

# PUBLIC EXPORT INSPECTIONS IN THE UNITED STATES AND THEIR PRIVATIZATION

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Transacting in the marketplace can be a very costly activity. Economic growth, in part, depends upon the development of institutions that minimize the cost of exchange (Barzel 1982 and 1989). An important component of that cost is measurement cost. When measurement cost is significant, market participants have an incentive to cheat by making false claims as to the quantity and quality of goods they are selling. Companies that are large in relation to their market depend upon repeated sales among groups of customers who exchange information. Cheating thus is constrained by the need to establish a good reputation. The optimal scale of reputation and production, however, are often very different. Consumers find it costly to learn the reputation of the thousands of companies with which they may potentially do business. Institutions have arisen, both private and public, to guarantee quality: Underwriters' Laboratory, the Food and Drug Administration, and the Securities and Exchange Commission are examples of such institutions. Each inspects a large number of goods or services and certifies certain dimensions of their quality. The services offered by these organizations are potentially valuable because they permit a separation in scale between production and reputation. They will be most valuable for competitive markets in which a uniform good is produced by many small-scale producers. As Ronald Coase (1988: 9) points out, the closer a market approaches perfectly competitive conditions, the more regulated transactions tend to become.

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In early 19th-century America, most producers of export goods, typically farmers, were very small relative to the increasingly impersonal international market. Good will was difficult to accumulate, so producers had a significant incentive to cheat their anonymous customers. Attempts, both private and public, were made to establish mechanisms that would discourage cheating. Within the public sphere, the most prominent of such mechanisms was the state inspection. In a commercial center like New York City few wholesale transactions took place that did not involve some government official. These inspections were valued by democratically elected politicians partly for the patronage opportunities they offered. Until the 1840s inspections were always treated as a government monopoly. Their widespread use by producers even when not required by law shows that they rendered a sometimes valuable service, but the service might have been rendered better by the private sector. Beginning in the 1840s, larger ports began to render voluntary those inspections which had been mandatory or to get out of the inspection business altogether. Private means of enforcing quality were allowed to more fully develop. Trademark legislation was drafted and enforced, private brand names gained importance, and trade associations arose to offer private inspection services. The abandonment of mandatory public inspections in New York, by far the nation's largest exporter, was followed by a significant increase in the proportion of U.S. exports shipped through New York harbor. This increase may have been coincidental, but states competing with New York for export business seemed to have linked the increase with the change in policy, and they responded by privatizing or making voluntary many of their own public inspections.

Ronald Coase (1994: 12) has called for research into market institutions, most recently in his Nobel lecture, but research into their historical development is still a relatively new field and examples are scarce. Paul Milgrom, Douglass North, and Barry Weingast (1990) and Avner Greif (1989, 1993) have examined the development of institutions to establish and communicate the reputations of merchants in the medieval European economy. Craig Pirrong (1995) describes the role played by the Chicago Board of Trade in overcoming transaction costs and the problems the Board encountered. The only other American market that has received significant attention is that of 17th-century Chesapeake tobacco (Schweitzer 1980).

The lack of research into export inspections is unfortunate since export quality control is still handled by the public sector in many developing countries and the development and enforcement of trademark law is an ongoing problem. The American colonial governments originally got involved in inspections apparently to meet a need that

was not otherwise being addressed, but inspections then came to be a politically profitable institution that was largely taken for granted. The American experience privatizing its export inspections is interesting mainly for the role played by competition between local governments. Early struggles over inspections generally involved conflicts between localities with different interests. The New York privatization in the 1840s followed close on the heels of the transportation revolution that increased competition among the states. The desire to attract more commerce from other states was a prominent reason given for ending state inspections, and other states felt they too needed to loosen restrictions to continue competing with New York.

In this paper, I first examine the costs and benefits of government quality control and how this influenced the spread of the system. Then I consider the organization of inspectors and weighers and how this affected their service. Finally, I look at the privatization of quality control.

## State Inspection and Measurement Costs

John Wallis and North (1986) show that transaction costs have been a large and growing part of the U.S. economy. A major component of transaction cost is the measurement of the quality and quantity of goods and services exchanged. This process often involves significant expense. Minimizing measurement costs is a major factor in determining a market's organization.

In a traditional economy, trading takes place between people who know each other. If one person cheats, others may refuse to do business with him. Such ostracism may be sufficient penalty to deter cheating without legal sanctions. As markets grow, anonymous transactions become increasingly important and measurement costs grow. The problem of measuring American produce in the 18th and 19th century was exacerbated by the large differences in optimal scale economies for production and for reputation. International markets had grown very large but American exports were typically produced by many small, competitive production units. Throughout the period the size of production units was increasing but so was the markets' size.

The problem of quality control could to some extent be handled through the common law. The law provided a mechanism by which a cheated buyer could not only boycott the seller who had cheated him but further take the seller to court and gain reimbursement. The problem with that approach, however, was that it was a lengthy, uncertain process. In the export market, frauds might go undetected until the produce was already shipped overseas. It would no longer

be clear whether the producer, the exporter, or some other middleman had perpetrated the fraud, and prosecuting most of those people would be impractical. Beyond reliance on the common law, Americans had three basic strategies to keep measurement costs low. First, the public sector legislated standards to supplement the common law to make legal redress less costly and more certain. Second, within the private sphere, hierarchies of middlemen developed—factors and brokers who could buy and sell among those whose reputation they knew. Finally, the government could establish inspections and weighings.

Legislated quantity and quality controls have been quite common throughout American history. Their purpose was to make the settlement of disputes cheaper by fixing certain dimensions of quantity and quality or, at least, the means of their measurement. A typical requirement legislated was that all firewood must be sold in cords (*Colonial Laws of New York* 1894: I, 164 and *Revised Statutes of North Carolina* 1837: 346). This may have simplified firewood measurement without causing too much inconvenience to those in the firewood market. Similarly, in many states, grain could only be sold by weight (*General Statutes of the Commonwealth of Massachusetts* 1860: 265). Detailed specifications were often set for containers (*Compiled Laws of the State of Michigan* 1872: I, 474). New York bricks need all be of one particular dimension (*Colonial Laws of New York* 1894: I, 554–57) and Rhode Island charcoal could be sold only when measured in specific-sized bushel baskets approved and sealed by a state official (*Revised Statutes of the State of Rhode Island* 1857: 265). Controls such as these were enforced by informers who received half of any fine recovered.

The second alternative to inspections was an extensive use of middlemen. This alternative was used in Southern markets with relatively large-scale plantation production. There was little government regulation of the cotton market beyond the common law. Leading citizens of Mobile worried that poor inspections by factors lowered the value of Mobile cotton, but instead of going to the legislature, the Chamber of Commerce simply passed a resolution requesting that factors change their practice (“Mobile Cotton” 1841). Cotton factors formed long-term relations with those with whom they bought and sold. The ability to build a reputation within such a market made producers less apt to cheat. It is not very clear why some products relied on middlemen while other production relied on inspections. Scale economies may have been important, but sometimes the deciding factor may have simply been political entrepreneurship.

The third approach to dealing with measurement costs (the approach dealt with in this paper) was to institute public inspections. Inspections were a method of bringing many small producers together to form one large state brand. The state brand would hold a sufficient market share to gain a reputation for quality which should have raised the export's price. Inspections were first instituted for Virginia tobacco (Hening I, 1823: 203–7) and then in the 18th century were adopted throughout the colonies for meat, flour, and other exports. After the Revolution the use of government inspections continued to increase. For example, New York's session laws show that inspections of pork and beef, flour and bread, rum, molasses, potash, sole leather, and hemp were required before the Revolution. After the Revolution, inspections of lumber, staves and heading, fish, fish oil, salt, hops, flaxseed, shingles, tobacco, green hides, sperm oil, and oak bark were added. Western and Southern states often had fewer inspections, but even a relatively less-regulated state like Louisiana had mandatory inspections of pork, beef, flour, and tobacco (*New Digest of the Statute Laws of Louisiana* 1841).

An organized inspection system had several advantages over a system leaving inspection to the buyer. Although in either system all goods needed to undergo inspection by someone—either a buyer or inspector—one who examined a particular commodity's quality as a full-time job may have done the work more efficiently than a merchant who traded in numerous commodities. An official inspection could also make multiple inspections unnecessary when produce passed through several hands within a short period of time. Finally, inspections simplified trading by dividing produce into a small number of standard grades (Telser and Higinbotham 1977).

Inspections were seen as a means of assisting producers and centered primarily on export goods. Inspecting goods for export markets while neglecting home markets might seem an unusual policy to those who think of inspections as consumer protection. Inspecting produce bound for distant consumers, however, makes more sense economically since information and enforcement costs for distant consumers are higher. Not only did inspections of exports yield greater benefit, but they also cost less. Exports were much easier to monitor than in-state sales.

The most obvious cost to the inspection system was the payment required to maintain inspectors and inspection facilities. The official inspection fee was generally 0.5 to 4 percent of an item's price. The inconvenience of bringing goods in for inspection was sometimes a greater cost. This cost limited the inspections that could be established in rural areas. In New York, for example, leather and lumber inspec-

tions were only extended gradually by county as population grew throughout the early 1800s (for example, New York State Legislature 1808: chap. 124 and New York State Legislature 1829: chap. 51). Those who wished to export goods liable to inspection from towns in the Northwest Territory without inspectors had to pay the nearest inspector's travelling expenses (Northwest Territorial Legislature 1802: chap. 8).

A less obvious cost to inspections was their inflexibility. Fixed government standards not only forbade modifications that might otherwise be useful, but also made the experimentation upon which progress depended illegal. Thus, a trade-off existed between standardization and variation. Over time, as the economy grew more complex, state governments moved toward a greater variety of standards. In early colonial New York, only one size brick had been allowed. By the 1790s, when Maryland passed its brick regulations, two sizes were allowed (Maryland State Legislature 1791: chap. 49). In the colonial period, there was typically one grade of beef, pork, and flour in each state. By 1800, at least three qualities of these goods were permitted in virtually every state.

The immediate problems of inflexible standards are best seen in the mistakes and controversies that inspection systems entailed. Rigid standards could get in the way of trade between areas in which standards differed. In 1781, Maryland passed laws specifying the dimensions a flour cask must have to pass inspection and be shipped out of Baltimore (Maryland State Legislature 1781: chap. 12). These dimensions were different than those specified by Pennsylvania and Virginia law so that flour from these states could not be shipped through Baltimore until the law was modified the next year (Maryland State Legislature 1782: chap. 5). A more serious problem was beef exports to Britain. British liked their beef less salty than Americans (Perren 1978: 72). Beef sales to Britain were held back by mandatory state requirements that beef be processed only after the American-style. This became particularly important after the British revised their tariff system in 1842. The opening of this potentially lucrative market was instrumental in pushing inspection reform through the New York State Legislature in 1843.<sup>1</sup> A special export of meat in tubs had always been sent to Europe, in spite of the inspection laws, and was eventually legalized (New York State Legislature 1801: chap. 138).

<sup>1</sup>The only individual exemption from the inspection laws made in New York was the special permission given to Joseph Sparrow, an Irishman, to process meat in the Irish fashion for export to Ireland (New York State Legislature 1808: chap. 63).

Besides differing regional standards, simplistic standards could also hurt quality. When the New York colony first imposed a flour inspection, inspectors were only to inspect flour for fineness. Some mills overground their flour to meet this requirement, damaging the flour in the process so that it would not rise properly. Complaints were made that the value of New York flour was falling and the law was changed to give the inspector wide discretion in determining a flour's merchantability (*Colonial Laws of New York* 1894: V, 1096–98). The long-run danger of inspections was that they would establish a static level of quality which would not advance with technical change. There is no hard evidence that this was the case, although accusations that inspections slowed quality improvement were voiced by inspection opponents.

Inspection systems not only existed to create state brands but also to provide political patronage—"to create fat offices for political workers" (*Albany Argus*, 13 March 1843). Of the 2,238 positions filled by the New York governor, 372 were inspectorships and 109 were weighers and measurers (*New York Evening Post*, 13 July 1846). These amounted to 22 percent of state political appointees. New York inspections garnered more than a third the amount raised by state taxes (*New York Evening Post*, 17 December 1842). Inspections and inspectors thus bulked large in state politics. Many inspectorships in small towns were only income supplements, but some important New York City inspectors were accused of earning four or five times as much as supreme court judges while doing very little work (*New York Tribune*, 6 August 1846). The political importance of inspectorships was made obvious by the big political battles waged in the legislature over relatively small changes in the inspection law (*Albany Argus*, 30–31 March and 17 April 1843). To politicians, the patronage allowed by the inspection system was a benefit that increased the attractiveness of the system. The political overhead inherent in the government inspection system, however, raised costs to producers and consumers and was certainly a factor in their eventual privatization.

## The Organization of the Inspection System

The structure of the inspection systems varied from state to state and was occasionally changed within states. Overall, however, the form of inspection laws differed little from late colonial times to the mid-19th century. Inspectors were supposed to work for a set fee. They passed the great majority of goods they examined, usually branding them the highest quality.<sup>2</sup> When a producer disputed an inspector's ruling, an arbitration panel of three people was generally convened.

<sup>2</sup>In New York City, in 1842, approximately 95 percent of flour inspected was branded

Those who tried to dodge mandatory inspections risked a fine and confiscation of their produce. Transporters of uninspected goods also faced fines. In Maryland, ships, wagons, horses, and oxen used in transporting such goods illegally were confiscated (Maryland State Legislature 1785: chap. 65). Inspectors were commonly given the right to search suspect ships without obtaining a warrant. In some states, places of business and even homes could be searched at will (*Digest of the Laws of Pennsylvania* 1862: 547–48 and *Code of Tennessee* 1858: 383). To control smuggling and protect inspectors' local monopolies, New York passed a law forbidding uninspected timber from being transported across county lines (New York State Legislature 1801: chap. 59).

Controversies concerning state inspection centered on four questions. First, should the system be administered by local government or should it be a state-wide organization? Second, should inspectors be given monopoly power or should they be forced to compete among themselves? Third, should inspection be mandatory or should it be offered as a voluntary service? Finally, and most importantly, should inspections be offered by the public sector at all? (This last question—the question of privatization—will be treated in the next section of this paper.)

Control of inspections was sought both for the patronage it allowed one to bestow and to create favorable inspection policies to give advantage to one's constituents. An example of a struggle for control is found in New York City, where flour inspection was first begun at the municipal level. Colonial legislation followed later regulating the city inspection and setting up other inspectorships controlled by the legislature itself. The colony as a whole was unhappy that the city repacked meat without regard to the colony of origin. Southern colonies shipped meat to New York City for re-export. The colonial legislature saw this Southern meat as inferior. The legislators believed that labeling Southern meat with the same brand as New York meat lowered the quality of the New York brand, thus cheapening the prices their constituents received for their exported meat. The colony required that barrels of meat from Maryland, Virginia, and North Carolina be clearly branded M, V, or NC to distinguish them as lower quality produce (*Colonial Laws of New York* 1894: III, 77–79).

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"superfine." Approximately 3 percent was found "bad." Approximately 75 percent of potash was found to be of "first quality" while only 2 percent was condemned. Over 95 percent of the hops inspected was "first quality" while less than 1 percent was condemned. Meat inspectors divided the meat they inspected fairly evenly between the top two categories: 9 percent of the pork and 5 percent of the beef was condemned (Young 1843).

A more interesting issue economically was whether inspectors were best given monopoly power. In some cases, a number of inspectors had overlapping jurisdiction. In other cases, an inspector had control over all production in his area. A blatant disregard for inspection legislation could lead to a trial or the overturning of his decision by an arbitration committee, but otherwise no producer in his area could export without his approval. The fee received for inspection services, whether competitive or monopolistic, was legally fixed; but illegal kickbacks made the fee variable in practice (New York State Legislature 1808: chap. 63). Other dimensions of service could also be varied—the promptness of inspection or the strictness of standards.

The argument for competition among government inspectors is simply that, in a market for well-defined goods and services without externalities, increased competition will move the market toward a Pareto-optimal equilibrium. The trouble with competition from a politician's point of view was that the important patronage tax was competed away. The inspectors would no longer receive the monopoly profits that they expected for their political service. Instead, they were forced to work harder and give back their profits as kickbacks to attract customers. Economically, competition along some of the dimensions of inspection services did have negative external effects. In particular, competition could drive rival inspectors to lower their standards. This would not be a problem if each inspector had a well-distinguished personal brand. In such cases, lowering the quality of one's own brand would only affect the price received for goods of that brand. The point of the inspection system, however, was to achieve a sufficient market share to maintain a reputation by bringing a state's goods all under *one* brand. To the extent such a policy was successful, the lowering of standards by an individual inspector would mean a smaller drop in price spread over the entire state brand. Giving the inspector monopoly power lessened his incentive to lower standards by lowering the elasticity of demand he faced for his services.

The best-documented political struggle over such a monopoly was the fight over the official weighing system of New York City. Weighers can be treated as a special type of inspector who only inspected one particular quantity dimension of a good. In New York City all wholesale transactions of goods measured by weight had to be weighed by an official. Furthermore, laws specified a number of important goods that were required to be sold only by weight. An official weighing system was thought very important to country buyers who bought in bulk with no convenient method of checking weight claims (Ross and Smith 1844). Until 1835, weighing was considered a city government affair. All weighing had to be done by official appointed weighers,

but there were 50 or 60 such weighers who were in constant competition for work. Big companies made a practice of permanently hiring weighers or obtaining an official appointment for one of their own employees (“Report of the Select Committee” 1832). Weighers often could not extract the high fees legislated.

In one case, a weigher received a fixed salary of \$500 per year plus one-fourth of his fees from a company that had permanently hired his services. It was estimated that his fees would have come to several thousand dollars per year at the legislated rate. The large establishments who sought out and hired the city weighers not only extracted fee concessions, but could also pressure weighers to weigh heavy or light—if either was to the business’ advantage (McDonald 1835). The system that actually functioned, therefore, was little different than a private system. Each company was restrained from cheating mainly by the need to maintain a reputation. The city’s weighing system may have increased cheating since blame for incorrect weights could be apportioned to the nominally independent weighers. Several witnesses before the legislative committee testified that they had stopped buying and selling by weight to avoid the corruption. In 1835, a bill was brought before the legislature creating a state weighing system for the city. A weigher general with 30 subordinate weighers was to be given a weighing monopoly. Work and fees were to be shared equally among the subordinates (New York State Legislature 1835: chap. 183). City businesses fought hard against the inconvenience this would entail (Lenox 1835) and as a compromise, the city system was allowed to continue. City weighers were left in charge of weighing all produce to be consumed and produced within the city. The state weighers were to weigh produce leaving or entering the city (Ross and Smith 1844). The state, however seems to have had trouble enforcing this law (Downing 1838).

A third question was whether inspection should be mandatory. American producers who benefited from inspections would presumably use them voluntarily. Many inspections were voluntary but most important inspections were not. There were several reasons why an inspection may have been made mandatory. First, and probably most importantly, they were the livelihood of a group of men who had powerful political connections. If the cost to the voters of making inspections mandatory was not too much greater than any benefit that they might gain, then the benefit to office seekers would probably determine the issue. There were three possible benefits that producers might gain to offset costs. First, by making inspections mandatory, the number of producers within the state brand was enlarged. If reputation was subject to economies of scale, then allowing a producer

to drop out could have hurt the other producers of that brand. Second, mandatory inspection might also protect the reputation of state brands from dilution among unsophisticated consumers who did not differentiate between inspected and uninspected produce coming from a certain state. Finally, uninspected produce could be fraudulently branded at sea. After inspection was made voluntary in New York in 1843, inspectors did complain that producers imitated inspection brands to fool consumers (Benton 1845).

## The Shift toward Private Quality Control

Until the 1840s, inspection was virtually always a public monopoly. Few private enterprises attempted to set up inspection companies. One difficulty to be faced was that any brand they used would not have received much legal protection. The common law protected the trademarks of vendors and manufacturers exclusively (Upton 1860: 203, 209). There was no precedent for protecting a company selling inspection services.

In any case, such protection was largely moot. No trademark cases were brought to court in the United States until the British began suing U.S. companies for trademark piracy in the mid-1840s. Once a government service was set up any private competition was foolhardy. Inspectors were men who had demonstrated effective political power in gaining their positions. In rare instances when private inspections were attempted, special bills were introduced specifically forbidding competition in the area threatened (New York State Legislature 1830: chap. 306).

Attempts were made by producers to band together informally to establish premium brands without inspection. This usually occurred when there was large differences in quality between different regions within a state. Tobacco products manufactured in Richmond, for example, were known to be of high quality. Consumers paid more for the Richmond label although they might not know all the small Richmond businesses by name. In the 1830s, some tobacco manufacturers outside of Richmond were using "Richmond" as part of their name to mislead customers. The tobacco manufacturers in Richmond pushed a bill through the state legislature in 1835 forbidding any tobacco manufacturer outside of a city from using that city's name on its label (Virginia State Legislature 1835: chap. 64). Similarly, Genesee valley flour from western New York sold at a premium although many customers were not acquainted with the particular mills. This allowed eastern New York competitors to fraudulently claim to be producing Genesee flour without pirating any particular

company's brand (*Rochester Democrat* May 18, 1843). In the Colonial and Early Republican eras, giving government agents a vested interest in a brand of inspection may have been the only feasible means of protecting it.

In the early 19th century, there was some movement away from government inspections, primarily in the South. Most notably, South Carolina in 1810 made inspections voluntary in Charleston and Georgetown (South Carolina State Legislature 1810: no. 1973). Kentucky followed, making inspection of flour and tobacco voluntary in 1810 and 1815, respectively. In general, however, inspections in the South slowly increased and in the mid-19th century a number of inspection regulations were reintroduced in Charleston. The privatization of quality control was primarily a New York phenomenon which occurred in the 1840s and spread in part to other important port states in the late 1840s and 1850s.

By the 1840s, the free-market Locofoco Democrats of New York had long been ideologically opposed to state inspections. Their opposition was sometimes seconded by Whigs who, when out of office, would denounce the political corruption in the system. After the mid-1820s, a series of counties had got their residents exempted from mandatory sole leather inspections. Individuals who produced over 100 barrels of meat got themselves exempted from inspection also (New York State Legislature 1802: chap. 117). Presumably, they took this step because they were of sufficient size to establish their own reputation. Until the 1840s, however, the inspection system showed no sign of being in serious political trouble.

Two political events sparked the rebellion against the New York inspection system. First, the British revised their tariff. This opened a potentially lucrative market for beef, but only beef processed, pickled, and packed after the British manner. State laws had the unintended side effect of making the export of British-style beef illegal and this caused an uproar (*New York Evening Post*, 12 January 1843 and *Albany Journal*, 11 March 1843). People worried that the port of Boston, which had no meat inspection, would now gain advantage. Smuggling uninspected British-style beef became common (*New York Evening Post*, 25 March 1843). Second, the 1842 state elections removed the Whigs from power. The result was a Democratic legislature, a Democratic governor and a complete set of Whig inspectors (*New York Evening Post*, 21 November 1842). Horace Greeley's Whig *Tribune* egged on barnburning Locofocos to stick to their principles and not simply replace Whig inspectors with Democratic office seekers (*New York Tribune*, 4 April 1843). The conservative faction in the Democratic party was reluctant to oppose this reform openly. Whig

inspectors were replaced by Democrats, but in the spring of 1843, a bill was put forward to make all “inspection, measurement, gauging, branding, culling, approving, examining, weighing, sealing, marking, stamping or sampling” at the state, county, or city level voluntary (*Albany Journal*, 11 March 1843).

The voluntary inspection bill was to pass, somewhat amended, by a huge majority (*New York Evening Post*, 18 April 1843). It was very popular but it was not universally liked. The traditional suspicion of unchecked capitalism was voiced by an “Old Hunker” writing to the *Evening Post* who argued that the end of inspections could well mean chalk in the flour and paving stones in hogsheads of tobacco. He predicted:

Allow any man to send his goods abroad without being branded as to quality by a legally constituted sworn and highly respectable and responsible state official and see the consequences. Incongruous shingles will rot on every West Indian wharf. Our beef and pork will lose that fine moral effect which springs from uniform size of package and the Inspector’s brand. Foreign bakers will grow suspicious of New York millers, and all that beautiful order and arrangement so satisfactory to the foreign purchaser . . . will be precipitated into one rude chaos of commercial confusion [*New York Evening Post*, 23 March 1843].

Locofocos who opposed mandatory inspection argued with two voices. Some felt inspections superfluous. The problem of small producers maintaining a reputation abroad was minimal. Proponents of this view pointed to the fact that individual brand names were becoming important. Massachusetts had no meat inspection, but the provisions of Winchester’s packing house in Boston were well-respected throughout Britain (*New York Evening Post*, 14 January 1843). At home, people no longer simply bought New York flour but wanted Kempshall’s flour or Beach’s flour (*New York Tribune*, 6 August 1846). The growing importance of private trademarks was real. The first common law trademark case in the United States was tried in 1844 (Cox 1871: 14), and in 1845 New York became the first state to legislate private trademark protection (Rogers 1914: 48). The aftermath of quality control privatization, however, proved that inspections were still important.

The second argument made was that inspection could be best handled within the private sector. The state tobacco inspection was very popular with producers (Corn’s Dubois, Jr. & Co. et. al. 1839), and the tobacco inspector was chosen according to the recommendation of the tobacco dealers (*New York Evening Post*, 21 November 1840). Why could not tobacco dealers be left to handle their own affairs

without state help? Competition among state inspectors led to corruption while monopoly led to bad service (*Albany Argus*, 20 February 1843). Both systems meant patronage. Moreover, most politically appointed inspectors had no expertise in the goods they were supposed to inspect (*Albany Argus*, 7 August 1846). The *New York Tribune* (16 March 1843) gave the following case of a hypothetical Boston merchant passing through New York harbor with a thousand barrels of Ohio flour:

He wants no inspection—the highest privilege he asks is to be left alone. Yet the moment his vessel touches our dock, a gang of Flour inspector’s deputies jump aboard and proceed to bore into his barrels, haul out and waste his flour, mark and plug and hammer, and at last the owner who has protested against the whole proceeding and whose property is seriously damaged by it is called on to pay a round bill for the mischief done him! If this is justifiable then our country was very wrong in making war on Algiers and Tripoli for doing substantially the same thing.

New York businessmen worried that mandatory inspection lost them Southern and Western trade. It was asserted that Virginia flour was loaded for abroad in the James River rather than shipped through New York to avoid receiving a New York brand which would lower the value of the premium Virginia flour in the eyes of suspicious foreign customers (Carow 1841). It was likewise claimed that New York’s inspections lost the state \$500,000 of business to New Orleans in 1842 (*Albany Journal*, 4 April 1843).

New York Secretary of State Samuel Young was one of the most impassioned opponents of the state inspection system. Examining those fields of production dominated by very small producers, Young concluded that an individual could not obtain a reputation for quality in the market. He must rely on an inspection that would assure the quality of his goods. Young’s anger toward state inspections was due to their low unchanging standards. Under the state system, individuals had no incentive to produce better goods than would be approved by the inspector, and the inspector had little incentive to risk his business and his political patron’s popularity by raising his standards. Young believed that under a system of competing private inspectors less conservative standards of quality would develop. Young (1843:9) facetiously stated: “It is hardly a hyperbole to affirm that if government from the beginning had appointed and rigidly maintained inspectors of human raiment and habitations, mankind would now occupy caves and huts and be clothed in the skins of wild animals.”

Inspections were made voluntary as of December 1843. Laws were passed in 1844 and 1845, however, forbidding private inspection in

the city and county of New York, and in Kings county respectively (New York State Legislature 1844: chap. 276 and New York State Legislature 1845: chap. 218). Returns of inspected goods show a decrease in inspection of meat and lumber relative to exports. The meat inspector complained in 1844 that his customers had become limited to out-of-state shippers in the coastal trade. Inspection was an integral part of the distribution network for items such as potash, hops, and tobacco, and the government's continuing inspection monopoly forced producers to sell through the government inspector. The returns show no decline in these inspections (Young 1843, 1844; Benton 1845, 1846). In New York City, the law that all grain must be weighed by a public weigher was invalidated, but it was still illegal for anyone but a public weigher to weigh grain. Attempts by producers to legally return to a competitive weighing system were defeated (Ross and Smith 1844).

New York State held a constitutional convention in 1846. Opponents of inspections dominated the convention and vociferously denounced the continuance of public inspection services (*Albany Argus*, 7 August 1846). Inspectors lobbied hard but to no avail, and in November 1846 a constitution abolishing all state inspections and weighings was adopted.

Information on the private inspections that arose to take the place of public inspections is fragmentary, but it is clear that private companies competed vigorously to gain a market share in this newly opened service industry. In January 1847, just as the new constitution went into effect, two rival potash inspection firms opened in New York City and began advertising their services. One was run by the ex-official inspector. Both businesses advertised rates 20 percent lower than had been charged under the state system (*Shipping and Commercial List*, 2 January 1847, and 6 January 1847). An article in the *Shipping and Commercial List* (23 January 1850) reports that in January 1850 the Association of Receivers of and Dealers in Flour met and, "after a full discussion of the evils consequent upon the existence of two Boards of Inspectors, and the competition between them," resolved to establish a single board with a uniform standard. By this time private brands seem to have become much more important in the New York market. Wholesale prices were no longer quoted in price lists simply under the rubrics "superfine," "fine," and "middling." Now price lists referred to "common brands," "extra brands," "fancy brands," "straight brands," and "favorite brands." Another article in the *Shipping and Commercial List* (19 January 1853) reports a private meat inspector as stating that almost all meat arriving in New York City underwent private inspection and repacking as this was found

“more profitable and safe in the end.” He claimed that the lack of inspection in Boston made its meat less valuable.

Prices were separately listed for “city” and “country” meats with inspected city meats sold at a premium. In 1852, *Wilson’s Business Directory of New York City* listed seven meat inspectors, two liquor inspectors, eight flour inspectors (at four addresses), one inspector of leather, twelve inspectors of lumber, three inspectors of mahogany, one inspector of potash, and one inspector of tobacco. Some of these inspectors may have been working together within one organization and some inspectors may not have been listed. Mahogany seems to be the only new inspection created in the private sector. The system that evolved in New York was probably similar to that which developed in Chicago for which much more information exists (see Pirrong 1995).

Trade statistics from this period suggest that the mandatory inspection system had indeed outlived any usefulness it might have had in the past. As the figures show, the 1843 reform coincided with a major upswing in New York’s relative importance as an export center for American goods. In the five years before the change, October 1837 to September 1842, 20.9 percent of U. S. exports passed through New York. This jumped to 28.2 percent in the five-year period July 1843 to June 1848. Impressive increases in imports and foreign re-exports also occurred, although these rose less than exports. Given existing data, it is not possible to prove any definite link between the ending of public inspections and the contemporaneous jump in exports, but contemporaries seem to have been convinced that ending export inspections played a significant role. New York never considered returning to the old public system, and other exporting states emulated New York’s reform in an attempt to better compete.

New Orleans was New York’s chief rival in America’s export trade. The basic difference was that New Orleans was primarily a cotton port. Cotton was the one major export that was not publicly inspected;<sup>3</sup> thus fewer inspected goods passed through New Orleans. Louisiana shippers observed the increase in trade that followed the elimination of mandatory inspection in New York and may have felt some diminution in their own exports. In 1848, Louisiana abolished their state inspection system (Louisiana State Legislature 1848: no. 62). No private inspections seem to have been established in New Orleans to take the place of the government inspection system. This might have been due to either market failure or a failure in the local legal system. The state government was not completely satisfied with the results of its policy, and in 1855 it reinstated the most important public

<sup>3</sup>It was weighed in New York by government weighers (Benton 1845, 90).

inspections, but on a voluntary basis (Louisiana State Legislature 1855: no. 330).

Other states also followed New York's lead. Maryland made inspections of leather, lumber, casks, liquors, firewood, lime, oak bark, and coal voluntary in 1854. Furthermore, any person willing to pay a fixed sum for a license was allowed to inspect these articles (*Laws Made and Passed by the General Assembly of the State of Maryland* 1854: chap. 200). Pennsylvania and Rhode Island limited their response to making meat inspections voluntary—this being the great stumbling block to reaching the British market (*Digest of the Laws of Pennsylvania* 1862: 109 and *Revised Statutes of the State of Rhode Island*, 1857: 246). Less commercial states kept their inspection systems intact.

## Conclusion

Inspections were developed due to the large differences in scale economies between production and reputation. To become part of a large-scale brand, small producers had to give up some of their autonomy and produce according to state specification. The state had important legal advantages over any private company that might want to develop its own inspection brand. In the 1840s and 1850s, state inspections suffered important political setbacks. Those setbacks were largely due to inefficiency and inflexibility in the public inspection system. The inefficiency of inspections stemmed primarily from their dual role as an inspection and patronage service. Their inflexibility was best illustrated by their lack of response to the changing international beef market. Inspections, once instituted, changed very slowly over time, probably due to administrative rigidities. They may have overcome important transaction costs in the market place, but eventually they fell victim to the serious transaction costs that plagued the political market for publicly provided services.

Export inspections are a typical example of the heavy state and local government regulation common in the early U.S. economy (Handlin and Handlin 1947, Hartz 1948, Horwitz 1977, Hughes 1976). This regulation was not a traditional remnant of Colonial times but in many respects was more prominent after the Revolution than before. The privatization in New York State of the inspection system is an important example of the increasing role the market was allowed to play in the era leading up to the Civil War. The most prominent examples of this liberalization were free banking and general incorporation laws. The role competition between states played in the ending of mandatory inspections suggests that the improvements in transportation and communication occurring at this time may have had a

strong impact on such policy decisions. Arguments concerning the inefficiency of state inspections were often based on cross-state comparisons. If the inspection system had been unified and administered by the federal government, it would have quite likely remained unaltered into the 20th century.

Making inspections voluntary seems to have been a striking success, as indicated by both export data and the fact that New York's competitors, Louisiana in particular, imitated the policy. The effect of the complete elimination of public inspections is unclear. In New York, the rise in exports seems to have begun in 1843 before privatization. Inspections of some kind were important to international trade, and the establishment of effective private inspections may have taken time and been difficult in smaller ports. Inspections at ports gradually became less important as commodity exchanges which required inspection and grading became more prominent.

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