

# The Institutional Dynamics of Early Modern

## Eurasian Trade:

### The *Commenda* and the Corporation

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**Abstract:**

The focus of this article is on legal-economic institutions that organized early-modern Eurasian trade. It identifies two such institutions that had divergent dispersion patterns, the corporation and the *commenda*. The corporation ended up as a uniquely European institution that did not migrate until the era of European colonization. The *commenda* that originated in Arabia migrated all the way to Western Europe and to China. The article explains their divergent dispersion based on differences in their institutional and geographical environments and on dynamic factors. It claims that institutional analysis errs when it ignores migration of institutions. It provides building blocks for the modeling of institutional migration.

## **1. Introduction**

The first generation of new institutional economists took institutions as given and as exogenous, and studied their effect on the market and on economic performance. They dealt with questions such as what types of institutions allow economic growth, or what kinds of exogenously endowed institutions facilitated the rise of the West (North and Thomas, 1973; North and Weingast, 1989).<sup>1</sup> In the second generation of studies, the question was how institutions developed. The initial answer was that economic change, in the form, for example, of expanding markets or new technologies, changed the incentive for creating and altering institutions (Alchian and Demsetz, 1973; Libecap, 1978). The more advanced answer was that legal-economic institutions were not supplied submissively by the state upon demand. Scholars (e.g., Libecap, 1989; Rosenthal, 1992) began to recognize the effect of political and social factors, of pre-existing institutions and legal building blocks, of historical paths and contingencies, on the development of legal-economic institutions. Elements in the environment as a whole were seen as potentially relevant, requiring theoretical modeling and empirical investigation, to the study of the dynamic evolvement of institutions. In addition, a feedback loop was identified between the evolvement of institutions and the performance of the economy. In other words, an attempt was made to endogenize both economic and institutional factors, in order to account for changes in both.

In recent years, a comparative perspective was added. The new comparative question was why did one environment give rise to one type of institution while another gave rise to an institution of a different type? For example, why did North African merchants organize their agency relationship in multilateral and reciprocal reputation-based coalitions while the Italians relied on bilateral and single-directional agency relationships enforced by the State

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<sup>1</sup> For a survey of the development of institutional economic history and theory, see Harris (2003).

(Greif, 1994. See also Greif, 2006b)? Why did the corporation develop in Europe and not in Islamic civilization (Kuran, 2005)? Why was the English East India Company based on a more voluntary and democratic model while the Dutch East India Company was based on a more oligarchic and coercive model (Harris, 2008)? Why were guilds formed in some parts of Europe but not in other (Gelderblom and Grafe, 2007)? Why did the US give rise to dispersed ownership of public corporations while Germany developed concentrated (La-Porta et al., 1998. See also Roe, 2006; Roe and Gordon, 2004)? The general framework was still that institutions reciprocally shaped and were shaped by their environment. The comparison helped to isolate and identify the elements in each environment that molded its studied institution.

A crucial element that is missing from this analysis is the possibility that institutions may have been transplanted from one environment to another. If institutions can indeed migrate between environments, then the explanation for the appearance of a specific institution in a given environment may result not only from the indigenous and reciprocal interaction between the environment and the evolving institution. It may be the outcome of a different mechanism that affects the migration of institutions and their transplantation. This is a neglected aspect in the theory of the development of legal-economic institutions.<sup>2</sup> A main objective of this article is to call attention to this neglect. I will present in this article an example that demonstrates how our understanding of the evolvement of institutions is enriched by the study of the migration and transplantation of institutions.

The example is the distinctive use of the business corporation and the *commenda* partnership in early modern Eurasian trade. While the corporation was used only by Western Europeans, the *commenda* was used in Europe, the Middle East and throughout the Indian

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<sup>2</sup> For an early study of institutional transplantation see Guinnane (1994). For a survey of the legal transplants literature see Graziadei (2006).

Ocean.<sup>3</sup> A comparative study of interactions between the different environments and the institutions developed endogenously in each is not sufficient for understanding the observed institutional pattern. Only an account that takes into account the migration and transplantation of institutions, and explains why the *commenda* migrated and the corporation did not, can provide an understanding of the institutional pattern.

I believe that a concrete contextual discussion may provide more insight than a general and abstract discussion of the migration of institutions. In order to do this, I focus in this article on the migration of legal-economic institutions that organize maritime trade. To make things even more concrete, I analyze institutions that were applied in Eurasian trade. Merchants from at least four major civilizations – Chinese, Indian, Arab-Muslim and Western European – were involved in the early-modern Eurasian trade. They used two main routes: the overland caravan routes known as the Silk Road, and oceanic routes to and across the Indian Ocean. This article focuses on the oceanic trade.<sup>4</sup> The merchants using the oceanic routes in question shipped similar goods within the same geopolitical environments, using not very different maritime technologies. All merchants faced similar problems: uncertainty, high risk, high investment threshold, shortage of reliable collateral, asymmetric information between traveling merchants and passive investors, augmented agency problems, concern over the protection of their property rights by foreign rulers, and more.<sup>5</sup>

In other words, the general question is how each of these civilizations confronted these problems and organized its trade. Did they use similar or different institutions for performing similar tasks? Insofar as they used similar institutions, was this because each

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<sup>3</sup> The corporation migrated worldwide in the 19<sup>th</sup> and 20<sup>th</sup> century, mostly through colonial transplantation of European law and through competitive market pressures in the age of globalization. But this migration of the corporation is beyond the scope of the present article. The article calls attention to the divergent expansion of the two institutions roughly between 1200 and 1700.

<sup>4</sup> The institutional analysis of overland trade involves different sets of questions and merits a separate study.

<sup>5</sup> For a discussion of the obstacles faced by oceanic merchants, see Harris (2005).

reached a similar institutional design independently, through dynamic interaction between a unique environment and the evolving institutions? It is possible that some of them imported and transplanted institutions that were developed in other civilizations within different environments. In so far as transplants failed to occur why were institutions that proved efficient in one civilization not imported by others?

The comparison among civilizations is more thought provoking than the comparison between political entities or regions within the same civilization because each civilization represents a radically different environment, political, social, cultural and religious, for the institutions to evolve in. It is also particularly intriguing because the migration of institutions from one civilization to another represents more of a challenge and is likely to elicit more insights than migration within the same civilization.

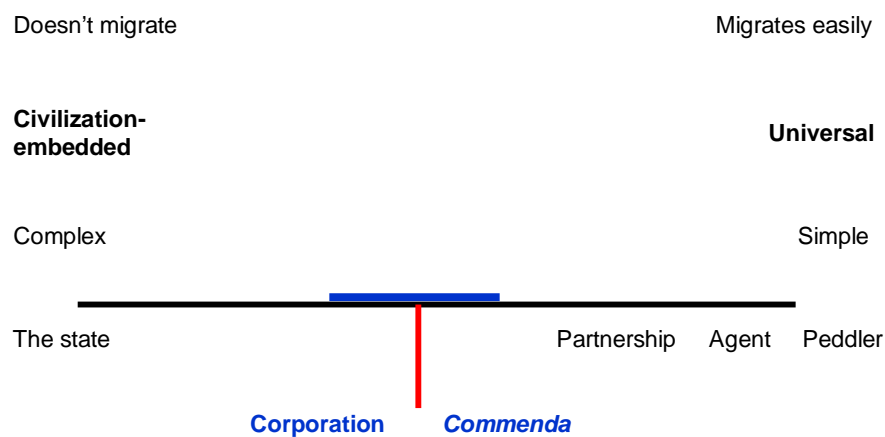
To focus the study we will use a working hypothesis that offers a continuum. On one end lies the simplest form of trade organization: the individual peddler. The peddler moved as a passenger on board a ship from one marketplace to the next, with a small pack of goods literally on his back. Further along the continuum is the individual merchant traveling with a larger quantity of goods and selling them to wholesalers in a destination port, and the merchant who does not travel with his goods but instead uses traveling agents or representatives in the destination port. Around the middle of the continuum are the general partnership, the *commenda* and the business corporation, relatively complex forms of business organization. At the far end is the state taking the role of an organizer of trade. My hypothesis is that the state is the institution most embedded in its civilization, while the individual peddler is the least embedded.<sup>6</sup> Thus, state-level institutions for the organization of Eurasian trade were more likely to be developed indigenously and to differ fundamentally

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<sup>6</sup> In terms of methodology, an understanding of the organization of the state and its role in maritime trade requires answers based on the conglomerate of state, society, religion, and culture. An understanding of the individual trader and the institutions he employs requires an analysis of the basic universal building blocks of trade: contract, agency, property rights, cooperation, reputation, and information.

across civilizations. They were likely to be embedded in their civilization in the sense that they were part of a conglomerate that included religion, social structure, the bureaucracy, agricultural and geopolitical environments. Institutions on the individual trader level were likely to be more uniform among different civilizations, either because similar elementary institutions emerged indigenously and independently, or because such institutions could be more easily imported and transplanted.

## Analytical Framework



My hypothesis leads me to select institutions that are located closer to the middle of the continuum. The more fascinating and less predictable stories are most likely to be found not at the ends of the continuum but closer to the middle.<sup>7</sup> In this article, I will focus on two such institutions, the corporation and the *commenda*. What makes them particularly insightful is their radically different fate. The corporation ended up as a uniquely European institution that was not developed independently anywhere else and was not imported by any other civilization. The English and the Dutch were the first to establish corporations, the East India

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<sup>7</sup> I do not wish to claim at this stage that the analytical framework has strong predictive capability or that the ends of the continuum do not justify a close scrutiny. I hope to study in the future other organizational forms, including the State and the peddler. Accumulation of more studies will allow us to evaluate the predictive validity of the analytical framework.

Companies for Eurasian trade; and other European states followed. No other civilization developed or imported this institution in our period. By contrast, the *commenda* traveled very well. Originating in Islamic law and in Middle Eastern trade practices, it was imported into most of our civilizations. It could be found anywhere from North Western Europe to India, Indonesia and China. It was in use in maritime trade all across the Indian Ocean from the Arabian Sea to the South China Sea. A major contribution of the present article is that it identifies their contrasting fates.

Other institutions that deserve study cannot be dealt within the limited scope of the present article. The general partnership will not be discussed in the present article. It was a multilateral contract, whose partners had more symmetric status than that of the *commenda*, a contract that was less popular in maritime trade than in overland trade and in manufacturing.<sup>8</sup> Ship owning partnerships, in the form known in Europe as part ownership, are also a worthy subject for research that is beyond the scope of the present article. Some of the maritime loan contracts, the sea loan, the bottomry loan and the *responantia*, were somewhat complex because they coupled an element of risk allocation. They will also not be dealt here.<sup>9</sup>

On a more theoretical level, the article demonstrates the important insights that a comparative cross-civilization institutional analysis can offer. It asserts the essentiality of the study of the migration of institutions between environments and civilizations to comparative institutional analysis. On a more fundamental level, it claims that accounting for the migration of institutions is essential for the study of how the environment forms legal-economic institutions and ultimately the ways in which institutions affect economic

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<sup>8</sup> A study of the use of general partnerships in maritime trade in general and in Eurasian trade in particular is a worthy undertaking that lies beyond the scope of the present article.

<sup>9</sup> Each of these contracts was a loan contract with ex-ante fixed return. They all involved an element of risk allocation. But the nature of the risk covered, the party to which it was allocated and the collateral, were different in each. These interesting contracts are beyond the scope of the present paper.

performance. Such an account can be satisfactory only when the theoretical and empirical tools for understanding migrations are sufficiently robust.

The article proceeds in the following way. It begins with the *commenda*, presenting its complex features, the debate about its origins and its migration pattern. It moves on to the corporation, discusses its origins, points to its centrality in European long-distance trade, asks whether there existed non-European institutions akin to the corporation, and explores the European characteristics that gave rise to the corporation. Finally, the article addresses the divergent dispersion of the *commenda* and the corporation. It does so by examining differences in the institutional environment, paying particular attention to the family and to religious institutions; differences in the geographical environment of the Mediterranean-Atlantic region on one hand and the Indian Ocean region on the other; and the role of dynamic processes such as path dependency, timing and contingencies.

## **2. The *commenda***

The three subsections of this section survey the organizational characteristics of the *commenda*, its origins and its later migration. A methodological caveat is in order. The available sources on the early history of the *commenda* are partial and of varying sorts. In some localities they consist of juristic books or responses to practical questions. In other places, they consist of contracts or correspondence between merchants. Only rarely are the sources in the form of mercantile codes. Sometimes they are as indirect as historical and religious narratives or as problems posed to students in math books. It is rare to find in the sources a thick presentation of the characteristics of the *commenda*. Historians have often had to determine whether a contract or a practice constituted a *commenda* based on the display in the sources of only a few characteristics. The task of a comparative project is thus complicated by the fact that sources of different legal status and different levels of detail have to be compared to each other in order to determine the mere existence of similar institutions,

the extent of their similarity, the timing of their appearance, and their relative importance in various civilizations.

The task of following the migration of the *commenda* is even more complicated. Different localities used different terms to describe what we now call *commenda*. This is true for different Italian cities and certainly true for different civilizations using different languages. To confuse things even further the Arab-Islamic civilization used three different terms interchangeably for the *commenda*. In some localities, for example Indonesia, it was contemporary travelers coming from the outside with their own legal conceptions and terms that identified local institutions as *commenda*. Although the travelers' records were preserved, local records were not. Consequently, we lack the native description and understanding of these institutions. As the characteristics of surviving records differ across localities and civilizations, it is impossible to trace all the links through which the institution migrated. For example, because Arab jurist books were better preserved and Italian contracts were better preserved it is not clear whether the Italians learned about the institution through a books-books link, contracts-contracts link or books-contracts link. The surviving records suggest the last link but the second link that is unsupported by the records may make more sense.

The state of the surviving evidence also renders the task of identifying the agents of cross-civilization institutional migration. In the Arab–Italian exchange the agents could have been merchants, codifiers of merchant practices or jurists. In the migration east to India and beyond the sources are even scarcer and the literature offers little to determine whether the agents of migration were Muslim or Jewish merchants, outgoing Indian Merchants, Muslim conquerors or jurists. When the links are not identified, a distinction between importation and indigenous development cannot be made with certainty. With respect to Indonesia and China, the wider context is helpful. The timing of appearance, the likelihood for the existence of agents and links, the level of local demand and the availability on the supply side of local

resources and building blocks can assist in assessing the likelihood of each of the possibilities and in making the distinction.

The evidence that can be provided with respect to the history of the *commenda* is not as precise as one may desire. The surviving historical records are incomplete and unbalanced. The survey offered here is not conclusive; future historians will undoubtedly refine and advance it.<sup>10</sup>

## 2.1 The characteristics of the *commenda*

This section surveys the basic legal and economic features of the prototypical *commenda*.<sup>11</sup> The basic *commenda* was a bilateral contract, involving only two parties, an investing party (called in Italy *commendator* or *stans*) and a traveling party (*tractor*). It is a predecessor of the limited partnership, which is an asymmetric multilateral contract.<sup>12</sup> The *commenda* was an equity investment contract, specifying investments and payoffs. The investing party provided capital in the form of goods and cash that was used for the purchase of the trade goods and for travel-related costs. He was entitled to a share of the profit. The traveling party typically did not invest capital. The *commenda* was also a labor contract. The traveling party invested his labor. This also included expertise, information, contacts and bodily risk. The profits of the *commenda* were split between the two parties. A common arrangement was 75% to the investing partner and 25% to the traveling partner. But other splitting arrangements could be found, including 50% to each, or 2/3 and 1/3. The *commenda* was also an agency contract. The traveling party was geographically separated from the

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<sup>10</sup> Our understanding of the history of the corporation is also bounded by the available records and by analogous methodological difficulties, but not to the same extent. Its history is based on better preserved European records. Also, beyond its early history state records tend to be better preserved. The corporation did not migrate and the complications related to migration do not apply to it.

<sup>11</sup> The most authoritative sources on the *commenda*, are Weber (2003) on Europe, and Udovitch (1970) on Islam. For examples of *commenda* contracts of several types, see Raymond and Lopez (2001).

<sup>12</sup> The emergence of the limited partnership out of the *commenda* occurred in Europe after the time covered here. The *commandite* the French limited partnership was recognized by Colbert's 1673 Ordinance. The history of the transformation of the *commenda* into the limited partnership deserves further research.

investing party. He did not work under direct instructions and supervision. He had some discretion as specified in the contract.

The relationship created by the *commenda* obliged the traveling partner to make the needed effort and not to shirk. In other words, it imposed on him fiduciary duties. The *commenda* contract could also be viewed as one that determines control over the assets and business affairs of the joint enterprise. Internally, the traveling party would be liable towards the investing party only when he breached his agreed-upon mandate or did not act according to common merchant customs and practices.

The liability of each of the parties towards third parties was not clearly defined; as such, it had been the subject of debate among historians. A traveling party who borrowed money, bought on credit, pledged to deliver goods at a certain place, time or quality, or to buy or sell at a pre-determined price, and failed to do so, would bear responsibility toward the relevant third parties. The investing partner would not bear responsibility beyond his investment in the fund of the *commenda*. It has been argued that the investing party was a limited partner. However, as far as I can tell, this was not a contemporary term. The *commenda* contract may be conceptualized as creating a new pool of assets, a fund, separated from that of either party.<sup>13</sup> The *commenda*'s pool of assets was reachable to creditors of the *commenda*. But the investing party's private pool of assets was not. It is not fully clear whether it was not reachable because an extra-contractual sovereign on merchant law exempted these assets from liability, because the traveling party was not empowered to commit them, because the identity of the investing party was not known to the third parties or because his assets were physically removed from them. The upshot is that the traveling party could subject the investing party to liability towards third parties only up to the sum the latter invested in the *commenda*.

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<sup>13</sup> This analysis is based on Hansmann et al. (2006).

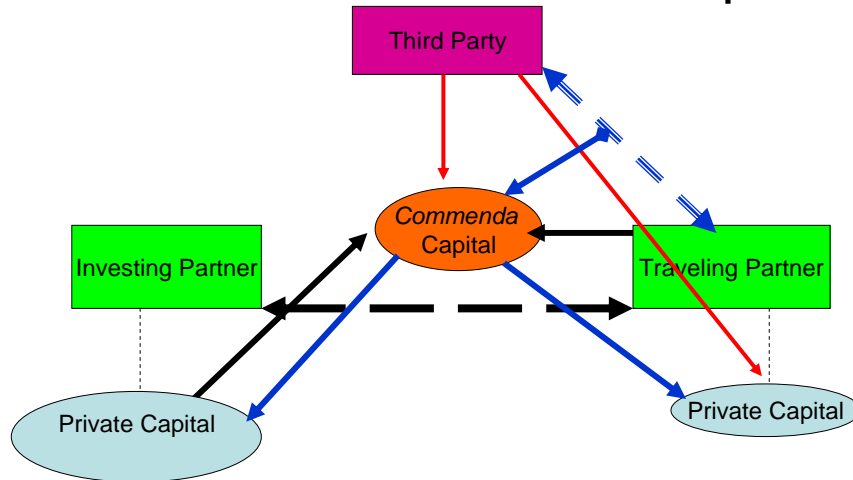
Some scholars view the *commenda* as an agency contract; some as an equity investment or profit sharing contract. Yet, as detailed above, the *commenda* was a more complex institution than one may grasp at first sight. It determined the relationship between parties on several levels, including investment, agency, managerial control, risk allocation, profit allocation, and creation of a separate pool of assets. Hence, it should be viewed as a nexus of contracts, and also as a template or standard form contract. When selecting the *commenda* contract the parties selected a fixed and detailed contract that contained only a few default rules that could be tailored to their needs. They selected a well developed and detailed form of business organization.

The *commenda* was a voluntary contractual institution, but it could not fully function outside the realm of a legal system or without the support of a learned juristic community.<sup>14</sup> A legal system, including third party (state, city or merchant community) enforcement was needed. Dispute resolution required more than enforcement or fact-finding. *Commenda* contracts could not be complete due to the complexity of the arrangements and the unpredictability of all the circumstances. A legal system was needed for ascertaining norms, specifying and applying general standards of conduct and developing more detailed rules. A good example of such a need is the requirement that the traveling party follow common merchant practices (Udovitch, 1970). Failure to follow such practices would amount to a breach of the *commenda* contract. But the support of a legal system was needed in order to turn this general standard into operative rules of conduct and enforcement. The *commenda* could thus be expected to be reflected in codes, particularly merchant and maritime codes, in scholarly legal books, in dispute resolution records and in practical manuals.

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<sup>14</sup> This point was recently reiterated in Edwards and Ogilvie (2008).

# Commenda Partnership



The *commenda* had several variations. A basic variant according to Raymond and Lopez (2001) was one in which the traveling party also invested money, typically a third of the investment. This affected the splitting of profits. In a second variant, the traveling party could, if not prohibited, create a second *commenda* in which he placed all or part of the goods in the hands of a third person who traveled to a more distant market. The traveling party of the first *commenda* became the investing party of the second. Another variation was that the *commenda* assets could be not only distinct goods but also a share in a pool of goods or in a ship. The bilateral *commenda* could appear as part of a complex multilateral system. For example, a single traveling party could pool together goods from numerous investing parties into a *commenda*. This would allow him, and them, the benefits of economy of scale.

Conversely, an investing party could split his investment among several traveling parties.<sup>15</sup> This would serve as a method of risk spreading.<sup>16</sup>

To sum up, the *commenda* was a complex institution. In modern terms, we can call it a nexus of contracts. It combined several issues within a single legal-economic institution. The single *commenda* contract was not only a nexus of several contracts, it was itself part of a complex web of contracts. Each of the parties to that contract could, and often was, a party to other *commenda* contracts.

## 2.2 The debate about the origins of the *commenda*

Late-nineteenth century European historians such as Weber (2003) and Goldschmidt, asserted that the *commenda* had its roots in Roman law, made its early appearance in vulgar Roman law of the early Middle Ages, and became widespread with the revival of trade in 10<sup>th</sup> and 11<sup>th</sup> century Italy. But later studies of Europe admit that there are only a few vague hints at the existence of the *commenda*, in law or practice, before the second Crusade, around the middle of the 12<sup>th</sup> century.

Historians of Islamic law, notably Udovitch (1970), writing in the 1960s, claimed, on the other hand, that the institution appeared with its full features for the first time in the Arabian peninsula before the rise of Islam.<sup>17</sup> It was termed by the Arabs *mudaraba*, *qirad* or

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<sup>15</sup> For example, the estate of Venetian Doge Renieri Zeno upon his death in 1268 included investment in 132 *colleganze* (the Venetian term for *commenda*) to the sum of 22,935 lire. The value of his real estate was only 10,000 lire. See Lane (1973).

<sup>16</sup> The best available documentation for the multilateral use of the *commenda* is that of the contracts made in connection to the sailing of the "Saint Esprit" from Marsais to Acre in 1248. Of 150 contracts connected to that voyage, 132 were *commenda* contracts. This is the largest depository of *commenda* contracts referring to a single voyage. For example, a single merchant on board had 13 *commenda* contracts with 11 different investing parties. For a fascinated study of these contracts, see Berlow (1979).

<sup>17</sup> See also Udovitch (1962). Pryor speculates that the Italian *commenda* may have had its origins in Roman and Byzantine institutions, but he does not reject Udovitch's conclusion. See Pryor (1977).

*muqarada*.<sup>18</sup> The Arab institution may have been inspired by older Middle Eastern institutions, the Jewish *isqa* or the Byzantine *chreokoinonia*. But the full features of the Arab and Italian *commenda* cannot be found in these institutions. The use of the *commenda* extensively for long-term trade developed for the first time by the Arabs to meet the needs of merchants involved in the caravan trade along the Incense Route and other ancient routes connecting south Arabia with the Mediterranean.<sup>19</sup> According to Udovitch the prophetic and legal texts reflected pre-Islamic and early Islamic practices that originated in caravan and long-distance trade in and around the Arabian peninsula. Though the *commenda* was an indigenously developed Arab-Islamic institution, it is explicitly mentioned as such in the Quran. However, numerous Muslim traditions attribute its use to the Prophet himself. The Prophet, before his prophethood, traveled to Syria to trade there in goods given to him by Khadijah his wife-to-be (Hasan, 1989). According to the tradition the Prophet was the traveling partner and Khadijah the investing partner in this *commenda* like partnership. Early Islamic texts make frequent references to the *commenda*. The religious and legal texts written in the first two centuries of Islam include a well developed discussion of various aspects of this institution. The notable Europeanist historians of the Mediterranean trade, Raymond and Lopez (2001), agree that the *commenda* can be found in a commercial manual published in Damascus in the late 9<sup>th</sup> or 10<sup>th</sup> century.<sup>20</sup>

### 2.3 Migration of the *commenda* across civilizations

From its origins in the Arab peninsula the *commenda* traveled both west and east. It traveled with the rapidly expanding Islam to Iraq and Syria, to Palestine and Egypt and to the

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<sup>18</sup> Initially the first two terms were used in the Arab peninsula and the third in Iraq but eventually all three became interchangeable.

<sup>19</sup> I will use throughout this article the more familiar term "*commenda*" when referring to this institution in all civilizations, localities and periods, including the Arab-Muslim.

<sup>20</sup> They refer to *The Beauties of Commerce* by Abu al-Fadl Jafar ibn Ali. There is a controversy over the dating of the book. Udovitch, following Ritter, dates it to the 11<sup>th</sup> century. See Raymond and Lopez (2001), Udovitch (1970).

Maghreb. The earliest *commenda* contracts in Christian Europe are found in Venice and Genoa in the late 11<sup>th</sup> and the 12<sup>th</sup> centuries (Raymond and Lopez, 2001; Lane, 1973). There is no clear evidence in the literature for the exact timing, routes and agents of the importation of the *commenda* to Italy. But today there is little debate about the Muslim origins of European *commenda* (Cizakca 1996, 2006). *Commenda* contracts were first used by Italians on trade routes to the Eastern Mediterranean around the time of the first and second Crusades, which suggests that this was the link.<sup>21</sup> The travel of the *commenda* further west, to Spain, and north, to Germany, is well documented. There is some controversy over whether the *commenda* reached England. Legal historians, for instance Postan (1973a), argue that it contradicted basic concepts of the common law and even customary law, and that the common law developed substitutes for this institution. Some English historians, notably Postan (1973b), Holdsworth (1922), Plucknett (1929) and Rogers (1995) argue that even though the English did not use a distinct name for the *commenda*, they in fact used and recognized contracts similar in content to those of the *commenda* by the late 13<sup>th</sup> century. Some 14<sup>th</sup> and 15<sup>th</sup> century yearbook cases indeed refer to transactions between parties that have profit sharing elements in them. It is likely that these were *commenda* contracts because at least one of them was between Italian merchants who often used this type of contract, because of the asymmetry in the inputs of the parties – one providing only capital and one only labor, and because they were identified as such by notable historians. Yet these transactions were litigated within the framework of the writ of account that gave rise only to disputes between partners, not to disputes between partners and third parties. As a result, it is

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<sup>21</sup> There is a considerable evidence for the importation of Arab business institutions to Europe. See Lieber (1968); Panzac (2002). It is possible that the *commenda* was imported also through Spain or Sicily. For the purposes of this article it is not necessary to reach a conclusion.

not possible to clearly determine whether these transactions involved *commenda* or general partnerships.<sup>22</sup>

The *commenda* appears frequently in the Cairo Geniza records, which contain correspondence and contracts dealing with the overseas trade of Cairo Jews. They reflect the wide use these merchants made of the Muslim *commenda* (*qirad* or *mudaraba*), termed in Hebrew *qirad al-goym* (*qirad* of gentiles) as distinct from the Jewish partnership (*qirad betorat isqa*). Goitein, the leading historian of the Geniza, concludes that the Muslim *commenda* was in much more frequent use in the maritime trade of these Jewish merchants than the Jewish partnership. The earliest appearances of the *commenda* in the Geniza are from the first decades of the 11<sup>th</sup> century. They can be found in some of the oldest documents that were preserved. This is supportive evidence for the claim that the origins of the *commenda* are Muslim. The *commenda* was used in contracts with both Jewish and Muslim partners. Disputes were resolved according to the relevant Muslim law (Goitein, 1967). This serves as an additional support for my argument that the *commenda* was not a simple contract but rather a complex institution requiring the support of a legal system for both enforcement and creating detailed governing rules.

Though the Geniza relates primarily to Mediterranean trade, it provides evidence also on trading with India, usually via Aden. The *commenda* was a common form of contract in the India trade of Jewish merchants based in Cairo.<sup>23</sup> The Geniza records are thus relevant not only to the origins of the *commenda* but also to its migration and both routes and agents of migration. The Jewish traders traveling from Cairo to the Indian Ocean ports may have served as the exporter of this institution to India.

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<sup>22</sup> It is impossible to reach a conclusive assessment whether the common law recognized the limited liability of the investing partner or subjected him to a full joint and several liability towards creditors similar to the case of partners in general partnerships. *Odi v. Aringi* (14 Edw. II 217, 1321); *Coleman v. Marham* (14 Edw. II 353, 1321); *Septvaux v. Marchaunt* Y.B. 8-10 Rich II 187 1377); *Selby v. Palfrayman* (13 Richard II 79, 1389).

<sup>23</sup> On the Jewish trade between Cairo and India, see Goitein (1954 , 1966 ,1987}. See also Goitein and Friedman (2008).

The surviving evidence for the trade of Muslim traders with India is not as complete as the Geniza records. Yet, the remaining records, such as documents found in the excavation site called the "Sheikh's house" in the Red Sea port of Quseir, indicate that the *commenda* was a common form. Quseir was a major transit port on the route from Fustat (old Cairo) and the Nile Valley to the Indian Ocean (Guo, 2004). The *commenda* was carried eastwards with these Muslim and Jewish traders. *Commenda* contracts were also used by European traders when they reached Asia, using the Cape route, in the 16<sup>th</sup> century. Portuguese merchants funded by *commenda* contracts sailed on board Crown ships taking the Crown routes (*carreiras*) to Asia (Prakash, 2006). The *commenda* was also used by the first Dutch traders who arrived in the Indian Ocean shortly before 1600, and served as the basis for pre-companies that initiated the first Dutch voyages to Asia.

The use of traveling agents was a common practice in Indian maritime trade. They were used on eastward routes to Basra, Aden and the like, and on western routes. The *nakhuda* was either a senior traveling merchant or a representative of the ship's owner. He was appointed commander of the voyage. Lesser agents were employed by other merchants and investors (Das Gupta, 2001; Das-Gupta and Pearson, 1999). Agents were sometimes employed on fixed salary or allowed to trade privately. However, according to Das Gupta (2001) *commenda* contracts in which the principal and the agents split the profits and allocated the risk, were quite common. Chaudhuri (1985) also believes, based on scattered evidence, that *commenda* contracts were used in Indian Oceanic trade. The institution could have been copied from Arab or Jewish merchants arriving in India or imported by Muslim Gujarati merchants trading with Persia and Arabia or making the pilgrimage to Mecca.

The migration of the *commenda* further east is not well documented in surviving records. The reconstruction of this migration involves significant methodological problems as discussed above. In his travel book written around 1510, Tome Pires (1990), one of the first

Portuguese to arrive in Indonesia, provided a first-hand impression of local trade practices before the disruptive arrival of the Europeans. He reported on a practice of splitting profits and risks between merchants and junk ships owners. The leading historians of the early modern Indonesian trade (see, for example, van Leur, 1955 and Meilink-Roelofs, 1962) view this and other records as evidence of the use of the *commenda* in the trade between India and Indonesia, in inter-island trade, and even in trade with China. They also mention Chinese merchants investing in *commenda* and foreigners using *commenda* in Chinese port towns. This was the last missing link in the migration of the *commenda* from Arabia to China.

There is also evidence of the use of *commenda*, or at least transactions quite similar to the *commenda*, in China, as early as the Song Dynasty (960-1279). Yoshinobu (1970) and So (2000) have found evidence, in 12<sup>th</sup> and 13<sup>th</sup> century texts, of investment in shipping both for fixed interest and for a share of the profits.<sup>24</sup> The latter contractual form is akin to *commenda*.

Eventually, this complex institutional form, which was designed specifically for long-distance trade, was used by investors and their agents from the northwestern edge of Europe to the easternmost parts of Asia. As such, it became a common characteristic of many of the circuits and links of Eurasian trade.

### **3. The corporation**

As will be shown below, the conception of the corporation as a separate legal entity is uniquely European. In order to substantiate this observation and explain it, a working definition of the corporation has to be offered. A corporation is an association of individuals that has a legal entity distinct from those of these individuals. It has the capacity to own property separately from that of its individual members. It can contract with third parties in

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<sup>24</sup> They found some supporting evidence in less conventional sources such in mathematics books and in shipwreck excavations.

its corporate capacity. A corporation can regulate its internal affairs, discipline its members and resolve their disputes. A corporation has a hierarchical and centralized governance structure, through which regulations and decisions are made and agents are empowered. By the 13<sup>th</sup> and 14<sup>th</sup> centuries, the legal concept of the corporation was well defined in the high legal texts of the revived Roman law and of Canon law. The corporation was used in a variety of contexts, including church entities, universities and colleges, municipalities and guilds. By the 16<sup>th</sup> century a few other features were added to that conception. Its purposes were made sufficiently flexible to be used for business and profit purposes. It raised capital for the purpose of conducting business. Entry and exit to membership in the corporation could be voluntarily and based on a payment. As a conception that embodies all these features, even those that were present as early as the 14<sup>th</sup> century, the corporation is a unique European conception.

### **3.1 The debate about the origins of the corporation**

A long-standing debate surrounds the early history of the corporation. I identify four different approaches in the historiography of the corporation. The first, which views the corporation as a Roman jurists' invention, was advanced by law scholars and historians of Roman law, such as Duff (1971). They interpreted Roman legal texts and the *corpus juris civilis* as containing evidence for the existence of a corporate conception in classical Roman Law. Recently Malmendier (2007) suggested that the *Societas Publicanorum*, a society of government leaseholders, was the earliest predecessor of the modern corporation. But this institution, which appeared in the 5<sup>th</sup> century BC and reached its height during the republic, was not reflected in later legal texts such as *corpus juris civilis*. Thus, even if the identification of corporate features in the *Societas Publicanorum* is accepted by scholars, this institution had no direct continuation into the high middle ages.

The second approach argues that the corporation is a product of 11<sup>th</sup> to 13<sup>th</sup> century revivers of Roman legal scholarship. According to that view, the glossators and commentators, the interpreters of Justinian's Code, read into a few scattered statements by Roman jurists a coherent legal concept unrecognized by contemporaries. They did so not as a scholastic exercise but rather to serve the new needs of their age (Avi-Yonah, 2005). Specifically, they responded to their changing environment, in which associations such as independent cities, universities and guilds, were gaining importance. These associations needed an institutional platform for owning property, setting governance structures, resolving disputes and the like, that the corporation provided.

The third considers the corporation a Church and canonic law invention. Berman (1983) is a typical presenter of this approach (see also Grant, 2001). For him, the corporate concept was developed primarily for the organizational needs of the Roman Catholic Church. The emerging law of corporations was the constitutional law of the late mediaeval Church. The Investiture struggle between the Pope and the Holy Roman Emperor led the Church to independence, uncommon in other religions. The Church needed a legal-constitutional conceptual framework because it aspired to separation from the secular state. The corporation provided legitimacy and working tools for the full range of ecclesiastical organizations, from the Papacy to the monastery.

The fourth views the corporation as originating in medieval Germanic tribal traditions. It points to the communal spirit of German tribes as evidence of a corporate ideology. This view was advanced by German nationalists, notably Von-Gierke (1990, 2001), in the late 19<sup>th</sup> century. Unlike the Roman law and the south European Latin culture that were individualistic in their orientation, the basic Germanic orientation was toward the group, the association, the fellowship.

In this article, the debate about the origins of the corporation plays a different role than the debate about the origin of the *commenda*. There, the issue at stake was from where the *commenda* began its migration, European civilization or Islamic civilization. Here, it is clear that the origins are European. However, two other issues are at stake. The first is the timing of the origins. Was the corporation around, and available for importation and transplantation, since the 1<sup>st</sup> or 2<sup>nd</sup> century CE? Or was it available only since the 12<sup>th</sup> and 13<sup>th</sup> century? More concretely, was it available earlier than the *commenda*? Was it available before the formative period of Islamic law? Only the first and least widely held of the four approaches responds positively to the last two questions. The common view about timing, shared by three of the approaches, leads to the conclusion that the corporation became available only three or four centuries after the *commenda*. I shall return to this point when discussing dynamic explanations. The second issue at stake is whether we can learn anything from the environment that gave rise to the European corporation regarding the uniqueness of that environment and the possibility that in other civilizations, a similar environment existed and could indigenously give rise to similar institutions. I shall return to this issue when discussing the institutional environment as an explanation for the divergence in dispersion.

### **3.2 Did there exist non-European corporations?**

So far, I have assumed that the corporate conception was uniquely European. In principle this assumption could be based on a methodological bias nested in a Eurocentric perspective. Instead of looking for migration, would it not make sense to look for indigenous growth? Other civilizations could have given rise to institutions that used different terms and that configured their corporate-like features differently than the European corporation. I will first deal with the Islamic *waqf*, then with the Chinese family lineage organization and finally with the Hindu *sreni*. In doing so, I will not ask whether these institutions substituted for the

corporation by performing similar functions. Leaving the question of substitutes until later, I will ask whether any of them was, in fact, a corporation in disguise.

### 3.2.1 *The Islamic waqf*

As a legal entity detached from individual human beings, the corporation was not recognized in Islamic legal texts. Nor was it used in Arab civilization. It is argued that the *waqf* was the Islamic institution that served as a substitute for the corporation. *Waqf* is often translated as charitable trust. Indeed it has similarities to the English trust.<sup>25</sup> The *waqf* was a created by a person who endowed land or other immovable property for the advancement of a public or a family purpose. The purpose had to be considered charitable or pious. The property given to the *waqf* was inalienable. The *waqf*'s purpose was advanced by enjoyment of the property itself or of the income generated by utilization of the property. A trustee (*mutawalli*) was appointed by the founder, or according to the founder's instructions, to oversee the *waqf*'s property, implement the purpose of the *waqf* and make sure that the *waqf*'s beneficiaries would get their share of the usufruct. The local judge (*qadi*) served as a general supervisor of all *awqāf* (plural of *waqf*) within his jurisdiction (Schacht, 1983). What was the legal status of the *waqf*'s property? The beneficiaries were not the owners of the property. The trustee held in trust but did not own it. The common interpretation in the Hanafi School of Islamic law was that the property was not owned by anyone as long as it remained *waqf* property. A non-orthodox modern interpretation argues that because the property was owned by the *waqf* the *waqf* should be viewed in retrospect as a corporate entity (Zahraa, 1995). Yet the common view is and was that the *waqf*, like the English trust, and unlike the European corporation, was unincorporated.

Though the *waqf* did not embody all the features of the corporation, the two shared features. The *waqf* allowed the holding of a separate pool of assets. This feature implied both

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<sup>25</sup> For the supposition that the English trust originated from the *waqf*, see Gaudiosi (1988); Avini (1996).

perpetual holding of property and a degree of entity shielding from creditors of the beneficiaries. It enabled the separation of ownership from control and the employment of agents. However, it did not constitute a property-owning institution in a fuller sense. It did not provide governance or decision-making bodies. Its activities, unlike those of a corporation, were constrained by the "dead hand" of its creator. There were practical ways to circumvent the creator's instruction but the legality of these practices was questionable. The bottom line was that the *waqf* did not provide a full substitute for the corporation (Kuran, 2001).

### 3.2.2 *The Chinese family lineage organization*

The Chinese kinship organization, sometimes called the clan Corporation, is considered by Ruskola (2000) and other scholars as the Chinese equivalent of the European business corporation. The kinship organization is based on lineage, a fundamental element of Chinese society, and to understand it, we need to survey the attributes of lineage.<sup>26</sup> Individuals on the same genealogical patrilineal line, who maintained significant social relationships, were considered members of the same lineage. The lineage was the highest social organization short of the state. Members of the same lineage usually lived near each other, in the same community, village or set of villages. The core bond of a lineage, however, was religious. All members of the lineage, and only members of the lineage, worshipped the same ancestors. Often the common ancestral roots went back many generations. Ancestral worship took place on lower levels as well, the family, the branch and the sub-lineage. However, the lineage level worship was the most important, because it represented the widest circle connected to the same ancient ancestor. The worship ceremony involved gathering in ancestral halls, making sacrifices, and other rituals.

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<sup>26</sup> A classic discussion is Freedman (1958). The book gave rise to extensive literature, debating issues of typology, periodization, methodology, regional variations and more. For a glimpse of the literature see Ebrey and Watson (1986), Faure (1986).

The assets of the lineage – ancestral halls, graves, genealogical lists and other resources needed for the worship – were built and held by the lineage. Some anthropologists refer to this property as corporate property and to the lineage as a corporate entity, for example Cohen (2004). Historians, more cautious when using Western legal terminology outside Europe, and lawyers, more aware of the legal features of corporations, term them lineage estates or lineage trusts. The lineage organization held property in separation from individuals and families. It did not have a clear governance structure. It was not involved in legal transactions with outsiders or in profit-maximizing activities. Over time, the lineage organization assumed political, economic, military, charitable and educational functions, in addition to the traditional social and religious functions. I will return to the changing usage of the lineage, examining dynamic factors.

### 3.2.3 *The Indian sreni*

The *sreni* organized craftsmen and merchants in the Indian subcontinent. It was an association of persons rather than capital or property. Each *sreni* organized an identified branch in a defined locality. Some scholars date the *sreni*, which appears in ancient Hindu texts, back to 800 BCE or even earlier. In these texts, several corporate features are identified in the *sreni*, a central feature being the power to regulate its members. The *sreni* issued rules of conduct, judged and disciplined its members, and litigated disputes among them. Rules were promulgated in *sreni* assemblies. Membership in the *sreni* was hereditary. The *sreni* held property for performing its main functions and could be a party to transaction in assets (e.g., Majumdar, 1918; Khanna, 2005). There is some evidence that the *sreni* lent money to their members and performed charitable services. The *sreni* was similar in some respects to the European guild. Recently, Khanna claimed that the *sreni* was in fact a predecessor of the business corporation, but there is no evidence that they were actually used for the same range of functions as the corporation. We know that they were not used as profit-maximizing

enterprises or in maritime trade. From the texts, it can be inferred that the *sreni* had some of the organizational features of the corporation but not others. They developed indigenously in India long before the development of guild or of the corporation in Europe. They were not imported by any other neighboring civilization, and declined before the arrival of Europeans and their corporations in India.

In sum, institutions outside Europe, the Islamic *waqf*, the Chinese family lineage and the Indian *sreni* had some, but not all or even most, of the features contained in the concept of the corporation in its early stages and none of the features added to it by the 16<sup>th</sup> century.

### **3.3 The centrality of the corporation in the long-distance maritime trade of Europe**

By the 16<sup>th</sup> century, the European corporation appeared in a new context, as a platform for the operation of maritime trade enterprises, in two basic variations. The regulated corporation was a reincarnation of the merchant guild. It did not engage in trade on its own account. It coordinated the activities of its merchant members, provided them with infrastructure, represented them vis-à-vis political entities, and supervised their compliance with price, quantity and quality directions. The regulated corporation was formed by an explicit state charter that incorporated it and granted it monopoly. The second variation, the joint-stock corporation, first appeared in England in the middle of the 16<sup>th</sup> century with the formation of the Russia (1553) and Levant (1581) Companies. It used the legal platform of the regulated corporation, and of earlier non-business corporations, and added to them the elements of pooling together of joint stock and making the investors in the stock shareholders, with rights to share in profits and voting. The joint-stock corporation performed the actual trade using its own capital and assuming risks. Its shareholders, who could become passive investors, did not view the corporation as an organization that would provide them

with infrastructure for their own trade as active merchants (a role played by the guild and the regulated corporation).<sup>27</sup>

At the turn of the 17<sup>th</sup> century, the joint-stock corporation became the major institution used for organizing European trade with Asia. The formation of the English East India Company (EIC) in 1600 and of the Dutch East India Company (VOC) in 1602 epitomized the shift of European Eurasian trade to the corporate form of organization.<sup>28</sup> The French and the Danish, Ostend and Brandenburg also established East India Companies (Gepken-Jager et al., 2005). Even the Portuguese, who in the 16<sup>th</sup> century organized their trade as state-owned and later as state-licensed, formed an East India Company in 1628 (Antunes and Torres in Gepken-Jager et al., 2005 and Disney, 1977). The corporation was thus the standard form of organization for European Eurasian trade at its 17<sup>th</sup> century height. This organizational form controlled the longest-distance Eurasian trade, that used the Cape route. It played important role in mid-distance trade, connecting the three sub-regions of the India Ocean (Arabian Sea, Bay of Bengal, South China Sea). However, it was not dominant in shorter routes where Asian traders remained active.<sup>29</sup> The corporate form of the EIC and the VOC is often considered a major reason for their success and for the rise of the Europeans to a position of dominance in the Eurasian oceanic trade. Steensgaard (1974) views the use of the corporation in Eurasian trade as revolutionary, compared to Asian and Portuguese trade, because it internalized military and political costs and placed investment and business decisions on a rational, profit maximizing, capitalist basis. In the same vein, North (1990) views the corporation as a key institution in the rise of the West because it economized on

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<sup>27</sup> For the early development of English regulated and joint stock trading corporations see Harris (2000)

<sup>28</sup> For the formation of the English and Dutch companies see Harris (2005, 2008)

<sup>29</sup> The Cape Route was used in our period exclusively by Europeans. In the years 1495-1595 the route was used exclusively by Portuguese who did not use the corporate form but rather State organization. From 1600 most of the ships using the Cape route were operated by corporations. About 80% of the 10,000 ships that used the Cape route between 1600 – 1795 on their way from Europe to Asia were employed by the English and Dutch East India Companies alone. See de Vries (2003)

transaction costs and spread risks. For their part, Carlos and Nicholas (1988) view it as an efficient merger of the various links in the chain that connected East Asian producers with European consumers.

#### **4. The divergent dispersion of the *commenda* and the corporation**

One has to address two sets of issues in order to explain the divergent dispersion of the *commenda* and the corporation. The first is why the corporation developed endogenously where it did. The more singular the European circumstances were, the less likely the corporation was to evolve indigenously elsewhere. The second is why the *commenda* migrated widely whereas the corporation did not migrate beyond its place of origin. An explanation cannot always separate the two sets of issues.<sup>30</sup> I will begin by discussing differences in the institutional environment, from the state, to institutions of higher learning, to the family, and finally to religious institutions. These differences can explain both why the corporation developed in Europe and why other civilizations neither needed it nor imported it. I will move on to geographical differences between the places of origin of the two institutions. The more central place of origin of the *commenda* and the openness of the Indian Ocean can partly explain the spread of the *commenda*. Finally, I will show how historical dynamics, such as timing, path dependency and contingencies also influenced the divergent outcome. The purpose of the next three sub-sections is to demonstrate plausible explanations, suggest a constructive research agenda and offer building blocks for more formal models of institutional migration.

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<sup>30</sup> Two other questions will not be addressed here because they are not crucial to the question at hand. The first is why the *commenda* evolved in Arabia and not elsewhere? A definitive answer would be difficult due to the scarcity of sources about its origins. In any case, I do not make a strong claim against the possible indigenous and independent emergence of the *commenda* in other places and civilizations. The second is why the corporation migrated beyond Europe in the last two centuries? The dominance of Europe, its political empires and its economies in this period created a new environment that lies beyond the timeframe and conceptual scope of the current article.

#### 4.1 The Institutional Environment

A first intuitive response to the question of why the corporation did not migrate out of Europe is that it is strongly linked to the European state. This is in line with the initial hypothesis generated by the framework used to shape this project. Recall that along our constructed continuum the corporation was placed closer to the state. The issue at hand can be broken down to three distinct sub-issues: Was the corporation a state - created institution? Why was it created only by European states? Why did the link to the state inhibit its migration to other states?

Intuitively, the corporation may not have migrated because it relied on the State as its exclusive creator and as the provider of some of its advantageous characteristics, including limited liability and longevity. But this intuitive response is not conclusive, for the early European corporation was created neither by the state nor within the state. Corporations were created voluntarily and by non-state organizations such as the Church and various cities. Only later did states assume a monopoly position over formation of corporations. It is sometimes suggested that only states could provide the corporate features that are most important for overseas trade, longevity and limited liability. While longevity was an important attribute of merchant corporations, limited liability was not. But longevity was achieved in other civilizations as well without resort to the corporation, in institutions such as the *waqf*, the family lineage and the *sreni*. By the same token, limited liability on the other hand was not highly relevant for the early long-distance trading corporations for the same reasons it was not relevant to the *commenda*. The most significant reason was that investors back home were unlikely to be exposed to debt liability incurred overseas.

Let us turn now to the second sub-issue: why non-European states did not indigenously develop corporation-like institutions? What was singular in the European states that gave rise to the corporation? Preliminary explanations can be the more fierce

competitions among the numerous states in Europe, the federal structure of some European states, the uniqueness of the relationship between State and Church in Europe, the distinctive European conception of sovereignty and the relative autonomy of the European city. These are all tentative and preliminary factors that require further research.

The third sub-issue involves the divergent migration patterns. It can be argued that the corporation could only migrate "from above" with state support while the *commenda* could migrate also "from below" by merchants adopting contractual practices. Since the corporation migrated quite freely between various states within Europe one wonders why the migration stopped at the borders of Christian Europe. The *commenda* on the other hand, as I argued above, was not a mere contractual form that could easily be learned and copied. It needed a supportive legal system and this could not be transferred by the practicing merchants themselves. Some level of migration "from above", at the level of juristic scholarship, of merchant code compilation, or even of state court litigation was needed. While I find the relationship to the state as having some value, and as providing some justification for the analytical framework offered in the introduction, I aim at examining additional explanations for the migration pattern.

The view that the corporation is an offspring of the Church is the most plausible in my view and most uniquely European. There were no parallels to the Roman Catholic Church in terms of the monolithic and hierarchical structure of its organization.<sup>31</sup> Insofar as the Church was the main factor that led to the development of the corporation, as Berman claims, we would not expect the corporation to develop independently and indigenously elsewhere. This Church-based explanation can be complemented by the explanation that connects the development of the corporation to the existence in Europe of independent cities, self-

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<sup>31</sup> The Eastern Orthodox Church also had a hierarchical structure. Its relationship to the rise of the corporation deserves a separate study.

governing merchant and trade guilds, and autonomous academic establishments, none of which existent in other civilizations.

A new explanation for the appearance of corporations specifically in Europe, which goes beyond the state, was recently suggested by Greif (2006a). Western Europe was singular in not having a social structure based on the extended family. A combination of demographic and religious factors led to the scattering of extended families in Europe and to the rise of the nuclear family as a core unit in society. Increased fertility in the 9th and 10th centuries led to an increase in the number of children per family and increased the size of extended families up to a point at which joint habitation became impossible. The Christian Church, for both theological and demographical reasons, prohibited polygamy, discouraged endogamic marriages up to four and at some point even seven degrees of kindred and made incest a sin and a crime, making the exogamic family the norm (Fossier, 1996). This splitting up of the extended family into nuclear families created an institutional vacuum that may have fueled the rise of non-family institutions designed to promote cooperation and collective action. What other civilizations managed through extended families, lineages, clans, social networks and other informal institutions, in the relatively impersonal European society had to achieve formally and through law.

Greif's explanation also complements Kuran's (2005) explanation that the extended family of the Middle East was an institution that provided wealth, security and permanence. Similarly, the Chinese extended family organized along multi-generation lineage lines performed many social, economic, political and religious functions that could not be performed by the European nuclear family.

The Europeans developed the corporation, then, not because they enjoyed an advantage in institutional design capability but, rather, because they needed substitute for what was missing in their society – the extended family. The reliance of other civilizations on

the family as a platform for business served them well in the short run. However, in the longer run it inhibited them from developing impersonal institutions such as the corporation.

This explanation is not free of criticism. Certain historians of the family hold that the nuclear-extended distinction is too reductive for the complexity of familial relationships. One should focus not only on the number of children and on cohabitation, they say, but also on emotions, dependence and trust. It can further be argued that in banking and long-distance trade even in Europe families played an important role. The family rather than the corporation was the organizational platform of the giant Medici and the Fugger enterprises.<sup>32</sup> It is clear, then, that the structure of the European family cannot explain fully the rise of the corporation in Europe. Nevertheless, I do wish to suggest a further inquiry along this line.

Since the nuclear European family is said to be the outgrowth of Christianity, and specifically of its marriage and inheritance laws, Greif's and Berman's explanations overlap. While for Berman, the institutional structure of the Papacy and the Church made all the difference; for Greif, it is the theological and normative family rules that mattered. But these rules, in turn, were influenced by the institutional interests of the Church.

Was the *commenda* connected in a similar way to the institutional environment in which it evolved? The view adopted above is that the *commenda* originated in pre-Islamic Arabia, among the merchants of Mecca and other towns and oases that were involved in long-distance trade. It evolved from below, in trade practices, possibly borrowing from earlier Jewish or Byzantine practices. It did not have religious origins. We should not be confused by the fact that historians trace the first references to it to the Quran and to early Muslim law books. These are the earliest references probably because its earlier history was mostly oral

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<sup>32</sup> It is worth mentioning that family firms, such as the Fuggers and the Welsers, did not operate independently when it came to long-distance Asian trade. They cooperated with the Portuguese state apparatus, the *estado da Índia*. By the late 16<sup>th</sup> century these family firms, which were organized based on the general partnership model, lost ground to Dutch pre-companies based on the *commenda* model and in the early 17<sup>th</sup> century to the Dutch and English East India Companies.

and left no traces in written documents. The context of the discussion of the rules governing the *commenda* is in the more secular parts of Islamic law. Because of these origins, the *commenda* could more easily be detached from its environment, transferred, and transplanted into other religious, social and political environments where it performed similar long-distance trade functions.

#### *4.2 Geographical explanations*

The travel distance of ideas and institutions that were developed in a civilization closer to the center of the Eurasian land mass was shorter than that of ideas and institutions developed on its western edge. The place of origin of the *commenda* was closer to the Indian Ocean than that of the corporation. It was more central to the main business routes going east. It happened to emerge in a place and time that enabled it to be carried first westward and then eastward with Muslim religion, conquest and trade. It migrated to south and east Asia with the general flow of Islamic ideas, technologies and institutions.

Interaction between civilizations does not take place only on frontiers and through conquests.<sup>33</sup> The Indian Ocean is a prime example of interaction and diffusion in multiple sites and forms. Arab merchants probably visited Indonesia before the arrival of Islam. They definitely visited China by the 8<sup>th</sup> century (Hourani, 1951; Richards, 1970). Chinese merchants traveled to Indonesia and India in Song times, if not before, and in the early 15<sup>th</sup> century, with the fleets of the eunuch admiral Zheng He, also to Arabia (Deng, 1999; Jung-Pang, 1955; Levathes, 1994 and Fitzgerald, 1972). Networks of merchants, with overseas branches and agents, spread over the major entrepôts of the Indian Ocean (Abu-Lughod, 1989; Chaudhuri, 1985). The geography of the Indian Ocean and the streams and monsoon regime made the straits of Malacca an essential passage between the South China Sea and the Bay of Bengal and beyond. Malacca became a meeting place for Chinese, Indian and Arabian

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<sup>33</sup> For the methodological and theoretical approaches, see Trivellato (2002).

merchants, and, from the 16<sup>th</sup> century, also for European merchants. Ships often harbored in Malacca for several months, awaiting the shift in the monsoon regime (see Meilink-Roelofs, 1962; Pires, 1990 and van Leur 1955). Malacca was the ultimate Indian Ocean cosmopolitan entrepot. The dominant legal view around the Indian Ocean, unlike in Europe and the Atlantic Ocean, was that of a free ocean and freedom of access to ports (Alexandrowicz, 1967). These cosmopolitan encounters were one of the triggers for the passage of individuals from one civilization to another as interpreters, navigators, agents and the like. Ships with crews from a mixture of civilizations were not uncommon in the Indian Ocean. Europeans were outsiders, or very late arrivals, to these sites of commercial, cultural, technological and institutional exchanges. While the conception of the *commenda* floated around the Indian Ocean since the 8<sup>th</sup> or 10<sup>th</sup> centuries, the conception of the corporation did not. To reach Indonesia or China, it had to be taken along overland routes, through other civilizations.

#### *4.3 Institutional dynamics*

In the first subsection of the present section we discussed institutional substitute, the family, and institutional demands, the Church, in a static setting. Here I will add the dynamic element. I will focus on two examples that expose two types of dynamics. The first come from Islamic civilization and deals with the development of the waqf. The second example comes from China and deals with the development of the family lineage organization. In Islam the institution that was adopted and adapted for semi-public functions could not be adapted as did the European corporation for business purposes. In China the institution that was adopted was in the process of adaptation for business functions and could potentially become quite similar to the corporation in its features. But its development was blocked exogenously. Timing, path dependencies and contingencies play an important role in analyzing the two types of dynamics.

#### ***4.3.1 The spread of the waqf as a substitute for the semi-public corporation***

The *waqf* appeared in the middle of the 8<sup>th</sup> century and increasingly came into use in the 9<sup>th</sup> to 12<sup>th</sup> centuries for semi-public purposes such as the building and running of mosques, hospitals, caravansaries (roadside inns), among these other social and charitable services (Kuran, 2001). It was used not only by Arabs but also by Iranians, Turks, Slavic Muslims and even non-Muslim minorities. It is clear that the Arabs or other Muslims did not use it to organize their Eurasian trade. This is a path dependency explanation: because the *waqf* was introduced first, it was adopted for semi-public purposes. Because of this the demand for importing the corporation for semi-public purposes never emerged. By using the *waqf* for semi-public purposes they did not have to encounter the absence of the corporation at that stage. Although demand for a new institution for business and trade purposes did appear at a later stage, the people of the Middle East that were already locked-in the *waqf* path.

It is interesting to note that the *waqf* did not substitute for the corporation in two important semi-public functions performed by corporations in Europe. Municipalities and universities were not organized and governed by the institution of the *waqf*. Historians of the Muslim *madrassa* and of cities in the Arab Middle East (e.g. Stern, 1970; Johansen, 1981; Raymond, 1994; Makdisi, 1970 and Arjomand, 1999) recognize that one of the main differences between these and their European counterparts is that the latter were organized based on the corporation model while the former were less formal, their governance less structured, and their legal status more ambiguous. This observation has several implications. First of all, it supports the above argument that the *waqf* was not a corporation bearing other name. It suggests that the *waqf* had features and history that prevented it from being adapted to employment in municipalities and *madrasas*. Second, it challenges the conclusion that the corporation did not develop in the Arab-Muslim civilization because the *waqf* fully supplied

the institutional demand in the semi-public sphere. Finally, it stresses the consequences of the non-migration of the corporation.

The *waqf* partly responded to the demand for some semi-public functions. But what about demands from merchants? Kuran (2005) has discussed the reasons for the absence of corporations in Islamic law. To the effect of the *waqf*, he adds the effect of family structure. The communal and family-oriented vision of early Islam disfavored the introduction of larger and more formal social and organizational forms. Larger impersonal entities could end in factionalism of the kind that is unlikely to emerge in family- and tribe-based entities. Also, demand for an institution that would serve large-scale business enterprises did not develop because inheritance and partnership law splintered business entities in the Islamic Middle East into small economic and social fragments. Atomistic enterprises were unable to act collectively to make political and legal elites introduce corporate forms of organization.

The absence of the corporation limited the organizational choices for Middle Eastern trade either to the *commenda*, or to partnerships, agents, traveling peddlers and the like. It will not be correct to assert, because the *waqf* was available before the corporation, that in the Middle East it met demand that was later met in Europe by the corporation. Some needs were satisfied by the *waqf*, some by the extended family and some by the *commenda*. Yet some, including the organization of long-distance maritime trade on a long-term basis, remained unsatisfied. As long as the *waqf* served the provision of utilities and public services reasonably well, and the *commenda* served the needs of maritime trade very well, there was no reason to import the corporation. The usefulness of the corporation to Eurasian trade was demonstrated by the VOC and the EIC only in the 17th century. Even then, there was only slow appreciation of the contribution of institutional factors to northwestern European success. Even when Arab and other Middle Eastern merchants recognized the advantages of the corporation, they could not introduce it without some support from the political and legal

elite. By the time the advantages of the corporation were fully appreciated by wider circles, European corporations already dominated Eurasian trade.

#### ***4.3.2 The transformation of the family lineage organization into a business corporation***

Over time the holding of ancestral property by the Chinese family lineage over time led to the adaptation of the lineage organization also to economic purposes. In the economic context, it was first used in support of agriculture and domestic manufacturing. The institution of the family lineage was used to promote cooperation, pool assets, spread risks, split profits and discard non-productive family members. Zhenman (2001) indicates that these objectives were achieved by a combination of lineage shaping strategies, including marriage alliances, adoption, family naming, the invention of common ancestors, the disjoining of a branch from a lineage and the conferring of property to the lineage ancestral estate. Wealthier lineages that held more common property gradually became active in manufacturing or trade, using the lineage's institutional structure for the organization of their business enterprises.<sup>34</sup> Business-related property was owned by the lineage. The lineage allowed, it is argued, not only the owning of common property, but also the formation of concentrated management, the appointment of agents and the division of profits.

Zhenman (2001) argues that by the Ming era, some of the richer and more active lineages were transformed into what he terms "contractual lineages." These lineages were based on common interests rather than on agnatic links. They actively used all the above strategies. Thus they allowed more flexibility in deviation from traditional lineage traditions. They were based on providing the investment in return for a share in the profits and control. Such shares experienced commoditization, and eventually they could be bought and sold. By

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<sup>34</sup> A forthright statement of the role of lineage, the "patricorporation," in the rise of petty capitalism in China can be found in Gates (1996).

Qing times, the organization of share-based lineages, and their trust property, had become sufficiently sophisticated to allow their use in large-scale business enterprises, such as the Zigong salt industry (Zelin, 2004, see also Ruskola, 2000 and Zelin, 1988, 2006).

Family lineages were used for maritime trade. So, in his examination of the case of two lineages of different standing in South Fukein concludes that reliance on a cohesive and wealthy lineage provided an enormous advantage. Merchants coming from such lineages could raise capital for maritime ventures within the lineage. They were also considered more credible by outsider equity investors, joint-venture partners, and creditors. These outside investors could turn to the lineage for mediation and compensation, in case of failure or dispute. Merchants from respectable lineages were more determined to protect their reputations. A merchant from an eminent lineage was much less likely to flee the homeland leaving debts and settle elsewhere (So, 2000). The lineage lowered the risk of investment by outsiders in the maritime venture and lowered the financial costs. The family lineage was gradually transformed into an institution that provided infrastructure for individual merchants.

In some of their functions lineages resemble European guilds and regulated corporations. But they were drastically different from the European joint-stock business corporations that started to play a role in Eurasian trade around 1600. In its corporate capacity, using common property, the lineage was not used for maritime trade. Why? A response to this question is not yet available in the literature. I can only offer preliminary and tentative hypotheses. When Chinese maritime trade expanded in Song times (960-1279), the lineage institution was not well adapted to commercial uses. It reached a degree of flexibility, contractual freedom and commoditization to make it applicable to maritime trade, or to industrial production, very late in its history, well into the Ming and even the Qing dynasties (16<sup>th</sup> to 18<sup>th</sup> centuries). Song dynasty maritime ventures relied on more basic types of

cooperation, such as loans, joint ownership of ships or goods, partnerships and *commenda*. The Yuan dynasty, as a Mongol invader, gave priority to foreign traders, including Muslim traders, over Chinese traders. When China made its own leap into the Bay of Bengal and the Arabian Sea lead by Zheng He in the early Ming period (early 15<sup>th</sup> century), the state, and not individual merchants or merchant organizations, served as the organizer of these massive long-ranging voyages. Thereafter, the Ming rulers reversed their foreign and mercantile policy, and turned to one of closure and isolation, denying Chinese merchants free access to overseas markets. There was no strong and long-lasting pressure to transform the lineage organization into an institution that carries out maritime trade. By the time the lineage was sufficiently flexible and contractual for the conduct of business within its framework, and could serve as a substitute for the European business corporation, the European merchant corporations in the Indian Ocean and South China Sea had become substantial and detrimental to Chinese maritime trade.

To conclude, I have offered an analysis of two distinct processes of institutional dynamics. In Arab-Islamic civilization the demand for public and semi-public functions was supplied by the *waqf*. The early adoption of the *waqf* for semi-public purposes yielded high returns in the short run. But on the longer run that adoption led to a lock-in on an institutional path that limited the development of business organization. In China the family lineage organization gradually evolved into an institution that can function for business functions. But intervention from the outside, by the Europeans and their corporations, before the completion of the process, blocked further evolution. The institution that was adopted gradually evolved to meet the new functions. China was not locked in to a dead-end path. But along the path exogenous shocks blocked the institutional transformation of an institution that was flexible enough to develop further on its own.

#### **4.4 Timing**

Timing is crucial in dynamic processes and in institutional development. According to most accounts, the *commenda* had earlier historical routes than the corporation. It appeared before the rise of Islam. Thus, its lack of tight connection to Islam facilitated its migration outside of Muslim-governed territories. It was available when Islam expanded rapidly and could migrate with it. It was used in a relatively advanced form by the 8<sup>th</sup> century, if not before, while the corporation only appeared no earlier than the 12<sup>th</sup> century. The *commenda* had an early start. It had four more centuries in which to migrate. It was formed in a unique conjuncture which enhanced its migration.

The *waqf* also had an early start compared to the corporation. As a result, by the time that the corporation emerged in Europe and became available for importation to Arab-Islamic civilization, much of the institutional demand by semi-public organizations was already supplied by the *waqf*.

The corporation was also designed in unique timing and conjuncture of circumstances. The dismantling of the extended family and the appearance of the nuclear family at the beginning of the second millennium were important factors in increasing European demand for the corporation. Another component of the contingency consisted of struggles between secular states and the Pope, which created new institutional needs of the Church at about the same time.

At the other end of the timeline, it was very late before the corporation proved to be an advantageous institution for the organization of Eurasian trade. Only several decades after the establishment of the EIC in 1600 and of the VOC in 1602, did the long-term economic performance of the corporate form, in its joint-stock variation, become evident. Earlier applications of the corporate form, which were domestic in nature, did not interact with Asian civilizations. As such, they did not present themselves as relevant to the activities of Indian

Ocean merchants. By the 17<sup>th</sup> century, Asian civilizations had less time and more obstacles to adopt the corporate form.

## 5. Conclusion

This article has focused its historical research in several stages. It began with legal-economic institutions perceived to have significant effects on economic performance: institutions for the organization of long-distance trade. It recognized that such institutions evolved in different forms in different environments. Thus, it was shaped as a comparative project that examined the institutions of four major civilizations: Western European, Arab-Muslim, Indian and Chinese. Such a comparison across civilizations is likely to generate interesting insights because of the radically different religious, social and political environments.

We have focused on the performance of similar functions, namely the organization of long-distance maritime Eurasian trade, conducted mostly in the Indian Ocean. In the period under consideration, roughly the early modern era, all four civilizations were involved in that trade. These temporal and functional foci have turned the project from one that compares institutions in the abstract to one that compares them in a very specific context. Of the various institutions involved in Eurasian trade, ranging from the state to the peddler, the project has pinpointed two institutions, the corporation and the *commenda*. The two were selected because they are located around the center of the proposed continuum for predicting of the likelihood of institutions to migrate. This enabled the article to focus on a conjuncture in which both the migration of institutions and their indigenous evolution are likely and should be examined.

The article has noted that the *commenda* migrated from Arabia all the way to northwestern Europe and to China. In sharp contrast, only the western Europeans used the

corporation in maritime trade. The distinct migration patterns of the two institutions direct us to the institutional environment, the geographical environment, and institutional dynamics as factors likely to affect institutional migration. The unique family institutions and religious institutions of Europe gave rise to the corporation. The locational origins of the *commenda*, closer the middle of the Eurasian continent and closer to the Indian Ocean, gave it an advantage with respect to migration. The Indian Ocean itself was more conducive to cross-civilization interactions and influences than the Mediterranean or the Atlantic. The migration patterns were clearly affected by the timing of the development of the institution. It was the older institution, the *commenda*, that migrated. The early origins of the *waqf* compared to the corporation allowed it to supply much of the institutional demand for semi-public organizations and by this to decrease the demand for the corporation. The late start of the process of adapting the family lineage organization to business and maritime trade resulted in blocking the adaptation dynamics with the arrival of European corporations in East Asia. Just as the English trust was on the verge of completing a successful transformation process that would make it suitable for use for business purposes so was the Chinese lineage organization.<sup>35</sup> The Chinese family lineage organization went through constant adaptations. It was not an obsolete institution when the Europeans arrived in Asia. It may well have been further adapted for business purposes or even for maritime trade. But unlike the English trust, which was defeated by the corporation within the same state and legal system, the family lineage lost ground to outsiders and its further adaptation was repressed.

The *commenda* was widely used in Eurasian maritime trade around 1600, prior to the arrival of the English and Dutch East India Companies. Thereafter, the corporation rose to dominance, first in the Levant and Russia trade, then Cape-route trade between Europe and Asia, and gradually also in intra-Asian trade. Eventually, corporation-based economies

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<sup>35</sup> On the triumph of the corporation over the trust, see Harris (2000).

became global leaders. One of the key differences between the two institutions is that while the *commenda* was basically a single-venture contract, the corporation was a lasting institution that allowed the accumulation of capital over time and even intergenerational transfer of locked-in capital. The correlation between the diffusion patterns of these institutions and the later economic performance of the civilizations that used them speaks volumes.

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