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# Anglo-American Regimes

When the thirteen states that had won independence from Great Britain adopted the Constitution of the United States in 1788, they created a federation and a federal government with the power to tax its citizens. A federation and federal taxation were new to America. However, beginning in the early seventeenth century, the thirteen colonies had already experienced taxation by a higher level government – the large and sometimes seemingly remote imperial government of England and Britain (after England's union with Scotland in 1707).

The tax regimes that developed in British North America before the American Revolution were integral components of the world's first modern fiscal state, one that had emerged following the crisis of the English Civil Wars in 1642. In both metropolitan England and the colonies, the Crown and Parliament had expanded taxation on domestic consumption and international trade, collected the taxes indirectly (meaning through third parties), established those taxes as the primary source of revenue, and leveraged their new tax revenues to expand long-term borrowing. From the revenue raised from external taxation of its colonies, England funded most of the routine costs of administering colonial governments. However, these revenues were inadequate to support British military forces in North American during wartime, so the British government often taxed and borrowed within the British Isles for that purpose.

Until 1763, British taxation of the colonies was largely external, applied to trade between the colonies and the rest of the world and trade among the colonies themselves. As such, this tax system served both as a source of revenue for Britain and a component of a complex system of British trade regulation – the system that came to be known as mercantilism. On the whole, before 1763 this external taxation was relatively light in its extent and effects and well tolerated by the colonists. Meanwhile, the British government left its American colonies relatively free to develop systems of both domestic self-governance and autonomy in funding a variety of public services. In 1763, however, to pay for the costs of fighting a major war and administering an expanded North American empire, Britain ramped up its tax effort in the colonies. In effect, it created a new tax regime for the colonies – one that was more ambitious, internal, and centralized. But the imposition of the new regime triggered a crisis of tax consent.

In 1775, the American Revolution began the destruction of this colonial regime. In 1776, the self-declared independent states replaced the British tax regime with a very weak alternative managed by the Continental Congress. In 1781, toward the end of the Revolution, they created a stronger version under the Articles of Confederation. But even this version lacked the ability to tax. Into the early 1790s, the new republic groped its way toward the formation of a fiscal state that was up to financing the debts incurred during the Revolution and to managing a public domain that had vast economic promise but also the potential for causing bitter strife. The most important milestone in that process was the adoption of the Constitution in 1788. The fiscal transitions between the end of the Revolution and the ratification of the Constitution seemed volatile and economically painful at the time, but the new nation actually created its modern fiscal state quickly and very effectively. This was largely because America's financial leaders, notably Secretary of the Treasury Alexander Hamilton and Robert Morris, had extensive familiarity with the fiscal state that Britain had forged. They readily adapted it to American circumstances.

## British Taxation

Between 1607 and the late eighteenth century, a collection of trading posts, fishing stations, and simple agricultural communities within the British-controlled areas of North America turned into a large, complex, diversified economy that was not far from experiencing an industrial revolution. Between 1640 and 1700, the transplanted European and African populations in the areas that later became the United States increased nearly tenfold, reaching about 250,000. Another one million people were added by 1750, representing a rate of population growth at least twice that in Western Europe at the time. For the free population, per capita incomes, insofar as they can be measured for this period, increased on the order of 1–2% per year, or about the same levels as experienced in contemporary England and Wales.

The settler societies in the British colonies achieved this impressive record of expansion partly because of the natural resources they controlled and the spectacular growth of complementary trade – exchanges of the products of fields, mines, woods, and waters for manufacturing goods and services – between colonists and highly commercialized and affluent metropolitan centers like London. But market conditions alone do not explain the success of the British colonial project. In achieving wealth and power, the aggressive members of the settler class in the New World and the organizers of commerce in metropolitan Britain benefited from the power provided by the fiscal state that was emerging at the same time in Britain. The British government used its fiscal muscle to promote the expansion of colonial populations and their resources through a vigorous and often violent competition with other European empires and Native American societies. Taxes enacted by the British government and the funds borrowed on the basis of those taxes strengthened Britain in that competition. The revenues provided the means to conduct war, to obtain and control more natural resources, and to protect and encourage trade.[1]

Until 1763, the colonists who paid the bulk of the British taxes collected in America were the merchants and shipowners engaged in international trade. They contributed to the tax revenues that funded the British fiscal state largely through the customs duties that they paid while

[1] The now-classic history of the emergence of what historian John Brewer calls "the British fiscal-military state," is his *The Sinews of Power: War, Money and the English State, 1688–1783* (New York: Alfred A. Knopf, 1989). Brewer correctly stressed the importance of the military functions of the growing capacity of the British government for taxing and borrowing. Richard Bonney, Patrick K. O'Brien, W. Mark Ormrod, and others have proposed a somewhat more general model for thinking about the meaning of the modern fiscal state. See, for example, Richard Bonney, *Economic Systems and State Finance* (Oxford: Clarendon Press, 1995) and Richard Bonney, ed. *The Rise of the Fiscal State in Europe, c.1200–1815* (Oxford: Clarendon Press, 1999). The formulation of Bonney, O'Brien, and Ormrod has encouraged scholars in fiscal history to move beyond Joseph Schumpeter's "tax state" model to incorporate debt finance and thus understand the crucial linkages between successful national states and financial markets. See Joseph Schumpeter, "The Crisis of the Tax State," in *International Economic Papers: Translations Prepared for the International Economic Association*, ed. Alan T. Peacock et al. (London: Macmillan, 1954). For an extension of the concept of the modern fiscal state to the experience of China and Japan, see Wekai He, *Paths Toward the Modern Fiscal State: England, Japan, and China* (Cambridge, MA: Harvard University Press, 2013).

bringing goods to and from ports in Britain. The colonists who produced these goods shared in carrying the burden of these taxes. During the seventeenth and eighteenth centuries the structure of the customs duties and the administrative procedures for collecting the duties in ports were complex and often in flux. As a result, no one has adequately measured the customs paid by importers of goods from the North American colonies or by merchants based in America who imported goods from America and elsewhere in the world, let alone estimated the final incidence of those taxes on the colonists.

The general significance, however, of customs duties to the political economy of colonial America is plain. The dynamic growth of colonial trade, and the participation in it by colonial merchants, increased the tax revenues received by the British government. In turn, these revenues contributed heavily to the financial viability of Britain, including its colonies in America. From the middle of the seventeenth century through the eighteenth century, indirect taxes, including customs duties and domestic excise taxes, dominated the tax revenues reaped by the British government. Customs duties usually accounted for between 25% and 30% of total tax revenues.[2] These revenues in turn facilitated an expansion of public borrowing on behalf of warfare and the protection of the colonies and their trade with metropolitan Britain. And, the cycle came full circle when British power fostered the economic expansion and prosperity of its mainland colonies.

Because of the well-understood linkages between customs duties and the exercise of British power, merchants and shippers in the mainland colonies accepted routine customs duties with relatively little complaint. Merchants in the British colonies understood the importance of the protection afforded by imperial power, particularly in the form of the British Navy, in a dangerous and competitive trans-Atlantic world. Until the last decades of the eighteenth century, the colonial merchants recognized that independence was not a practical option and that they were fortunate to receive protection from the nation that proved to be the strongest in the Western Hemisphere. Moreover, the merchants regarded themselves as loyal British citizens and respected the growing power of Parliament over taxing and spending.

[2] For revenue trends see Richard Bonney, "Revenues," in Bonney, *Economic Systems and State Finance*, 502–503; Patrick K. O'Brien and Philip A Hunt, "England, 1485–1815," in Bonney, *The Rise of the Fiscal State in Europe c.1200–1815*, 61–62; and Martin Daunton, *Trusting Leviathan: The Politics of Taxation in Britain, 1799–1914* (Cambridge: Cambridge University Press, 2001), 33–35.

On another level of calculated self-interest, the merchants tended to accept the customs system whenever, in assessing taxes on exports and imports, the English government treated the colonial merchants exactly like all other English merchants. This was the case in the early development of mercantilism. The English government structured the system to promote the interests of English merchants against those of merchants from other nations and provided the same benefits to merchants based in the Anglo-American colonies. Thus, in 1651, in enacting the first of the Navigation Acts, the government defined English ships to include those of its American colonists. It did so in the context of making two requirements. The first was that only English ships could carry the exports of English plantations. The second was that shipping goods from Europe to America had to be done either in English ships or ships from the countries in which the goods had originated. The major targets of this mercantilist measure were Dutch merchants, who lost trade, and their government, which lost revenue. England was waging economic war with the Netherlands, and the goal of the act was to reduce or eliminate the power of the Dutch in Europe's lucrative trade in sugar and slaves with the West Indies and to narrow the economic opportunities of the Dutch traders in their New Amsterdam colony on Manhattan Island. This was a pure mercantilist strategy designed to expand opportunities for English merchants, including English Americans, at the expense of the Dutch.

Formal military engagements ensued shortly after 1651 and continued until 1674. During the prolonged Dutch Wars, the English government enacted other measures that benefited British merchants and shipowners, including those who were colonists in America. But in contrast with the 1651 enactments, these later measures imposed some special costs on the colonists and had an impact beyond the merchant class. An example was the 1660 Navigation Act, which required that the most valuable products of colonial origin (called the "enumerated" items), including sugar, tobacco, cotton, and indigo, produced by the colonies (mainly in the West Indies and the colonies along the Atlantic coast from South Carolina to the Chesapeake Bay) had to be shipped directly to Britain. This act gave distinct advantages to consumers and merchants in metropolitan Britain by guaranteeing supplies of the products of the colonies. (Rice and molasses were added to the enumerated list in 1704, naval stores in 1795, and furs in 1724.) The measure limited the flexibility of colonial merchants who saw larger profits in taking goods like tobacco directly from America (the Chesapeake Bay region in the case of tobacco) to markets in Europe.

In 1663, Parliament placed another financial burden on the colonies by requiring that all goods exported from Europe to the colonies be unloaded first in England and subjected to a duty. If the goods were then carried to the colonies by English shippers, the duty would be remitted. Although the regulation posed no net addition to customs duties for colonial merchants, it raised costs for those who would have preferred to take manufactured goods from the European continent directly to America.

In 1673, England added one last major tax to its mercantile system crafted during the era of competition with the Dutch. This too was burdensome to merchants in the colonies. It closed a major loophole in the act of "enumeration." This loophole had allowed merchants to ship enumerated goods from one colony to another colony without going to England. Colonial captains, many of them based in Boston, obeyed the letter of the law by traveling from one colony to another and then proceeded to carry their transshipped tobacco, sugar, or other staples to a European continental port. Such trade took profits and customs revenue away from London. To close the loophole, the 1673 reform made merchants post bonds guaranteeing that they would take enumerated products only to certain British ports. If they did so, they would receive a refund of the bond. If colonial traders failed to post bond, they had to pay a Plantation Duty, which was usually equal to the entrance tax that all merchants paid when bringing enumerated items to England.

The English and the Netherlands made peace in 1674, and the English formally took over the thriving port of New Amsterdam, renaming it New York. The English had succeeded in replacing their Dutch rivals as the strongest commercial and military power in the Western Hemisphere. But a new imperial rivalry had already begun to heat up. England, now joined by the Dutch in an alliance, became deeply absorbed in a competition with France (and its ally Spain) over the Canadian fur trade, domination of the slave trade with Spanish colonies (a trade that the Dutch had previously controlled), the European and America markets for sugar from the Caribbean where both England and France had extensive plantations, and eventually for control of the vast lands in the North American interior.

As had been the case during the Dutch wars, the colonial merchants supported the English in the contests with the French, seeing opportunities for expanding the scope and profits of their own trade. But there was a growing point of contention. The wide-ranging commerce of ambitious merchants from Massachusetts, Rhode Island, and New York posed threats to British economic interests in the lucrative sugar plantations of the West Indies. The dynamic planters in the neighboring French West Indies produced higher quality, lower priced sugar than did those in the British West Indies, and trade with the French offered attractive opportunities for American-based merchants who wished to export food, slaves, and horses to French plantations in exchange for sugar and molasses for the North American market. In classic mercantilist fashion, Parliament tightened its administrative restrictions on the activities of the American merchants and, in 1733, enacted the Molasses Act. This established what the British intended to be a prohibitory duty on the import of French and Spanish sugar into the British mainland colonies. The tax remained an economic thorn in the side of American merchants until the American Revolution. However, some American merchants eased the pain by smuggling their way around the act.

The consensus of historians is that even when one takes into account the tightening of the British mercantile system in 1733, the central taxation and regulation of colonial trade by Parliament proved only moderately burdensome to the colonial economy, at least until 1763. The Navigation Acts slightly diminished colonial incomes, but the acts cannot be said to have either dramatically altered the patterns of colonial economic development or significantly reduced the returns available to the colonists in producing for export or in conducting trade.[3] Moreover, the most powerful commercial groups in the British colonies understood that the benefits of membership in the empire, especially the mobilization of naval power on behalf of the expansion of trade, far outweighed the costs of the mercantile system. With the onset of major conflicts with the French, however, both the potential costs and the potential benefits of warfare increased significantly.

The struggle between the Anglo–Dutch alliance and the French–Spanish entente encompassed five wars, grouped in two phases: two wars between 1689 and 1713 followed by three wars between 1739 and 1763. In all of these wars, the British successfully defended and expanded the scope of the commercial interests of the empire, including the American

[3] The seminal estimation of the economic impact of trade distortions was Lawrence Harper, "The Effect of the Navigation Acts on the Thirteen Colonies," in *The Era of the American Revolution*, ed. Richard B. Morris (New York: Columbia University Press, 1939), 3–39. For lower estimates, see Robert P. Thomas, "A Quantitative Approach to the Study of the Effects of British Imperial Policy upon Colonial Welfare: Some Preliminary Findings," *Journal of Economic History* 25 (January 1965), 615–638, and Peter McClelland, "The Cost to America of British Imperial Policy," *American Economic Review* 59 (May 1969), 370–381.

mainland colonies. But in each of the wars except for the French and Indian War (1755–1763), Britain concentrated its fighting, particularly its land campaigns, on combat in Europe. Through much of the fighting, France had the most potent military forces on the continent, making the campaigns exhausting and leaving relatively few resources to aid the British settlers, who fought over landed resources with the Spanish to the South and the French and their powerful Native American allies to the North and West.

Between 1748 and 1755, when the British and the French were technically at peace, tensions rose between the French and the British over their mainland colonies. The British became increasingly aware of the potential of the North American interior for supporting productive settlements and of the importance of the surging growth of their colonial populations in providing markets for British manufacturers and traders. The British challenged French control of the St. Lawrence River and the interior, while the French responded by building forts in the valleys of the Mississippi and Ohio Rivers.

At the beginning of the French and Indian War (called the Seven Years War in Europe), the British mobilized and shipped to North America the largest army ever seen in the colonies; however, during the next two years it suffered major reversals along the Canadian borders in the face of the tactically more proficient French and Native American forces. Prime Minister William Pitt responded by sending an even greater number of British troops to the American theater, despite the fact that war now also raged on the European continent. And, under Pitt's leadership, the British government for the first time provided significant funds to pay for the troops that the governments of the colonies mobilized. With the advantages of much greater numbers, incorporation of tactics favored by Native Americans, and the effectiveness of the British Navy in cutting off supplies from France, the combined British and colonial forces recaptured lost territory in the Ohio valley, the fortress of Louisbourg, and, in 1759, the city of Quebec, which commanded the St. Lawrence River.

The Treaty of Paris that concluded the war in 1763 confirmed that the British intended to secure and expand their control of landed resources in North America for the aggressive growth of the settler communities. For the first time, the British placed the acquisitive territorial priorities of the colonists ahead of traditional mercantile commercial policy. Most important, the British took possession of virtually all of French Canada and most of the territory the French had claimed in the valleys of the Ohio River and the Mississippi River, which now became the Western boundary of British North America. (The major exception was New Orleans and Louisiana, which Britain transferred to its ally Spain while acquiring most of Florida from Spain.) But powerful Native American groups still controlled most of the newly acquired lands. For British Americans, the major outstanding issue was the determination of how they would be able to exploit the new conquests and the resources they offered. To do so would require massive public resources – that is, tax revenues and the additional financial resources they could generate – and an effective government.

## American Experiments in Fiscal Autonomy

Throughout the colonial era until 1763, the British government retained the power to tax and regulate the external trade of the colonies but left the Americans largely in control of their internal taxes.[4] This control developed under the powers that most of the governments of British colonies derived from royal charters and commissions or instructions to royal governors. These documents usually replaced the charters that the Crown had originally granted to great lords (proprietors) or corporations in order to promote development of colonies.[5] For example, in 1642, when Sir William Berkeley arrived in Virginia to serve as royal governor he had instructions from the king to summon a colonial assembly (the House of Burgesses). The instructions gave the assembly the "power to make acts and laws for the government of that plantation correspondent, as near as may be, to the laws of England." That power was understood to encompass internal taxation, although the instructions made clear that in all matters "the governor is to have a negative voice [the veto power]."[6]

4 The only possible major exception was the quit-rent. This was a payment that many colonial landowners were obliged to pay to the Crown or a founding corporation or proprietor. Quit-rents could be substantial and were similar to taxes in that they were earmarked for support of British officials or representatives of a proprietor who served in the colonies. But quit-rents, which landowners owed in lieu of feudal obligations, were actually more like rents than taxes in that they were fixed and the only sanction for non-payment was performance of the feudal obligation. The authoritative history remains Beverly W. Bond, *The Quit-Rent System in the American Colonies* (New Haven: Yale University Press and London: Humphrey Milford and Oxford University Press, 1919).

5 Pennsylvania and Maryland were founded under charters to proprietors William Penn in 1681 and Lord Baltimore in 1632, and Rhode Island and Connecticut were established under corporate charters.

6 "Instructions to Sir William Berkeley as Governor of Virginia (1642)," in Merrill Jensen, ed., *English Historical Documents, American Colonial Documents to 1776*, (New York: Oxford University Press, 1962), 187. In 1639, the previous governor of Virginia, Sir

Later, when the crisis that led to the American Revolution took hold, the colonists would claim that the power of assemblies to legislate was a right that English citizens enjoyed under the nation's unwritten constitution. However, in 1642, and throughout the colonial period, the Crown and Parliament assumed that the colonists enjoyed only those rights that were granted by royal charters and instructions.[7]

As a practical matter, until 1763, the strong, and growing, interest of the British government in fostering the successful economic and social development of the North American colonies led Britain to extend great latitude to the colonies in establishing internal systems of taxation and public finance. Tax rates and types of taxation varied substantially from colony to colony, and even from community to community within particular colonies, depending on modes of political organization and the distribution of economic power. British taxing traditions were diverse, and the various colonies and local communities had a rich array of institutions from which to choose: taxes on imports and exports from other colonies; property taxes (taxes on the value of real and personal assets); poll taxes (taxes levied on citizens without any regard for their property, income, or any economic characteristic); excise (sales) taxes; and faculty taxes, which were taxes on the implicit incomes of people in trades or businesses. The mix varied, but each colony made use of virtually all these different modes of taxation.[8]

The New England colonies relied on property taxation more heavily than did the other colonies, and such taxation or its equivalent usually formed the core of the revenue systems of New England. Taxation by towns accounted for most tax revenues in New England. In the

Francis Wyatt had been the first royal governor in the colonies to arrive with instructions to call an assembly, but Berkeley's instructions were much clearer and elaborate. Charles M. Andrews, *The Colonial Period of American History: The Settlements* (New Haven: Yale University Press, 1934), 204–205.

7 Leonard W. Labaree, *Royal Government in America* (New Haven: Yale University Press, 1930), 174–175.

8 We now have the benefit of two superb surveys of colonial taxation. These are Alvin Rabushka, *Taxation in Colonial America* (Princeton: Princeton University Press, 2008), which is detailed and comprehensive, and Robin L. Einhorn, *American Taxation, American Slavery* (Chicago: University of Chicago, 2006), especially 11–109. Einhorn's book is valuable for understanding the long-term implications of the tax-regime differences, North and South, which developed during the colonial era. The best overview of the faculty tax remains the chapter on "The Income Tax in the American Colonies," in *The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad*, ed. Edwin R. A. Seligman, Second Edition (New York: Macmillan, 1914), 367–387.