

**THE IMPACT OF GOVERNMENT ON ECONOMIC DEVELOPMENT AND GROWTH  
IN PRE-INDUSTRIAL EUROPE\***

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**ABSTRACT:** In pre-industrial Europe, the pace of economic development and growth varied across territories and over time. Much of this variation was due to the changing impact of government on the economies in question. Government affected the economy principally through its command of violence. We therefore begin by exploring the relationship between violence and economic activity and the relationship between government and violence. We then examine in turn the three major channels through which government and its command of violence affected the economy—exaction, peace and order, and association. Lastly, we compare the economic impact of different government regimes. Was weak government or strong government more conducive to economic development and growth?

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### **GOVERNMENT, VIOLENCE, AND ECONOMIC ACTIVITY**

The pace of economic development and growth depends on the nature of the economic environment. Some environments are conducive to economic activity; others are not. We can characterize the economic environment in terms of three conditions—security of possession, freedom of disposal, and freedom of association. Violence affects economic activity through its effect on these three conditions.

#### **Three conditions for economic activity**

Economic activity requires the giving of hostages to time—by requiring the commitment of resources to production and to trading and by requiring reliance on promises of future performance by others. The commitment of resources increases one's vulnerability to the taking of those resources—to predation. Reliance on promises leaves one vulnerable to those promises being broken—to default.<sup>2</sup> The greater the danger of predation and default, the less certain the fruits of economic activity, and consequently the less attractive it becomes. Moreover, even when economic activity does take place it is less productive. One reason is that processes of production and of trading that take a long time are the most vulnerable to predation and default but also often the most

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<sup>1</sup>Authors who have emphasized the importance of understanding the relationship between violence and economic activity include Lane ((Lane 1950), (Lane 1958)); (North 1981); (Olson 1993); (Hirshleifer 2001); and (Greif 2005).

“Economic theorists have traditionally defined their subject so as to exclude analysis of the use of violence. One of the tasks of economic history is to overcome that exclusion.” (Lane 1958) p402

<sup>2</sup>Predation and default are similar in that predation involves the taking of one's actual possessions, while default involves the taking (non-delivery) of that which is owed to one.

productive. Long processes will be avoided in favor of shorter ones that are less productive but less vulnerable. Another reason productivity will be lower is the diversion of resources to defending against predation and default—resources that could otherwise be employed productively. An economic environment relatively free of the threat of predation and default—one in which there is *security of possession*—is one that encourages economic activity and increases productivity.

Economic activity is motivated by the desire to capture the gains from trade. To capture these gains to the fullest possible extent, people must be free to make what use they wish of the resources they command—including their own labor—and they must be free to exchange them with one another as they please. That is, there must be *freedom of disposal*. Any restriction on the freedom to use or to alienate possessions will place some gains from trade out of reach. This will discourage economic activity and make it less productive.

It is often possible to increase the productivity of economic activity by means of joint action. By combining their efforts, individual producers and traders can achieve results that they are unable to achieve when each acts separately. To exploit the potential benefits of joint action, individuals must be free to organize. That is, they must have *freedom of association*. Restrictions on the freedom of association will limit the gains from joint action and will thereby reduce the productivity of economic activity and make it less attractive.

### **Violence and the economic environment**

The effect of violence on these three conditions can be either positive or negative. Violence can be used to sustain security of possession through protection against predation—the provision of *peace*—and through protection against default—the provision of *order*. Or violence can be used to violate security of possession through predation.

Similarly, violence can be employed—through economic intervention—either to uphold freedom of disposal or to restrict it. And violence can be employed either to ensure freedom of association or to deny it. So the exercise of violence can create a favorable economic environment through the provision of peace and order, the removal of harmful restrictions on trade, and the protection of freedom of association. Or it can create an

environment inimical to economic activity through predation, harmful economic intervention, and suppression of association.

### **Violence and government**

The relationship between government and violence grows out of the properties of violence as an activity. First, as with all activities, there are benefits of specialization in the exercise of violence. Second, there are benefits of scale: a larger force can generally overcome or intimidate a smaller one. Third, when violence is applied to predation there is a ‘commons problem’: multiple predators preying on the same territory will tend to take too much, to their mutual disadvantage. This means that predation will be more moderate—and so in the long run more efficient—if the territory ‘belongs’ to a single predator.

These properties of violence as an activity shaped the structure of government in pre-industrial Europe. Specialists in violence tended to have exclusive control over large territories, and large territories tended to be under the exclusive control of specialists in violence.<sup>3</sup> As a result, territorial government, was usually in the hands of a predatory class of kings, princes, and lords. These predatory rulers were specialists in violence and they employed violence to take territory and to hold it. To support themselves and to finance their deployment of violence, they exacted resources from their territories. Predatory governments also used their command of violence to raise revenue through the provision of violence services to the inhabitants of the territories that they controlled. These services included the provision of peace and order as well as economic intervention of various kinds.

There was an alternative response to the benefits of scale in the deployment of violence—joint action. People could come together to protect themselves against predation—not least that of predatory governments. Numbers could sometimes compensate for a lack of specialization. The need for protection was a major motive for joint action and therefore for the formation of various types of association. Some of these, such as villages and cities, were defined territorially and therefore constituted governments. To distinguish it from predatory government, we shall call this type of

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<sup>3</sup>(Lane 1958)

government associational government. Associational governments, too, provided violence services: they maintained order and engaged in economic intervention. To fund the deployment of violence, associational governments—no less than predatory governments—were obliged to raise revenue.

While the motives of predatory and associational government may have differed, there was therefore a great deal of similarity in their functions. Both were engaged in the deployment of violence; both provided violence services; both needed to raise funds to finance these activities.

In addition both types of government suffered, in different ways, from a problem inherent in the deployment of violence—the need to delegate power to others. Rulers of large territories had to delegate power to local agents to act for them, and these agents tended to pursue their own interests rather than those of the rulers. Since violence as an activity is easily divisible, it was relatively easy for these agents to set up in business for themselves. This resulted earlier in the period in feudal fragmentation and later in the period in the development of predatory bureaucracies. In the case of associational government, decision-making and execution of policy required that power be delegated to a leader or leaders. Such leaders too had a tendency to set up in business for themselves by becoming predatory oligarchies or tyrants.

These problems of reliance—both of territorial governments and of associational governments—grew worse with scale. The control of agents and the control of leaders became more difficult as the size of the territory or the size of the association grew larger.<sup>4</sup>

### **Constraints on government violence**

The exercise of violence by rulers was constrained by law and custom. Subjects possessed certain rights that in some cases restricted the ruler's ability to act and in others required his action. Conversely rulers possessed certain prerogatives that allowed them greater discretion in the exercise of their powers or obliged action on the part of their subjects. Subjects' rights abridged rulers' prerogatives and vice versa.

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<sup>4</sup>For more on the problem of delegation and its consequences, see (Kohn forthcoming) Ch. 21.

Rulers' prerogatives and subjects' rights were generally economic rather than political.<sup>5</sup> For example, a ruler's prerogatives pertained principally to the kinds of exaction permitted to him and to the economic activities, such as minting and mining, that were subject to his control. Similarly, subjects' rights or 'freedoms' pertained largely to limitations on the ruler's exaction or to economic privileges of various kinds that the ruler was obliged to enforce.

Subjects' rights were not general rights of all subjects but particular rights of a specific individual, group or association. For example, the nobility or the clergy might be exempt from taxation. Or a particular city might have a monopoly—enforced by the ruler—on the trade in a certain commodity. Indeed, the winning and defending of such rights and freedoms was another major reason for joint action and for the formation of various kinds of association.

Why would rulers, with a command of violence, respect the constraints of law and custom? First of all, they themselves had an interest in legality and legitimacy, since their own dynastic claims to territory were generally framed in legalistic terms.<sup>6</sup> Moreover, their subjects' and their fellow rulers' recognition of the legitimacy of their rule reduced the need for the actual exercise of violence and so its associated expense. But a more compelling reason to respect the constraints was the balance of power between rulers and subjects. The existing technology of violence simply did not allow rulers to impose their will over the resistance of their subjects. Within a ruler's territory great nobles and cities commanded military forces that rivaled his own. Outside, the threat from rival rulers left him dependent on the military and financial support of these same nobles and cities. Rulers were also dependent on the active cooperation of their

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<sup>5</sup>“Pre-modern societies did not define liberty in nineteenth century liberal terms as equality before the law and as freedom of conscience and of action from state encroachment, but in terms of status and inequality of ‘privileges, immunities, or rights enjoyed by prescription or grant’. Pre-modern economic freedom was consequently not an abstract condition of ‘equality in law and market’, but a claim to legal privilege and to the income streams which privilege conferred. For this reason, pre-modern societies spoke of *freedoms* in the plural rather than of *freedom* in the singular and the abstract... [Pre-modern ‘freedoms’] were socially specific, temporally contingent and frequently legally transferable sources of privilege and exclusion.” (Epstein 2000) p15

<sup>6</sup>“The Renaissance monarchs were strongly motivated by dynastic considerations. They fought wars to make good dynastic claims, not to achieve nationalistic objectives. Their domains increased primarily when fiefs escheated to the crown. Marriage alliances were of the utmost importance, and legality was stressed, because territorial claims and inheritances depended on the law.” (Greif 2005) p368

subjects in administering their territories—not least in the collection of taxes. Again, the existing technology of administration did not allow them to accomplish these tasks in the absence of such cooperation.<sup>7</sup>

The constraints of law and custom were supported by an institutional structure consisting of representative assemblies and courts. The former provided a forum for consultation and negotiation to clarify rights and prerogatives and to allow for their alteration as circumstances changed. The latter provided a venue of adjudication for the many occasions in which the parties believed that their agreed rights or prerogatives had been violated. The existence of these institutions served the interests of both rulers and subjects.

The effectiveness of the constraints varied from territory to territory and over time, depending mainly on the relative bargaining power of the two sides. This was partly a matter of wealth and military strength. But it was also a matter of circumstances. A ruler's need for financial support generally made him more attentive to the concerns of his subjects. Likewise, subjects' need for the ruler's protection generally made them more willing to expand his prerogatives. In any event, there was a constant struggle between subjects and rulers over the boundaries of their respective rights and prerogatives. There was simultaneously a struggle among the subjects themselves, since the rights of one group often came at the expense of the rights of others.

In principle, there was no need for constraints on the exercise of violence by associational government, since associational government was created to serve the needs of the members of the association. However, as we have noted, there was a danger that the leaders of associational government would turn themselves into predatory rulers. To prevent this, associational governments too had laws and customs that constrained the powers of their leaders. They also had institutions, such as city assemblies and councils, to enforce those constraints. As in the case of predatory government, the effectiveness of the constraints ultimately depended on a balance of power. Abuses by city leaders could lead to revolt by the populace or to their migration to other cities. They could also lead to outside intervention—by the territorial ruler, for example, if the city was subject to such a

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<sup>7</sup>See (*Kohn forthcoming*) Ch. 21 for a thorough discussion.

ruler. Sometimes, as in Venice, the constraints were effective; sometimes, as in Milan and Florence, they were not.

We shall examine the impact of government violence on the economy under three headings—exaction, peace and order, and association. Government exaction was the greatest threat to the security of possession and to the freedom of disposal. As we shall see, exaction took various forms that affected the economy in different ways. Some of these were particularly harmful. Governments could also contribute positively to security of possession by providing peace and order. However, as we shall see, they were not the only providers nor necessarily the best. Governments had a mixed relationship with associations. Sometimes they saw them as useful instruments of delegated administration. Sometimes they saw them as a threat: indeed, one important form of joint action was revolt. So governments variously encouraged, co-opted, or suppressed associations. Since associations also fulfilled important economic functions, these differing policies towards associations had important economic implications.

Our focus here is on the impact of government on the economy through its exercise of violence. Governments did affect the economy in other ways too—particularly through the provision of infrastructure and public services. They created transportation infrastructure (roads, bridges, river improvements and canals); market infrastructure (organized markets and coinage); and utilities (water supply, public baths and latrines, churches and cathedrals). Public services included education and welfare. However, the provision of infrastructure and public services was generally a function of local associational government. We therefore neglect these other activities of government here because it is primarily the effect of territorial government on the economy that concerns us. Moreover, it was government exercise of violence rather than these other functions that were decisive in determining whether an economy thrived or not.<sup>8</sup>

## **EXACTION**

Government exaction involved the redistribution of resources by force or by the threat of force from a target population to the government in question. The deployment of

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<sup>8</sup>On transportation infrastructure, see (Kohn forthcoming) Ch. 5. On market infrastructure, see (Kohn forthcoming) Ch. 17. On services, see (Kohn forthcoming) Ch. 21.

violence by governments made exaction possible, but it also made it necessary. Pre-industrial Europe was the scene of frequent and widespread warfare—wars between predatory rulers over territory, civil wars over succession, wars to suppress rebellions, wars between independent cities over trade, private wars between nobles to settle disputes. Indeed, the overwhelming majority of government expenditure in the period was on war. Predatory rulers also relied on exaction to support themselves—preferably in a style sufficient to impress their rivals with their wealth and so with their potential military power. Associational governments also needed to finance their provision of infrastructure and services. So both predatory and associational governments were under constant pressure to exact resources from the territories under their control.

It must be emphasized that it was not only the predatory governments of kings and princes that engaged in exaction. Territorial government was fragmented in a feudal hierarchy of lords and vassals. At the top, the king or prince directly controlled a portion of his territory—his domain—but controlled the rest only indirectly through the agency of his vassals. These in turn possessed domains and vassals of their own. Each lord was the government within his domain and within it possessed prerogatives of exaction. ‘Lord’ in this context means not only feudal nobles but also bishops, religious houses, and in some cases cities. So while the following discussion of the impact of exaction is couched largely in terms of the effects of royal or princely exaction it applies in equal measure to exaction by local lords and by associations. Not infrequently, populations were subject to exaction from several of these authorities simultaneously.

The first thing to note about exaction was that the losses to the victims of exaction greatly exceeded the ultimate gains to the governments responsible for it. ‘Transactions costs’ ate up a good part of the gross take: net resources reaching the government were much less than the resources taken from the target population. In particular, the administrative structure charged with executing exaction was costly, and it generally pocketed a significant part of the proceeds. Then, beyond the direct loss to the victims, there was considerable ‘collateral damage’ to the economy through the adverse effect of exaction on incentives. Exaction discouraged productive activity and caused resources to be diverted to protection, avoidance, and evasion. There were factors that either exacerbated or mitigated the harm done. A greater urgency on the part of government—

mostly due to the pressure of war—resulted in its resorting to more harmful forms of exaction. On the other hand, when governments were able to borrow, they could spread the burden of exaction over time, reducing the overall damage to the economy.

Was the harm of exaction offset by any compensating benefit from government expenditure? As we have seen, the expenditure of predatory governments—both of territorial rulers and of lords—was primarily on war. Such wars were redistributive: their purpose was to take territory from one ruler or lord to the benefit of another. Since the whole exercise was generally accompanied by considerable destruction, the economic effect was strongly negative. The wars of associational governments, of cities in particular, were sometimes economically motivated—to conquer territory for colonization or to capture markets from a commercial rival. In some cases, these wars did pay off for the victorious city. However, the result was again generally redistribution from one city to another rather than an overall increase in output or welfare. Apart from their expenditure on war, the expenditure of predatory governments on consumption brought little economic benefit. The expenditure of associational governments on infrastructure and public services did enhance economic productivity to some extent.

### **Forms of exaction**

Exaction took a variety of forms. It is useful to divide them into four main categories—the arbitrary seizure of goods, taxes, economic intervention, and exploitation of the coinage.

The feudal prerogatives of rulers and lords permitted them various forms of arbitrary seizure.<sup>9</sup> Goods brought to market under their control were subject to the *droit de prise*—their right to first purchase at a price set by them.<sup>10</sup> They also enjoyed a right of hospitality—*droit de gîte*—that obliged their subjects to feed and house them (usually together with a large entourage) as long as they chose to stay. Of course, only wealthy subjects were so honored. They also had the right to the property of a foreigner who died while in their territory (*aubain*) and to any goods washing up on shore after a shipwreck (salvage).<sup>11</sup> In addition to these legitimate forms of seizure, rulers and lords engaged in

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<sup>9</sup>(Wolfe 1972) Ch. 1; (Ormrod and Barta 1995)

<sup>10</sup>For details, see (Kohn forthcoming) Ch. 17.

<sup>11</sup>(Favier 1998) Ch. 4

other forms that were of doubtful legitimacy or even clearly illegitimate, such as banditry against merchants traveling through their territory and piracy against ships at sea<sup>12</sup>

In times of war, the scope of arbitrary seizure expanded significantly. It was the main way to supply armies on the march: armies took what they needed—or wanted—from the territory through which they passed.<sup>13</sup> If the territory was friendly this constituted ‘requisition’, which meant that the victims were, in principle, to be compensated later for the goods taken. In practice, however, compensation was at best partial.<sup>14</sup> Troops were billeted with the population of towns and villages along the way: this ‘hospitality’ to the king’s army was considered an extension of the *droit de gîte*. Sometimes troops wintered in this fashion in a given region for months at a time. Agents of the government charged with supplying armies and navies often did so by purveyance—by taking what they wished from the population against promises of future compensation. They took not only food but also means of transportation—carts, wagons, and draft animals. If the army was passing through enemy territory, then the seizure of property of all kinds constituted plunder—a legitimate perquisite of conquering armies—and no compensation was even contemplated. For most of the period, there were no standing navies, so the requisition of trading vessels was the only way to create a fleet when one was needed.<sup>15</sup> In times of war, there was a tremendous increase in piracy, now legitimized as ‘privateering’. Banditry too became legitimate: merchants unlucky enough to find themselves in enemy territory when war broke out had their goods taken and sometimes their persons held for ransom.<sup>16</sup>

Rulers also indulged periodically in the expropriation of individuals or groups. Sometimes this was legitimate. For example, when a vassal died without an heir, his lands reverted to the ruler (*escheat*).<sup>17</sup> Sometimes, the expropriation of a wealthy individual or group was legitimized by charges of treason, as in the case of Jacques Coeur in France. And sometimes, in the case of foreigners or Jews who had no real rights and

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<sup>12</sup>See (Kohn forthcoming) Ch. 5 for details.

<sup>13</sup>(Tilly 1990)

<sup>14</sup>(Kaeuper 1988) Ch. 1

<sup>15</sup>(Miller 1971) Only towards the end of the period were warships beginning to be differentiated from trading vessels: see (Kohn forthcoming) Ch. 5.

<sup>16</sup>(Moore 1985)

<sup>17</sup>(Wolfe 1972) Ch. 1

were therefore dependent on the favor of the ruler, no legitimization was thought necessary. In general, accumulations of wealth always presented a tempting target to rulers perennially pressed for funds.<sup>18</sup>

In contrast with the arbitrary seizures of goods, taxes were regular payments, in kind or in cash, demanded by governments. While arbitrary seizure involved the taking of resources by force, taxes involved the taking of resources under the threat of force and usually in a more orderly fashion.<sup>19</sup> Early in the period taxes were mainly in kind—quantities of grain, days of labor, or periods of military service. Later, with increasing monetization of the economy, existing taxes in kind were commuted to cash payments and new taxes were levied in money. Governments levied taxes wherever they could, but they were limited to taxing what they could see or find. So taxes tended to fall into two broad categories—direct taxes on property and indirect taxes on trade. In rural areas, direct taxes were, in one way or another, mostly taxes on land; in the cities—especially in the independent cities of northern Italy—they were taxes on commercial wealth and movable property. Taxes on trade were collected wherever it was possible—essentially wherever there was a choke-point through which trade had to pass. This included tolls on transportation collected at bridges, fords, rivers, mountain passes, and harbors, and taxes on markets collected at city gates or in public markets.<sup>20</sup>

Economic intervention by governments mostly took the form of constraints—backed by force—that were imposed on trading and production.<sup>21</sup> Those who found their freedom of disposal so constrained were thereby harmed—usually by a worsening in the terms under which they could trade (but sometimes by the complete loss of potentially beneficial opportunities for trade). For example, requiring peasants in a city's *contado* to sell their grain only in the city itself reduced the potential market for their produce and so the price they could obtain for it. The harm or loss to those whose trading or production was constrained usually had its counterpart in benefits to someone else—in this case, to

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<sup>18</sup>(Reynolds 1952). See (Kohn forthcoming) Ch. 20 for more on the 'economics of expropriation',

<sup>19</sup>"A tax may be... defined as a payment demanded by a political leader in exchange for freedom from a sanction controlled by that leader." (Frohlich and Oppenheimer 1974) p44

<sup>20</sup>See (Kohn forthcoming) Ch. 17 for more on taxes on markets and (Kohn forthcoming) Ch. 5 on tolls collected on transportation.

<sup>21</sup>There was also some direct economic activity on the part of governments such as the trade fleets of Venice and Spain and the luxury manufactures of France. See (Kohn forthcoming) Ch. 22 for more details.

the citizens of the city in question. So economic intervention, like arbitrary seizure and taxes, was a method of redistributing resources by force.<sup>22</sup>

Economic intervention could be turned into an instrument of exaction in either of two ways. First, the government could itself be the direct beneficiary of the intervention in question. An important example was manorial agriculture. The manorial lord—the government in this case—restricted by force the freedom of disposal of his villeins' land, labor, and produce, so distorting the terms of his transactions with them in his own favor.<sup>23</sup> Second, when others rather than the government benefited from the economic intervention in question, the government could collect payment from the beneficiaries either voluntarily or in the form of a tax. For example, when the government of England restricted the export of wool, it was able both to increase the tax on this export and to sell the trading monopoly to a particular group of merchants—the Merchants of the Staple. Alternatively, of course, governments could collect payment from those harmed by an intervention in order to suspend it.

Governments intervened in their economies for a variety of reasons—many of them unrelated to exaction.<sup>24</sup> However, the potential for exaction was always there. And as the period progressed governments became more aware of this potential and increasingly intervened with exaction primarily in mind. The seeking out of new interventions purely for the purpose of exaction was the most distinctive characteristic of the syndrome of economic policies that came to be known as Mercantilism.

A set of economic interventions of particular importance derived from the ruler's *jus moneta*—his right to control the coinage. These interventions included a monopoly of the minting of coin and rights over the mining of precious metals. The monopoly of minting provided the ruler with monopoly profits from the production of coin (seigniorage) and also provided him with the opportunity to manipulate the currency to his own advantage.<sup>25</sup> For example, if he owed debts denominated in units of currency, he could reduce the burden of those debts by reducing the amount of bullion that each unit of

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<sup>22</sup>(Lane 1958)

<sup>23</sup>“As always, the level of rent was partly dependent upon the degree of non-economic compulsion which landowners could apply.” (Hilton 1978) p14

<sup>24</sup>See (Kohn forthcoming) Ch. 22.

<sup>25</sup>See (Kohn forthcoming) Ch. 7 for details.

currency contained (debasement). Rulers' rights over the mining of bullion—which some attempted to extend to mining in general—allowed them to purchase mine output at submarket prices (preemption), to tax mining, and to sell mining monopolies.<sup>26</sup>

### **The direct burden of exaction**

Exaction involved a forcible transfer of resources from populations to their governments. How large was this transfer? We must divide this question into two parts—what did governments gain and what did populations lose? The answers to the two questions differ, because populations lost much more than governments gained.

One possible measure of what governments gained from exaction is their net revenue from taxes, monopoly profits, and other sources. Only a few estimates are available for the period. Government revenue in Castile, considered to be one of the most heavily taxed territories in Europe in the sixteenth century, has been estimated at some five per cent of total income at the start of the century and perhaps ten per cent by century's end.<sup>27</sup> In contrast, government revenue in England, considered to be among the most lightly taxed, was perhaps only two per cent of national income at the end of the sixteenth century.<sup>28</sup> The net revenue of most territorial rulers in our period probably lay somewhere in this range of two to ten per cent. For reasons that we shall see, associational governments were able to take a significantly larger part of income than predatory governments, especially in times of war. For example, during its war with Milan in the early fifteenth century, Florence was collecting in direct taxes alone some 13% to 16% of income plus an additional 18% in forced loans.<sup>29</sup>

Government net revenue, however, understates the gain from exaction, because it omits that part that did not accrue in the form of cash. It omits the gain from arbitrary seizure—for example, the value of purveyance and billeting in excess of the compensation paid. It omits the gains from manipulation of the currency—for example, the reduction in the real value of debt repayment as a result of paying it in debased coin.

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<sup>26</sup>(Glamann 1977), (Nef 1987)

<sup>27</sup>(Thompson 1998)

<sup>28</sup>(Rodger 1998)

<sup>29</sup>(Veseth 1990). The Dutch Republic also had relatively high levels of taxation: see (de Vries and van der Woude 1997) Ch. 2.

And it omits part of the gain from economic intervention—for example, when this came in the form of lower prices paid by the government for its purchases.

The loss from exaction substantially exceeded governments' gain for two reasons. First, central governments were not alone in exacting resources. For rural populations and for subject cities, the exactions of the ruler were merely added to those already imposed by their local lords, by the Church, and by the cities themselves.<sup>30</sup> Second, even if we restrict our attention to exaction by the central government the loss to the population exceeded the government's net revenue by a significant margin due to 'collection costs'.

Some of the collection costs were incurred by the government. Exaction required the employment of an apparatus of administration to execute it. The cost of this apparatus had to be subtracted from the gross take to obtain the net take of the central government. The cost of administration could take the form of explicit payment to the agents involved. Or it could take the form of the agents' keeping a part of what they collected for themselves—either legitimately in the case of tax farmers or illegitimately when government agents engaged in corruption and peculation.<sup>31</sup> For example, reformers in sixteenth century Spain asserted that no more than a third of the revenue that was collected actually reached the treasury.<sup>32</sup>

Another part of collection costs was incurred by the population subject to exaction. For example, the payment of tolls often involved long and uncertain delays, and sometimes damage, as goods were unloaded and unpacked for inspection and merchants had to wait in line for the privilege.<sup>33</sup> When officials in sixteenth century Spain requisitioned supplies for the military, representatives of towns and villages had to travel two or three times to the regional center to negotiate compensation and then again to receive payment: the expense of these trips often exceeded the value of the requisition.<sup>34</sup>

Populations incurred considerable costs too in evading exaction. For example, merchants sometimes hauled their goods overland at great expense to avoid the many

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<sup>30</sup>“Thus, without being relieved of the demands of the lords close at hand, the peasants had also to support other, more distant, but none the less burdensome fiscal powers” (Duby 1968) p245

<sup>31</sup>“Any attempt to produce a quantitative estimate of the size of governmental demands on population is bound to be wrecked on this unknowable but formidable structure of wrongdoing.” (Fryde 1979) p830

<sup>32</sup>(Thompson 1994)

<sup>33</sup>(Wolfe 1972) p347

<sup>34</sup>(Thompson 1976) Ch. 8

tolls along the waterways.<sup>35</sup> Governments incurred additional costs, of course, in trying to prevent evasion.

In all, between the evasion, fraud, and non-payment of the population and the peculation of government officials, no more than a fraction of the potential revenue of a given tax actually reached the central government. Contemporaries quoted numbers such as a fifth or a third.<sup>36</sup> Some taxes were easier to collect and provided a higher yield—for example, England’s export tax on wool; others were more problematic, such as France’s general sales tax (*aides*).<sup>37</sup>

Mostly, exaction only required the threat of violence. However, sometimes actual violence proved necessary. Peasants might refuse to pay their taxes or they might hide their grain or animals from tax collectors or purveyors. The latter would then be obliged to employ force. This was costly and dangerous both for the collectors and for their victims, and often resulted in property damage and physical injury to both sides. Sometimes resistance to exaction would escalate into tax rebellion or even war, at great cost to all involved. Peasant uprisings were frequent, and they were largely motivated by resistance to exaction. Similarly, unrest in the cities was often motivated by overly onerous taxation. The most expensive war of the period—the Dutch revolt against Spain—was essentially a tax revolt on a grand scale. Economic intervention, too, sometimes required the actual application of violence for its enforcement. For example, the trading monopoly of Spain in the Americas required a fleet of ships to keep out foreign interlopers. The interlopers responded by arming themselves, defending themselves against the Spanish ships and, in addition to their illicit trading, raiding coastal settlements.

So the overall burden of exaction was probably high. While a quantitative assessment is impossible, the indirect evidence suggests that the burden often became intolerable. Peasants starved or were driven to abandon their land and flee. Peasants and townsmen alike were frequently driven to open rebellion. The burden was not however uniformly high: it did fluctuate over time and differ from place to place. For example, taxes were

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<sup>35</sup>See (Kohn forthcoming) Ch. 5.

<sup>36</sup>(Thompson 1998)

<sup>37</sup>(Levi 1988) Ch 5; (Wolfe 1972) Ch 1.

often fixed in money terms, so that rising prices eroded the real burden. This happened throughout Europe during the general inflation of the sixteenth century. In Castile in particular the real burden of taxes declined significantly in the middle third of the century as prices there rose relatively rapidly.<sup>38</sup> Similarly, in England the inflation brought about by Henry VIII's 'Great Debasement' was a major cause of Elizabeth's low level of net revenue later in the century.<sup>39</sup>

### **The impact on economic activity**

In addition to the direct effect of exaction—the direct losses it imposed on the population—it also had an indirect effect through its impact on economic incentives. By reducing the rewards of production and trading it made these activities less attractive and so depressed economic activity. Moreover, since exaction fell unevenly on different types of economic activity, it caused shifts from one to another and changed the mix of goods produced and traded.

Exaction was sometimes so severe as to halt production altogether. This was especially true in agriculture, where many producers lived close to the margin of subsistence and possessed little in the way of reserves. Excessively high taxes and rents left peasants destitute and caused them to cease production and to abandon the land. For example, high levels of exaction by the Spanish Hapsburgs laid waste to agriculture both in Castile and in Italy, with extensive areas being abandoned.<sup>40</sup> In the vicinity of Cremona, "except where land was turned over to a church exempt from taxation, a thriving countryside was transformed to a great extent into a deserted waste."<sup>41</sup> The effect was greatest on land that was marginal, because taxes were adjusted poorly or not at all to account for differences in the productivity of the soil.<sup>42</sup>

In manufacturing, high levels of exaction could raise the costs of producers in a particular place to the point that these producers were no longer competitive with producers elsewhere who were not so burdened. For example, in Cremona again "a

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<sup>38</sup>(Tracy 2002)

<sup>39</sup>(Palliser 1983) Ch. 5; (Schofield 2004)

<sup>40</sup>(Braudel 1972). In Castile, by the end of the century the total burden of dues, taxes and rents absorbed half the peasant's harvest ((Anes 1994)); about a third of the land previously cultivated was abandoned.

<sup>41</sup>(Laven 1966) p40

<sup>42</sup>(Anes 1994); (Vicens Vives 1969)

resilient industry was sucked dry as its artisans left for kindlier circumstances.”<sup>43</sup> In mining, regalian rights were a strong disincentive to exploration and exploitation, especially for less valuable minerals. The 1568 decision of the Court of the Exchequer that rights to the mining of base metals belonged to the landowner and not to the Crown was a major factor in the subsequent expansion of mining in England.<sup>44</sup>

The impact of exaction on production was amplified by poor design. Indirect taxes, for example, were generally levied on gross output or on total value rather than on net output or on value added. For example, tithes collected by the Church took one tenth of gross output. Taxes on gross output particularly penalized—and so discouraged—those forms of production that required expensive inputs, either in the form of raw materials or in the form of fixed capital. In agriculture, for example, horticulture and animal husbandry were penalized relative to arable farming.<sup>45</sup> Manufacturing was very vulnerable to such misconceived taxes because raw materials were typically expensive relative to labor. For example, in the manufacture of fine cloth, fiber and dyes might account for 80% or more of the total cost. So, with value added of only 20%, a tax of ten per cent on total value could wipe out any profit.

Apart from the effect of exaction in halting or reducing production, differences in levels of exaction on different activities could cause producers to switch from one to another. The most striking example was the English export tax on wool. The tax was first imposed in 1275 at the modest rate of 6s. 8d. per sack (of 364lb) or about 7% of value.<sup>46</sup> In 1336, on the eve of the Hundred Years War, another 20s. was added to the tax, and it was increased several more times during the fourteenth century, rising by the 1390s to about 100% of value. The demand for English wool was increasing at this time as Flemish and Italian manufacturers were switching to high-quality woolens in response to the wartime interruption of trade.<sup>47</sup> Nonetheless, because of the rising burden of tax, shipments of wool peaked at 32,000 sacks in the 1350s and declined to 19,000 by the 1390s. However, while the tax on raw wool was becoming prohibitive, that on cloth

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<sup>43</sup>(Laven 1966) p40

<sup>44</sup>(Palliser 1983) Ch. 8

<sup>45</sup>“...the tithe tends to bring about the abandonment of types of farming that require large expenditures of capital or other factors.” (Ardant 1975) p183

<sup>46</sup>(Munro 1998)

<sup>47</sup>See (Kohn forthcoming) Ch. 4.

made from wool remained low— about 2% to 3% of value. In the face of these incentives, exports of English cloth rose from 5,000 cloths to 37,000 cloths over the same period (each cloth contained about a quarter sack of wool).<sup>48</sup> English merchants initially exported finished cloth, but gradually learned that they could do better by selling it unfinished in the Low Countries—previously the principal market for English wool—where it was finished locally.<sup>49</sup>

Exaction could also distort decisions on the direction of effort. For example, in some places, notably France and Spain, nobles were exempt from many forms of tax. However, noble rank—and so the exemption from tax—could be lost as a result of engaging in activities unbecoming to a noble, such as trade and manufacturing. This was a powerful disincentive to economically productive enterprise on the part of nobles and channeled their energies instead into violence and government administration.<sup>50</sup>

Exaction made trade less profitable and so reduced its extent. As we have seen, trade was particularly exposed to exaction. There were tolls and market taxes everywhere.<sup>51</sup> Brigands and pirates, official and unofficial, preyed on merchants on land and at sea. The resulting reduction or even interruption of trade was particularly harmful, because it was trade that was ultimately responsible for raising productivity. By providing producers with access to wider and to larger markets and by exposing them to competition, trade encouraged the reorganization of production to achieve greater efficiency and promoted specialization in the most productive activities.<sup>52</sup> Consequently, while trade provided governments with an easy target for exaction, this form of exaction was particularly costly in terms of the harm it did to the economy.

Local taxes on transactions had much the same adverse effect. The Spanish *alcabala* of was a particularly egregious example. It was a 10% *ad valorem* tax levied on every sale of goods or property, including sales of intermediate products.<sup>53</sup> Since increasing

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<sup>48</sup>After further increases in the tax in the fifteenth century, by the end of the reign of Henry VII England was exporting 5,000 sacks of wool and 82,000 cloths (8% and 92% respectively of the combined value). (Ramsey 1963)

<sup>49</sup>(Postan 1987)

<sup>50</sup>(Nef 1940) Ch. 5; (Vicens Vives 1969) Ch. 20

<sup>51</sup>See (Kohn forthcoming) Ch.s 5 and 17.

<sup>52</sup>See (Kohn forthcoming) Ch.s 3 and 4.

<sup>53</sup>(Ruiz 2001);

productivity in manufacturing required ‘vertical disintegration’, with each producer specializing in a single stage of production and adding only a small percentage of value, the tax was particularly harmful to productivity.<sup>54</sup>

Governments intervened in their economies to promote ‘legibility’—to ensure that taxes could be collected. For this reason, they often required that all trading be conducted in organized markets where it could be observed. For forms of trading that would otherwise have taken place elsewhere, this raised the cost of trading.<sup>55</sup> Conversely, for forms of trading that were suited to organized markets, the presence of the tax collector encouraged off-market trading which again raised trading costs.

Governments also intervened to establish monopolies: this both generated monopoly profits that could be taxed and also made it easier for the government to collect taxes. For example, exports of English wool were required to pass through the staple of Calais and the right to export wool was sold to an association of merchants—the Merchants of the Staple. The merchants enjoyed monopoly profits, mainly at the expense of growers, and also became tax collectors for the crown. In some cases, the creation of monopolies harmed productivity. For example, urban craft guilds generally failed when they tried to monopolize their crafts: it was too easy for non-members to compete from outside the city limits. However, once the government began to regulate and to tax guilds—as it did in France—it enforced their monopolies and suppressed any such competition. Protected from competition, the guilds were able to restrict labor mobility and to resist technological change with impunity.

Exaction also harmed productivity by reducing productive investment. One way it did so was through the redistribution of resources. The burden of exaction left agricultural producers, who otherwise would have invested in production, without the means to do so. The beneficiaries of this exaction—local lords and territorial rulers—dissipated the proceeds on war and conspicuous consumption.<sup>56</sup> Direct taxes on property also depressed

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<sup>54</sup>(Miskimin 1977)Ch. 4. The destructiveness of the *alcabala* was noted by Adam Smith ((Smith 1976 [1776]) p431)

<sup>55</sup>See (Kohn forthcoming) Ch. 17.

<sup>56</sup>“...per capita productivity of agriculture was stationary or falling in the late thirteenth century...[partly as a] result of the pressure of landowners for rent, jurisdictional fines, death duties and entry fines, and of the state of taxation and purveyance—pressures which had been growing during the thirteenth century, which removed all cash surpluses and prevented even the most elementary investment.

investment, because visible investment demonstrated one's wealth to the assessor and invited an increased tax burden.<sup>57</sup> In Renaissance Florence, personal dwellings and their furnishings were exempt from property tax, while productive capital was not. This stimulates the construction of palaces and patronage of the arts.<sup>58</sup> In sixteenth century Venice, high indirect taxes reduced the profitability of commerce and manufacturing while direct taxes on land and financial assets were relatively low. This encouraged the wealthy to shift their assets out of commerce and manufacturing and into land and financial assets.<sup>59</sup>

Exaction not only prevented or discouraged the accumulation of capital, it sometimes depleted capital directly. For example, livestock was particularly difficult to hide from plundering soldiers and from government purveyors. In one documented case in 1332, the sheriff of Nottingham purveyed twenty-four oxen, taking the plough teams of four families. The affected families were consequently unable to sow their winter crop and were forced to sell their land to pay their debts.<sup>60</sup>

Exaction typically fell more heavily on the less well-to-do and this had the effect of reducing their demand for manufactured non-food items such as clothing and household utensils.<sup>61</sup> However, it was precisely the expanding production of such mass-produced cheap goods that was the key to raising productivity. With these goods, the emphasis on price competition and the lesser importance of quality stimulated cost-reducing technological progress—especially mechanization.<sup>62</sup> In late sixteenth century England, the declining level of exaction impoverished those who benefited from it—the royal family, the clergy, and the old landed classes—to the benefit of the population as a

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Not that the landowners gave much of a lead in the improvement of demesne agriculture. In spite of some interest in rational estate management the diversion of aristocratic income into war and largess resulted in a low level of investment of profit in the estate with, as a consequence, low or stationary yields." (Hilton 1978)p11 (ital in original)

See also (Kaeuper 1988) Ch. 1

<sup>57</sup>(Ardant 1975)

<sup>58</sup>(Veseth 1990)

<sup>59</sup>(Knapton 1988)

<sup>60</sup>(Kaeuper 1988) Ch. 1

<sup>61</sup>(Elliott 1989) Ch. 10 offers this as one reason for the retardation of industrial development in late sixteenth century Castile.

<sup>62</sup>See (Kohn forthcoming) Ch. 4.

whole. The growing demand for inexpensive goods on the part of the latter was a major stimulus to industrial expansion and development.<sup>63</sup>

The adverse impact of exaction was amplified by uncertainty.<sup>64</sup> A known and predictable charge could be included in calculations. If it was not too high, production and trading remained profitable and proceeded nonetheless—if at a reduced level. However, unpredictable and possibly confiscatory exaction made any such calculation impossible and so strongly discourage any economic activity. Better not to expose oneself to such risks. For example: “Giles Hoffmann, a Fleming bringing masts and sailcloth from the Baltic, had masts worth 150 ducats seized at Cadiz. He was offered 30 ducats compensation, which was not paid; so he stopped coming to Cadiz...”<sup>65</sup>

Arbitrary seizure was by its nature random, often hitting poorer areas and sparing more prosperous ones: “[An official] simply descended on a village and took what he wanted, often quite arbitrarily, without payment (or at best with payment deferred through the giving of tallies), and in a way which bore little relation to the owner’s ability to sustain the prise.”<sup>66</sup>

But taxes too were often unpredictable—especially direct taxes. These were generally one-time levies rather than regular payments and they were imposed *ad hoc* whenever needed.<sup>67</sup> “The arrival of the collectors heralded a catastrophe, a scourge whose surprise and whose incidence could be likened to a climatic calamity or an epidemic.”<sup>68</sup>

Of all the different forms of exaction debasement was probably the most harmful to the economy—the one that did the most collateral damage for a given benefit to the government.<sup>69</sup> For most of the period, the value of money changed only imperceptibly and all forms of contract were therefore written in terms of nominal sums of money. When governments engaged in debasements (and the associated strengthenings), market-determined prices adjusted relatively rapidly to the change in the value of the coinage. As

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<sup>63</sup>(Nef 1940) Ch. 5

<sup>64</sup>(Hoffman 1996)

<sup>65</sup>(Thompson 1976) p212

<sup>66</sup>(Kaeuper 1988) p111. On purveyance in Castile and its effects see (Thompson 1976) Ch. 8.

<sup>67</sup>See (Veseth 1990) on the unpredictability of the Florentine *estimo*. Even where, as in France, the *taille* became a permanent tax, its amount fluctuated widely from year to year according to the needs of the government ((Wolfe 1972) Ch. 1).

<sup>68</sup>(Duby 1968) p246

<sup>69</sup>See (Kohn forthcoming) Ch. 7.

a result, the terms of existing contracts were drastically altered. With a debasement, tenants, employers, and debtors saw their obligations reduced, sometimes drastically; conversely, landlords, employees, and creditors saw their incomes and assets devalued. The disruption to the economy was enormous. Renegotiation of contracts was next to impossible, so impoverished landlords and employees responded instead with violence. Uncertainty about the value of money dried up credit, the lubricant of trade. Even the government itself was a victim of its own actions. Since many forms of government revenue were fixed in money terms, debasement eroded their value.

The English Great Debasement of the sixteenth century provides a case study in the sorts of disruption that manipulation of the currency could cause.<sup>70</sup> Debasement caused a depreciation of the English pound, making English goods cheaper abroad. This provided a strong stimulus to the export of woolen cloth and caused a significant expansion in its production. The sharply increased demand for wool had a major impact on agriculture—causing the conversion of arable land to pasture (which gave a boost to enclosures and created local shortages of grain). As we have seen, government revenue from land and taxes was greatly reduced. Later, with Elizabeth’s reform of the currency, much of this was reversed. The currency appreciated, exports of woolens and their production slumped—creating unemployment—and land shifted back to arable. Some merchants moved their capital into privateering. Government policies in response to the disruption—exchange controls, price controls, and protectionism—only made matters worse.

### **The structure of administration**

Exaction required the efforts of many people to carry it out—to seize the goods, to collect the taxes, to mint the coins, and to enforce interventions in the economy. With the exception of the minting of coin, which was concentrated in a few government mints, these functions were performed by local officials. As we noted earlier, such a delegation of power was problematic. The technologies of information and communication then available simply did not permit effective monitoring and control. This left officials free to

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<sup>70</sup>(Fisher 1940)

use their power to their own benefit. In particular, they appropriated part of the proceeds of exaction.

Often, officials simply pocketed a part of what they took.<sup>71</sup> Since governments rarely knew how much to expect from a given tax, such speculation was hard to detect. Similarly, tax-payers did not know what was due from them, so it was easy to charge them extra and pocket the difference: the more complicated the tax system the easier this was to do.<sup>72</sup> When officials collected taxes in cash they kept the good coins and passed on the poor quality ones (this practice was known as *billonage*).<sup>73</sup> Officials sometimes colluded with tax-payers—accepting bribes to assess a smaller tax.<sup>74</sup> Officials delayed in sending the money they collected to the central government, using it in the meantime to finance their private business transactions.<sup>75</sup> Arbitrary seizures were even more open to abuse than the collection of taxes. Purveyors routinely took more than required and sold the excess for their own gain; indeed, they sometimes sold what they had taken back to the original owners.<sup>76</sup> Purveyors accepted bribes from communities ‘so that they would take no more’ and instead go elsewhere. The proceeds from economic intervention were similarly subject to appropriation: the officials responsible for enforcement accepted bribes to look the other way. Officials not only accepted bribes for not performing their duties, they also accepted ‘gifts’ from those who benefited from their performing them.<sup>77</sup> Last but certainly not least, officials reduced the government’s yield from exaction through their negligence and incompetence in performing their duties—that is, they

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<sup>71</sup>“Supervisory laxity tended to encourage the embezzlement of public monies at all levels.” ((Blockmans 1999)p1 ). Officials disbursing funds stole too: it was estimated that as much as a quarter of the total amount spent was lost in ‘networks of speculation’ ((Hale 1985)).

<sup>72</sup>“Since royal officials and tax farmers exploited and abused the system at will, it was small wonder that Pegolotti recommended that no ship cast anchor in the Kingdom [of Sicily] until the master had reached agreement with the customs officials on the amount of the tax to be paid.” (Pryor 1979)p50

From the 1570s, publishers produced pocket-sized guides to tariffs and tolls in France, leaving merchants less at the mercy of collectors. (Wolfe 1972) Ch. 1

<sup>73</sup>(Wolfe 1972)

<sup>74</sup>“The bribes paid to tax collectors might have to be quite high, but the king certainly got less.” (Fryde 1979) p832

<sup>75</sup>(Wolfe 1972) p293

<sup>76</sup>(Thompson 1976); (Kaeuper 1988) “Fraud and brutality seem to have been frequent companions of the purveyors. The king was sometimes cheated and his subjects more often were.” p111

<sup>77</sup>“Mediæval propriety was not outraged by public officers receiving gratifications in money or kind from all who came to transact business with them. It was natural that the receiver of a favor should pay a fee to the source of his satisfaction.”(Tout and John Rylands Library. 1916) p21

appropriated some of the proceeds in the form of leisure or of time that they devoted to their private dealings.<sup>78</sup> Governments made occasional efforts to curb these various abuses—trying everything from sumptuary restrictions to the death penalty—but with little expectation of success.<sup>79</sup>

It was clear that given the available technology efficient exaction by means of a centrally controlled, salaried bureaucracy was simply not feasible. So governments found alternative ways to organize things. These all involved, in one way or another, the sale of exaction rights to individuals or groups in exchange for an agreed payment. To obtain a fair price for the exaction rights they sold, governments often relied on competitive bidding. The purchasers, now working for themselves, had more powerful incentives than salaried employees. Consequently, the government was able to capture not just a larger part of a given total of exaction, but a larger part of a total that was itself larger because of the stronger incentives.<sup>80</sup>

There is an illuminating analogy between a government's sale of exaction rights and a landowner's sale of rights to farm his land. Large-scale manorial agriculture was inefficient for much the same reasons that exaction by a salaried bureaucracy was inefficient—poor incentives and poor control. A landowner could do better by dividing up his land into smaller parcels, each suitable for a family farm. The tenant paid a rent for the land, and since anything he earned above this was his to keep, he had a strong incentive to work hard and intelligently. Because of the greater efficiency of the family farm, the landowner would earn more from renting out the land than he would from managing its cultivation himself.

There were many different ways in which governments sold exaction rights.<sup>81</sup> One was the feudal system of lord and vassal. The lord granted the vassal a territory over which the latter had exclusive rights of exaction; the vassal paid for this territory with military service (later commuted to the payment of money as scutage). Similarly,

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<sup>78</sup>See (Kohn forthcoming) Ch. 21 for more on the difficulties of local administration.

<sup>79</sup>(Wolfe 1972) Ch 1

<sup>80</sup>For example, in England under Elizabeth the Crown gave up on reform of a customs system “riddled with mismanagement and corruption” and chose instead to lease out parts of it for a fixed sum each year and “left the lessee to seek greater rewards from customs than the Crown had hitherto been able to obtain.” (Hurstfield 1973) p308

<sup>81</sup>See (Kohn forthcoming) Ch. 20.

exaction rights over specific territories were granted to ecclesiastical entities—in exchange for payment in the form of prayer and rewards in the world to come—and to cities in exchange for hard cash.

Exaction rights were also sold on a more commercial basis. In this case, the rights sold were usually specific rather than general and of fixed rather than indefinite duration. One example was the farming of revenues: the farmer advanced a fixed sum in exchange for the right to collect a particular stream of revenue. Farmers were employed to collect indirect taxes, domain revenues, and mining royalties and to operate mints. Similar in principle was the sale of the right to collect a certain tax to a city (*encabezamiento*).<sup>82</sup> Governments also sold monopolies.<sup>83</sup> These constituted rights to collect streams of monopoly profits rather than taxes, but as we have seen the two were essentially equivalent.<sup>84</sup> Sometimes the farming of a tax would be combined with a monopoly, with the latter enhancing the value of the former.

Since a good part of total exaction was, as we have seen, illicit—in the form of peculation, corruption, and extortion on the part of government officials—it was difficult to sell this overtly. What governments did instead was to sell the positions themselves. An official purchasing a position bought the right, implicitly, to all of its illicit benefits. Purchasers of office “recouped themselves for their capital outlay, not only by the legitimate profits of office but still more by the unlawful but customary peculations and extortions in which the early mediaeval functionary delighted.”<sup>85</sup> The possibilities of exaction from a particular office depended on the duties associated with it. Governments therefore enhanced the value of offices—and so their sale value—by adding new taxes for incumbents to collect and new interventions for them to enforce. The addition of new taxes and new interventions also opened the way for the creation and sale of additional offices.<sup>86</sup>

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<sup>82</sup>(Miller 1971);

<sup>83</sup>(Ekelund 1997) Ch. 3

<sup>84</sup>“In effect such monopolies were a form of indirect taxation, heavy and at the same time unproductive, subsidizing the treasury at the cost of generally inflated prices; both restrictive of supply and of economic and personal liberty...” (Thompson 1976) p259

<sup>85</sup>(Tout and John Rylands Library. 1916) p15

<sup>86</sup>(Swart 1949). See also (Kohn forthcoming) Ch. 21.

The sale of exaction rights led to the formation of a predatory class, making its living from exaction. Early in the period the landed nobility was such a predatory class. Later, in some countries, it was a predatory bureaucracy of tax farmers and venal officials (the new predatory class tended to merge with the old). Returning to the analogy of the landowner, the creation of a predatory class increased the ‘efficiency’ of exaction. The members of the predatory class, working for themselves, were more energetic and more ingenious in squeezing out the maximum possible from the population. How the gains were split between the predatory class and the ruler was determined by the intensity of competition for positions in the predatory class. The predatory class itself, of course, did its best to suppress or subvert such competition.<sup>87</sup> For example, in France, the officials charged with auctioning tax farms would accept bribes from bidders to award the farm at less than a fair price.<sup>88</sup>

The creation of a predatory class increased the gain of the ruler from exaction, but it increased the loss of the population by much more.<sup>89</sup> More efficient exaction meant a greater burden of exaction. The sale of exaction rights tended to produce a level of exaction that was ‘too high’ even from the point of view of the beneficiaries of exaction themselves because of a variety of incentive problems. For example, each noble taxed the trade passing through his territory without regard for the cumulative effect of the myriad tolls in reducing the overall volume of trade and so the total take from tolls. Similarly, members of the predatory bureaucracy did not have exclusive territories. Rather, each had different exaction rights, but applied to the same population. Consequently, each had an incentive to take what he could, even if it impoverished the population and ultimately reduced the overall take.<sup>90</sup> Moreover, to the extent that exaction rights were temporary, as they were with tax farmers, there was an incentive to maximize exaction in the short run at the expense of reducing the potential for exaction in the long run.<sup>91</sup>

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<sup>87</sup>See (Kohn forthcoming) Ch. 21.

<sup>88</sup>(Wolfe 1972) Conclusion

<sup>89</sup>“If jobs are distributed among officials through an auction mechanism, whereby those who pay the most for a job get it, then the prospective officials who do not collect bribes simply cannot afford jobs.” (Shleifer and Vishny 1993) p603-4

<sup>90</sup>Both of these examples are ‘commons’ problems.

<sup>91</sup>(Smith 1976 [1776]) p434-5

### **The effects of war and of government borrowing**

War generally increased the harm done by exaction. Governments were under pressure to exact more resources from their territories, so they increased existing taxes and added new ones. However, additional taxes brought in less and less additional revenue. As tax levels rose, more effort went into resistance and evasion and an increasing proportion was lost to ‘collection costs’. As tax revenues reached their limit and still proved inadequate, governments resorted increasingly to arbitrary seizures, to the sale of monopolies, to the creation and sale of new offices, and to debasements.<sup>92</sup> It was the growing reliance on these more harmful forms of exaction, rather than increasing levels of taxation, that made wartime exaction so destructive. However, the resulting long-term damage to the economy, even when rulers understood the consequences of their actions, weighed little against the urgency of the moment.

The destructive effects of war finance were mitigated—at least potentially—when governments were able to borrow. Borrowing allowed the burden of exaction to be distributed over time: it reduced the urgency of exaction and so the recourse to the more damaging forms. However this potentially beneficial effect was often offset by an increase in the size and frequency of wars, because borrowing made them easier to finance.<sup>93</sup> To a large extent, predatory governments were restrained in their propensity to go to war only by limits on the resources available to them. Borrowing eased these limits.

The contrast between the wars of the long fourteenth century and those of the long sixteenth century illustrates both of these effects. The wars of the fourteenth century, especially those among predatory governments, were financed largely by concurrent exaction; those of the sixteenth century were financed largely by borrowing, with the exaction deferred. However, access to credit meant that the wars of the sixteenth were conducted on a far larger scale.<sup>94</sup> Despite this, the wars of the fourteenth century seem to have been far more destructive of the economies concerned.

The acquisition of resources by governments through borrowing—so long as it was voluntary and so long as the borrowing was repaid—was not itself harmful. Government

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<sup>92</sup>See (Kohn forthcoming) Ch. 20 for more details.

<sup>93</sup>See (Kohn forthcoming) Ch. 19.

<sup>94</sup>See (Kohn forthcoming) Ch.s 19 and 20.

borrowing did not usually ‘crowd out’ investment, because commerce—the principal source of lending—generally generated more profits than could usefully be reinvested in its own ventures.<sup>95</sup> Moreover, war often interrupted trade, so merchants were happy to divert their now idled funds into government loans. Government debt, when it was sound, was more a substitute for investment in land than for investment in commerce and industry and so it is unlikely that it did much to reduce the latter.<sup>96</sup>

Forced borrowing was, of course, a different matter. To the extent that the borrowing was on unfavorable terms, it was merely another form of exaction. The difference between the amount taken by the government and the market value of the debt was the amount of the tax.<sup>97</sup> Moreover, forced borrowing by the government could deprive lenders of funds that they would have preferred to invest in commerce or industry.

Governments frequently defaulted on their debt. This was true, however, more of predatory territorial governments than of associational governments. The latter, dominated by merchants, were more cognizant of the long-term consequences of destroying their credit. The major sovereign defaults—by England in the fourteenth century and by France and Spain in the sixteenth—wreaked havoc with contemporary financial systems. The English default contributed to the failure of the great Florentine banking houses; the French and Spanish defaults devastated the money markets of Antwerp and Lyons.<sup>98</sup> The resulting damage to the financial system reduced the general availability of credit, thereby increasing the costs of trading and production. For example, the collapse of the major merchant banks in Florence caused a chain reaction of failures in the city, a credit crunch, a collapse of the real estate market, and a recession in manufacturing that lowered both wages and the price of raw materials.<sup>99</sup> Moreover, once rulers had destroyed their credit, they had little choice but to fall back on those same damaging expedients that borrowing had helped them avoid. In Spain, for example, with a series of defaults beginning in 1557, the government was forced to raise taxes sharply, increase arbitrary seizures (especially of shipments of private bullion from America), and

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<sup>95</sup>See (Kohn forthcoming) Ch. 10.

<sup>96</sup>(Thompson 1998)

<sup>97</sup>See (Kohn forthcoming) Ch. 11.

<sup>98</sup>See (Kohn forthcoming) Ch. 10.

<sup>99</sup>(Cipolla 1982)

redouble its efforts to sell offices. The economy, which had until then prospered as inflation had eroded the burden of taxation, faltered and then began a long decline.<sup>100</sup>

### **The constraints on exaction**

As we have seen, rulers and subjects was constrained by law and custom: rulers had prerogatives; subjects had rights. Rulers prerogatives of exaction were limited initially to their own domains, plus certain general prerogatives such as the control, and exploitation, of the coinage and public markets. Rulers were also entitled to demand military and financial support from their subjects in time of war. The rights of subjects included exemptions for particular groups from certain types of exaction and various monopoly rights (which rulers were obliged to enforce). Subjects possessed too the right to be consulted about the nature and the amount of military and financial support demanded of them.

Rulers respected their subjects' rights because they had to: as we have seen, they lacked the power to impose their will over their subjects' resistance and they needed their subjects' support and cooperation. Moreover, rulers often relied on their subjects—on cities in Castile and on unpaid local officials in England—to collect their taxes. In these cases, their subjects' refusal to administer a tax or simple foot-dragging could be as effective a weapon as rebellion.<sup>101</sup>

Rulers also had an additional—reputational—interest in respecting the rights of their subjects and indeed of foreigners, because they were in the business of selling rights. As we have seen, rulers sold exaction rights. But they also sold other rights—for example, exemptions from tolls and rights of self-government to cities and safe conducts to foreign merchants. If they subsequently violated the rights they had sold, they could hardly expect to get much for any rights they attempted to sell in the future. For example, rulers were able to sell offices only so long as incumbents could be reasonably sure that the ruler would not take those offices back again arbitrarily.<sup>102</sup>

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<sup>100</sup>(Thompson 1995)

<sup>101</sup>(Tracy 2002) Ch 5; (Greif 2005). For more details, see (Kohn forthcoming) Ch.s 20 and 21.

<sup>102</sup>Outside of Europe "...one of the factors which hampered the growth of this institution [sale of offices] was that the status of officials was not secured against caprices of princes.... As a result, offices in Oriental governments seldom became an object of legal transactions." (Swart 1949)p111

While rulers were generally obliged to respect their subjects' rights, this was much less true of the rulers' agents. Rulers claimed prerogatives publicly and formally. So their subjects could organize effectively to resist such claims. Officials, on the other hand, simply exercised their power 'informally' and generally against specific individuals. Violations of rights were therefore more difficult to prove, and since each violation affected only a single individual, it was much harder to mobilize general resistance to it. The less effective constraints on the exaction of agents was one of the reasons the sale of exaction rights increased the overall take from exaction.

Rulers and subjects negotiated their prerogatives and rights, and particularly changes to them, in meetings of representative assemblies. Local lords negotiated with their peasants in much the same way in regular assemblies of their villages. In both cases, courts adjudicated alleged violations.<sup>103</sup>

Did the constraints on exaction reduce its overall level? Representative assemblies rarely refused outright a ruler's request for additional taxes. They did, however, bargain down the amount of the tax.<sup>104</sup> Where the constraints were most effective—as in England—rulers were kept on a short leash. Indeed, their difficulty in obtaining financing constrained their ability to go to war. While the English Parliament was particularly effective, the French Estates were much less so. As a result, by the early seventeenth century government revenue per capita in France was perhaps three or four times its level in England. The kings of France were claiming an ever-increasing share of national income while those of England were claiming an ever-shrinking one.<sup>105</sup>

There was, however, a downside to the ability to constrain taxes. Rulers who were unable to obtain the resources they needed through taxation were more likely—especially under the pressure of war—to turn to other, more harmful, forms of exaction over which their subjects had no control. The control of the coinage was an unquestioned royal prerogative, so rulers were wont to resort to manipulation of the currency when frustrated in their attempts to obtain new taxes.<sup>106</sup> France, for example, went through six cycles of debasement and strengthening between 1346 and 1355: “Philip VI and John preferred to

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<sup>103</sup>See (Kohn forthcoming) Ch. 21 for details on these institutions of governance.

<sup>104</sup>(Koenigberger 1995); (Strayer 1970) Ch. 2

<sup>105</sup>(Nef 1940) Ch. 4

<sup>106</sup>(Spufford 1988)

raise funds from the mints rather than to haggle with assemblies and communities about taxes.”<sup>107</sup> The appointment of officials too was a royal prerogative, so that the sale of offices was also a way of evading the constraints.<sup>108</sup> Economic intervention was yet another prerogative. It was supposed to be exercised for the public good, but in practice rulers were left with a great deal of discretion. So the creation and sale of monopolies was one more way for rulers to evade the constraints on taxation.<sup>109</sup>

While subjects had no formal right to object to these and other forms of non-tax exaction, they were often able to negotiate their limitation or even cessation. It was relatively easy to strike a deal, because both sides stood to gain: the ruler would receive more revenue; his subjects would be relieved of harmful forms of exaction at a cost lower than the damage prevented.<sup>110</sup> For example, after a few rounds of debasement, the nobility, which found its income from land rents being seriously eroded by inflation, was often ready to grant new taxes in exchange for promises by the ruler to desist from debasement (not always kept).<sup>111</sup> The more effective representative assemblies were able to negotiate an end to arbitrary seizures. For example, the royal prerogative of prise was one the barons specifically wished to limit in the Magna Carta of 1215.<sup>112</sup> A hundred years later Parliament forced Edward II to give it up entirely.<sup>113</sup> Representative assemblies were sometimes able to negotiate—again in exchange for greater cooperation in the granting of taxes—limits on the sale of exaction rights through tax farming, the sale of offices, and the sale of monopolies.<sup>114</sup> Representative assemblies also sought to replace tax collection by the ruler’s officials with collection by local associational governments. In France and in the Low Countries, for example, regional assemblies

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<sup>107</sup>(Fryde 1979) p843

<sup>108</sup>“Where... the power to raise revenue [was] restricted by political inhibitions or the unco-operativeness of subjects and estates, the Crown turned to the contractor and the tax-farmer. It is for this reason that the farmer, the contractor, and the monopolist were so much hated by parliamentary and constitutionalist oppositions.” (Thompson 1976)p285

<sup>109</sup>(Ekelund 1997) Ch. 3

<sup>110</sup>Economists call this a Coasian bargain ((Coase 1960))

<sup>111</sup>(Bisson 1979) For more on the politics of debasement, see (Kohn forthcoming) Ch. 7.

<sup>112</sup>(Miller 1971)

<sup>113</sup>(Fryde 1979) p832

<sup>114</sup>(Swart 1949). When the English Parliament was in a strong position during the Hundred Years War, it managed to prevent the sale of exaction rights. When its power declined after 1453 it was less effective in doing so and this practice became more common under the Tudors and Early Stuarts ((Ertman 1997) Ch. 4).

would promise to raise fixed sums for their rulers in lieu of taxation by their officials.<sup>115</sup> In general, the ability to influence the form of exaction was no less important than the ability to constrain its level.<sup>116</sup>

It was not only representative assemblies that negotiated and struck deals over the form of exaction. Individual cities negotiated charters that allowed them to pay a fixed amount in place of the dues and charges to which they were subject and which were both onerous and difficult to collect: “The supreme objective in seeking a charter was... to secure exemption from oppression and arbitrary extortion.”<sup>117</sup> The payment of a fixed amount often had the additional benefit that its real value was eroded over time by inflation. For example, for a long period in the sixteenth century the cities of Castile were able to buy out the *alcabala* with a regular annual payment (*encabazimiento*).<sup>118</sup> The level of these payments was fixed in nominal terms in 1536 and was not adjusted until 1578, by which time the price level had more than doubled.

Villages, too, sometimes bought out the many burdensome payments and services they owed their lords with a fixed payment. For example, the men of Hemingford in England bought out all the rents and services they owed for a period of seven years beginning in 1280 in exchange for a payment of £40 a year.<sup>119</sup> Similarly, in France in the same period the villagers of Thiais in the Ile de France agreed to pay their lords 2,200 livres and the neighboring village of Orly 4,000 to be free of arbitrary levies and prises. These were enormous sums, much larger than their lord had succeeded in collecting from them. Their size was a measure of how harmful these random exactions had been.<sup>120</sup>

Cities and villages were free to raise the fixed amounts they paid their lords in ways of their own choosing—ways that were economically less damaging. Moreover, in doing so, they were free to govern themselves and to rely on their own elected officials to

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<sup>115</sup>(Strayer 1970) Ch. 2; (Hart 1993) Ch. 3

<sup>116</sup>“Although the Cortes of Castile did not refuse the king supply..., it did negotiate and modify royal demands,, and determined, if not so much the absolute level of its services, the way those services were levied, on what, from whom, and at what rates.” (Thompson 1998) p277

<sup>117</sup>(Reynolds 1997) p133

<sup>118</sup>(Tracy 2002). (Gelabert 1994) credits the *encabazimiento* and its erosion with the general economic expansion in Castile in the first half of the sixteenth century.).

<sup>119</sup>(Homans 1960)

<sup>120</sup>“The poor wretches had wished above all things to know in advance what they would have to pay; they were willing to pay so much, and maybe more, merely in order to ensure that the impositions should no longer be arbitrary.” (Duby 1968) p244

collect the necessary taxes: “The free election of officials was probably at first valued more because it would avert oppression by corrupt officials than because of any general desire for free elections as such.”<sup>121</sup> As we have seen, much of the harm of the ruler’s taxes came not from the taxes themselves but from the exactions of the officials charged with collecting them.<sup>122</sup>

Other associations and bodies were also able to buy out harmful exactions. In England, counties and religious houses purchased exemptions from purveyance.<sup>123</sup> For example, in 1337 the people of Lincolnshire paid 2,000 marks to be freed of purveyance. Merchant associations also negotiated changes in exaction: for example, they sometimes bought out seigniorial tolls along important trade routes.<sup>124</sup>

The constraints on associational governments were both more and less effective than those on predatory governments. Leaders were monitored and controlled by a structure of governance consisting of assemblies and councils. So long as the association was small this worked reasonably well. In addition, because government was closer to the people, officials were under more effective scrutiny and so less able to abuse their offices for personal gain.<sup>125</sup>

However, when it came to levels of exaction, independent cities were much less constrained than territorial rulers. Since government was ‘by the people’, there was no concept of prerogatives and rights: ‘the people’ could decide to tax themselves as they pleased. In contrast, cities subject to a territorial ruler could only impose taxes to the extent allowed by the ruler. If an independent city was taken over by a tyrant, as happened increasingly often in northern Italy in the fifteenth century, the tyrant was much more powerful than any predatory territorial ruler, because he was not constrained by the system of prerogatives and rights that constrained the latter. The result of the weakness of constraints in independent cities was that exaction often reached levels that would not

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<sup>121</sup>(Reynolds 1997) p133

<sup>122</sup>For example, “...the worst excesses of [the alcabala] derived not so much from the absolute levels of taxation as from an overinflated and abusive semi-private machinery of collection and enforcement.” (Thompson 1998) p280

<sup>123</sup>(Kaeuper 1988) Ch. 1

<sup>124</sup>(Wolfe 1972). For more on the role of merchant associations in buying out exaction and securing other privileges, see (Kohn forthcoming) Ch. 16.

<sup>125</sup>See (Kohn forthcoming) Ch. 21.

have been tolerated by the subjects of a territorial ruler. On the other hand, because associational government was inherently more responsive than predatory government, it was more sensitive to the harm done by exaction, and it tended to rely predominantly on the less damaging forms.<sup>126</sup>

Some independent cities, especially in northern Italy, themselves became rulers of extensive territories, which included subject cities. The relations between the dominant city and its territories were then constrained by custom and contract much as were the relations between predatory rulers and their territories. Here too, respect for subjects rights was supported by a balance of power.

### **Politics and rentseeking**

The struggle to constrain and to modify the form of exaction was not only a struggle between rulers and subjects. It also pitted subject against subject. Different groups had different and conflicting interests. Some were beneficiaries of exaction—the many tax farmers and venal officials, as well as the cities and the merchant associations that purchased monopolies. Others were its particular victims—the peasants squeezed by both lords and rulers and the urban poor and middle class who paid prices inflated by indirect taxes and monopolies. Everyone preferred to see the burden of exaction shifted to someone else.

Subjects pursued their particular interests by forming coalitions with others or with the ruler, by lobbying the ruler for favors, by scheming against their opponents and rivals—in short, by politics. The royal court, the representative assembly, the bureaucracy—all were important forums in the political struggle for advantage.<sup>127</sup> Great nobles and high officials pursued their interests as individuals, but most subjects did so through groups and associations. Indeed, this was a major reason for the formation and existence of associations: there were significant benefits of scale in bargaining—larger groups could offer bigger threats and greater inducements.

The English tax on the export of wool provides a good case study in political struggle over exaction.<sup>128</sup> Although taxes on trade were a royal prerogative, Edward I found it

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<sup>126</sup>See (Kohn forthcoming) Ch. 20

<sup>127</sup>(Williams 1979) Ch. 1; (Henshall 1992) Ch. 1. See also (Kohn forthcoming) Ch. 21.

<sup>128</sup>(Power 1942) Lecture IV

expedient to negotiate his new custom on wool with the domestic and foreign merchants involved in the trade. In exchange for their cooperation in collecting the tax, he agreed to end an existing embargo on trade with Flanders, with which England had a dispute. The wool tax was initially low and it was argued that it would fall mainly on the foreign purchasers. However, with the onset of war at the end of the thirteenth century, the level of the tax was increased sharply, and it became abundantly clear to English growers—through the much lower prices they received for their wool—that the bulk of the burden fell on them. Opposition to the tax brought together the great lords and bishops (major growers), the knights of the shire (minor growers), and the majority of merchants (mostly not involved in the wool trade and for whom the growers were important customers). Together they campaigned through Parliament, where they were represented as the Lords and Commons, to have the tax abolished. Since it was inconceivable that the king would give up his most important source of revenue, they did not succeed. So, in 1350, they settled instead for the king’s recognition of the right of Parliament to control the tax. This victory was aided by the defection to the side of the opponents of the tax of a majority of the wool merchants. These were angry, because they had been shut out of the action after the king had granted a monopoly of the wool trade to a small group of merchants willing to make him substantial loans. Throughout this period, it was opposition to the custom on wool that galvanized political action, and it was mainly this issue that was responsible for transforming the English Parliament into an effective representative assembly.

This case is perhaps unusual in that it united the bulk of the population against the ruler and a small group of merchants. More often, the struggle for advantage was divisive. For example, when the count of Holland sold staple rights on the lower Maas to the city of Dordrecht in 1334, the rival cities of Delft and Rotterdam were furious. Indeed, the quarrel created two opposing parties in Holland—the ‘Cod-Fish’ and the ‘Hooks’—who fought each other in a series of civil wars over the next 150 years.<sup>129</sup> In fact, even in England the unity did not last long. The custom on wool soon created a significant constituency that benefited from it, since the much lower domestic price of wool gave the woolen cloth industry a huge advantage over its foreign competitors.<sup>130</sup>

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<sup>129</sup>(Israel 1995) Ch. 2

<sup>130</sup>(Miller 1971)

The rival interests fought it out in Parliament for centuries—now one side gaining the advantage, now the other.

In principle, associational governments—such as those of cities—existed only to further the interests of their members. In practice, however, they tended to be captured by leadership factions. The larger the association the more likely this was to happen. Not surprisingly, the controlling faction ran affairs to its own advantage. What this meant in terms of exaction was that those in power shifted the burden to others and appropriated to themselves as much as they could of the proceeds. For example, since it was generally the wealthy who were in power, city taxes tended to be taxes on consumption rather than taxes on property. This could not be overdone, however, because revolt was always a threat. Moreover, excessive taxation could cause people to migrate to other cities not so heavily burdened. Since control of city government was valuable to the incumbents, there were constant struggles among rival groups, frequently violent, for the leadership.

A considerable effort, therefore, went into the struggle over the distribution of the burdens and gains of exaction. This was yet another of its cost—and a substantial one. This struggle was a zero-sum activity: the gains of one came at the expense of another. None of this effort added one iota to the total amount of resources available. And of course, the effort expended in this way was diverted from more productive endeavors.<sup>131</sup>

## **PEACE AND ORDER**

The second major way in which the deployment of violence by governments affected the economy was through the provision of peace and order—peace meaning security against others taking or destroying one's possessions; order meaning the observing of agreements, regulations, and laws.

A lack of peace and order was harmful to economic activity in much the same way as exaction. There were direct losses to predation and to default. There was the associated uncertainty that amplified the effect of these losses in discouraging economic activity. There were the costs of protection: for example, ships had to sail heavily armed and merchants on land had to hire armed guards and travel in caravans. And there were the

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<sup>131</sup>Economists call the struggle over the distribution of the gains of exaction rentseeking (see (Tullock 1989), for example). The struggle over the distribution of the burden of exaction has no specific name but it is a very similar phenomenon.

costs of mitigation: for examples, merchants diversified the risks by dividing their cargoes among several small ships rather than sending them in one, more efficient, large one. Finally, there were the costs of economic activity foregone—trade that did not take place because transportation was too dangerous or because transactions among strangers were too risky. The absence of peace and order therefore increased trading costs, reduced the actual or potential extent of markets, and blocked the productivity gains that came from expanding markets.<sup>132</sup>

The main difference between exaction and a lack of peace and order was in the identity of the beneficiaries. With exaction, governments and their agents were the beneficiaries. With a lack of peace and order, the beneficiaries were the private individuals who engaged in theft and brigandage and who defaulted on their agreements. Not only were governments not beneficiaries of a lack of peace and order, they were indirectly its victims because of the damage done to their exaction base.

Governments therefore had an interest in promoting peace and order. Government command of violence also provided them with the means. In general, it is possible to promote peace and order by altering the balance of prospective gain and loss for potential violators. Since the exercise or threat of violence is one way of doing this, governments were in a position to offer such a service. However, governments were by no means the only providers of peace and order.

### **Self help and group peace and order**

Individuals to a considerable extent relied on their own efforts to secure their possessions and to ensure that others honored their agreements with them. They protected themselves and their possessions by means of violence: everyone carried a weapon and was ready to use it.<sup>133</sup> They promoted compliance with agreements by imposing sanctions on those who defaulted and by providing guarantees for their own performance.<sup>134</sup>

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<sup>132</sup>For more on the effects of predation on transportation costs. see (Kohn forthcoming) Ch. 5. For the importance of order for transactions costs, see (Kohn forthcoming) Ch. 17. For the effects of trading costs on the economy, see (Kohn forthcoming) Ch. 1.

<sup>133</sup>(Kaeuper 1988) Ch. 2

<sup>134</sup>Today, self help is defined as “legally permissible conduct that individuals undertake absent the compulsion of law and without the assistance of government officials in efforts to prevent or remedy a wrong.” ((Special Project 1984) p 850). However, the use of “legally permissible” assumes the existence of

The unit of self help was in fact the family rather than the individual.<sup>135</sup> Families could mobilize violence on a larger scale. Also, being longer-lived and commanding greater resources, they could threaten and promise more credibly. Families therefore provided more effective protection to the persons and property of their members. They also deterred aggression through vendetta or feud: if you harmed a member of the family, you could expect retribution on yourself and on your own family.<sup>136</sup> Families supported agreements by boycott or reprisal against defaulters, and through the provision of guarantees of performance for their own members.

Individuals and families did not however exist in isolation. They belonged to all kinds of groups engaged in a wide variety of activities—economic, religious, and social. Most such groups possessed an informal system of internal peace and order that supplemented and reinforced the self help of their members.<sup>137</sup> Again, greater scale made for a more effective and less costly deployment of violence in defense of persons and possessions. Also, ostracism and exclusion from the group were more powerful deterrents to default than boycott by a single individual or family. In addition, groups developed norms, customs, and conventions that helped to regulate behavior.<sup>138</sup> For example, feud was governed by a set of conventions. The aggrieved party was obliged to announce publicly the intention to wage feud and was required to cease when the other party agreed to settle the claim in question.<sup>139</sup> Such conventions made feud more effective and less destructive. Groups also supported systems of reputation or credit through the diffusion of information on violations of peace or order.<sup>140</sup> This, of course, raised the cost of such violations to potential offenders and so acted as a deterrent.

Often a group undertook some form of joint action and for this purpose created formal institutions for decision and execution—thus becoming an *association*. Some associations, such as merchant associations and religious orders, were defined by the

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state-made law which determines what is and is not permissible. Self help existed before state-made law and did not then require its blessing.

<sup>135</sup>See (Kohn forthcoming) Ch. 13.

<sup>136</sup>(Pospisil 1971) Ch. 1

<sup>137</sup>See (Kohn forthcoming) Ch. 13.

<sup>138</sup>(Reynolds 1997) Ch. 1; (Schlicht 1993)

<sup>139</sup>(Volckart 2002)

<sup>140</sup>(Greif 1997)

nature of the joint activity. Others, associational governments, were defined geographically, by the territory in which they operated—for example, villages and cities. Associations usually possessed, in addition to the informal peace and order of mere groups, formal legal systems. These consisted of three parts. The first was a set of explicit laws and regulations. The second was an apparatus of adjudication to judge violations of these laws and regulations and to sanction punishment. The apparatus of adjudication was generally available too to resolve disputes between members of the association over the performance of agreements. The third part of any legal system was a mechanism for the application of violence to enforce its decisions—sergeants, bailiffs, or a militia.

Formal legal systems emerged because they offered some advantages over self help and the informal peace and order of the group.<sup>141</sup> Self-help was costly and, because it relied heavily on the actual exercise of violence, destructive. In contrast, a legal system, because of its greater credibility, could rely more on the mere *threat* of violence. Similarly, in the enforcement of agreements, a formal legal system based on contract was less costly than self help through reprisal and more effective than informal order based on reputation alone.

The advantage of a formal legal system was indeed a primary reason for groups to organize into associations. One of the most important liberties sought by towns and enshrined in their charters, was the right to their own legal systems with jurisdiction over their own citizens.<sup>142</sup> Initially the forum for justice was the town assembly, but as towns became larger they delegated this responsibility to courts of law. The larger cities even had courts specialized by type of case. Villages, too, had legal systems. Typically, these were established by the local lord, but sometimes, as in Louvre near Paris in 1270, the villagers would disregard the lord's prerogative of justice and set up their own legal system without his participation.<sup>143</sup> However, even in seigniorial courts disputes between lord and tenant were settled much as were those between tenants—according to the

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<sup>141</sup>(Benson 1990)

<sup>142</sup>(Reynolds 1997) Ch. 6

<sup>143</sup>“The members were bound together by oath, possessed a communal chest which was fed by contributions paid in corn, ignored seigniorial justice and elected ‘masters’ to settle disputes. Disregarding the fact that law enforcement was also a seigniorial monopoly, they issued their own police regulations, whose contravention was punished by a fine. Any inhabitant who jibbed at joining the association was boycotted; men refused to work for him, a time-honoured weapon in village hostilities.” (Bloch 1966) p171

custom of the manor. Judgment was either by jury or by the body of the assembled villagers.<sup>144</sup> Members of an association were expected to bring their disputes to its legal system and not to seek redress outside it. In Ombersley, England in 1418, a man was fined twenty shillings for ‘vexing’ his fellow villagers in other courts.<sup>145</sup>

Formal legal systems, however, had their limitations. They did no more than reinforce and moderate the informal mechanisms of peace and order: they certainly did not replace them. In fourteenth century Ghent, for example, even most cases of homicide were settled privately out of court: “When the extended families agreed to a blood price, the justices would record the agreement.”<sup>146</sup> Individuals still had to protect their own property. It was just less costly for them to do so because the legal system provided some deterrence of potential offenders. Moreover, legal systems could play only a limited role in enforcing agreements.<sup>147</sup> They were well suited only to forms of agreement in which performance was clearly defined—contracts of debt, for example. But they were of less use in enforcing other forms of agreement—for example, relationships of employment or of equity financing—where performance was not so clearly defined.<sup>148</sup> In the latter case, informal mechanisms remained the most effective. Moreover, recourse to a legal system was costly both in time and in money. So members of associations generally attempted to resolve their disputes through negotiation or mediation whenever possible, turning to litigation only as a last resort.

One group that was notoriously unsuccessful in establishing internal peace and order, and which thereby constituted a serious problem for others, was the nobility.<sup>149</sup> The nobility was indeed a group—one engaged in the common activity of violent predation.<sup>150</sup> However, this activity was by its very nature rivalrous rather than

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<sup>144</sup>“The lord of a manor was recognized at law as holding arbitrary power over his villein tenants. But cases at issue between the lord and any of his men were not ended by the arbitrary action of the lord. They were supposed to be settled, and often in fact were settled, by a jury of the hallmote declaring the custom of the manor in the matter.” (Homans 1960) p323

<sup>145</sup>(Hilton 1975) Ch. 4

<sup>146</sup>(Nicholas 1990)

<sup>147</sup>(Barzel 2001). See also (Kohn forthcoming) Ch. 14.

<sup>148</sup>“When the information the parties use for enforcement is subjective, self-enforcement has an edge.” (Barzel 2002)p3.

<sup>149</sup>(Kaeuper 1988)

<sup>150</sup>“Violence in the Middle Ages, as in our own day, could be quite respectable. It was a way of life shared by noblemen and thugs.” (Cheyette 1970)

cooperative. So there was little in the way of joint action—except occasionally in war against a common external enemy or in rebellion against a ruler. The only formal institution of this group was the ruler’s great council, which occasionally served to resolve disputes among nobles. In general, however—and not surprisingly given their profession—nobles preferred to settle their disputes themselves through violent self help—through feud, duel, and private war. As with other groups, such violent self help was regulated by custom and convention—in this case, by the code of chivalry.

Both noble predation and the collateral damage of the resolution of inter-noble disputes were major threats to the peace of others.<sup>151</sup> For example, one noble might ‘punish’ another by laying waste to his villages and slaughtering his villagers. The Church was much concerned with the problem—not least because it was often a victim itself. In the tenth century, it instituted campaigns promoting the ‘Peace of God’ and the ‘Truce of God’—the former claiming immunity from violence for noncombatants (such as clergy) and the latter banning all violence on specified holy days. These campaigns were not notably successful. More effective was armed defense. Indeed, the need for common defense against noble violence was a major stimulus for various groups to transform themselves into associations. For example, it was the prime motive for the organization of cities and villages into ‘communes’ of mutual protection.

As this example illustrates, associations played a role not only in internal peace and order, but also in external peace and order. As in the defense against noble violence, they protected their members against predation and violence by non-members. Once again, economies of scale in violence made joint action more effective than individual efforts. In another example, merchant associations provided joint protection for their members on the road or at sea through the organization of armed caravans and convoys.<sup>152</sup> Cities and merchant associations played a role too in external order—in facilitating agreements between their members and outsiders. They did this as both as enforcers, backing their members in disputes, and as guarantors, guaranteeing performance by their members.<sup>153</sup> Under the custom of reprisal, for example, a merchant of one city who was owed money

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<sup>151</sup>(Kaeuper 1988) Ch. 2

<sup>152</sup>(Kohn forthcoming) Ch. 5.

<sup>153</sup>See (Kohn forthcoming) Ch. 13.

by a merchant of another, could seize the property of any citizen of the debtor's city.<sup>154</sup> In a similar fashion, villagers were collectively responsible for the obligations of their members to outsiders.<sup>155</sup>

### **Third-party providers of peace and order**

There were, in addition, third parties willing and able to provide peace and order external to the group or association. As we shall see, territorial rulers were one of these third parties, but there were others.

The organizers of markets found it in their interest to ensure peace within the confines of the market and on the routes leading to it. They also provided order in the form of a legal system that could resolve disputes among traders belonging to different associations.<sup>156</sup> Exclusion from the market was an effective sanction, especially when applied collectively to the association of the offending trader. Fairs, because they were judicially 'extraterritorial', were able to develop and adjudicate their own system of custom and law tailored to the needs of traders—the Law Merchant.<sup>157</sup>

The Church was another third party that offered to resolve disputes between strangers.<sup>158</sup> It had an interest in doing so to promote moral behavior, and it had the means to enforce its judgments through the threat of excommunication. The Church already possessed its own system of internal, ecclesiastical courts. So it was relatively easy to open these to others for certain types of case. The Church claimed jurisdiction in cases involving usury and failure to perform oaths and vows, which made it an alternative venue for actions of debt and contract. Many such cases that arose in organized markets,

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<sup>154</sup>"If a man from one city, Bologna, let us say, was injured, defrauded, or robbed by a man of another city, Florence for example, he might recoup his loss or avenge his injury on the goods of his injurer's compatriots. The Bolognese—with the law on his side—could get his money by taking the goods of any Florentine. The same was true in the case of uncollected debts. When a Florentine banker or merchant operating abroad went bankrupt, all Florentines living or trading in the places he did business were liable to see their goods seized to pay his creditors. It happened indeed that innocent people lost not only their goods but their freedom as well on such account." (Cheyette 1970)p54-5

Greif emphasizes the importance of this system—which he calls the Community Responsibility System—in supporting agreements among strangers (Greif 1997) (Greif 2001)

For more on the role of associations in providing external peace and order see (Kohn forthcoming) Ch. 16.

<sup>155</sup>"Just as merchants of a borough could be distrained for the debts of a fellow citizen, so could villagers be distrained." (Homans 1960) p338

<sup>156</sup>See (Kohn forthcoming) Ch. 17.

<sup>157</sup>(Mitchell 1904) Ch. 2

<sup>158</sup>(Finer 1997) V. 2 Ch. 5

were consequently heard in ecclesiastical courts.<sup>159</sup> The Church also helped to resolve disputes between cities, nobles, and rulers through mediation—in important cases, by the pope himself. And, as we have seen, the Church took an interest in promoting external peace. Ecclesiastical courts had jurisdiction too over certain matters of internal order—for example, the crimes of incest, adultery, and bigamy.

The commercial structure also provided *substitutes* for external order. Agreements between strangers are problematic. One solution is to provide a legal system to adjudicate breakdowns of such agreements, thereby strengthening the incentives of the parties to keep their word. However, this is a very partial solution. An alternative and often better solution is to develop ways for strangers to trade with one another without having to enter into agreements at all. That is one of the major services provided by organized markets and intermediaries. Organized markets provided trustworthy systems of settlement and remittance in the form of deposit and merchant banks. They also provided commission merchants to arrange and execute trades. Financial intermediaries such as deposit and merchant banks also provided credit so that strangers were able to trade with one another on a cash basis.<sup>160</sup>

Clearly, then, peace and order did not depend on the action of territorial rulers. There were other mechanisms in place, and relatively effective ones. If we define property rights as *socially enforced* security of possession and freedom of disposal, then action by territorial rulers was clearly not necessary for the existence of property rights. Indeed, not even formal legal systems were necessary, since groups were able to support substantial property rights through their provision of informal peace and order.<sup>161</sup> Neither was it true that peace and order depended solely on the deployment of violence. A great deal was achieved by groups, associations, markets and the Church through reliance on non-violent sanctions such as ostracism and exclusion.<sup>162</sup> Nonetheless, territorial rulers had

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<sup>159</sup>See (Kohn forthcoming) Ch. 17.

<sup>160</sup>For more on the role of markets and intermediaries as substitutes for order, see (Kohn forthcoming) Ch. 17.

<sup>161</sup>“the history of the West does not support the view that the legal system is key for the operation of market economies” (Greif 1997)p240

<sup>162</sup>(Greif 2005) provides an illuminating discussion of the development of institutions that promoted peace and order, which he calls Contract Enforcement Institutions and Coercion Constraining Institutions.

always played a role in the provision of peace and order. Indeed, from time immemorial this had always been considered one of their primary obligation to their subjects.<sup>163</sup>

### **Ruler provision of peace and order**

As territorial government had fragmented in much of Europe with the disintegration of the Carolingian empire, the provision of peace and order—like other functions of government—had largely devolved on local lords and on associational governments. In France, where the fragmentation was greatest, royal courts had been replaced entirely outside the royal domain by seigneurial courts.<sup>164</sup> In Castile, peace and order were completely in the hands of cities and local lords. City charters usually gave the *concejo*, the general assembly of heads of families, the right to choose its own judicial officials or *alcaldes*.<sup>165</sup> In the Low Countries, Germany, and northern Italy too, local lords and cities had taken over the government responsibility for peace and order.

England was different. It had not been part of the Carolingian empire, and at the time the latter was disintegrating, the West Saxon kings were integrating England's many independent kingdoms into a unified territory. Within it, they created a system of peace and order based on local associational government.<sup>166</sup> They divided their territory into shires, the shires into hundreds, and the hundreds into tithings. Each tithing consisted of some ten neighboring households who were jointly responsible for maintaining local peace and order (and also for the payment of taxes). All men over twelve were required to be members of a tithing. Four members of each tithing had to attend assemblies of the hundred, where offenders were tried and disputes between tithings were resolved. The relationship between hundred and shire paralleled that between tithing and hundred.

In the twelfth and thirteenth centuries, as territorial rulers expanded their power and reasserted their authority, they began to play a greater role as well in the provision of peace and order. There were both supply and demand reasons for this. On the supply side, there were economies of scope. Rulers were expanding their systems of local administration, principally for the purpose of exaction. Their local officials were charged

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<sup>163</sup>(MacDonald 2003) Ch. 2

<sup>164</sup>(Kaeuper 1988) Ch. 2

<sup>165</sup>(Elliott 2002)

<sup>166</sup>(Benson 1990) Ch. 2; (Reynolds 1997). This system was similar to, and presumably modeled on, the one established by the Carolingians. (Kaeuper 1988) Ch. 2

with enforcing their laws—especially those relating to exaction and to economic intervention. It was relatively easy and inexpensive to add to the responsibilities of these officials the provision of peace and order. Indeed, since courts generated revenue in the form of fines and fees, it actually helped to defray the cost of local administration.

On the demand side, ruler provision of peace and order, unlike ruler exaction, was generally popular. Actions by rulers to reduce predation on trade routes reduced losses and lowered the costs of self protection.<sup>167</sup> The expansion of commerce also created an increasing need for the settlement of disputes between strangers, which existing mechanisms satisfied only partially and imperfectly. The ruler's courts were popular not only with merchants. By providing an alternative to seigniorial and municipal courts, they offered tenants and citizens a choice and imposed on other courts the discipline of competition.<sup>168</sup> For the nobility, too, the ruler's courts offered an alternative to costly self help. The regulation of noble violence, while resisted by some nobles as an infringement of their traditional rights, offered benefits not only to the non-noble victims of this violence, but also to the nobles themselves.<sup>169</sup> Indeed, one of the demands of the English barons in 1215 was for an expansion of royal justice. In France, the nobles were less enthusiastic about the extension of royal justice and continued to defend their seigniorial prerogatives.

So the provision of peace and order offered rulers an effective way to expand their reach, recapturing authority that had been lost earlier to local lords and cities. It was a way of extending the ruler's authority beyond his domain and into the territories of his vassals.<sup>170</sup> Such an extension of the ruler's authority was given added legitimacy by the enthusiastic support of the Church. The Gregorian reforms had promoted the rule of law—emphasizing the ruler's responsibility for justice, both in his own actions and in his provision of peace and order throughout his territory.<sup>171</sup>

Ruler-provided peace and order expanded at the expense of other mechanisms. It did so partly by coercion and partly by competition, with the mix varying from territory to

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<sup>167</sup>See (Kohn forthcoming) Ch. 5.

<sup>168</sup>(Britnell 1996) Ch. 6

<sup>169</sup>(Cheyette 1970)

<sup>170</sup>(Strayer 1970) Ch. 1

<sup>171</sup>(Kaeuper 1988) Ch. 2

territory. Sometimes, rulers' courts simply asserted exclusive jurisdiction over certain types of case or in certain areas. In England, for example, since nobles held land by grant of the king, disputes over land naturally came within the jurisdiction of the royal courts.<sup>172</sup> Royal courts in England also expanded their jurisdiction by steadily adding to the list of crimes defined as 'offences against the king's peace'.<sup>173</sup> Sometimes, rulers' courts offered themselves as alternative venues for litigating cases that could also be litigated in other types of court. This was particularly true for cases involving merchants. As we shall see later in the chapter, rulers generally saw associations as a potential threat and so worked to suppress them or to incorporate them into the state apparatus. This had the side effect of reducing the importance of associations as competing providers of third-party enforcement.<sup>174</sup>

Rulers' courts developed differently in different territories. In both England and France, local royal officials—sheriffs and *baillis*—established courts to hear certain types of case. In France, the system of royal justice encompassed only the royal domains, but these domains expanded dramatically during the thirteenth century. Elsewhere in France, royal courts did not attempt to replace the seigneurial courts: given the size of the country, doing so would have been beyond the administrative capacity of the government.<sup>175</sup> Instead, the government established superior courts, *parlements*, initially in Paris and later in the provinces, to which cases decided in other courts could be appealed. In Flanders, too, the counts appointed officials to which appeal could be made against judgments of the city aldermen.<sup>176</sup> In Castile, the crown eroded the independent authority of the towns by appointing royal officials, *corregidores*, to chair the town councils. By the end of the fifteenth century, the towns had lost the right to appoint their own *alcaldes*, and justice was dispensed by the *corregidor* and his deputies.<sup>177</sup>

In England, as the case load expanded beyond the capacity of the sheriffs to handle it, their judicial function was largely taken over by circuit judges sent out from the central

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<sup>172</sup>(Strayer 1970) Ch. 1

<sup>173</sup>(Benson 1990) Ch. 3

<sup>174</sup>(Barzel 2002)

<sup>175</sup>(Kaeuper 1988) Ch. 2

<sup>176</sup>(Nicholas 1992)

<sup>177</sup>(Elliott 2002) By the late sixteenth century, the central government had succeeded in eroding seigniorial justice in much the same way, by placing it under the control of royal *corregidores*.

courts. However these too were overwhelmed by the rising tide of litigation, and in 1326 the crown created a new type of unpaid local official, the Justice of the Peace (JP), to supplement the circuit courts. These JPs, appointed from among local notables, were initially responsible only for ‘keeping the peace’, but their responsibilities steadily expanded over the years to include the arrest of offenders, summary conviction for lesser offences, and conducting jury trials for more serious ones.<sup>178</sup> The traditional courts also continued to function. Manor courts heard many more cases than the royal courts—cases involving land, agricultural practices, debt, and petty offences. The larger boroughs had their own justices and held regular quarter sessions as well as providing lesser courts for minor offences and disputes. Ecclesiastical courts continued to have jurisdiction over the clergy and over matrimonial and testamentary disputes in general.<sup>179</sup>

Rulers also contributed to peace and order outside their territories. Their interest in trade, and especially in the taxes on trade, gave them an incentive to do so. The Hapsburg rulers of Spain, for example, organized convoys for ships sailing to and from their possessions in the Americas and provided royal warships to defend them.<sup>180</sup> They similarly organized convoys and protection for the herring fleets of the Spanish Netherlands. Rulers increasingly regulated the system of reprisal by requiring the aggrieved party to obtain authorization in the form of a letter of marque before he could seize anyone’s property or person.<sup>181</sup> The possessor of such a letter could have it enforced by the ruler’s officials anywhere in the ruler’s territory, rather than having to perform the sometimes dangerous task himself. Outside the ruler’s territory, especially at sea, he was still on his own, but the letter of marque provided legitimacy and distinguished its bearer from a common pirate.

It must, however, be emphasized, that while rulers contributed to the keeping of peace, they were themselves the greatest violators of the peace. Their wars were enormously destructive. Their armies wreaked havoc on the regions through which they

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<sup>178</sup>(Benson 1990) Ch. 3. The hundreds and tithings played a declining role, although they still existed in the sixteenth century. As more and more of their business focused on cases arising from the gathering of royal revenue, it became increasingly difficult to get villagers to take part in the process.

<sup>179</sup>(Palliser 1983) There were also several specialized courts—for example, the Stannaries Count for tin miners and the Admiralty courts for maritime issues.

<sup>180</sup>(Glete 1999) Ch. 9

<sup>181</sup>(Cheyette 1970)

passed. For example, in 1339 one small campaign by the English army in France, which resulted in no actual battles, laid waste to some 200 villages. Some of the damage was pillage to support the army—a form of ‘legitimate’ exaction—or vandalism on the part of the troops, but much of it was the result of deliberate economic warfare intended to deny resources to the enemy. While cheaply-constructed housing could be readily replaced, the loss of tools, livestock and stores of seed set back agricultural production for years.<sup>182</sup> The damage only increased as armies became larger. During the revolt of the Netherlands against Hapsburg rule in the late sixteenth century, Flanders and Brabant, where most of the fighting took place were laid waste.<sup>183</sup> The population of the typical community fell by a half to two thirds; around Ghent, the area under cultivation declined over a period of ten years by 92%; the major cloth manufacturing center of Hondschoote was burned to the ground, its population falling from 18,000 to 385. When armies passed through friendly territory, there was no deliberate destruction, but the damage was nonetheless considerable. For example, in the sixteenth century, the depredations caused by the constant passage of troops along the major highways of Spain drove many peasants to abandon their land and flee their villages.<sup>184</sup>

At sea, while rulers made some attempts to suppress illegal predation—piracy—they simultaneously sponsored and encouraged legal predation—privateering.<sup>185</sup> In fact, the large number of corsairs or privateers, armed with general letters of marque from their rulers, were a far greater danger to shipping than the relatively few ‘illegals’. Rulers supported privateering because it too was a form of economic warfare, causing great damage to their enemies. It was also extremely lucrative for the rulers, who generally received a share of the booty. For example, when the sixteenth century English privateer Sir Francis Drake captured Spanish treasure ships carrying over £600,000 in bullion, some £250,000 went to Elizabeth (an amount equal to several years’ of her normal income).<sup>186</sup> Apart from the direct damage of ruler-sponsored piracy, the resulting sharp

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<sup>182</sup>(Kaeuper 1988) Ch. 1. “...[R]elatively tranquil countries like England which were able to build up livestock resources may have had a vital advantage in the early stages of economic expansion of modern times.” (Hilton 1975)p205

<sup>183</sup>(Parker 1979)

<sup>184</sup>(Vassberg 1984) Ch. 7

<sup>185</sup>(Cheyette 1970); (Katele 1988)

<sup>186</sup>(Unwin 1927) Part 2 Ch. 5

increase in transportation costs reduced trade or stopped it altogether. This had devastating consequences for agricultural regions and cities that earned their livings from exports and depended on imports for their food and raw materials.<sup>187</sup>

### **The economic impact of ruler-provided peace and order**

There were both advantages and disadvantages to the increasing encroachment of ruler-provided peace and order. The advantages largely derived from benefits of scale and of specialization. With respect to the provision of peace, rulers were specialists in violence, and they already deployed it on a large scale to seize and hold territory and to exact resources from it. They could therefore ‘produce’ protection at relatively little incremental cost. Consequently, their subjects could purchase this service from them at lower cost than they could produce it for themselves. That is, there were gains from trade in protection. Consequently, cities that purchased protection from their rulers generally had lower protection costs, and so lower taxes, than independent cities that had to provide for their own protection.<sup>188</sup>

There were also benefits of scale in the provision of order. While initially the provision of peace and order was just one of several functions performed by general-purpose local officials, the increasing amount of litigation justified the establishment of courts devoted solely to this purpose. As systems of courts expanded—those of the Church and of independent cities as well as those of rulers—there was a process of legal specialization and professionalization. A distinct legal profession emerged, trained either in the universities or by apprenticeship. Another benefit of scale was the ruler’s command of violence over an extensive territory, which provided him with a superior ability to enforce judgments in disputes between strangers within that territory. He could therefore

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<sup>187</sup>See (Kohn forthcoming) Ch. 1.

<sup>188</sup>(Epstein 2000) Ch. 2 makes this point and contrasts the (pre-Revolt) Dutch cities with those of northern Italy.

“I would like to suggest that the most weighty single factor in most periods of growth, if any one factor has been most important, has been a reduction in the proportion of resources devoted to war and police. Those princes and statesmen who organized government in such a way as to reduce the costs of protection contributed to economic growth just as did the industrial or agricultural innovators who reduced the costs of other products.” (Lane 1958) p413

provide order between citizens of different cities at lower cost than the existing system of reprisal.<sup>189</sup>

Rulers did not, however, simply provide the same ‘product’ at lower cost. The change in provider changed the nature of the product. Associations and rulers offered different types of legal system.

For associations, the basis of law was custom and reciprocity: law evolved organically to meet the needs of the group.<sup>190</sup> The law was not usually codified, and it was therefore flexible. Property rights preceded the legal system, which was established to protect and to solidify them. As we have seen, conformity to the law relied heavily on self help and on informal mechanisms of peace and order. It was reinforced too by feelings of guilt and shame for on the part of violators. Offenses were treated as torts—private wrongs or injuries. For example, a homicide could be settled by the family of the perpetrator paying ‘blood money’ in compensation to the family of the victim.

The basis of ruler law was the will of the ruler.<sup>191</sup> It was top down, and in order to be administered by dispersed local officials it needed to be codified. It was therefore less flexible and less well tailored to local conditions (this uniformity did, of course, have the advantage of providing a more predictable legal environment for strangers). Property rights were granted by the ruler and regulated by his law, so in this case the legal system preceded property rights.<sup>192</sup> Conformity with ruler law relied on external enforcement in the form of inducements and sanctions, mainly the latter. There were generally no feelings of guilt or shame on the part of offenders. Offenses were crimes—wrongs against the ruler or against ‘society’. They were generally settled by punishment rather

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<sup>189</sup>See (Kohn forthcoming) Ch. 16.

<sup>190</sup>(Benson 1989) (Benson 1990). Benson uses the terms customary law and authoritarian law rather than associational law and ruler law. He emphasizes the voluntary, reciprocal, and mutually beneficial nature of customary law and its similarity, therefore, to market exchange.

<sup>191</sup>(Benson 1990); (Benson 1998)

<sup>192</sup>The different relationship between property rights and the legal system in associational and ruler law was reflected in different *theories* of the origin of property rights ((West 2003)). So long as territorial government was predatory, property rights were seen as deriving from the government (the ruler). Once associational government was established at the territorial level, thinkers began to see property rights as logically precedent to government and government as being created to protect property rights. For example: “Till there be property there can be no government, the very end of which is to secure wealth...” ((Smith 1956)p. 15)

than compensation of the victims—either fines that went to the ruler or violence that was intended to deter other offenders.<sup>193</sup>

The nature of ruler law did however differ from place to place. In England, ruler law took its principles from existing associational law, attempting only to standardize it—creating by 1536 a ‘common law’ throughout the kingdom.<sup>194</sup> On the Continent, ruler law took its principles much more from Roman civil law. The difference was partly a result of the earlier development of ruler law in England—before Roman law had been rediscovered in the twelfth century after long neglect.<sup>195</sup> The difference was also partly a result of the different nature of the regimes. In England the Roman heritage of government had been completely lost and the system of administration had been built up out of local associational government—the system of shires, hundreds, and tithings. On the Continent, the Roman heritage of government, while eroded, had survived, and it remained the model to be emulated as rulers reasserted their authority.<sup>196</sup> Of course, Roman law itself had been a codification of pre-existing associational law—largely derived from custom rather than from the arbitrary decrees of a ruler. So common law and civil law were not so different in practice. They differed mainly in their flexibility—codified civil law adapting more slowly to changing circumstances.

Moreover, even though ruler law depended formally only on the will of the ruler, we have seen that the exercise of a ruler’s will was constrained by the customary rights of his subjects. Rulers were not therefore free to legislate as they pleased.<sup>197</sup> In some territories there were formal constraints. In England, for example, legislation required the consent of Parliament. Elsewhere, as in France, formal constraints were weaker, but rulers were still constrained in practice by their need for the acquiescence and cooperation of their subjects. Moreover, in many places, rulers’ courts achieved a significant degree of

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<sup>193</sup>(Reynolds 1997) Ch. 2

<sup>194</sup>(Cohn 1971)

<sup>195</sup>(Kaeuper 1988) Ch. 2; (Finer 1997) V. 2 Ch. 5.

The rediscovery of Roman law was motivated by the desire to justify the position of the Emperor in his struggle with the pope (the Investiture Controversy). See (Kohn forthcoming) Ch. 18.

<sup>196</sup>See (Kohn forthcoming) Ch. 21.

<sup>197</sup>“The king could issue particular laws, but could not arbitrarily change the legal basis of society. He held office not as the creator, but as the conservator of law and justice. To change the laws—which included regulations sanctioned by custom—was considered an exceptional measure, tantamount almost to the alienation of a valuable possession...” (Marongiu 1968) p32

independence—in France and Spain as well as in England. They could, and sometimes did, decide against the ruler and sometimes rejected his legislation. Such rejection might be formal or it might consist simply of foot-dragging—a reluctance on the part of the courts to enforce legislation they opposed.

The flexibility and responsiveness of ruler law in England was greatly enhanced by competition. There was extensive competition not only between the ruler's courts and other courts, but also among the ruler's courts themselves. There existed a multiplicity of ruler's courts. Apart from the circuit assize courts, there were various central courts—King's Bench, Common Pleas, Exchequer. To these were added in the fifteenth century the courts of 'equity' for those who found the procedures of the common law courts too slow and formalistic. These consisted of the courts of Star Chamber, Chancery, and Requests. All of these courts competed with one another for business. They had an incentive to compete, because judges and other court officials received a good part of their compensation from court fees. They were able to compete, because jurisdictions overlapped and were ill-defined. Each court, therefore, in its desire for more business, exercised considerable ingenuity in encroaching on the jurisdictions of the others and considerable effort in lobbying to have its charter changed to expand its jurisdiction.<sup>198</sup> Because in civil cases it was the plaintiff who chose the venue, competition among the courts made English law increasingly plaintiff-friendly. Contracts were very strictly enforced and the treatment of debt, which had earlier been favorable to debtors, became much more favorable to creditors.<sup>199</sup> Another consequence of competition was the general adoption by ruler's courts in England, when dealing with mercantile cases, of Law Merchant principles and practices.<sup>200</sup>

Whatever the differences in the nature of associational and ruler law, there was a much more fundamental difference between peace and order provided by associations and that provided by rulers—their essential purpose. The purpose of associational peace and order was to further the economic interests of the members of the association. The

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<sup>198</sup>(Ekelund 1997) Ch. 3

<sup>199</sup>(Klerman 2004) When the courts became too plaintiff-friendly, the balance tended to be restored through parliamentary legislation.

<sup>200</sup>(Rogers 1995); (Benson 1990) Ch. 3; (Mitchell 1904)

purpose of ruler-provided peace and order was to further the economic and political interests of the ruler.

In furthering the interests of its members, associational peace and order was generally economically beneficial. It reduced the cost to individual members of protecting their property, and it facilitated economic interaction between them by reducing transactions costs. However, associational order also furthered the interests of members by enforcing their ‘freedoms’ and ‘rights’ against non-members—for example, by excluding non-members from trading or by enforcing taxes that discriminated against them. For example, Venice severely curtailed and regulated the trading of foreigners in the city itself and used its military power to establish a virtual monopoly of trade with the Levant for its own merchants.

Ruler-provided peace and order furthered the interests of the ruler mainly by enhancing and facilitating exaction.<sup>201</sup> This was generally economically harmful. A large part of the business of the ruler’s courts was related to exaction—hearing appeals against assessments and punishing those who failed to pay their taxes. However, much of the negative economic impact of ruler-provided peace and order came, paradoxically, from its protection of certain property rights.<sup>202</sup> This is because not all property rights are economically beneficial. As we have seen, rulers depended heavily on the creation and sale of exaction rights—tax farming, the sale of offices, and the sale of monopoly rights (economic intervention). The value of these rights, and so the ruler’s proceeds from selling them, depended on their being enforced and on their being secure.<sup>203</sup>

Rulers’ courts provided enforcement and security of possession of these rights. For example, when Elizabeth wished to create a new office in 1587 for her favorite Cavendish, the royal courts blocked her from doing so.<sup>204</sup> They argued that the new office would have reduced the profits of existing office-holders, depriving them of their

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<sup>201</sup>“The primary functions of governments are to act as a mechanism to take wealth from some and transfer it to others...” (Benson 1990)p43

<sup>202</sup>“Governments operate by assigning, reassigning, modifying, or attenuating property rights.” (Benson and Baden 1985)p392

<sup>203</sup>The value of these rights was further enhanced if, as often happened, they became alienable and could be transferred, sold or bequeathed just like other forms of property. See (Kohn forthcoming) Ch.s 20 and 21.

<sup>204</sup>(Swart 1949) Ch. 3

property—thereby violating rights granted by Magna Carta. As an example of enforcement, English purchasers of overseas trading monopolies could turn to the royal courts to punish English interlopers. Court systems, however, could do nothing to protect overseas trading monopolies against interlopers from foreign countries. For this, rulers used military force. The rulers of Spain and Portugal in particular employed their fleets to exclude unauthorized traders—French, Dutch, and English—from their overseas empires.

While furthering the fiscal interests of the ruler was generally economically harmful, there were exceptions. For example, rulers wished to attract foreign merchants so as to increase trade and so their tax revenues from it (foreign merchants also provided an important source of lending). One of the ways in which rulers made foreign merchants welcome was by providing them with impartial justice.<sup>205</sup> Fairs did this too, but outside the fairs foreigners were otherwise at the mercy of the particularism of associational courts.<sup>206</sup>

## **ASSOCIATION**

As we have seen, there were advantages to joint action. Sometimes these were advantages of scale—production of some goods and the provision of some services were less costly or more effective when undertaken on a larger scale. We have seen, for example, that there were advantages of scale in the deployment of violence, so that individuals benefited from the joint provision of protection. Sometimes joint action was advantageous because the actions of one affected the welfare of others—for example, in the use of common resources or in the effect of one individual’s behavior on the reputation of the group. Sometimes, particular goods or services, once provided, were available to all without further cost—for example, rights and freedoms obtained by a group from a ruler. In these cases, joint action was required to prevent free-riding and to

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<sup>205</sup>Edward I’s introduction of the enrollment of debts in 1283 and his simultaneous prohibition of reprisal seems to have been motivated largely by the needs of foreign merchants visiting England ((Miller 1971)). He sought to remedy a situation in which “many merchants are put off from coming to this land with their merchandise to the detriment of merchants and the whole kingdom” (quoted by (Greif, Milgrom et al. 1994) p746),

<sup>206</sup>“There are hints that local pressure sometimes operated powerfully in favour of local men in debt disputes and this may have been one reason for using the royal courts.” (Kermode 1998) p236

ensure that everyone bore his fair share of the costs of providing such public goods.<sup>207</sup> For a group to exploit the advantages of joint action, it had to create institutions of decision-making and administration—that is, it had to become an association.

Associations tended to develop when the need for them was strong and when substitutes were not readily available.<sup>208</sup> The need was strong when groups faced serious challenges that demanded joint action. The most frequent such challenge was the need for common defense against predation.<sup>209</sup> There were other challenges too of an economic and social nature. However, associations were adaptable. Once formed, an association created for one purpose could easily serve others.<sup>210</sup> There were sometimes substitutes for associations—other institutions that could perform the same or similar functions. These included families and clans, territorial governments, the Church, and market institutions of various kinds. Where these substitutes were available and effective, associations were less likely to form and existing associations were likely to decay.

Early in our period, territorial governments were weak and ineffective, the Church was in disarray, and market institutions had yet to develop. Relatively rapid economic development and migration to the cities and to new agricultural lands weakened links to family and clan. In this environment associations proliferated and thrived. Indeed, a culture of association developed that facilitated the formation of additional forms of association.<sup>211</sup> This could be described as an accumulation of ‘social capital’ that lowered the cost of joint action—economic, social, and political.<sup>212</sup>

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<sup>207</sup>Economists describe situations in which joint action is advantageous as ‘market failures’. By this they mean situations in which individuals acting separately to further their own interests (the ‘market’) do not produce the most desirable outcome. The three common causes of ‘market failure’ are economies of scale, externalities, and the existence of public goods—the three cases described above.

<sup>208</sup>That is, the potential rewards to ‘institutional entrepreneurs’ for setting them up had to exceed the cost. (Olson 1971)

<sup>209</sup>“cooperation, with a few obvious exceptions, occurs only in the shadow of conflict.” (Hirshleifer 2001) p11

<sup>210</sup>(Reynolds 1997)

<sup>211</sup>“[People’s] behavior was strongly and frequently collective, not because each person belonged to any single close community (outside the household), but because people seem to have been ready and able to act collectively in any group that had common interests in the matter at hand.” (Reynolds 1997)p138

<sup>212</sup>The term was first used by (Jacobs 1961). Others have described the capacity for joint action in terms of the level of ‘trust’: “...a nation’s well-being, as well as its ability to compete, is conditioned by a single, pervasive cultural characteristic: the level of trust inherent in the society” (Fukuyama 1995) p7

### **The economic and social role of associations**

Associations played an essential role in every form of economic activity. In agriculture, villages coordinated the use of land for arable and for grazing, as well as the exploitation of common woodlands and pastures; they also negotiated with lords over rents.<sup>213</sup> Polder boards in the Low Countries coordinated the draining of marshes and the maintenance of dykes and canals. In industry, artisan guilds regulated quality and set conditions for apprenticeship.<sup>214</sup> In commerce, merchant associations organized protection for traveling merchants, negotiated trade privileges with foreign rulers, and provided a system of order to lower transactions costs.<sup>215</sup> In all of these ways, associations acting in the interests of their members also furthered the general good. They raised productivity directly and, by lowering the costs of trading, they raised it indirectly through the expansion of markets.

However, associations also furthered the interests of their members in ways that were harmful. In particular, they attempted to tilt the playing field in favor of their members whenever they could by acquiring and defending privileges and monopolies. This was especially true of merchant associations but also, to a lesser extent of artisan guilds. While associations often attempted to gain market power, their efforts were usually undermined by competition from other associations. Generally, it was only when associations could enlist the coercive power of governments to enforce their privileges or monopolies that these were effective.

Associations also played an important social and religious role. This was true for associations created specifically for this purpose, like the parish, but also for other associations that were primarily economic in function like artisan and merchant guilds.<sup>216</sup> Associations provided a social framework for their members and a framework for religious observance—building churches and hiring priests and ministers. Social interaction played an economic role too, facilitating the sharing of information. Associations provided a safety net for their members—helping widows and orphans and

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<sup>213</sup>See (Kohn forthcoming) Ch. 3.

<sup>214</sup>See (Kohn forthcoming) Ch. 4.

<sup>215</sup>See (Kohn forthcoming) Ch. 16.

<sup>216</sup>On the parish see (Reynolds 1997) Ch. 4. On the social and religious functions of merchant associations, see (Kohn forthcoming) Ch. 16.

members down on their luck. The existence of this safety net made it easier for members to engage in enterprises that involved risk and danger. Moreover, the social and religious benefits that associations offered increased their ability to discipline their members by raising the cost of ostracism and expulsion.

Associations played a particularly important role for those who migrated to the cities and thereby lost the support of their extended families and clans. Associations of various kinds fulfilled many of the same functions. By providing a substitute for the family, they facilitated geographic mobility. More generally, by providing a substitute they weakened the hold of the family and helped to usher in a more individualistic society.

### **Associations and government**

As we have seen, associations played an important role in government. In fact, they played two distinct roles.

First, associations acted as governments—deploying violence and raising the necessary funds. The basic units of associational government were the cities and the villages. Sometimes these participated in associational government on a larger scale—in shires, provinces, and city leagues. In the case of the Dutch Republic, cities and provinces came together to create a form of associational government for an entire territorial state. An important role of associational governments that were subject to a territorial ruler was to defend and to promote the interests of their members against the power of the ruler. Indeed, the benefits of scale in negotiation and benefits of solidarity were important reasons for the existence of associations.<sup>217</sup>

The second way in which associations played a role in government was as *agents* of government. Territorial rulers had great difficulty in administering their territories. Given the available technologies of monitoring and control, effective local administration by a centrally-controlled bureaucracy was impossible. So rulers turned instead to various indirect forms of administration, delegating functions of government to other bodies.<sup>218</sup> These bodies included local associational governments and other forms of association such as merchant associations and artisan guilds. In addition, associational governments

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<sup>217</sup>(Hirschman 1987)

<sup>218</sup>See (Kohn forthcoming) Ch. 21.

themselves often delegated functions to various associations, such as guilds, wards, and parishes.

The delegation of authority by rulers to associations gave the latter a certain amount of power over the former, which they used to the benefit of their members. For example, as we have seen, they negotiated to substitute fixed payments for particularly burdensome forms of exaction. Moreover, just as territorial rulers used associations to be their agents, so did associations use rulers to be theirs. For example, as we have seen, associations purchased economic intervention by rulers to enforce their monopoly privileges.

While associations could be useful to governments, they also constituted a potential threat.<sup>219</sup> Governments, not without cause, lived in constant fear of rebellion. Associations organized people for joint action. Whatever their original purpose, once they existed, they could be turned to other uses—including insurrection. So associations were a natural focal point for sedition. Rulers' suspicion of associations was shared by the Church, which saw them as potential hotbeds of heresy. It was even shared by associational governments: cities sometimes feared their independent guilds and fraternities as sources of subversion.<sup>220</sup> Governments of all kinds tried to address the problem by controlling or co-opting their associations whenever possible, and when not by suppressing them.<sup>221</sup> Conversely, associations strove to maintain their independence, and subjects and citizens struggled to defend their freedom of association.<sup>222</sup>

#### **A COMPARISON OF ALTERNATIVE REGIMES**

What sort of regime was most conducive to economic growth and development? The first regime we shall consider—the one most common at the start of our period—is one in which predatory territorial government was weak and local associational government relatively strong. We shall see that as an economic environment this regime had both advantages and disadvantages. Over time, predatory rulers grew stronger while local associational governments, correspondingly, grew weaker. Our second regime, therefore, is one of strong predatory territorial government and weak local associational

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<sup>219</sup>(Reynolds 1997) Introduction to Second Edition, Ch. 3.

<sup>220</sup>(Nicholas 1997) Ch. 7

<sup>221</sup>More on this below.

<sup>222</sup>“One liberty, or freedom, that all men took for granted was the freedom to act collectively, provided that their activities were not subversive.” (Reynolds 1997)p liv

government. Not surprisingly, its advantages and disadvantages as an economic environment were largely the mirror image of those of the first regime. The last regime we shall consider is one in which territorial government is associational rather than predatory. The first true example was the Dutch Republic, which emerged, as a sort of association of associations, towards the end of the sixteenth century. England too, while not there yet, was tending towards this third regime. The third regime overcame the disadvantages of the first without introducing the disadvantage of the second.

### **Weak territorial rulers**

The disintegration of the Carolingian empire left territorial government in most of western Europe weak and fragmented. Weak territorial government both permitted and stimulated the development of associational government at the local level. Rulers and local lords often encouraged cities and villages to take on responsibilities that they themselves were unable to fulfill. In addition, in the constant struggles among rulers, local lords, and the Church, each saw the cities as potential allies against the others. At the same time, in the absence of effective territorial government, people had little choice but to organize themselves to provide essential services—primarily protection, but other services too. Non-government associations also proliferated in this environment for much the same reason: there were no obstacles to their formation and, in the absence of alternative solutions, there were many needs that could only be satisfied through joint action.

The system of bottom-up government that this produced—a ‘civil society’ of local associational government and non-government associations—was generally more effective and more responsive to people’s needs than the top-down government of territorial rulers. Exaction was relatively light and forms of exaction that were harmful to economic activity were generally avoided. As we have seen, this environment generated systems of peace and order well suited to facilitating economic activity. Government that was close to its ‘customers’ was more attuned to their wants. For example, transportation infrastructure was built where it was most needed. Close proximity also made for better governance. At least while communities remained small, leaders were kept under effective control. Administration was on a smaller scale, making it easier for

governments to control their officials and facilitating monitoring by the population at large.

The weakness of territorial government meant that the burden of ruler exaction was low. Rulers were unable to impose taxes against the will of their subjects and were forced to consult and to negotiate over the level and form of exaction. Weak rulers also had limited capacity to intervene in their economies.

Many of the benefits of weak territorial government stemmed from the freedom it allowed its subjects, permitting them to pursue their own interests more or less freely. Generally, such self-interested behavior was also in the general interest. For example, merchants in their selfish pursuit of profit expanded markets and increased opportunities for others.<sup>223</sup> In some cases, however, self-interested behavior was not to the common good. Both nobles and cities were guilty of such harmful behavior.

Weak territorial government left nobles free to indulge their taste for violence as they saw fit. As we have seen, this created a serious problem for the rest of society. Nobles fought each other for territory, causing widespread death and destruction. The absence of constraints also allowed local lords to oppress their peasants and to engage in various forms of banditry.

One form of noble banditry that was particularly harmful was predation on trade routes. Cities too were guilty of such predation, imposing tolls on goods in transit. The cumulative effect along a given trade route was to increase the cost of transportation significantly and so to reduce the flow of trade.<sup>224</sup> For example, in the fourteenth century there were over 60 tolls along the Rhine, and some 120 along the Loire, with each individual tolls amounting to as much as 10% of value.<sup>225</sup> This 'over-predation' harmed all those concerned, not least the predators themselves who saw their revenues declining along with the volume of trade. However, no individual lord or city along the way had any incentive to take less.

The lack of external constraints on cities could have other harmful consequences. For example, as independent cities in northern Italy grew larger, there was an increasing

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<sup>223</sup>See (Kohn forthcoming) Ch. 1.

<sup>224</sup>See (Kohn forthcoming) Ch. 5.

<sup>225</sup>(Heckscher 1935) Ch. 2; (Wolfe 1972) Ch. 1

danger of leaders exploiting their control of violence to install themselves as predatory rulers or *signori*. The absence of external constraints made this easier. Even in Venice, where this did not happen, an oligarchy was able to monopolize power and run the city for its own benefit.

Cities often gained control over their surrounding areas, including villages and smaller cities. They generally treated their subject territories no better, and sometimes worse, than predatory rulers treated theirs.<sup>226</sup> For example, the subjects of such cities, unlike those of territorial rulers, were rarely able to defend their rights and interests through a representative assembly.<sup>227</sup> Cities often imposed higher burdens of exaction on their subject territories than on their own citizens. For example, in the 1280s residents of the *contado* of Pistoia paid direct taxes at a rate six times higher than citizens of the city.<sup>228</sup>

Ruling cities also restricted the production and trade of their subject territories to their own advantage.<sup>229</sup> Cities in the Netherlands, for example, prohibited markets in neighboring villages and banned industries there such as food processing and the manufacture of textiles.<sup>230</sup> Generally, the weaker the external constraints on the city the greater the exploitation of the neighboring countryside. It was worse in the Low Countries and in Spain, where cities enjoyed considerable power, than it was in France and in England, where they did not. It was worst of all in northern Italy where there was no territorial ruler at all to constrain the behavior of the cities.<sup>231</sup>

City governments engaged as well in other forms of economic intervention to benefit their own citizens at the expense of others.<sup>232</sup> They often employed coercion to capture trade for their own merchants and to exclude merchants from other cities. In their own markets, they did this through direct control and in foreign markets through diplomacy and war. Usually, one city's gain was just another city's loss, with the resources both

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<sup>226</sup>(Epstein 2000) Ch. 2; (Spruyt 1994) Ch. 8

<sup>227</sup>(Koenigberger 1995)

<sup>228</sup>(Nicholas 1997) Ch. 2.

<sup>229</sup>(Epstein 2000) Ch. 2. Also: "...communes and city-states never saw jurisdictional and territorial expansion except instrumentally as a means to achieve economic hegemony." (Epstein 1999) p8

<sup>230</sup>(Hoppenbrouwers 2001); (de Vries and van der Woude 1997) Ch. 8

<sup>231</sup>(Epstein 2000) Ch. 5.

<sup>232</sup>For details see (Kohn forthcoming) Ch. 22.

invested in the struggle a net waste for society as a whole. Sometimes, however, a city succeeded in establishing a monopoly, enabling it to increase the sum total of mercantile profits. However, this gain came at the expense of producers and consumers, and once again there was a net loss for society. In either case, the employment of coercion to capture trade was a negative-sum activity—a fight over the division of the pie that reduced the size of the pie for everyone.

Cities engaged in yet other economic policies that ultimately harmed themselves as well as others. For example, each city in northern Italy attempted to ensure the supply of grain for its own residents by restricting exports from its own territory.<sup>233</sup> But this interference with trade exacerbated local shortages and discouraged specialization in arable farming, so reducing the total amount of grain available. However, so long as other cities restricted their exports, it made no sense for any individual city to do otherwise.

As we have seen, local governments were quite successful in providing local peace and order but less so in promoting peace and order across jurisdictions. In the absence of a framework for resolving disputes among nobles and among cities, self help was a major reason for noble violence and for inter-city warfare. While community responsibility and reprisal did provide order of a kind among merchants from different cities, it was a costly system and one subject to increasing problems of moral hazard.<sup>234</sup> The provision of peace by local governments—by local lords and cities—was also relatively costly, because it failed to exploit fully the potential benefits of scale in the deployment of violence.

Some of these disadvantages of weak or absent territorial government were mitigated by cooperation among the cities. They formed military alliances to capture the benefits of scale in protection, and they worked together to improve external peace and order. For example, in Germany, groups of local princes and cities established “territorial peace associations” to suppress banditry and crime.<sup>235</sup> Cities also negotiated bilateral agreements, as early as the thirteenth century, to regulate the system of reprisal.<sup>236</sup> (As we have seen, the commercial structure and the Church provided alternative mechanisms of

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<sup>233</sup>(Epstein 2000) Ch. 7; (Herlihy 1967)

Cities also took other measures in support of this ‘policy of provision’. For more details, see (Kohn forthcoming) Ch. 22.

<sup>234</sup>See (Kohn forthcoming) Ch. 16.

<sup>235</sup>(Volckart 2002)

<sup>236</sup>(Cheyette 1970)

external order.) In the thirteenth century, a group of six independent cities in northern Italy even attempted, unsuccessfully, to create a monetary union among them.<sup>237</sup>

Other disadvantages were mitigated by competition—which also enhanced some of the advantages. The very multiplicity of local governments offered alternatives to those who were dissatisfied. Cities that did not function well and that did not meet the needs of their inhabitants found themselves losing population to those that did. Urban populations consisted largely of migrants from the countryside: they did not hesitate to move on if another city offered better opportunities. Similarly, cities that discriminated against foreign merchants lost business to those that did not: the most successful trading center of the period was Antwerp which was known for its fair treatment of foreigners.<sup>238</sup> Ruling cities that treated subject cities badly risked having them defect to the protection of another ruling city.<sup>239</sup> Local lords too faced competition: if they treated their peasants poorly, the latter could flee to a town or to one of the areas of new colonization.<sup>240</sup> Competition even served to mitigate the problem of excessive predation along trade routes—especially for long distance trade. If the burden of predation on one route became too great, merchants would develop another.<sup>241</sup>

### **Strong territorial rulers**

Over the centuries, predatory territorial governments, initially weak and fragmented, grew stronger and consolidated into larger states. This strengthening and consolidation were the result both of economic development and of the benefits of scale in the waging and financing of war.<sup>242</sup> The territorial governments of England and of southern Italy and Sicily were exceptions from the general pattern in that they were strong from the

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<sup>237</sup>The cities were Cremona, Brescia, Pavia, Bergamo, Tortona, Piacenza. “A unified currency, by reducing the costs and inconvenience of monetary exchange would have greatly facilitated commercial traffic in this region.” (Mazzaoui 1981) p86

<sup>238</sup>See (Kohn forthcoming) Ch. 17.

<sup>239</sup>Subject cities were not always taxed at a higher rate. The citizens of Pescia, for example, paid a lower rate in the fifteenth century than those of their ruling city, Florence ((Brown 1982)). Neither were they always economically oppressed: “On the whole the balance of economic returns [for Pescia] seems to have outweighed the economic costs of integration into the Florentine territorial state.” p202. It all depended on bargaining power.

<sup>240</sup>See (Kohn forthcoming) Ch. 3.

<sup>241</sup>See (Kohn forthcoming) Ch. 5.

<sup>242</sup>See (Kohn forthcoming) Ch. 18.

beginning. In each case, their Norman conquerors had found strong structures of government in place and had simply adapted them to their own use.

Having a strong territorial ruler offered some economic advantages. A strong ruler was able to constrain the self-interested behavior of local lords and cities when such behavior was injurious to the common good.<sup>243</sup> It was in the ruler's interest to do this, because the common good coincided, to some extent, with his own.<sup>244</sup> Rulers had a direct interest in economic prosperity, because it increased the potential gains from exaction.<sup>245</sup> They had an indirect interest, as well, because their subjects were more likely to acquiesce in their rule and less likely to resist their exaction if they were seen to be contributing to their subjects' prosperity.<sup>246</sup>

Strong rulers acted to constrain the power of local lords and to suppress noble violence. Apart from any concern about the economic consequences of noble violence, powerful local lords were potential rivals for the crown. To some extent, the cities were the beneficiaries. Cities that had been oppressed by local lords often allied themselves with the ruler and were rewarded with greater freedom. Strong rulers were also able to prevent the governments of cities from being taken over by factions or by individual tyrants. In England, for example, the rulers supported non-elite groups in the cities to weaken the hold of oligarchies on city government.<sup>247</sup>

Rulers replaced the predation of nobles and cities along trade routes with their own. One way they did this was by selling merchants of one city exemptions from the tolls of others.<sup>248</sup> Predation by rulers was preferable to the free for all that it replaced because it overcame the 'commons' problem of predation by multiple nobles and cities: the ruler, taking the larger view, was less likely to kill the goose.<sup>249</sup> Internal tolls in England, for

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<sup>243</sup>(Epstein 2000) has argued strongly for the benefits of strong territorial states. For example:  
"The reason why economic growth occurred despite demographic collapse was the dynamic force of the state. Centralization underlies all the major changes to market structures.... It lowered domestic transport costs, made it easier to enforce contracts and to match demand and supply, intensified economic competition between towns and strengthened urban hierarchies, weakened urban monopolies over the countryside, and stimulated labor mobility and technological diffusion." p69

<sup>244</sup>(Olson 2000) calls this an 'encompassing interest'.

<sup>245</sup>(Spruyt 1994) Ch. 8.

<sup>246</sup>See (Kohn forthcoming) Ch. 18,

<sup>247</sup>(Ertman 1997)

<sup>248</sup>(Masschaele 1997) on England; (Epstein 1991) Ch. 3 on Sicily.

<sup>249</sup>(Olson 2000)

example, were never the problem they were in France and Germany (although the ready availability of alternative maritime transport in the former was another constraining factor).<sup>250</sup>

Strong rulers strove to overcome the negative-sum particularism of individual cities by removing barriers to internal trade.<sup>251</sup> There is evidence, for example, that the strengthening of territorial rulers from the fourteenth century onwards contributed to the integration of grain markets within their territories and to a consequent reduction in price volatility.<sup>252</sup> The internal market for grain in England was already well integrated in the thirteenth century.<sup>253</sup> As we have seen, strong rulers also promoted foreign trade by ensuring the safety and fair treatment of foreigners, often against the vigorous opposition of their own merchants.<sup>254</sup> They were also able to restrain the economic oppression by cities of their surrounding countrysides.<sup>255</sup> In some cases, to facilitate trade, rulers even invested their own resources in transportation infrastructure. For example, the Angevin rulers of southern Italy funded harbor improvements, and the Burgundian rulers of the Low Countries funded the development of inland waterways.<sup>256</sup>

We have seen that strong rulers expanded their systems of peace and order. In doing so they provided the citizens of different cities with an impartial mechanism of external order to resolve their disputes. In general, this system of order was more predictable and less costly than the system of self help that it replaced.

Strong rulers attempted to standardize currencies, taxes, laws, and weights and measures within their territories. They did so in the pursuit of legibility—to facilitate exaction from their economies and to simplify administration.<sup>257</sup> However, to the extent

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<sup>250</sup>(Heckscher 1935)

<sup>251</sup>“In brief, the rise of larger, more powerful states helped overcome the market failures and prisoner’s dilemmas associated with competition between protected food markets.” (Epstein 2001) p16

<sup>252</sup>(Epstein 2000) Ch. 7

<sup>253</sup>See (Kohn forthcoming) Ch. 2.

<sup>254</sup>(Miller 1971)

<sup>255</sup>(Brown 1982) argues that there was some improvement of city behavior in this respect under the *signoria*. The Medicis, for example, behaved more like territorial rulers, seeking to promote the prosperity of Tuscany as a whole rather than exploiting it to the benefit of Florence as had the oligarchy which had previously governed the city.

<sup>256</sup>(Pryor 1979) on the Angevins; (van Werveke 1971) on the Burgundians.

<sup>257</sup>“Sovereigns had a vested interest in rationalizing the overall economy because it led to higher revenues and larger military capacity.” (Spruyt 1994)p 159

See (Kohn forthcoming) Ch. 22 for more details.

their attempts were successful, standardization also had the side effect of reducing transactions costs and facilitating trade.<sup>258</sup>

These then were the advantages of strong territorial government—or at least the potential advantages. The potential, it must be said, was rarely realized. First, good intentions did not necessarily mean good policy. Most interventions by rulers in their economies were harmful rather than helpful. For example, ‘policies of provision’ that were intended to ensure their subjects’ supply of food and raw materials, often had just the opposite effect.<sup>259</sup> Second, the ability of even relatively strong rulers to actually execute their policies was limited. Their systems of administration were corrupt, incompetent, and ineffective.<sup>260</sup> Laws, both helpful and harmful, had only limited impact in practice.

Moreover, whatever the actual advantages of a strong ruler, we must weigh against them the disadvantages. While rulers did indeed have a long-term interest in promoting the prosperity of their territories, they had other, more pressing concerns that played a greater role in shaping their behavior. As we have seen, territorial rulers were members of a warrior class of specialists in violence. They used their command of violence to acquire and to hold territory. This meant that they were constantly at war. Their wars were not national in purpose but dynastic: their purpose was power and glory for the rulers, for their subjects they offered little but expense and destruction.<sup>261</sup> And most important in time of war was to win. The long term prosperity of a territory mattered little if it was lost to someone else.

Since ‘money is the sinews of war’, the primary concern of every ruler was always exaction.<sup>262</sup> As we have seen, the urgency of war forced desperate rulers to raise the level of taxes and to rely increasingly on forms of exaction that were harmful to their

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<sup>258</sup>“The king’s interest in rationalizing and improving the overall economy coincided with the interests of the mercantile elements in society.” (Spruyt 1994)p155

<sup>259</sup>See (Kohn forthcoming) Ch. 22.

<sup>260</sup>See (Kohn forthcoming) Ch. 21.

<sup>261</sup>The Hapsburgs are perhaps the primary example: see (Ertman 1997) Ch. 3. On the growing resentment in the Low Countries of being used in this way as a factor in the Dutch Revolt, see (Israel 1995) Ch. 7.

<sup>262</sup>(Moselle and Polak 2001) notes that maximizing revenue is not the same as maximizing output or popular welfare: “To expect a predatory state to do the latter out of enlightened self-interest is wishful thinking.”

economies—arbitrary seizures, debasements, and the sale of monopolies and offices,. The same strong rulers who lowered transactions costs by standardizing their currencies made transactions impossible by debasing their currencies. The same strong rulers who addressed the commons problem of excessive predation along trade routes, gave rise to another, much worse commons problem of excessive predation by a predatory bureaucracy. Moreover, the creation of a predatory bureaucracy provided rulers with a strong incentive for economic intervention—and harmful intervention was the most lucrative.<sup>263</sup> The stronger the ruler—that is, the less constrained by representative assemblies, by independent courts, and by a balance of power with his subjects—the freer he was to indulge in these harmful forms of exaction.<sup>264</sup> Also, the stronger the ruler the harder was it for his subjects to evade his exaction and to defend their property rights. And the stronger a ruler, the worse—other things equal—was his credit.<sup>265</sup> This meant that strong rulers were less able to mitigate the ill effects of exaction by spreading the burden over time.

Another result of the urgent need for money was that it corrupted the very sorts of policy we have listed as the potential advantages of strong rulership. Rulers' interventions in their economies were generally motivated more by fiscal need than by a desire for greater economic efficiency.<sup>266</sup>

In promoting trade, rulers played both sides of the street. Not only did they sell cities exemptions from tolls, they also sold cities the right to impose tolls. Of course, these rights often conflicted. But this was not a problem from the ruler's point of view. On the contrary, it generated lucrative litigation for his courts.

Rulers made much less of an effort to integrate their internal markets than they might have. The large states that strong rulers controlled were conglomerate states, consisting of multiple disjoint territories. The removal of barriers to trade among these territories

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<sup>263</sup>Rulers sold offices in the predatory bureaucracy. The purchasers expected to recoup the price out of the fruits of office—mainly speculation and corruption. Subjects were unlikely to bribe officials not to enforce helpful regulation.

<sup>264</sup>For example, the harm done by the Angevins in southern Italy in the late thirteenth century was due less to the level of exaction than to its form. (Pryor 1979). (Wolfe 1972) makes the same argument for sixteenth century France.

<sup>265</sup>See (Kohn forthcoming) Ch. 20.

<sup>266</sup>See (Kohn forthcoming) Ch. 22.

would have required the expenditure of considerable political capital on the part of rulers to overcome strong particularist objections.<sup>267</sup> Rulers rarely found this worthwhile. While economic integration had the potential to increase their revenue in the long run, the impact of a lack of cooperation on the part of disgruntled local elites and institutions was a much larger and more immediate. For example, the Angevins, in the thirteenth century, did nothing to integrate economically the various parts of their empire—Sicily, Provence, southern Italy, Achaea, and the Kingdom of Jerusalem.<sup>268</sup> Similarly, in the sixteenth century, the Spanish Hapsburgs did nothing to integrate the various parts of their empire—not even within Spain itself.<sup>269</sup>

While in some cases strong rulers did suppress local particularism, more often they supported it—for a fee. Rather than ending urban repression of industry in the countryside, rulers often acted as enforcers.<sup>270</sup> Rulers also sold exclusive trading rights to cities or to groups of merchants by creating staples or by granting monopolies over particular segments of foreign trade. Of course, only a strong ruler was able to sell such rights because only a strong ruler was able to enforce them.

In general, even when local protectionism was suppressed, it was replaced by protectionism at the national level. At the same time that they removed barriers to internal trade, rulers simultaneously erected barriers to external trade. Earlier in the period, when rulers were weak, protectionism was a policy of cities. Later, when rulers grew stronger, it became a policy of states—an important element in the syndrome of policies known as mercantilism. Indeed, mercantilism has been described as municipal economic policy raised to the level of the state. Rulers were ‘captured’ by mercantile interests, to their mutual profit. These policies were more economically damaging at the level of the state, because strong rulers had greater powers of enforcement. Moreover, at

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<sup>267</sup>In some cases, the different territories of the same state were not even natural trading partners. In France, for example the northern provinces were a part of the northern zone of European trade, centered on the North Sea and Atlantic, while the southern provinces were part of the southern zone centered on the Mediterranean. See (Kohn forthcoming) Ch. 2.

<sup>268</sup>(Pryor 1979).

<sup>269</sup>“Everything was geared to the conservation of the traditional economic, social and political order, and to the protection of the local producer against the outsider and the local product against the competition of other cities.” (Thompson 1998) p282

<sup>270</sup>(Miskimin 1977) on England and France; (de Vries 1974) on the Hapsburg Low Countries.

the level of the state, the mitigating effect of competition which, we have seen, moderated the ill effects of city policies, was weaker.

The concentration of power at the level of the territorial government and the greater ability of strong rulers to grant favors meant that there was an enormous increase in rent seeking.<sup>271</sup> This was witnessed by the growing size, importance, and opulence of rulers' courts where subjects lobbied and competed for favor. Resources were diverted from productive activity to negative-sum redistribution.<sup>272</sup>

Strong rulers tended to suppress associations. As we have seen, all rulers considered them a potential threat. However, only strong rulers had the power to do something about it. For example, the strong territorial governments of southern Italy and Sicily, under a succession of dynasties, largely succeeded in stamping out all forms of association.<sup>273</sup> Moreover, where predatory bureaucracies developed, they were even more assiduous in suppressing associations, because they saw them as rivals in the business of local administration.<sup>274</sup>

Just as the proliferation of associations created a culture of association and made the creation of new associations easier, so did the suppression of associations destroy this culture and make subsequent joint action more difficult.<sup>275</sup> This served the needs of strong rulers in reducing the danger of rebellion, but it also made economic joint action more difficult and less likely.<sup>276</sup> For example, the merchants of southern Italy and Sicily

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<sup>271</sup>(Ekelund 1997)

<sup>272</sup>“The most serious cost of fiscal ‘absolutism,’ however, is the perversion of entrepreneurial talent it entailed...entrepreneurial talent was diverted into redistributing the nation’s wealth rather than into increasing wealth through improvements in trade, manufacturing, and finance.” (Wolfe 1972) p249

<sup>273</sup>Under Frederick II in the early thirteenth century, “Self-government by the cities... was not allowed, for urban communities could not be permitted to escape the net of imperial authority.” ((Mack Smith 1968) p55). This was a continuation of Arab and Norman policy, and it was continued in turn by Frederick’s successors. “The seeming informality, even incoherence of urban social structures...—despite a very high rate of urbanization—clearly distinguishes late medieval Sicilian society from that of central and northern Italy and other lands in the western Mediterranean such as Catalonia or Provence.” ((Epstein 1991)p 348) “The civic life of artisans and merchants was regulated from the center and from above, not (as in the North) from within.” ((Putnam 1993)p123)

<sup>274</sup>“The local royal officials also tried to wrest control of the towns from the bourgeoisie in spite of all the king in council could do to restrain them.” (Major 1971)p55. See also (Zeller 1971).

<sup>275</sup>“The cycle is vicious; loss of group membership in one generation may make men less capable of group membership in the next.” (Homans 1950)p457

<sup>276</sup>On southern Italy (Gambetta 1993) quotes Paola Mattia Doria , an eighteenth century Neapolitan thinker, “...as a result of a deliberate policy of divide and conquer implemented by the Spanish Hapsburgs, *la fede publica*—the public trust, the basis for a well-ordered society—was undermined. All that remained

were at a huge disadvantage relative to their northern Italian competitors because they were unable to organize. As a result, they could not provide for themselves the diplomatic and military backing that was essential for trade in the Mediterranean. Their rulers, who had deprived them of the means of doing so themselves, were either incapable of providing the necessary backing or uninterested in doing so.<sup>277</sup>

However, as we have seen, associations were not only a threat to the ruler, they were also potentially useful to him. So some strong rulers, rather than suppressing associations, subverted them. They generally did so by absorbing them into the predatory bureaucracy. The rulers of France and Spain, for example, replaced election to city office with royal appointment and sold municipal offices to the highest bidder.<sup>278</sup> These rulers took over the guilds in much the same way, effectively turning them into instruments of royal administration.

Strong territorial governments also weakened associations in another more subtle way—by depriving them of their *raison d'être*. We have seen that associations flourished when rulers were weak, because association was the only way to get things done—for example, the provision of peace and order and the building of infrastructure. When rulers grew stronger it became possible to get things done instead by soliciting government action. For example, if a trade route was plagued by bandits or if a new road was needed, it was easier to lobby for government action than to organize it at the local level. However, as we have seen, territorial government was less effective and less responsive in performing such functions. The shift of power from the city to the capital reduced the importance of local politics as rent seekers focused their attention on the ruler's court.

### **Associational government at the territorial level**

With a weak territorial ruler or no territorial ruler at all, subjects had the freedom to pursue their own interests with minimal interference. In some cases, this led to outcomes

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was *la fede privata*, that private realm populated only by kin and close friends in which people take refuge from high levels of social unpredictability, aggression, and injustice.” (p 77).

(Putnam 1993) writes on the decline of trust and of civil society in southern Italy.

<sup>277</sup>(Pryor 1979). See (Kohn forthcoming) Ch. 16 on the essential role of merchant associations.

<sup>278</sup>On Spain, see (Elliott 2002)

that were undesirable for the society as a whole.<sup>279</sup> Strong rulers offered a potential solution, because they were able to restrain the harmful pursuit of individual self-interest. They were, in addition, able to exploit certain benefits of scale not available to individuals and also to provide public goods. However, while rulers had an interest in economic prosperity, this was not their first priority. Indeed, more pressing interests caused them to behave in ways that were economically harmful. There is a fundamental dilemma here. A ruler powerful enough to restrain socially harmful behavior by his subjects is also powerful enough to violate their security of possession, their freedom of disposal, and their freedom of association. And, unfortunately, it is often in his interest to do so.

There is of course an alternative way to restrain socially harmful behavior, to reap the benefits of scale, and to provide public goods—joint action. We have seen that individuals came together in associations of various kinds for precisely this reason. However, in the larger context, the associations they formed behaved much like individuals, pursuing the interest of their members (or of the members who controlled them) even when this was harmful to the society as a whole. The formation of associations solved certain problems among individuals, but these same problems then reappeared among associations. But if joint action provides a solution to these problems at the level of the individual, why not at the level of the association? Just as an association of individuals can do better than individuals acting alone, so can an association of associations do better than associations acting alone. Moreover, an association of associations should be able to advance the common good more reliably than a ruler because it has no interests of its own to stand in the way. Practice, of course, will always fail to live up to the promise of theory: associations—including associations of associations—are not without their own problems, particularly problems of governance. However, the association of associations does seem to offer a solution to our fundamental dilemma.<sup>280</sup>

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<sup>279</sup>“The real problem is not how to keep social groups wholly independent and autonomous but how to organize their relation to social control in such a way that they can maintain their own life while contributing to the life of organized society.” (Homans 1950) p467

<sup>280</sup>Another way of thinking about this is suggested by a comment of Lane’s ((Lane 1958) p414): “I am tempted to call government the earliest natural monopoly.” The problem with a monopoly is that it uses its

Associations of associations were in fact quite common.<sup>281</sup> Cities formed leagues, the most successful of which was the German Hansa, which included at its peak some two hundred cities. Villages too formed associations, for example the alliance of the three small mountain communities of Uri, Schwyz, and Unterwalden, that later expanded to become the Swiss Confederation. These leagues and alliances were mostly formed for purposes of defense, to exploit the benefits of scale in violence. However, they often took on other functions, particularly peace and order among their members. The main problem with these associations of associations as regimes of government was their weakness. They were unable to prevent free-riding by their members or conflict—even armed conflict—among them. Indeed, they could hardly be described as states.

The first association of associations that could reasonably be described as a state was the Dutch Republic.<sup>282</sup> It was formed, almost accidentally, out of an existing territorial state by removing the predatory ruler and by turning its representative assembly into a government. The members of this representative assembly, the States General, were representatives of the States of the seven individual provinces, and these in turn were made up of representatives of the cities. So the Dutch republic could be fairly described as an associational state. Quite explicitly, ultimate power rested with the provinces and with the cities, which devolved certain specific and limited powers to the central government.

A second state that had aspects of an associational state was England.<sup>283</sup> While, at the end of the sixteenth century, it was still formally under the control of a predatory ruler, the powers of that ruler were quite limited. The ruler was completely dependent on local elites for administration, and these same local elites sent representatives to parliament. Parliament was an unusually powerful representative assembly and quite effective in

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power to take advantage of its customers. A common solution for this problem with other types of natural monopoly is to have ownership of the monopoly rest in the hands of the customers ((Hansmann 1996)). Examples include securities exchanges and various kinds of producer and consumer cooperatives. One can think of an associational state as a monopoly that is owned by its ‘customers’—a sort of co-op of government. Unfortunately, governance is an increasing problem as the scale of associations increases. So an entire state governed by a single association would not work very well. The association of associations offers a solution to this problem of scale.

<sup>281</sup>See (Kohn forthcoming) Ch. 21.

<sup>282</sup>See (Kohn forthcoming) Ch. 21.

<sup>283</sup>See (Kohn forthcoming) Ch. 21.

constraining the actions of the ruler. The regime could therefore be described as an uneasy division of power between a weak predatory ruler and—if not an association of associations—then at least an association of groups, with the groups being the local elites. This uneasy balance would subsequently collapse into civil war, with the associational element eventually emerging victorious in 1688.

The associational state offered many of the advantages of a strong ruler, but with fewer disadvantages. The associational state was generally controlled by its commercial classes, and their self interest in promoting economic prosperity was stronger than that of a predatory ruler.<sup>284</sup> They were also more likely to understand what sorts of policies were helpful and harmful. The central government provided effective peace and order beyond the confines of the association or group. The particularism of the constituent associations or groups was not eliminated but it was constrained. For example, improvement of internal water transportation in the Low Countries had been blocked in the sixteenth century and before by cities that feared losing toll revenue if traffic was diverted. In the early seventeenth century, under a different regime, Dutch cities began to cooperate on improvements and on the construction of new canals.<sup>285</sup> Within a competitive political environment each association or group fought for its own interests against the others—non-violently.<sup>286</sup> Rent-seeking took on a different aspect: rather than favors being sold by the ruler, they were traded among the associations.<sup>287</sup> As in the case of a weak territorial ruler, economic competition among local groups and associations imposed constraints on harmful behavior. As a result of political and economic competition, the most harmful forms of rent creation were avoided.

Not motivated by dynastic aggrandizement, the associational state was less belligerent. Its wars were defensive or at least motivated by economic interests. Consequently, they were more likely to bring some benefit in return for their cost.

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<sup>284</sup>(Olson 2000) talks of an ‘encompassing interest’ in economic prosperity and argues that this is stronger for a democratic government than in is for an autocrat. Early modern associational states were not exactly democracies, but it seems clear that their governing classes would have had a stronger encompassing interest in prosperity than predatory rulers.

<sup>285</sup>(de Vries and van der Woude 1997) Ch. 2

<sup>286</sup>“No powerful central institutions existed which acted as an arbiter deciding what those ‘vital interests’ should look like, and Dutch policies... were determined by continuously changing coalitions of provinces, cities, and factions.” (Hart 1993)p6

<sup>287</sup>(Root 1994)

Exaction was either lighter, as in the case of England, or at least better designed to minimize its harmful economic impact, as in the case of the Dutch Republic.<sup>288</sup> Government functions were generally performed at the lowest feasible level of government, with the result that they were more responsive to the needs and wishes of the public.<sup>289</sup> Canal-building in the Netherlands, for example, was at the initiative of the cities rather than of the central government. Therefore, unlike the road-building programs of territorial rulers elsewhere, it was driven by commercial rather than by military or strategic considerations.<sup>290</sup>

The associational state, naturally, provided a friendly environment for the development of associations. For example, it was no coincidence that it was in England and in the Netherlands that large joint-stock trading companies first developed as a more structured form of voluntary merchant association.<sup>291</sup> These trading companies were much more successful than those of Spain and Portugal which were essentially state owned enterprises.<sup>292</sup>

### **The bottom line**

On balance, how did the three different regimes measure up as environments for economic development and growth, and how did they compare with one another.

The advantages of the first regime, that of a weak or absent territorial ruler, outweighed the disadvantages. We can understand this in terms of the three conditions with which we began our discussion. Security of possession was generally good. Associations and commercial institutions provided reasonable peace and order. Exaction by territorial rulers was constrained and modest, and although the governments of independent cities sometimes imposed heavy taxes, they generally avoided the forms of

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<sup>288</sup>See (de Vries and van der Woude 1997) Ch. 4 and (Kohn forthcoming) Ch. 22.

<sup>289</sup>There are two reasons why lower levels of government provide better services (Qian and Weingast 1997). First, because they have better information, they are better able to provide them (Hayek). Second, because of citizen voice and potential exit, they have stronger incentives to do so (Tiebout).

See too (Olson 1969): "... there is a need for a separate government institution for every collective good with a unique boundary, so that there is a match between those who receive the benefits of a collective good and those who pay for it. This match we define as 'fiscal equivalence'." p483

<sup>290</sup>(de Vries 1981)

<sup>291</sup>(North 1991). See also (Kohn forthcoming) Ch. 14.

<sup>292</sup>(Ekelund 1997) "the economic performance of the trading companies in the mercantile economies was directly [and inversely] related to the degree of state involvement in the affairs of these enterprises." p163

exaction that were the most harmful. Freedom of disposal was generally good. Associational governments did impose some restrictions, but their ability to do so was constrained by competition. Freedom of association was good. Indeed, the proliferation of associations was a notable characteristic of this regime. A further advantage of this regime was that, because economic units and units of government were generally small, it was characterized by a great deal of economic and political competition.

In any event, the evidence is clear. The period in which the first regime predominated was one of notable economic progress. Historians have attributed the onset of the Commercial Revolution to the fragmentation of territorial government that followed the collapse of the Carolingian empire. And they have attributed the continuation of economic progress to the emergence in the fourteenth and fifteenth centuries of ‘medieval constitutional government’, a system of government that constrained the power of territorial rulers.<sup>293</sup>

While our first regime was successful economically it was unstable politically. The benefits of scale in war meant that small political units, whether territories or independent cities, could not survive. The result was constant war and increasing internal and external consolidation. As independent cities grew and came to command larger territories, their associational governments tended to be taken over by factions or tyrants. As territorial rulers came to command greater territories the scale of their wars increased commensurately. Their desperate need to finance these wars pitted them against their subjects and against the constitutional constraints on their power. When the rulers prevailed, the result was our second regime, one of strong territorial rulership—the

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<sup>293</sup>“Many historians and archaeologists, however, have come to locate the roots of the qualitative change in the western economy which lay behind the 10<sup>th</sup>-century takeoff in the political sphere: more specifically, in the disappearance of centralized authority across East and West Francia, Italy and northeastern Spain ushered in by Carolingian decline.... the collapse of central authority permitted the economy to establish, perhaps for the first time, a substantial measure of autonomy vis-à-vis the political order.” (Ertman 1997) p51)

“There is much to be found in the thesis that really outstanding industrial and commercial development in the Middle Ages occurred only in areas of fragmentation of feudal political authority where the ability of governments to extract fiscal revenues was curtailed and where development of bourgeois freedoms could not easily be retarded.” (Pryor 1979)p54)

“The expansion of capitalism owes its origins and its *raison d’etre* to political anarchy” (Baechler 1976)p 77

See also, for example, (De Long 2000); (Van der Wee 1993) p 9; (Webber 1986) Ch. 4; (Burke 1988); (Bridbury 1962)

‘imperial state’. When the subjects prevailed, the result was our third regime, one of associational government at the territorial level—the ‘associational state’.<sup>294</sup>

With strong territorial rulership, the economic disadvantages outweighed the advantages. We can again understand this in terms of our three necessary conditions. There were indeed some improvements relative to the first regime in terms of external peace and order. Perhaps security of possession against others was improved. However, the burden of exaction was generally much heavier—not only higher levels of exaction, but more harmful forms. So security of possession against the government was much weaker.<sup>295</sup> And government proved to be by far the greatest threat to security of possession.<sup>296</sup> While strong rulers were able to remove some of the particularist restrictions on freedom of disposal within their territories, for fiscal reasons they imposed many more of their own. Strong rulers also suppressed or subverted associations within their territories, curtailing freedom of association and weakening civil society. Consequently, whenever economic conditions required joint action, it was the rulers who had to organize it—state-owned enterprises rather than private companies.<sup>297</sup> There was also a reduction in economic and political competition. Strong rulers sold monopoly rights, and their state-enforced monopolies were more effective than those enforced by associations. The consolidation of territories and the subjugation of independent cities reduced political competition.

Again, the evidence is clear. The very different trajectories of southern and northern Italy provide a case study in the very different economic consequences of our first two regimes. In the twelfth century, southern Italy and Sicily were far more prosperous than northern Italy and they were indeed the most economically advanced regions of Europe. The cities of the north threw off the control of their territorial master, while the south was subject to a succession of authoritarian rulers. The Angevin Charles I, who ruled in the

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<sup>294</sup>See (Kohn forthcoming) Ch. 18.

<sup>295</sup>“History does not provide even a single example of a long and uninterrupted sequence of absolute rulers who respected the property and contract-enforcement rights of their subjects.” (Olson 2000) p42

<sup>296</sup>In cross-country comparison of today’s economies (Acemoglu and Johnson 2003) finds that institutions that constrain government and elite expropriation (“property rights institutions”) have a much greater impact on economic growth and development than institutions that support private contracts (“contracting institutions”).

<sup>297</sup>(Fukuyama 1995) Ch. 2

late thirteenth century, was typical.<sup>298</sup> He attempted to stimulate the economy by building ports, but he also imposed heavy and complex taxes, suppressed urban liberties, and manipulated the currency. The net effect of authoritarian rule was strongly negative. By the sixteenth century, the positions of the two regions had been reversed. Northern Italy was the economically most advanced region of Europe and southern Italy and Sicily were economic backwaters.<sup>299</sup> The Hapsburgs provide another example of the consequence of strong predatory government: their rule of Spain, of their Italian possessions, and of the southern Low Countries all proved economically disastrous.<sup>300</sup> Urbanization is a good indicator of economic prosperity: on the whole, it increased where rulers were weak, and it declined where rulers were strong.<sup>301</sup>

The second regime was, however, politically more stable than the first. Strong rulers were able to overcome domestic challengers, and the benefits of scale in war gave them an advantage in external conflicts. However, over time, the damage they did to their economies undermined their military strength. Ultimately, they proved unable to hold their own against our third regime—the associational state.<sup>302</sup>

Our third regime scores even better than our first in terms of the three necessary conditions for economic development and growth. This is because it overcame some of the disadvantages of excessively weak central government. There was still security of possession against the government: exaction was either low or at least minimally harmful.<sup>303</sup> But because the associational state provided peace and order across the jurisdictions of local associational governments, there was also greater security of possession against others. Similarly, there was greater freedom of disposal, because the associational state to some extent constrained local particularism. The Dutch Republic was hardly free of it, but it was far better in this respect than northern Italy, and better than the Netherlands had been under Hapsburg rule. Because of effective political

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<sup>298</sup>(Pryor 1979)

<sup>299</sup>(Putnam 1993), (De Long 2000)

<sup>300</sup>The details will be discussed in a subsequent chapter.

<sup>301</sup>(De Long and Shleifer 1993)

<sup>302</sup>See (Kohn forthcoming) Ch. 18.

<sup>303</sup>“If many Englishmen prospered in the later 16C, they owed their good fortune in part to the low incidence of taxation and to the poverty of the Crown, or to put it another way, to the small size of the public sector.” (Palliser 1983) p107

opposition, associational states were less inclined than imperial states to sell monopolies and less able to enforce them. As with the first regime, there was more or less complete freedom of association. Economic competition was generally robust and, since local associational governments retained considerable power, there was also vigorous political competition.<sup>304</sup>

The evidence once more is clear. The economy of the new Dutch Republic expanded rapidly—despite its long struggle for independence from the Hapsburgs. The period 1570 to 1620 was one of rising real wages, high profits, and rapid urbanization in the Netherlands, at a time that those parts of Europe that remained under Hapsburg rule were declining economically.<sup>305</sup> Much of the prosperity in the Netherlands was due to the expansion and integration of the domestic market. During the same period there was significant economic expansion in England under its ‘proto-associational’ regime. There, too, much of this expansion was due to the development of its internal market.<sup>306</sup>

The associational state, as exemplified by the Dutch Republic, was politically stable. Internally, conflicts among interest groups were resolved through negotiation and horse-trading rather than through violence. Externally, it managed to support a large enough, and skillful enough, military to enable it to hold its own against much larger and wealthier imperial states.<sup>307</sup> It was able to do this because of its economic strength and because of its ability, due to public support and participation, to generate sufficient tax revenue.<sup>308</sup> The Dutch Republic soon re-established its credit and proved much better able to borrow than the imperial states that threatened it. This provided it with a huge military advantage. England would become a full-fledged associational state, with all the attendant political advantages, only at the end of the seventeenth century.

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<sup>304</sup>The Dutch Republic was an example of *market-preserving federalism* ((Weingast 1995)). A system of government is federal if it consists of a hierarchy of governments, each with a delineated scope of authority and if the autonomy of each level of government is institutionalized in such a way as to make it self-enforcing. Market-preserving federalism requires, in addition, that economic intervention generally be restricted to the lower levels of government, that the central government prevent lower levels from impeding internal trade, and that lower levels of governments pay their own way (no bailouts from the central government and no manipulation of the currency).

<sup>305</sup>(de Vries and van der Woude 1997) Ch. 13

<sup>306</sup>“There is abundant evidence that the phenomenal growth of London was part-cause and part-consequence of a developing national market for industrial and agricultural products, in which London came to dominate both internal and overseas trade.” (Palliser 1983) p234

<sup>307</sup>See (Kohn forthcoming) Ch. 19.

<sup>308</sup>See (Kohn forthcoming) Ch. 20.

## CONCLUSION

The associational state was economically and politically successful because it provided a solution to the problem of government violence. It made possible the external deployment of violence on a large scale—a necessity for political viability. But it constrained the use of government violence internally—a necessity for economic development and growth.

The impetus for bringing government violence under control was economic. The control of government violence was necessary to ensure security of possession, freedom of disposal, and freedom of association. However, the imposition of effective constraints on government violence was to have an important side effect—the promotion of personal liberty.<sup>309</sup>

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<sup>309</sup>(Olson 2000) sees causality as running in the opposite direction: “...there is a most profound and crucial connection between a lasting democracy or representative government and the property and contract rights important for economic progress. This connection is inherent in the logical conditions needed for democracy to survive... Thus, the same court system, independent judiciary, and respect for law and individual rights that are needed for a lasting democracy also imply some secure property and contract rights.” (p41)

(Greif 2005) argues that liberty and property emerge together, without either being a precondition for the other: “Markets and political institutions co-evolve, reflecting the dynamic interplay between coercion-constraining and contract-enforcement institutions. It is no coincidence that the modern market economy and the liberal state jointly emerged.” (p729)

(Pipes 1999) argues that property rights are prior in that they are a necessary condition for liberty.

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