunctional contracting institutions will be enough to support economic and financial growth as long as political institutions provide security against expropriation by elites and government. These findings reflect that the State, as the ultimate arbiter of contracts, cannot be constrained under insufficient political institutions – whether it fosters or hampers economic growth. The example of the Roman corporation, provided in the next Section, will further illustrate this point.

The second line of argument within the "political economy view" leads to a horse race between the importance of legal versus political institutions. In addition to Acemoglu and Johnson, Beck, Demirgüç-Kunt, and Levine (2003) relate cross-country differences in political systems to law and finance. Their proxies include measures of the de-

gree of competitive and executive elections, measures of the number of influential veto players in legislative process, and an overall index of national openness based on trade openness. They find that legal systems have strong predictive power, e.g. for equity market development, banking sector development, and the level of private property rights protection, after controlling for characteristics of the political environment.

The evidence about the rise and fall of the Roman shareholder company provides historical support for the view that political institutions can dominate the role of other institutions. As described in the next Section, the right set of political interests allowed the shareholder company to flourish under the Republic, when the legal environment was not (yet) sophisticated enough to allow for the concept of a non-public corporation. And, when the Roman legal system reached is height in the so-called classical period, but government interests changed, the corporation vanished.

3 A historical case study: the Roman corporation

During the five centuries of the Republic, the Roman government never assembled any sizeable continuous bureaucracy. Rather, numerous public services were contracted out and public income sources were leased to private entrepreneurs. These private contractors were called "government leaseholders" or publicans (*publicani*). As Ulpian writes in the Digest (D. 39,4,12,3 [38 ad ed.]):

Publicani autem dicuntur, qui publica vectigalia habent conducta.	Those are called *publicani* who conduct the exaction of public taxes.

In this section, we first provide some background information about the functioning of the economy and the legal system in ancient Rome (Subsection 3.1). We then describe the role and business activities of the publicans, from the 5th century B.C. until their demise under the Roman emperors (Subsection 3.2). We argue that, at the height of its development, the *societas publicanorum* was, de facto, assuming the role of a private corporation (Subsection 3.3). We conclude by discussing the likely causes of the corporation's demise under the Roman Empire (Subsection 3.4). In the next section (Section 4), we will return to the current debate about the nexus of law, politics, and finance and discuss the broader implication of our ancient empirical evidence, as well as more general insights about economic development with and without law.

3.1 Roman Economics and Roman Law

The historical evidence about the publicans stretches from the beginnings of the Roman Republic into the Roman Empire. The height of their activities falls into the last two cen-

turies BC. In this subsection, we will provide some background information about the economic development and the legal system in Rome at that time.

Economics

Until the Punic Wars in the middle of the third century B.C., the Rome was a rural community. During the late Republic, however, from the third to the first century B.C., the Roman power extended all over Italy and then beyond the Mediterranean, including West and South Europe, Asia Minor, the Near East, Egypt, and North Africa. Large-scale commerce, industry, and finance sectors developed, and the volume of trade, in particular seaborne trade, exploded. Hopkins (1980), for example, infers from the frequency of ancient shipwrecks that, in the period 200 B.C. to 200 A.D., interregional trade was higher than ever before – and than at any time during the following millennium. Kessler and Temin (2005) argue that the Roman grain market was integrated over all of the Mediterranean area.[6] Hopkins (1980) employs the spread of silver coins, minted at Rome, across the different regions of the growing Roman state to illustrate its integration into a single monetary economy. In the first century B.C., Rome had become the monetary centre of the known Western world (Cunningham, 1902, p. 164). Technical progress clearly supported the growth of the Roman economy. Wilson (2002) argues, for example, that the discovery, use, and ultimate abundance on water-powered devices had a causal impact on the development of the Roman economy, and Greene (2000) points to the role of technological transfer and its speed more broadly. In addition, Temin (2004) provides evidence of a well-functioning financial system, even beyond the question of a common currency. In particular, he argues for the presence of sophisticated financial intermediaries (*argentarii*), which allowed to pool funds effectively across the Roman economy.

These details about the ancient Roman economy suggest impressive economic development during the late Roman Republic and early Empire. In fact, Temin (2001, 2006) argues that the Roman economy during the Principate was more market-oriented than the medieval economy. These insights will also allow a better understanding of how business organizations as advanced as the *societates publicanorum* could exist in an ancient economy.

Law

From the period until the Punic Wars (in the middle of the third century B.C.), our knowledge of Roman law is limited to the Twelve Tables (450 B.C.). These XII Tables were not a codification of all or even the most important legal rules. Rather, they dealt

[6] See Temin (2001) for a summary of the evidence for other product markets.

specifically with the power struggle of plebeians and patricians and ensured basic economic and political rights for the plebeians (e.g. Kaser, 1980, p. 15).

The jurists of the last two pre-Christian centuries, the pre-classics, first developed a form of "legal science," with formal legal concepts and systematization. The encounter with Greek philosophy is often credited for this development (Kaser, 1980, p. 4).

Roman law reached its height in the period of the so-called "classical jurisprudence," during the first two and a half centuries A.D. The Roman law of this period has exerted a large influence on legal systems throughout the world and throughout history. The above discussion about "Roman-law origin" is only one example. Of the different branches of law, however, it is exclusively the "private" (or civil) law which has had such influence– either directly, as the foundation of modern private-law systems, or indirectly, through the modern Civil Codes.[7]

Roman private law never underwent systematic codification. It was developed only to a minimal extent by legislated statutes (*leges*, *plebiscita*, or *senatus consulta*). Rather, it emanated from the advice of legal experts to the judicature, notably Julian, Celsus, Gaius, Ulpian, and Paul. Roman law textbooks (e.g. Schulz, 1951; Buckland and Stein, 1963) characterize it as "juristic law."

The background is the following. In Rome, different magistrates administered justice: the *praetor*, the curule *aediles*, and the governors in the provinces. These magistrates appointed jurors, called *tribunales*. Neither the magistrates nor their jurors usually had any legal training. Instead, they appointed jurists into a committee of legal experts, the *consilium*. Based on the experts' opinion, the magistrates would grant actions (*actiones*), defenses (*exceptiones*) and other legal remedies. Those expert opinions shaped the legal system, even if they had no formal legal power.

Being an expert was not an honorable and desired appointment for lawyers (usually from the aristocratic class), who also advised plaintiffs and defendants. The lawyers would not discuss abstract concepts, but concrete cases of current interest. (Kaser, 1980, p. 4). Thus, Roman law developed very much in touch with day-to-day legal questions. In fact, Roman-law scholars like Kaser (1980) liken the Roman law to English law today: it was law free of abstract concepts and essentially "case law." This gave the Roman law an enormous degree of flexibility and, in particular, the ability to cope with the transformation of Rome from a rural community to a large empire. (Kaser, 1980, p. 18).

All of these features help to understand how the creation, i.e. legal recognition, of a quasi-corporation could occur without formal legislative changes.

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[7] The civil-law codifications replace for the direct application of Roman law in many countries since the end of the 18th century (Kaser, 1980, p, 2).

Finally, it is noteworthy that, under the Principate, the emperors' decrees (*constitutiones*) started to be recognized as binding legislation. Imperial law mostly continued to develop the pre-existing body of law, though it sometimes also served state politics (Kaser, 1980, p. 4).

3.2 Who were the *publicani*?

During the five centuries of the Republic, the Roman government never assembled any sizeable bureaucracy. Rather, numerous public services were contracted out and public income sources were leased to private entrepreneurs. These private contractors were called "government leaseholders" or publicans (publicani). Since the Roman aristocracy was not allowed to participate in the government leases, a separate class of entrepreneurs emerged, later known as *equites.*

In this Subsection, we describe the business activities of the publicans during the Roman Republic. We build upon the classic work on the *publicans*, Badian's *Publicans and Sinners* (1983).[8]

The earliest reports refer to the 5th century B.C. Ancient historians such as Dionysius of Halicarnassus and Livy give accounts of religious and ceremonial services as well as construction jobs contracted out to private entrepreneurs. Another famous example of these early times is the feeding of the white geese on the Capitol. These geese received government-sponsored meals since, in 390 B.C., their honking had warned the Romans of the attacking Gallic troops.[9] According to Pliny[10], the "geese feeding program" was leased out to the publicans.

Over the course of the Republic, an increasing volume of public works was leased out, until the publicans dealt with the business of each state department (e.g. Cunningham, 1902, pp. 157 and 162). We describe the growth of government lease holding from smaller firms to a major industry of large companies at the end of the Roman Republic. The publicans had three main areas of business:

1. the provision of services or supplies for the public,
2. the utilization of public property, and
3. the collection of public revenues.

We present evidence from numerous historical sources showing the far reach of these "privatizations," including army provisions; construction, renovation and maintenance of streets, city walls, temples, markets and other public buildings; grazing on the public domain (*ager publicus*), mining and fishing on public property; and finally even the collec-

[8] Older literature includes Ürödgi (1968).
[9] Livy, *Ab urbe condita* 5,47,4.
[10] Pliny, *Naturalis historia* 10,26,51.

tion of poll or land taxes from the provincials. We also point out that the scale of these businesses expanded vastly with the expansion of Rome.

Finally, we describe the demise of the *societas publicanorum* under the Roman Empire. With the decline of the Roman Republic, the *equestri*—and thus many of the *publicani*—were subject to new proscriptions.[11] Economically, legal reforms restricted the area of their activities one after the other. First, the activities of the publicans were limited to collecting taxes and dues.[12] Then, Augustus transferred the tax collection contracts in Gaul, Asia, and finally in all of the imperial provinces to a *procurator Augusti*.[13] Gradual restrictions continued to be implemented throughout the Julio-Claudian dynasty (Tiberius, Caligula, Claudius, and Nero; 14-68 A.D.). With the advent of the 2nd century A.D., Trajan (98-117 A.D.) limited the lease of collections contracts for private entrepreneurs to isolated types of taxes such as the inheritance tax (*vicesima hereditatium*). The large-scale operations of the *publicani* reverted to smaller-sized businesses of so-called *conductores* (contractors), similar to their origins in the early Republic.[14]

The demise of the *societas publicanorum* also explains why this form of business organization is not well-known among economic and legal historian. Most of today's knowledge about Roman law stems from the *Corpus Iuris Civilis*, the massive compilation effort in the Eastern Empire under Justinianus I. The *Corpus Iuris Civilis* aims at documenting and codifying the full body of Roman law. Its main parts were issued in 533 and 544 A.D.: the *Institutes*, comparable to an introductory textbook, the *Digest* (or *Pandects*), the core piece which documents various legal debates, and the *Codex* with imperial constitutions from the Principate. Thus, the compilation discusses legal opinions from the classical and post-classical periods (1st to 6th century AD), but not the pre-classics. Since the codex was compiled after the disappearance of the lease-holding companies, the jurists cited in the *Corpus Iuris Civilis* mention the publicans at most in the sense of smaller tax collectors. This lack of easily accessible evidence is likely the reason the *societas publicanorum* is relatively unknown in the history of the corporation.[15]

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[11] According to Appian (bell. civ. 4,5), 2000 *equestri* were killed; see also the detailed account of the brutality of the proscriptions in Cassius Dio (47,14). More on this in Ürödgi (1957), col. 1201.
[12] Cimma (1981), p. 99ff.; Hirschfeld (1963), p. 69ff.; Rostovtzeff (1902), p. 379 ff.
[13] Marquant (1884), pp. 301-318; Ürödgi (1957), col. 1200, 1202.
[14] See Pliny, *Epistulae* 7,14; *Panegyricus* 3,7,7; 39,5.
[15] See Malmendier (2002). In addition, most of the scarce surviving evidence about economic activities in ancient Rome comes from the period of the early Empire; see Temin (2006).

3.3 The *societas publicanorum* as a business corporation

To what extent were the large associations of the publicans "corporations"? In this section, we argue that both the increased access to capital markets and the recognition as legal entities allowed the *societates publicanorum* to function like modern corporations.

We first characterize briefly the available historical sources. As pointed out above, the primary source of Roman law, the *Corpus Iuris Civilis*, is unfortunately of limited use. We thus turn to two types of alternative sources – classical Roman and Greek literature and inscriptions. In particular, we exploit the *Monumentum Ephesenum*, an inscription discovered in Ephesus in 1976, which turned out to be the translation of a Latin tax law – the *Lex Portorii Asiae* – from 62 AD.[16] The nucleus of this law, paragraphs 1-36, originates in the late Republic, 75 or 74 BC[17] and reveals numerous details about the functioning of the lease-holding companies.

Based on these sources, we outline the evolution of the *societas publicanorum* in the context of pre-existing types of firms. Roman law recognized two types of "associations," the *collegium* and the *societas*. The only incorporated form of organization besides the public corporations (such as the *populus Romanus*, i.e. the state, or the *aerarium* and *fiscus*, i.e. the state and imperial treasuries) was the *collegium*. The *collegium*, however, was restricted to organizations with "public purpose" such as religious and political associations, not including government lease holding.[18] Thus, government leaseholders had to set up their companies as *societates*, the Roman version of partnerships. The Roman partnership differed from the modern corporation in many ways. The partners (*socii*) could not limit their liability; the partnership could not exist beyond the death or renunciation of a partner nor in case of legal disputes among the partners; and the firm could not assume rights or obligations separately from its members.[19]

This format was evidently insufficient for the large-scale and long-term operations of the government leaseholders. The Romans resolved this problem by developing a series of "reinterpretations" and exceptions, applicable only to the lease-holding companies. Four features differentiate the *societas publicanorum* from the simple *societas*:

1. *Representation*: A single person could contractually bind the firm and assume rights in the name of the firm.[20] The representative with whom the *censor*, the registrar and finance minister of Rome, interacted was called *manceps*.[21]

[16] Engelmann-Knippe (1989).
[17] Engelmann-Knippe (1989), p. 95 f. and 160.
[18] Duff (1938), pp. 95 ff.
[19] See, for example, Kaser (1980), pp. 225-227.
[20] *Digesta* 3.4.1.1.
[21] Festus p. 151 M.

2. *Continuity and Stability*: The firm did not cease to exist if a partner died or left the firm. Moreover, legal disputes among the partners, which led to the dissolution of the simple *societas*, did not necessarily affect the existence of the *societas publicanorum*.[22] As we can infer from paragraphs 46 and 54 of the *Lex Portorii Asiae*, even the departure of the key executive, the *manceps*, did not affect the contractual relationship between the company and the Roman government.
3. *External Financing*: Outside investors could provide capital and acquire shares (*partes*) without becoming a partner and, in particular, without being liable for the company's contractual obligations. Numerous ancient authors mention shareholders of the *societates publicanorum*, referred to as *participes* or *adfines*.[23] The shares were traded and had fluctuating prices. For instance, Cicero writes about 'shares that had a very high price at that time.'[24] Traders met on the *Forum Romanum*, supposedly near the Temple of Castor.[25]
4. *Rights and Obligations*. According to *Digesta* 47.2.31.2 the company of tax collectors, *societas vectigalium*, could file actions, including actions against fraud or embezzlement. The company could own property and inherit items.[26]

The *societas publicanorum* thus seems to satisfy the most important elements of the modern corporation. In fact, some other sources describe it almost directly as a separate legal entity. For example, Cicero reports about a *societas publicanorum* that 'consists of other *societates* [*publicanorum*],[27] and thus assumes the role of a natural *persona*. Gaius counts the *societas publicanorum* among the organizations with a '*corpus*' in *Digesta* 3.4.1.1. And *Digesta* 46.1.22 proposes that it could 'act like a person.' This corresponds exactly to the modern classification of corporations as legal *persona*.

These modifications appear to have had a far-reaching effect on the companies' access to capital. Cicero mentions that stock ownership in the *societates publicanorum* was widespread among the Roman population. According to Polybius, "almost every citizen" was involved in the government leases by the 2nd century BC.[28]

This being said, the *societas publicanorum* does not satisfy every criterion of a modern legal definition of a business corporation. However, applying modern standards ignores that the concept of the legal *persona* was formed slowly over the centuries. It underwent major re-interpretations in the 16th century and was the subject of extensive theo-

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[22] The special legal action was called *actio pro socio manente societate*, see *Digesta* 17.2.65.15.
[23] E. g. Cicero, *Pro lege Manila* 2.6, *Pro C. Rabiro Postumo* 2.4; Plautus, *Trinummus* 330-331; Livy, *Ab urbe condita* 43.16.2.
[24] Cicero, *In P. Vatinium testem interrogation* 12.29.
[25] See the references in Chancellor (1999), p. 4.
[26] *Digesta* 3.4.1 (*habere res communes*) and *Digesta* 37.1.3.4 (*bonorum possessio*).
[27] Cicero, *Epistulae ad familiares* 13.9.2 ("*constat ex ceteris societatibus*").
[28] Polybius, *Historiae* 6.17.3-4.

retical debates in the 19th century, most prominently between the "Romanist" legal scholar Friedrich Carl von Savigny and the "Germanist" Otto von Gierke.[29] Imposing the resulting modern systematization upon Roman law runs the risk of introducing much more structure than existed at the time.[30] The Romans were concerned with the rapid transformation of their small closed agricultural economy into an open system that spanned the entire known world. What is crucial is that they managed to accommodate the practical needs of their growing economy, even without revolutionizing company laws. From a practical, economic perspective, the historical sources draw a rather compelling picture of the *societas publicanorum* as the first business corporation.

3.4 Why did the *publicani* disappear?

Why did this development come to a halt, ultimately being reversed under the Roman emperors? Why did the *societas publicanorum* disappear instead of becoming the direct predecessor of the modern corporation? This takes us back to the debate on the political economy of legal developments. We showed above that the demise of the *publicani* is closely related to the rise of the Roman emperors, illustrating the importance of Rome's political economy for its financial and economic development. It is less clear what exactly the motivation for the politically induced change was.

Traditionally, historians have pointed to the abuse of power by the *publicani* as the cause of their demise. In the 16th century, Cujaz described the publicani as "unsurpassed in fraud, avarice, immodesty and audacity."[31] Over the last four centuries, this verdict has changed little. Deloume and Ürödgi represent the *publicani* as revenue-hungry exploiters.[32] Mommsen linked the gradual development of a class of profit-oriented entrepreneurs to the emerging social tensions in the Roman Republic and even the later disintegration of the Roman Empire.[33] Cunningham lists "avarice," "extortions," and "greed of gain" as the dominant influences in these transactions.[34] The elimination of government lease-holding and their replacement with public administration is then interpreted as an attempt to remedy the shortcomings of a system based on monetary incentives, similar to the reasoning in Akerlof and Kranton (2003). Augustus is hailed for organizing an effective public administration that eliminated the abuses of the publicans.

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[29] Von Savigny (1840-49), vol. 2; von Gierke (1887).
[30] A more detailed discussion of classification criteria for the ancient corporation is in Malmendier (2002).
[31] Cujaz (1595) characterizes the *publicani* in his commentary on *De publicanis et vectigalibus et commissis* (D. 39,4) as: *"Hi quam fraude, avaritia, immodestia, audacia superent ceteros homines nemo est qui nesciat…"* (p.54).
[32] Deloume (1890), p. 475 f.; Ürödgi (1968), col. 1191 f.
[33] Mommsen (1912), vol. II, p. 379 f.
[34] Cunningham (1902), pp. 157 and 165.

This explanation remains speculative. There is no direct historical proof of the emperors' motivation. Moreover, the traditional interpretation misses that the governing class had little interest in protecting the exploited inhabitants of the provinces. While there is certainly evidence of the *publicani*'s exploitation in the provinces, the proconsuls governing the provinces displayed similarly abusive behavior.[35]

Instead of invoking "benevolent paternalism" of the Roman government, we link the elimination of the government lease-holding companies more directly to changes in Rome's political economy. While history does not provide us with direct evidence on the emperors' true motivation, these explanations are consistent with economic arguments.

First of all, the political change triggered an important organizational change. During the Republic, the short tenure of the consuls and other magisterial office precluded a stable bureaucracy which would organize the public works. The emperors, instead, established an apparatus that allowed for the (re-)nationalization.[36] As pointed out by the historians cited above, the establishment of an imperial bureaucracy was a necessary condition for the change.

Still, why did the Emperors *prefer* to use their bureaucratic apparatus over outsourcing? One potential reason is the diversion of public funds. Rome's public treasury, the *aerarium*, lost its importance under the Principate as the emperors increasingly redirected public revenues, especially from the provinces, into their (private) pockets. It is easy to imagine that such diversion was easier when the emperors' own employees collected the public revenues rather than when the task was publicly auctioned off and performed by private entrepreneurs.

Moreover, the emperors gradually increased the tax burden. Taxation was generally viewed as intruding civil liberty and had caused violent resistance all over the empire, also among non-citizens.[37] It was easier to enforce taxation using government employees, i.e. representatives of public sovereignty with public enforcement rights, to collect the taxes (rather than private entrepreneurs). Thus, even if the auction-based outsourcing system had revenue-enhancing features – such as identifying the lowest bidder for the provisions of services and the highest bidder for revenue rights – the new system was likely income-maximizing for the emperors.

In addition, the emperors may have had concerns about powerful and large business organizations. In particular, they may have perceived the economic and increasingly political power of the publicans as a threat to their own imperial position, consistent with arguments in the modern political-economy debate (e. g. Rajan and Zingales, 2003).

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[35] See for example, Cary and Scullard (1975), p. 174.
[36] Heuss, 1960, p. 363; Rostovtzeff, 1957, p. 382.
[37] Laum (1926), p. 218; Meincke (1984), pp. 170-1.

Finally, it is questionable whether it was at all possible to sustain the *societas publicanorum* and the system of government leases, even if the emperors would have liked the system to persist. The issue is credible commitment on the side of the emperor. Even if the emperor had benefited, economically, from continued outsourcing, how could they convince the entrepreneurs that they would respect their property rights and honor their obligations towards the publicani? The Roman Republic was a system of checks and balances; but the emperors centralized power and could bend law and law enforcement in their favor. Eliminating the large companies was all the easier, given that their status was not enshrined in formal law.

All these factors point to the importance of political, rather than legal factors, in the establishment and persistence of corporations.

4 Conclusions: economics with and without law

We have shown that the Roman *publicani* were able to establish large-scale business operations when the governing class supported and in fact benefited from their operation. Laws were reinterpreted and adjusted to facilitate government lease holding without advancing the legal system. The concurrent switch from a Republic to an Empire and switch a privatized to a (re-)nationalized economy speaks to the role of politics in the financial and economic evolution in Rome. Moreover, since we observe economic regression at a time when the legal system reached its height, we can rule out that some underlying legal or economic evolution was driving these developments.

The case of the early Roman corporation shows that corporations can function without the legal infrastructure we usually presume they need, provided that the government is willing to take actions to grant their status and operation. It also shows that these corporations are then dependent on the government's continued support.

Interestingly, the political and economic interests of the government played a similar role in the later development of the corporation. The English East India Company developed slowly from a rather loose association of merchants, who contributed capital and divided profits one voyage at a time, into a continuous organization.[38] The incorporation was originally driven by the need to create a "body" to which the government could transfer monopolistic trading privileges and governmental authority in order to extract economic surplus that the public administration could not achieve without the help of the merchants.[39] However, the government withheld the right to continuous incorporation as long as it could exploit the renegotiation with the merchants to extract higher profits. Not

[38] For a detailed history see, for example, Davis (1973) and Scott (1910-12), vol 2.
[39] Gower (1969), p. 24.

surprisingly, partnerships and corporations were not clearly distinguished until the end of the 17th century and many of the joint stock companies evolved from partnerships.

Economic historians as well legal scholars have elaborated on the emergence of economic relationships "even without law," given the right set of institutions (Ellickson, 1991; Greif, 1989). Temin (2006) points to the growth-promoting quality of Rome's political institutions, such as granting security to private individuals during the famous *Pax Romana* (27 B.C. - 180 A.D.). The case of the *societas publicanorum* stresses the countervailing force: It is true that the economic growth of Rome during the late Republic and the early Empire indicate the quality and importance of Rome's political institutions. But it is also true that these institutions persisted only as long as and to the extent that they served the interest of the political elite. They were not stable or resistant enough to protect citizens when political interests reversed. This article posits that, more than specific legal rules and developments, political interests drove (or hindered) the emergence of the modern business corporation.

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