Fixing the Machine that Would Not Go of Itself:
State Constitutional Change and the Creation of an Open-Access Social Order
in the Mid-Nineteenth-Century United States

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Abstract: General histories of the United States focus almost exclusively on developments at the national level. This paper shifts the focus back to the states by reexamining aspects of economic development that the states are conventionally acknowledged to have led—the creation of a banking system, the construction of transportation infrastructure, the promotion of corporations. It shows how these efforts provoked a more fundamental restructuring of American democracy that transformed the United States from a “natural state” into an “open-access” social order, to borrow the terminology of Douglass North, John Wallis, and Barry Weingast in Violence and Social Orders (2009). Change occurred first in a small handful of states where, for highly contingent reasons, seemingly intractable problems of implementing democracy were solved by freeing up entry into banking. Subsequent events highlighted the benefits of the new institutional configuration, and in the aftermath of the financial crisis of 1839, states began to revise their constitutions according to the new model, requiring legislatures to enact general laws and prohibiting all kinds of special and local legislation. The federal government played essentially no role in this transformation and, indeed, never went through a similar set of constitutional revisions. However, the changes that occurred in the states altered the norms about how government should function, affecting practices at the federal level as well.

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The General Assembly shall not pass local or special laws, in any of the following numerated cases, that is to say: Regulating the jurisdiction and duties of justices of the peace and of constables; For the punishment of crimes and misdemeanors; Regulating the practice in courts of justice; Providing for changing the venue in civil and criminal cases; Granting divorces; Changing the names of persons; For laying out, opening and working on, highways, and for the election or appointment of supervisors; Vacating roads, town plats, streets, alleys and public squares, Summoning and empaneling grand and petit juries, and providing for their compensation; Regulating county and township business; Regulating the election of county and township officers, and their compensation; For the assessment and collection of taxes for State, county, township or road purposes; Providing for supporting common schools, and for the preservation of school funds; In relation to fees or salaries; In relation to interest on money; Providing for opening and conducting elections of State, county or township officers, and designating the places of voting; providing for the sale of real estate belonging to minors, or other persons laboring under legal disabilities, by executors, administrators, guardians or trustees.

—Indiana Constitution of 1851, Article IV, Section 22

In all the cases enumerated in the preceding section, and in all other cases where a general law can be made applicable, all laws shall be general and of uniform operation throughout the State.

—Indiana Constitution of 1851, Article IV, Section 23

Corporations … shall not be created by special act, but may be formed under general laws.

—Indiana Constitution of 1851, Article XI, Section 13

At least since the time of the Declaration of Independence the idea that “all men are created equal” has resonated deeply through American society and culture. In recent years, however, discussions of equality have increasingly focused on a relatively narrow set of issues,
such as the distribution of income and wealth and the extent of opportunities for upward social mobility. As a result, we have all but lost sight of a core aspect of equality: the idea that laws should treat everyone the same, that they should be general and impersonal, not special and individual. The purpose of this paper is to shift the focus of attention to this alternative conception of equality and document its embodiment in a new set of American institutions in the middle of the nineteenth century. To do so, however, we must revise substantially the standard narrative of American history. One simply cannot understand these changes by focusing, as so many of our histories do, on political and ideological struggles to implement egalitarian ideals, especially at the national level. The shift to general laws was a practical solution to a set of concrete problems faced by the states. It was a response to a crisis in public finance in the 1840s, and it took the form of a series of state constitutional revisions that very deliberately transformed the way government worked by forbidding legislatures from passing bills on behalf of particular individuals, groups, and localities and mandating instead that they enact general laws. Indiana’s 1851 constitution, quoted above, was the first to embrace fully the principle of impersonal laws, but by the end of the nineteenth century nearly all states had followed Indiana’s lead and revised their constitutions to prohibit special or private bills (see Tables 1 and 2). By contrast, the federal government has never to this day undergone a similar transformation.1

The constitutional provisions banning special and local laws dramatically altered the workings of state government. Before the revisions of the mid-nineteenth century, the bulk of the business of state legislatures (as much as 70-90 percent) consisted of the enactment of private

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bills on behalf of specific individuals, groups, or local governments. In the session of the Indiana assembly that began in December of 1849, for example, the legislature authorized Charity Ann Wise to file a bill for divorce, Chris Miller to enter into contracts as if he were of age, Andrew Jackson Keeth to change his last name to Wiggins, James Taylor to build a mill dam across the Salamonie River, Horatio G. Seeton and seven other men to incorporate the Rushville and National Road Plank Road Company, and John B. Anderson and two other men to incorporate themselves as the Trustees of the Anderson University. It also legalized the acts of the school commissioner of Marion County before abolishing the commissioner’s office in that county alone, and approved a statute compelling “speculators” in LaGrange and several other specifically named counties to pay the same tax as actual settlers.

After Indiana ratified its 1851 constitution, these kinds of private and local bills disappeared from the legislature’s agenda, and the assembly instead confined its enactments to laws that applied to broad categories of people or associations. A general incorporation act for manufacturing and mining companies, passed by the legislature on May 20, 1852, specified that any three persons could form a corporation by filing with the local county recorder a certificate specifying the company name, objects, first directors, and other similar information. A statute enacted on May 13, 1852 prescribed the circumstances under which divorces could be obtained.

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3 Indiana, *Local Laws Passed at the Thirty-Fourth Session of the General Assembly* (Indianapolis: John D. Defreed, 1850), 3, 108, 206, 344, 494-500; and *General Laws Passed at the Thirty-Fourth Session of the General Assembly* (Indianapolis: John D. Defreed, 1850), 179-80, 194. Before 1851 Indiana published its legislative acts in two volumes—one for “local” laws and one for “general” laws. The former greatly exceeded the latter in terms of number of pages, even though many of the “general” laws were not truly general, as the last to examples demonstrate. All state statutes referenced in this paper can be found in the Session Laws collected on [www.heinonline.org](http://www.heinonline.org).
and set up a court procedure for adjudicating petitions from couples wishing to dissolve their marriages. A statute of January 21, 1852, established a process that enabled people and corporations to apply to a court to change their names.4 Once the legislature enacted this first wave of general laws, it had much less regular business to conduct, and as mandated by the new constitution, it switched from annual to biennial sessions. Even so the number of pages required to publish the laws passed in each session shrank. The acts of the regular biennial sessions of 1853, 1857, 1859, and 1861 averaged 220 pages, whereas those of the annual sessions of 1846, 1847, 1848, and 1849 had been more than three times that size, averaging 769 pages each.

The general statutes that Indiana and other states adopted after these constitutional revisions did not, of course, treat everyone the same. For many purposes, such as regulation, legislatures had to be able to distinguish among different categories of persons and organizations. Not only was this ability constitutionally sanctioned, but some distinctions of this kind were embedded in the constitutions themselves. For example, Indiana’s 1851 document included sections treating corporations differently from other businesses and differentiating banking corporations from other types of business corporations. The new constitutions also allowed, and indeed sometimes overtly sanctioned, blatantly discriminatory treatment against specific subgroups of the population. Indiana’s, for example, declared that “No Negro or Mulatto shall come into, or settle in the State, after the adoption of this Constitution” and further stripped “Negros and Mulattos” already in residence of their right to vote. At the same time, it granted the right to vote to whites “of foreign birth,” who declared their intention to become citizens.5

5 Article II, Sections 2 and 5, and Article XIII, Section 1. Unless otherwise specified, all references to state constitutions are to “The NBER/Maryland State Constitutions Project,” http://www.stateconstitutions.umd.edu/Search/Search.aspx.
All these types of classification schemes and discriminatory practices would be challenged in the courts and in the public arena over the next century and a half. Some categorizations, particularly those that differentiated among types of businesses, would continue to be recognized as vital policy tools, so long as all entities within a given class were treated the same. Other distinctions, particularly those involving race and gender, would gradually lose legitimacy. The struggle against discrimination was long and hard, and is by no means over at the time of this writing. Nonetheless, if special laws still predominated, it is difficult to imagine how there could have been much progress. So long as legislatures routinely conferred favors on particular individuals or groups, discrimination both within and between groups was at the very heart of what governments did. Similarly, it is difficult to imagine an effective regulatory state emerging in a world where the targets were all individually the recipients of legislative largess.

The revolution in state government initiated by Indiana’s 1851 constitution had its proximate cause, we will show, in a transportation building spree that came to an abrupt end in 1841 when Indiana, seven other states, and the territory of Florida defaulted on their public debts, setting in motion a political earthquake that swept the old system away. In a deeper sense,

6 After the umpteenth attempt by large-scale businesses to overturn state antitrust laws on grounds that they were discriminatory violations of the Fourteenth Amendment, Supreme Court Justice Joseph McKenna demolished a suit brought by International Harvester, pointing out sarcastically that the corporation’s argument would mean that a “combination of all the great industrial enterprises … could not be condemned unless the law applied as well to a combination of maidservants or to infants’ nurses.” International Harvester Co. v. State of Missouri, 234 U.S. 199 (1914) at 212-213.

7 In the case of the Indiana constitution, most of the clauses involving corporations would persist to the present, but the discriminatory provisions against Negroes and Mulattoes would be repealed in 1881. Immigrants who were not citizens would lose the right to vote in 1921. See the amendments ratified on 24 Mar. 1881 and 13 Sept. 1921 respectively.

however, the change was a response to problems created by the first wave of institution building that followed the American Revolution. The constitutions that the states and the federal government wrote in the late eighteenth century had erected checks and balances among the different branches and levels of government with the aim of preventing any repetition of the tyrannical abuse of power that had spurred the revolt against Britain. At the same time, the new governments created in the aftermath of the Revolution were more democratic than Britain’s in the sense that a much wider proportion of the population could vote. These two changes made it difficult for the elites that controlled the government to maintain power, and so to cement their coalitions politicians resorted to techniques similar to those that had sparked the Revolution. Foremost among them was the use of legislative power to award valuable privileges to supporters, most notably the right to organize corporations to provide banking, transportation, and other vital economic services. This use of control over the economy to solidify control over the polity was in many ways the reverse of the Progressives’ later observation that “business corrupts politics.”

John Wallis has called it “systematic” corruption to distinguish it from the “venal” corruption that the Progressives decried. A well-known example, of course, is Alexander Hamilton’s attempt to use the assumption of the state debts and creation of the Bank of the United States to bolster support for the national government. As we will show, however, the practice was if anything more important and pervasive at the state level, and its incidence did not depend on which political party was in power.

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Opposition to legislative favoritism became a rallying cry for the political opposition in the early nineteenth century, but whenever control of the government switched hands, those who assumed power, whether they were Federalists or Republicans, Democrats or Whigs, more often than not behaved in the same way and dispensed access to privileged organizations to bolster their coalitions. If such a strategy seemed too difficult or uncertain of success, they might instead simply kill the organizations so that they could not be used for the benefit of their opponents. In New York, for example, Democrat Martin Van Buren skillfully exploited the award of bank charters, formerly a Federalist prerogative, to build the powerful Albany Regency political machine.11 At the federal level, by contrast, he encouraged President Andrew Jackson to destroy the Second Bank of the United States and move the federal government’s deposits into state banks controlled by their supporters.12 In a very small number of cases, however, something very different happened, and for highly contingent reasons, as we show below for the cases of Massachusetts and New York, competing factions within the elite came to understand that it was better to give up on the effort to control the financial system and open up access to bank charters to everyone.

The political earthquake caused by the state defaults helped spread these hesitant moves toward change and, more importantly, generalized them so that the idea that organizations should

12 The Second Bank was originally dominated by Republicans. By the late 1820s, however, Nicholas Biddle’s efforts to secure the bank’s future had swept him (and the bank) into the anti-Jackson coalition that was coalescing into the Whig Party. Ralph C. H. Catterall, The Second Bank of the United States (Chicago: University of Chicago Press, 1903); Bray Hammond, Banks and Politics in America: From the Revolution to the Civil War (Princeton, N.J.: Princeton University Press, 1957), Chs. 13-14; Robert V. Remini, Andrew Jackson and the Bank War (New York: W. W. Norton, 1967).
be structured by general and impersonal rules came to constitute a new norm for how governments should operate. The result was to bring into being, in Indiana and then elsewhere, what Douglass North, John Wallis, and Barry Weingast have called an “open-access” social order. At the time of the Revolution, no one could imagine that it was possible to structure society in this way. No one could imagine, for example, that it was possible for a society to allow anyone with the resources to form a bank or a corporation to do so without descending into chaos. And, certainly, the new regime was an imperfect one that by no means banished either economic crises or political turmoil. But because legislatures could no longer protect favored incumbents by awarding them monopoly privileges, the economy was inherently more competitive and dynamic—more capable of sustained growth.

Corruption now, moreover, was primarily of the venal sort. Of course, the rich and powerful would continue to try to use the resources at their command to secure advantages for themselves and their organizations. But once the constitutional revisions stripped legislatures of their ability to control who could form an organization and who could make use of the legal forms and tools that made organizations effective, it became easier for opponents to organize against such efforts, and attempts to return to older ways of dispensing rents for the purposes of political domination—that is, systematic corruption—were more readily blocked. What the legislature did was now of vital interest to everyone in the state, and groups would organize and counter-organize in an effort to shape the direction of policy.

Most societies throughout human history have been what North, Wallis, and Weingast call “natural states.” That is, they have been limited-access social orders in which ruling elites

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used the monopoly returns that came from restricting the ability to form organizations to consolidate power. The United States in the period after the Revolution was no different. In the next section, we develop the theoretical foundation for this argument. In the body of the paper, we then offer an alternative narrative of early American history that shifts the spotlight to changes at the state level that brought a radically different order into existence.

**Theoretical Framework**

The federal and state constitutions created in the aftermath of the Revolution were products of a particular view of how the political system worked that scholars have labeled the “republican synthesis.” In the late eighteenth century, republican thinkers in both Britain and North America believed that an activist British government had been corrupted by the King’s ministers. They had a historically specific understanding of how that had happened that focused on Prime Minister Robert Walpole’s systematic use of economic privileges to build a stable political coalition in Parliament in support of the King’s policies. But they also understood that the problem was a more general one—that political factions within the elite would always try to manipulate economic privileges to get control of the polity. Drawing on a larger set of ideas that can be traced back to Polybius and Machiavelli, these opposition thinkers were united in their belief that a mixed and balanced government was necessary for the protection of liberties.\(^\text{14}\)

Americans embodied these ideas about mixed government and separation of powers in

the state and national constitutions they wrote during 1770s and 1780s. The institutional rules
they drafted carry through to the present day and remain durable and powerful influences on the
operation of government. Yet, as we will show, these provisions did little to prevent the
manipulation of economic interests for political purposes during the early years of the Republic.
As factions within the elite competed for power at both the state and local levels in the decades
following the Revolution, they faced essentially the same pressing governance problems that
Walpole had faced earlier in the eighteenth century: how could they hold large enough political
coalitions together to secure control? And they adopted essentially the same solution,
deliberately manipulating the award of economic favors to coordinate their coalitions. Despite
the constitutions’ carefully constructed separation of powers, this “systematic corruption”
threatened to undermine the new republican governments in much the same way as it had
Britain’s mixed constitution. Nor did the more democratic character of these governments
provide much additional protection. If democracy depends on people voting their interest to
discipline the political process, and the political process is able to manipulate those interests,
then the people will vote their manipulated interests. During the period of the Early Republic,
there was swelling popular support for policies that promised to promote economic opportunity,
for example by opening up new lands for settlement, expanding the supply of credit, and
increasing trade. However, government interventions that promoted economic opportunity

15 On the state constitutions, see Marc W. Kruman, *Between Authority & Liberty: State
Constitution Making in Revolutionary America* (Chapel Hill: University of North Carolina
16 On popular support for policies that promoted economic development, see Joyce
Appleby, *Capitalism and a New Social Order: The Republican Vision of the 1790s* (New York:
Case for an Activist Government* (New Haven, Conn.: Yale University Press, 2016). See also
and growth also increased the potential for systematic corruption, and there seemed to be no way to avoid the problem except to foreshadow economic development.

In their study *Violence and Social Orders*, North, Wallis, and Weingast built a general framework for thinking about this kind of corruption and how it might be overcome. Rather than viewing the republicans’ fears as paranoid, the framework explains why their concerns were not only reasonable but represented a clear understanding of how politics and economics usually interact. Starting from a Hobbesian conception of the world, North, Wallis, and Weingast point out that the core problem all societies face is not anarchic, atomistic violence, but organized violence by powerful elites who use coercion against one another. They then ask what kind of social arrangements can limit intra-elite violence and establish a modicum of order, recognizing that violence can never be completely eliminated. The biggest threats to leaders of powerful organized groups are the leaders of other similar groups, but agreements among such leaders are inherently unstable. If one leader agrees to be peaceful and reduces his capacity for violence, the other leaders have an incentive to break the agreement. How can leaders credibly commit to a truce?

North, Wallis, and Weingast’s answer is that the economic returns (the “rents,” in economists’ terminology) that the leaders exploit to keep themselves in power can be a potent incentive to maintain the peace. Take a simple hypothetical example of two leaders, each of whom controls territory and profits from the labor, land, and other resources the territory contains. If the leaders fight with each other, the productivity of the land, labor, and resources they control falls because their clients must stop working and hide or defend themselves. Because fighting is costly, the leaders can reach a credible agreement in which each can see that there is a range of circumstances in which it is in the other’s interest not to fight but, instead, to
honor an agreement to respect each other’s rights to territory. In other words, the leaders can credibly commit to keep the peace because they realize that under a range of circumstances the costs of fighting exceed the benefits. Such a realization does not mean that leaders never fight. The range of circumstances in which the incentives for peace to hold may be quite limited in practice, and leaders may also misjudge the benefits and costs of fighting. Nonetheless, such agreements can create a minimum amount of social order and thus benefit everyone.

North, Wallis, and Weingast call societies structured around such agreements natural states because most societies throughout human history have maintained order in this way. An important characteristic of natural states is that they are governed by “identity rules”—that is, rules that are enforced differently according to the social identities of the persons involved. If there is a dispute between two parties, it matters whether they are both from the elite, from the bottom of society, or from different status groups. Although members of the elite have advantages in such a system, people at the bottom of society can also use the relationships that structure identity rules to secure redress of their grievances. As Laura Edwards has shown in The People and their Peace, if a lower status tenant farmer feels that he has been wronged by his higher status landlord, when he goes to court he does not want impersonal rules to be applied. He wants to be made whole and bases his appeal to the court on the obligations and relationships that higher status land owners have to lower status tenants, as well as on any special, idiosyncratic elements of his own relationship with his landlord.17

The privileges inherent in identity rules are critical to the rent-creating arrangements that hold natural states together. For these arrangements to work, leaders must deny to anyone

outside the coalition the right to form a competing organization that could challenge the members’ monopolies or reduce the returns from exploiting them. To do otherwise—to attempt, for example, to enforce more impersonal rules of access—would mean allowing the rents that make the agreement credible to dissipate, potentially leading it to collapse. Even without such a change, natural states are inherently fragile entities. Any shock to the system that upsets the balance of interests brings with it the potential for conflict. Groups within the coalition inevitably and continuously jockey to increase their share of the rents at the expense of other groups. To the extent that they succeed in this “tyranny,” they can drive those disadvantaged by the maneuvering to revolt, perhaps in alliance with excluded parties. Although the rebels typically justify their uprisings as attacks on corruption and tyranny, they rarely behave any differently when they come to power. Indeed, revolutionaries who take their own rhetoric too seriously risk losing ground to contenders willing ruthlessly to restrict access to organizational rents for the benefit of their supporters. In this sense, the limited-access social order is an equilibrium. Whenever the old order is overturned, the new order that emerges is typically structured along the same general lines.

American republican thinkers, like James Madison and Alexander Hamilton, lived in a natural-state society. It was a wealthy and prosperous society, but not one that had banished the fear of violence and civil war. Having just emerged from a decade of conflict provoked by the belief that Britain’s ruling coalition had abused its power, they deliberately focused their institution-building efforts on creating a system of checks and balances that would reinforce the existing peace by making it more difficult for any particular faction to take control of the national government. In this environment, organizations posed dangerous threats to the social
order, and American political leaders sought to limit their compatriots’ ability to form them.\textsuperscript{18} But they also recognized the value of rent-generating organizations for stabilizing their political coalitions. Although Madison opposed Hamilton’s bill to create the Bank of the United States, when faced with the necessity of chartering a second bank after the War of 1812, he did not scruple to pack its management with political supporters.\textsuperscript{19}

North, Wallis, and Weingast move beyond the limits of this kind of republican thinking by showing that it is possible to order societies in ways that do not rely on the manipulation of economic rents. They contrast natural states with “open-access” social orders governed by impersonal rules in which members can freely form organizations of all types—economic, social, and political—that the government and the larger society will recognize as legitimate and that can operate with the same legal tools as other similar organizations.\textsuperscript{20} Like natural states, open-access social orders are equilibria in the sense that they tend to maintain their structure over time rather than decaying into limited-access societies. To achieve the new equilibrium, however, a society must both grant its members the ability to form organizations at will and govern itself by impersonal rules. If, for example, a government enacts a general law enabling anyone to form a


\textsuperscript{19} Madison also pushed successfully to make William Jones, a Republican, but also an incompetent, president. Catterall, \textit{Second Bank of the United States}, 22; Hammond, \textit{Banks and Politics in America}, Ch. 10.

\textsuperscript{20} Again, it is important to emphasize that we are using the language on ideal types, and that actual open-access societies always feel short of that ideal. For limits on the open-access order of the United States, see Bloch and Lamoreaux, “Voluntary Associations, Corporate Rights, and the State.”
corporation but at the same time retains the power to grant favored groups corporate charters that contain additional privileges, then the general law will be of little avail. Similarly, just declaring rules to apply impersonally is not sufficient. Powerful groups will always seek to increase their advantages by pressuring politicians to grant them privileges not generally available, and it is only when other groups can easily and effectively organize against such efforts that impersonal rules can be maintained over the long run.

How then can a natural state become an open-access social order? There is no clear theoretical answer to this question. North, Wallis, and Weingast posit that natural states can achieve a set of “doorstep” conditions that make such a transition more likely, but it is still by no means inevitable. The U.S. had achieved these doorstep conditions by the early nineteenth century, but neither the checks and balances embodied in the federal and state constitutions, nor the increasingly democratic character of the franchise, provided a clear path to open access. To the contrary, in the early republican period not only could elite factions still use their privileged access to organizational rents to control the government, but the greater uncertainty about maintaining power they faced as a result of these developments gave them all the more incentive to try. At the same time as democratic political competition increased the imperative to use economic privileges to reward supporters and punish opponents, however, it also created the conditions under which elites might realize that it was in their interest to relinquish control of such tools in order to prevent their rivals from using them. In the next section, we trace the first steps toward open access in Massachusetts and New York, where controversies over the exploitation of bank charters for political ends induced elites to pull down political barriers to entry.
Banking and the Beginnings of Open Access

Alexander Hamilton’s efforts to use the Bank of the United States, in combination with the assumption of state debts, to build an elite coalition in support of the national government is well known. What is perhaps less well known is that political leaders at the state level pursued similar goals, strategically awarding bank charters to political allies to ensure their support while denying similar boons to opponents. In this section we focus on conflicts over the award of bank charters in New York and Massachusetts. Both states had structured the constitutions they wrote during the Revolutionary era to prevent the recurrence of tyranny by means of checks and balances and a separation of powers. In both, however, Federalist political leaders controlled essentially all the early financial institutions, and in both political competition intensified the exploitation of these institutions for political ends. Ultimately, the result in both states was a move toward open access, but there was nothing inevitable about this shift, and it occurred in the two places in very different ways. Moreover, although some states followed the Massachusetts and New York examples, most did not open access to bank charters until much later. Nonetheless, the developments in Massachusetts and New York were important because they demonstrated the feasibility of open access in the case where it was most suspect. Incumbents could and did claim that excessive entry into banking would undermine the stability of the

22 See the 1777 New York Constitution, Articles 2 and 3, and the Massachusetts 1780 Constitution, Part the Second, Chapter I, Section I, Articles I and II. More generally, see Kruman, *Between Authority and Liberty.*
financial system, and the Massachusetts and New York experiences made those kinds of charges less sustainable.

The Bank of New York was organized in 1784 by Hamilton and other Federalist leaders. Although it did not receive a charter from the legislature until 1791, its close connections with the state’s ruling coalition enabled it to block all efforts by rival political groups to found their own banks until 1799, when Republican Aaron Burr cleverly exploited a loophole in the charter for a water works to start the Manhattan Bank.23 Burr’s allies later credited the new bank with the destruction of the Federalist “empire,” crowing that it “emancipated hundreds who were held in bondage by the old institutions.” However exaggerated that claim, there is no question that Republicans made deliberate use of the Manhattan Bank to further the fortunes of their candidates, offering supporters accommodation in reward for their loyalty.24 As Brian Murphy has shown, moreover, the Federalists responded in kind by denying credit to Republican merchants. Previously, Federalist merchants had enjoyed privileged access to credit at the Bank of New York (and also the New York branch of the Bank of the United States) by dint of their control of these institutions, but until 1799 both banks had discounted commercial paper presented by other traders. Now they refused to accept notes from Republican merchants, underscoring the Republicans’ need for their own financial institutions.25 Not surprisingly, therefore, when the Republicans gained control of the New York legislature a few years later in

23 Hilt, “Early American Corporations and the State.”
1803, they took the opportunity to found a bank for their followers in Albany. At the same time, they refused to grant a charter to a new Federalist bank in New York, to be called the Merchants’ Banks, and when the bank went into operation anyway without a charter, passed a restraining act prohibiting any association from operating as a bank without a charter and giving the Merchants’ Bank a year to wind up its affairs. Although a Federalist resurgence enabled the bank subsequently to secure a charter, the restraining act remained in place and henceforth enabled the legislature strictly to control entry into banking.  

In Massachusetts, a similar dynamics shaped the early development of the banking system. The first bank in the state, the Massachusetts Bank, was chartered in Boston in 1784 as a monopoly that would serve the interests of the government as well as the Federalist elite who dominated state politics. However, the bank was too small to meet the demands for credit of all the Federalists that needed to be kept in the coalition, so to maintain their loyalty the legislature chartered a small number of additional banks. By the turn of the century most Massachusetts cities were home to one or two local banks, invariably controlled by Federalists. Members of rival political groups clamored for banks of their own but to no avail. For example, Salem had two banks, both run by Federalists. A number of the city’s prominent Republican leaders, including George Crowninshield, who would become Madison’s Secretary of the Navy, and Joseph Story, the future U.S. Supreme Court Justice, sought to start a bank, but their petitions for a charter were repeatedly denied.


Over the first decade of the nineteenth century, the Republicans steadily gained in political strength in Massachusetts until in 1811 they won control of both houses of the legislature as well as the governorship. Moving immediately to capitalize on their victory, they founded two new banks. One was in Salem, and Crowninshield became its first president and Story its second. The other, in Boston, was a massive new institution with a capital of $3,000,000, three times that of the largest bank that had to that time been chartered in the commonwealth. Named the State Bank, it was ostensibly a public institution: At least one third of its capital was supplied by the government; it would return a portion of its profits to taxpayers in the form of dividends on the state’s ownership share; and it would pay an annual tax to the state amounting to 0.5 percent of its paid-in capital. However, the fact that eleven of the State Bank’s twelve directors were Republicans suggested that the bank would also operate in the interests of that party.

The Massachusetts Republicans were not content just to found their own banks; they also sought to inflict real harm on the Federalists. All but one of the existing banks’ charters were set to expire in 1812, and Republican legislators vowed to block their renewal. They were not able to make good on this threat, however, because the Federalists retook the lower house and the governorship in 1812. The result of this political shift back toward the Federalists was something


28 Dennis, The Merchants National Bank of Salem, 57.

29 Lu and Wallis, “Banks, Politics, and Political Parties.” The Republicans took a variety of other steps to entrench themselves in power, including famously redrawing the state’s senatorial districts (giving rise to the term “Gerrymandering” after the Republican governor who signed the bill into law). See Elmer Cummings Griffith, The Rise and Development of the Gerrymander (Chicago: Scott, Foresman and Co., 1907), 19-20.
of a compromise. The act chartering the State Bank had provided that its terms, including the tax on capital, would apply to all banks chartered in the future. With the Republicans still in control of the Senate, this condition held. The Federalists got their banks rechartered but only on condition that all would be subject to the same constraints as the State Bank.30

In the context of the increasing competitiveness of state elections, this close brush with nonrenewal seems to have led politicians of both parties to rethink their coalition-building strategies. Although there is no “smoking gun” in the historical record, it seems that legislators agreed at least implicitly to take banking off the political table. Although few new banks were chartered during the turbulent war and depression years that followed, when economic conditions improved during the early 1820s and the demand for bank charters increased, the legislature responded by granting most of them. All of the new banks paid the 0.5 percent tax on their capital, and surely the state’s soaring tax revenues helped reinforce the new arrangement. In 1830, the first year for which data is available, the tax on bank capital accounted for fully 61 percent of the state’s revenue. Indeed, thanks to the bank tax, Massachusetts did not have to impose any property or poll taxes on its citizens in half the years between 1826 and 1855.31

What mattered most for the long run, however, was maintenance of the commitment that

30 Lu and Wallis, “Banks, Politics, and Political Parties.” In fact, the deal went even further and gave all the banks charters that (except in the details of their location and capital stock) were identical to that of the State Bank. See the Laws of the Commonwealth of Massachusetts from February 28, 1807, to February 27, 1813 (Boston: Thomas and Andrews, 1813).
all bank charters would henceforth be the same. This agreement was made formal in 1829 when the legislature enacted a general regulatory act for banking. Entitled “An Act to Regulate Banks and Banking,” the statute specified “[t]hat from and after the passing of this Act, every Bank which shall receive a Charter, from or by the authority of this Commonwealth, and every Bank whose Capital shall be increased, or whose Charter shall be extended, shall be governed by the following rules, and subjected to all the duties, limitations, restrictions, liabilities and provisions, contained in this Act.” The clincher was section 31: “Be it further enacted, That if, during the continuance of any Bank Charter, granted or renewed under the provisions of this Act, any new or greater privileges shall be granted to any other bank now in operation, or which may hereafter be created, each and every Bank in operation at the time shall be entitled to the same.”

From this point onward, whenever the Massachusetts legislature considered chartering a new bank or changing the charter of an existing bank, every bank in Massachusetts was potentially affected. There would no longer be special deals for any individuals or groups forming banks.

This is not to say that bank charters were never again a hot-button political issue in Massachusetts, just that charters were no longer reserved for the support of one elite political coalition and denied to others. As a way of limiting competition, incumbents from both parties pushed the idea that chartering too many banks would undermine the soundness of the banking system, a position that appealed as well to those hostile to the idea of banks more generally. In some years the anti-bank view won out, and the legislature refused to grant any more requests for charters. But the logjam usually burst the next year with a surge of approvals. By the height of

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32 “An Act to regulate Banks and Banking,” Laws of the Commonwealth of Massachusetts, Passed by the General Court, at their Session, Which Commenced on Wednesday, the Seventh of January ... (Boston: True and Greene, 1929), 144-161 at 144-145 and 160-161.
the 1830s boom, there were nearly 130 banks in the state, and Massachusetts’ citizens were better served by banking institutions—that is, there was more bank capital and more currency per capita in the state—than anywhere else in the United States except Rhode Island (which had adopted a similarly liberal chartering policy).\(^\text{33}\)

Increased political competition played out somewhat differently in New York. As in Massachusetts, power shifted from the Federalists toward the Republicans on the eve of the War of 1812, and the latter took advantage of the opportunity to charter additional banks for their supporters. Unlike in Massachusetts, however, the Federalists never regained control of the state government. Instead, during the so-called Era of Good Feeling that followed the collapse of the first party system, Martin Van Buren’s faction of the Republicans used its power over bank charters and other sources of patronage to build a formidable political machine, dubbed by opponents the Albany Regency.\(^\text{34}\) Although from time to time chinks appeared in the machine’s dominance, the Van Buren faction was able to maintain control of the banking system and use it to consolidate its position. For example, in 1824 and 1825 the Regency lost control of the legislature to a competing faction known as the “People’s Party,” which proceeded to charter several new banks and a number of loan companies. The latter financed their operation through the issue of post notes, payable at a fixed future date rather than, like banknotes, redeemable on


demand. The result was a rapid expansion of credit followed by a crash in 1826. The financial crisis reinforced incumbent bankers’ claims that an uncontrolled expansion of banking would undermine the system’s soundness. When Van Buren’s faction regained power, the legislature temporarily put the brakes on new charters while it passed a co-insurance scheme call the Safety Fund. This new law imposed a tax on bank capital to be paid into an insurance fund to protect holders of banknotes in the event of failures. Thus when the Regency began again to award charters to their supporters, they came with a “Good Housekeeping Seal of Approval.”

During the economic boom of 1830s the New York legislature received on average about 70 petitions for banks a year, but under the machine’s tight control only about ten percent of that number received charters. Not surprising, the large number of rejections helped fuel political opposition. When, despite the Safety Fund, the Panic of 1837 brought down the banking system, the Albany Regency collapsed as well. The opposition (now called the Whig Party) met the pent-up demand for charters and, at the same time took steps to insure that the Regency would never again be able to use bank charters for political purposes, by passing New York’s innovative free banking law in 1838.

To counter worries that open access to banking would undermine the soundness of the system, the legislature added an important regulatory provision to the act that required banks fully to back their currency issues by investing in specific categories of (mainly New York) government bonds. The result was a dramatic expansion in the

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number of banks, a decline in the number of bank failures, and an improved market for the state’s debt.\textsuperscript{37}

Free banking was not, it must be emphasized, a solution to the problem of instability in banking. Indeed, the history of bank regulation begins, not ends, with the achievement of open access. It was only when entry into the financial sector was reasonably free of political manipulation that policy makers could begin to grapple with the structural characteristics that periodically produce crises in fractional reserve banking systems. Free banking made the financial sector more competitive so that it better served the country’s needs, but only the rich had the resources to found banks so it tended to reproduce existing inequalities in the distribution of wealth. Nor did free banking eliminate the power that large financial interests exerted in the political arena. As the response to the recent financial crisis has demonstrated, what nineteenth-century commentators decried as the “moneyed interest” would continue to exercise a major influence over the formation of regulatory policy, including which banks should be deemed “too big to fail.”

What free banking did change was the ease with which access to bank charters could be used by elites to form sustainable coalitions to dominate the political process. This manipulation of the economy for political purposes—systematic corruption—did not arise because bankers were rich, powerful, and able to use their influence to secure political favors. Rather, it resulted from the discretion that politicians had over who could operate a bank. Nor was this potential for corruption unique to the banking sector. Control over access to other valuable economic activities could be (and was) used for similar ends. States would finally begin to confront these

\textsuperscript{37} In 1837 Michigan had adopted a free banking act without this backing provision to disastrous results. See Hilt, “Early American Corporations and the State.”
more general sources of corruption in the 1840s in the aftermath of a crisis in their public finances. When they did, free banking would spread across the country so that by 1860 almost all Northern states had laws modeled on New York’s, as did several Southern states.38 There would also be much more fundamental changes in the way politics and economics worked.

The Political Earthquake of Fiscal Crisis

The control of bank charters was a highly charged political issue in the early nineteenth century, but it was not, it must be emphasized, an issue that clearly distinguished the two major parties that emerged in the 1830s. Although the Federalists had dominated the first banks, by the time of the second party system the situation was completely different. In New York, as we have seen, it was the Democrats who firmly controlled access to charters, despite Jackson’s outspoken antipathy to banks, and it was the Whigs who would institute free banking when they finally came to power after the panic of 1837. In Massachusetts, access to banking had been effectively opened up by the 1820s, and as a result, elites from both parties were deeply implicated in the expansion of the banking system that occurred over the next two decades. Although the panic gave the Democrats control of state government for a time (they had campaigned on an anti-bank platform), the party’s elected officials had little room to maneuver on the issue because the institutions that were in the worst shape financially were their own—the so-called “pet” banks that had received Democratic largess in the form of federal deposits removed from the Second Bank of the United States.39

The politics of internal improvements was very much the same. Everywhere it was partisan, but nowhere did party positions emerge that were consistent across states or levels of government. Politicians everywhere sought to respond to constituents’ desire for improved transportation, yet they were also concerned that the resulting economic benefits could be manipulated by another faction for partisan advantage. As a consequence, the positions they took on this issue depended on who was in power and how well entrenched. At the national level, of course, Jackson opposed Henry Clay’s plan to provide federal support for internal improvements, vetoing legislation to fund the Maysville Road. At the state level, however, it was the Democrats who pushed through public funding for canal systems in New York, Pennsylvania, and Ohio, whereas it was the Whigs who did the same in Indiana.⁴⁰

Because canals were hugely expensive, financing them subjected the political system to enormous stress. The banks chartered by New York, Massachusetts, and other Northeastern states during this period did not require public funds to establish, and they had little or no economic impact beyond the towns in which they were founded.⁴¹ The same was true of the local turnpike projects that many states chartered around the same time.⁴² Thus banks and roads

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⁴¹ As our discussion of the State Bank of Massachusetts indicated, state governments did sometimes invest funds in early banks, but in the Northeast banks could be, and mostly were, established without public investments and the practice had largely ended by the 1820s. As Howard Bodenhorn has argued, the practice may have been more for the states’ benefit than for the banks’. See State Banking in Early America, 84-85.

⁴² Daniel B. Klein and John Majewski, “Turnpikes and Toll Roads in Nineteenth-Century
in, say, Rochester, New York, had little consequence for residents of, say, Binghamton, New York, and legislators from the latter city had no interest in blocking them unless they were likely to strengthen a rival coalition. Canal projects, by contrast, required millions of dollars of state investment. Regardless of the larger interests of their coalitions, legislators would not support them unless their own constituents stood to benefit; they did not want to tax their supporters for projects that advantaged other districts. To secure passage, therefore, promoters typically loaded up their proposals with enough secondary transportation projects to benefit a majority of districts.43

Canal projects that were expensive to begin with got even more expensive as a result. To raise the necessary funds, the states that undertook them borrowed heavily in international capital markets, sometimes levying taxes to service the debt but sometimes not.44 Not surprisingly, when economic conditions began to sour 1839, they found themselves in serious financial difficulty. Fully eight states (Arkansas, Illinois, Indiana, Louisiana, Maryland, Michigan, Mississippi, and Pennsylvania), plus the territory of Florida, defaulted on their debts in the early 1840s, and a number of other states, including New York, Massachusetts, Ohio, and South Carolina, teetered on the brink of default.45

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44 Wallis, “Constitutions, Corporations, and Corruption.”

45 Wallis, “Constitutions, Corporations, and Corruption.” The Southern states often intermixed transportation projects with borrowing for the support of plantation banks, with the same disastrous consequences. See Bodenhorn, *State Banking in Early America*, Ch. 9; and Larry Schweikart, *Banking in the American South from the Age of Jackson to Reconstruction*
In the political crisis that ensued a number of states rewrote their constitutions in fundamental ways. The revisions aimed, first of all, to prevent such crises from recurring by imposing procedural restrictions on future borrowing. But they also reshaped the way government worked. For the first time, voters began to see their states’ troubles as part of the more general problem of systematic corruption, and they moved to strip their legislatures of the ability to award special privileges. The first step in most places was to mandate that corporations be chartered under general laws (Table 1). A few states went further, however, and banned all types of private and local legislation (Table 2). As Figure 1 shows, most of states that initially restricted the mandate for general laws to corporate charters later extended it to all types of bills, and most other states followed by adopting both kinds of restrictions at the same time.

We focus our discussion of this transformation on Indiana because it was the first state to go through the full set of changes. As we will see, delegates to the constitutional convention held in the aftermath of the default explicitly connected the dots between the system of private bills and the financial crisis, and they deliberately and systemically transformed their government to prevent any recurrence of the crisis. They were able to connect the dots because the transportation projects that bankrupted the state had been put together in a particularly transparent and aboveboard way, laying bare for all to see the ways in which voters’ interests had been manipulated to enable the deal to go through.

Indiana was a big state with lots of rich agricultural land far from existing waterways. There had long been interest in a canal that would bisect the northern half of the state and make

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commercial production feasible in that region, but political leaders had faced the usual problem that residents in other regions of the state were not willing to support transportation projects from which they did not derive direct benefits. Farmers in the southern counties along the Ohio River were particularly opposed. They already had good access to transportation and did not want to pay taxes to improve the commercial prospects of farmers in the north.46

Political leaders solved this problem in two ways. First, they revised the tax system by shifting from a per-acre to an ad valorem system and by taxing all kinds of property—not just land. This revision insured that those who benefited most from the transportation system in terms of higher land values would pay the most for the improvements. Because the tax base would also grow, however, farmers with valuable land along the Ohio River were not expected to see their taxes increase.47 This change in the tax structure would have been perfectly appropriate under a system of general laws. However, it was not in itself sufficient to secure approval of the canal project, because voters who did not directly benefit had trouble believing that their taxes would not rise. Promoters, therefore, had to increase the scale of project until the expected improvements benefited most of the districts in the state. The resulting plan was called the Mammoth Internal Improvement Bill, and it deserved that name. As Figure 2 shows, it encompassed a massive system of canals, railroads, and turnpikes that crisscrossed the state with a total projected cost of more than $10 million. The bill was shepherded through the legislature by the Whigs, who controlled both houses of the legislature, as well as the governorship, but it attracted substantial Democratic support as well, and passed in January 1836 by overwhelming

46 For overviews of this history, see Carmony, Indiana; and Logan Esarey, History of Indiana: From Its Exploration to 1850 (Indianapolis, Ind.: W. K. Stewart, 1915).
majorities. The success of the bill was the result of a transparent, though nonetheless deliberate, manipulation of economic interests to build a broad coalition in support of the project.48

The bill created a new Board of Internal Improvement and authorized it to borrow up to $10 million in 5 per cent bonds, secured by the good faith and credit of the state. At the time, Indiana’s annual revenues amounted to just about $60,000—a full order of magnitude smaller than the $500,000 per year that would be needed just to service the debt. The plan was not quite as crazy as these numbers might make it seem, however. Indiana officials had good reason to expect that tax revenues would more than double by the early 1840s, even if the transportation projects did not generate any additional revenues for the state. The enabling act that Congress had passed in 1816 for Indiana’s statehood required it to forbear taxing any land sold within its bounds by the federal government until five years after the date of sale. In 1834, slightly more than 4.5 million acres of land were subject to state taxes. In 1835 and 1836 the federal government sold an equivalent amount of additional acreage within the state, so Indiana officials could reasonably forecast that tax revenues would at least double by the early 1840s. In fact, the amount of land that Indiana could tax increased to more than 10 million acres by 1841 and to more than 14.5 million acres in 1843. Second, Indiana officials expected, as a result of the new ad valorem tax system, that revenues would increase with land values in the areas with improved access to markets. Between 1835 and 1837, the average value of an acre of farm land in Indiana increased from $5.41 to $9.87, and the rise in the value of town lots was even steeper. Most of the increase, moreover, was in counties projected to benefit from the transportation projects.

Land values in counties without a transportation improvement rose on average by $2.74 an acre

48 Wallis, “The Property Tax as a Coordinating Device”; Esarey, History of Indiana, Ch. 16; Carmony, Indiana, Ch. 4.
during the boom years of 1835 to 1837, compared to $4.55 per acre in counties where there would be an improvement and $8.29 in counties where the proposed transportation routes would intersect (mainly counties with larger towns).  

These expectations depended, of course, on everything continuing to go well—on the economy prospering, on the transportation projects being completed, on settlers migrating to the lands with improved access to markets, on land values increasing. But all did not continue to go well. To the contrary, a major financial crisis in 1839 prevented the state from raising funds on the international bond markets, bringing construction to an abrupt halt. With the transportation projects in abeyance, property values, which had risen speculatively on the expectation of improved access to markets, plummeted, and so did tax revenues—from about $300,000 in 1840 to about $170,000 in 1841. Unable to continue to pay the interest on the bonds it had already issued, the state was forced to default.  

Indiana, along with several other states, had used the Morris Canal and Banking Company as an intermediary to sell their bonds, and the proximate cause of the state’s embarrassment was the Company’s failure to honor its obligations. Indiana officials had given the Morris Canal Company millions of dollars in bonds on credit to market on its behalf (the exact amount is uncertain) in exchange for a promise to pay the state $500,000 every six months until the debt was paid off. State officials found the deal attractive because they needed an agent to market the bonds internationally on their behalf, and they did not need all the funds from the sale of bonds at once. They seem to have been somewhat naïve, or perhaps corrupt, however, because it became apparent later that the state was liable for interest on the full amount of the

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49 Wallis, “Property Tax as a Coordinating Device.”
bonds, even though it had only been paid for part of them. The state had relied on the bank’s semiannual payments to finance construction, moreover, so work on the transportation system had to cease.\textsuperscript{51}

The collapse of the internal improvement scheme threw the state into political turmoil. The Whigs had dominated Indiana’s government during the 1830s. The Mammoth Internal Improvement bill was their doing, and blame for the state’s problems now fell on them, even though many Democrats had supported the legislation. The crisis gave the Democrats control of the lower house in 1841 and 1842 and then both houses of the legislature and the governorship in 1843. National controversies associated with the Mexican War, the annexation of Texas, and westward expansion of slavery helped the Whigs regain some ground in the mid-1840s, and the Democrats were not able to maintain their dominance of state government. With no party in clear control of legislature, proposals to get the state’s finances back on track languished, though in 1847 the assembly finally managed to ratify a compromise worked out with bondholders. By then, Democrats were making increasingly insistent calls for a constitutional convention to fix the problems with state government. When they regained control of the legislature in 1848, the effort succeeded, and the elections for delegates gave the Democrats a supermajority of two thirds at the convention.\textsuperscript{52}

One outcome of the convention was a constitutional ban on further borrowing by the state, except under a limited set of circumstances: “To meet casual deficits in the revenue; to pay the interest on the State debt; to repel invasion, suppress insurrection, or, if hostilities be threatened, provide for public defense.”\textsuperscript{53} Given the state’s fiscal troubles, one might think such

\textsuperscript{51} Wallis, “What Caused the Crisis of 1839?”; Esarey, \textit{History of Indiana}, Ch. 16.
\textsuperscript{52} Carmony, \textit{Indiana}, Ch. 6.
\textsuperscript{53} Article X, Sections 1 and 5.
a measure to have been the central goal of many of the delegates. However, even a quick glance at the convention’s proceedings suggests that the representatives had a more systematic understanding of what had gone wrong in their state and a bigger sense of what they wanted to accomplish. From the very beginning, the prohibition on borrowing was fairly far down on the lists of revisions proposed by the delegates. The first list submitted, for example, had it only fifth, after proposals mandating “that corporations shall be created under a general law” (2), “that special legislation shall be prohibited” (3), and “that the Legislature shall be prohibited from granting divorces” (4).\(^54\) Other resolutions submitted at the start of the constitutional convention had similar orderings of priorities, and among the standing committees set up to draft the new constitutions there were, in addition to those dedicated to review each branch of government, committees “On Special and Local Legislation, and Uniformity of Laws,” “On Currency and Banking,” “On Corporations other than Banking,” as well as on “On State Debt and Public Works,” and “On Finance and Taxation.”\(^55\)

This preoccupation with special legislation was a new political development that followed the defaults, but it did not come out of the blue in 1851. When a constitutional convention was first seriously proposed in 1846, banning private bills was among the list of desired revisions already being discussed in public meetings around the state.\(^56\) Moreover, it was the focus of repeated remarks by the Democratic Governor James Whitcomb, who declared in his 1848 address in favor of a constitutional convention that banning special legislation was such


a pressing issue that “[i]f calling a Convention to amend the Constitution were productive of no other result, than furnishing an effectual remedy for this growing evil, it would be abundantly justified.” Governor Paris C. Dunning echoed these remarks the next year when he announced the results of the referendum on a constitutional convention. “Special legislation,” he proclaimed, “is a growing evil which has attracted much attention amongst the masses of people, and to which much well founded opposition exists in the public mind.”

Speeches on the floor of the convention linked the state’s fiscal debacle to the problem of special legislation. Thus one delegate asserted that the proposed constitutional revisions would bring an end to “this special and local legislation that has … heaped upon us burdens of taxation for no good purpose.” Another argued that the influence that “corporations and combinations of wealthy men” exerted on the legislature “to secure special privileges and partial legislation” made it necessary to “have it explicitly declared in our organic law” that the legislature had no unilateral power to contract a state debt. Some delegates were more specific about how the connections worked. “The evil of vicious legislation under which we are now suffering,” one declared, “has arisen from local legislation.” It was important “to break up this system of legislation, and with it the log-rolling by which it was ever sustained” so that “combinations of local interests, which have heretofore been made, cannot … be entered into with any degree of success.” Another explained that the volume of special legislation, in combination with log-rolling, meant that “bills have often been passed through the General Assembly without being

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once read, without their true character being understood.” In this way, the delegate continued, powers “have been given to corporations which ought not to be intrusted [sic] to any man or set of men.” The new constitution would “prevent such evils, by providing that corporations shall exist only under general laws, which must be enacted deliberately, with the consent of not less than a majority of all the members to the House …”62

The proposal to ban all local and special legislation had widespread support at the convention. Almost no one spoke against it, and it passed overwhelming on the third reading by a vote of 116 to 13.63 The only real debate was over whether the constitution should simply state that “the General Assembly shall not pass local or special laws” or whether it should enumerate the kinds of special laws that would be prohibited.64 In the end, it essentially did both, listing nearly a score of specific types of special legislation that would be banned but also mandating that “in all other cases where a general law can be made applicable, all laws shall be general and of uniform operation throughout the state.”65 Once the constitution was ratified, moreover, there was no going back. The Democrats dominated the legislature during the next couple of sessions, and they got to work revising the statutes and enacting general laws where needed. When the new Republican Party got control of the lower house in 1855, its leaders tried to amend the constitution in a number of ways, including restoring some ability to enact local legislation. But the effort did not even succeed in the House.66

64 See Indiana, *Report of the Debates*, Vol. 2, 1768-1769. There was also debate over whether the ban should be accompanied by a decline in the number of legislators and a shift from annual to biennial or even triennial sessions.
65 Indiana Constitution of 1851, Article IV, Sections 22 and 23, and Article XI, Section 13.
There were, of course, plenty of charges of venal corruption in the aftermath of the crisis. But the catastrophe could not so easily be explained away. The Mammoth scheme had generated widespread enthusiasm. Although the Whigs were in charge of the statehouse, many Democrats had supported the plan. As one delegate to the 1851 convention reminded the others, news of the bill’s passage had been greeted with fireworks displays around the state. In Indianapolis “there was a general rejoicing; every pane of glass in the city was illuminated; and the population turned out on the streets as upon a great holiday.” The economic interests of voters had been manipulated in a systematic way to build a coalition in support of the project. Even though all of the manipulation was transparent, above board, and legal, the scheme’s catastrophic failure showed how easy it was for democratic institutions to be perverted to produce bad outcomes, checks and balances notwithstanding. Preventing the state from borrowing in the future was not enough. The logrolling that had produced the Mammoth bill thrived in an environment where special and local bills predominated—where no one was paying attention to the big picture. That environment had to be changed.

Other states that defaulted on their debts, or that came close to defaulting in the early 1840s, went through similar political upheavals at about the same time. Four of the other states that defaulted (Illinois, Louisiana, Maryland, and Michigan) wrote new constitutions in the late 1840s or early 1850s, as did two others with high levels of debt (New York and Ohio). All of these new constitutions included measures to prevent similar financial troubles in the future. None went as far as Indiana’s and prohibited the state from borrowing except under extraordinary circumstances; instead, the revisions typically instituted safeguards that required

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67 For an account that relies on such charges, see Esarey, *History of Indiana*, Vol. 1, Ch. XVI.

taxes to be levied to service the bonds and the resulting package to be submitted to voters in a referendum.\textsuperscript{69} All of these constitutions also included provisions prohibiting legislatures from chartering corporations except by general laws (see Table 1). Political discontent about the award of special corporate privileges to a favored few had reached the boiling point, and voters took the opportunity to rid their states of this form of legislative corruption and source of inequality.

Even states that did not rewrite their constitutions during this period (even those largely free of financial crisis) were affected by this discontent, and most responded by enacting their first general incorporation laws for business corporations. Although only four states had general incorporation laws for manufacturing in force in 1840, twenty-seven (all but six) had enacted them by 1860.\textsuperscript{70} Without constitutional bans on special charters, however, these statutes did little to prevent legislatures from continuing to dispense privileges to their supporters. Moreover, so long as business people feared that rivals might secure better terms from the legislature, they avoided organizing under the general laws and instead sought special charters for themselves. Five years after the passage of Pennsylvania’s 1849 general law for manufacturing, for example, less than a dozen companies had incorporated under it. Yet in 1855 alone the legislature passed 196 private bills chartering or amending the charters of for-profit business corporations.\textsuperscript{71}

\textsuperscript{69} These measures dramatically reduced levels of state borrowing. See, Wallis, “Constitutions, Corporations, and Corruption.”
\textsuperscript{71} Hartz, Economic Policy and Democratic Thought, 40. For the statutes, see Pennsylvania, Laws of the General Assembly (Harrisburg: A. Boyd Hamilton, 1855). See also George Heberton Evans, Jr., Business Incorporations in the United States, 1800-1943 (New York: NBER, 1948); and Susan Pace Hamill, “From Special Privilege to General Utility: A
Not until state constitutions banned special charters did significant number of companies turn to the general laws, and only then did the overall number of corporations begin to soar. Some idea of the brake on the economy imposed by the special charter system can be obtained by comparing the number of incorporations in Ohio, which banned special charters in 1851, with those in New Jersey and Pennsylvania, which did not take that step until a little more than two decades later. In the ten years following the Civil War, Ohio chartered 2.2 times as many corporations under its general law as New Jersey did under both general and special laws. After New Jersey banned special charters in 1875, the gap began to close. During the 1880s (that is, before New Jersey’s liberal revision of its general incorporation law set off a race to compete for out-of-state corporations), the ratio of new corporations in Ohio relative to New Jersey fell to 1.5, at the same time as the numbers of corporations founded in both states rose dramatically. Although there are gaps in the data for Pennsylvania, the story there seems to have been much the same, with the number of corporations converging on the number in Ohio only after the imposition of the ban on special charters in 1874. More generally, George Heberton Evans’ count of the number of new corporations in the United States shows a tremendous surge following the spread of mandatory general incorporation in the last third of the nineteenth century.

Most of the states that banned special charters in the 1840s and 1850s took longer to prohibit other kinds of private or local laws. Nonetheless, the concerns that led Indiana’s delegates to forbid such legislation echoed worries that were already being expressed elsewhere.


72 Evans, *Business Incorporations in the United States*, 12, and Appendix 3

When Governor Whitcomb spoke about the problem of local and special legislation in his annual message to the Indiana legislature in 1848, he called attention to the recent (1846) constitutional convention in New York, where, he asserted, “[t]he subject has been deemed of so grave importance that the constitution …, as lately amended, has a provision against this evil engrafted in it.”74 New York’s revisions were much more limited than those that Indiana adopted a few years later. Article 1, Section 9 required a two-thirds vote of each branch of the legislature to appropriate “the public moneys or property for local or private purposes”; and Article 3, Section 16 stipulated that “No private or local bill, which may be passed by the Legislature, shall embrace more than one subject, and that shall be expressed in the title.”75 These measures were not sufficient to eliminate the evil, however, and in 1874 New York adopted a constitutional amendment similar to Indiana’s.76 Further evidence that the debacle was changing norms about what legislatures should do comes from the constitutions written by new states later in the decade. Both Oregon (1859) and Kansas (1861) entered the union with constitutions that banned special and local laws (see Table 2). Moreover, most Southern states adopted similar prohibitions when they rewrote their constitutions during or after the Civil War. Pennsylvania and New Jersey proscribed private and local laws at the same time as they revised their fundamental law to ban special charters of incorporation (in 1874 and 1875 respectively). Most of the remaining holdouts soon followed suit, and all of the new states admitted to the union in the late nineteenth and early twentieth centuries included such bans in their constitutions (Table 2). As Charles Binney, author of the first legal treatise to analyze these restrictions, observed in 1894, “as time went on not only was the volume of special and local legislation needlessly

75 See the New York Constitution of 1846.
76 See Amendment 9 to New York’s 1846 Constitution.
increased … but private schemes were often pushed through the legislatures by unscrupulous men, to the sacrifice of public interests ….” The result was “the growth of a very general feeling of hostility to all local and special legislation. One State after another sought, by changes in its Constitution, to check the excesses into which its legislature had fallen in this respect, and the influence of the example so set is seen in the Constitutions of all the more recently organized States.”

Conclusion

Limited government occupies a prominent position in how Americans view themselves and their history. Debates over the powers enumerated in the federal constitution and the structure of checks and balances, both horizontally within national and state governments and vertically between the national government and the states, have given a concrete reality to our notions of “limits.” These limits are fine and good, but they are not the only ones that matter, and perhaps they are not even the most important limits. Neither the checks and balances inscribed in the federal constitution nor those imbedded in the early state constitutions prevented elite factions in government from manipulating the economy for political purposes. To the contrary, their initial response to the resulting uncertainties of power was to create and deploy economic privileges for precisely this end. Only in the 1840s and only at the state level would Americans reduce the opportunities for this kind of systematic corruption. They would do this by imposing on legislators a new kind of limit—the requirement that laws had to be general and impersonal—so that the favored few would no longer be able to write their own rules.

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77 Charles Chauncey Binney, Restrictions upon Local and Special Legislation in State Constitutions (Philadelphia: Kay & Brother, 1894), 6-7.
These changes did not, of course, eradicate corruption. Economic interests would always attempt to sway the course of policy in whatever directions they favored. That was venal corruption, and it would always be with us. Nor did the changes eliminate inequality. General laws did not prevent discrimination against minorities, elites did not disappear, and the distribution of income and wealth continued to be skewed toward the rich. However, elites now operated in a much different environment, an environment characterized by what Joseph Schumpeter called creative destruction.78 New firms could freely enter a wide range of economic activities (including banking) with the full legal and organizational support of the state; they could challenge existing enterprises; they could force resources to be reallocated from old low-value to new high-value uses. And new organizations could challenge the political and social hegemony of those associated with seemingly well entrenched elites.

The full sweep of these changes could not have been anticipated by mid-nineteenth-century Americans, because no one had yet lived in the kind of open-access society that enabled such a high degree of economic and social flexibility. They were the unintended consequences of a set of institutional reforms that Americans adopted to solve pressing problems with the institutions they had inherited from the Revolution. But although mid-nineteenth-century Americans were still grappling with the problems of the past, the reforms they embraced were emphatically not simple extensions of the republican ideas that shaped the first constitutions. Quite the contrary. Instead of attempting to limit and control the organized interests the framers had found so threatening, Americans now encouraged and empowered them—gave everyone the ability to found them. The new order that emerged was a society of contending organizations,

some able to muster massively greater resources than others, but none unable to forestall the emergence of new organized challengers.
Figure 1. Comparison of Dates of General Incorporation and General Law Provisions, by State
Figure 2. The Mammoth System of Internal Improvements

Table 1. Year in which a state first banned special charters of incorporation, sorted by year of provision

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