

Book review (penultimate draft), forthcoming in *Business Ethics Quarterly*

The Code of Capital: How the Law Creates Wealth and Inequality, by Katharina Pistor. Princeton, NJ: Princeton University Press, 2019. Hardcover, 297 pp. \$29.95, ISBN: 9780691178974; paperback \$19.95, ISBN: 9780691208602; ebook \$19.95, ISBN: 9780691189437

by Thomas Mulligan, Georgetown University, thomas.mulligan@georgetown.edu

Capital drives economic production and determines, in part, the distribution of income and wealth. Katharina Pistor's goal in *The Code of Capital* is to explain capital's inextricable link to the law: "Fundamentally, capital is made from two ingredients: an asset, and the legal code" (p. 2). When it is at its best, the book argues in favor of this thesis or discusses, in an innovative way, how the law affects economic life. Much of the book, however, is a frustrating jumble of platitudes, history, argumentation, and legal commentary. As a result, readers will walk away from *The Code of Capital* unenlightened about the nature of capital, and unconvinced that it has some profound connection to the law.

In conventional, economic terms, *capital* denotes a class of inputs to production—assets (to use Pistor's terminology) that are needed to produce goods and services.

Imagine a firm that manufactures hammers. This firm uses raw materials, like wood and steel; warehouses for storage; and cash to fund day-to-day operations (“working capital”). The raw materials, warehouses, and cash are examples of capital. The firm transforms these and other assets—most important, the *labor* of its employees—into hammers.

As Pistor points out, not everyone uses “capital” this way. The term has no commonly-accepted definition, and for her, “its meaning remains obscure” (p. 9). This is a fair point, but given that her book is explicitly about capital (in particular, about capital’s connection to the law) one would expect her to either bring clarity to this muddled term or provide a working definition. Pistor does neither. What she does do is survey different definitions which have been given over the years; tell us what capital is *not* (e.g. “it is critical to note that capital is not a thing” (p. 10)); and gesture at the need for a capacious definition (pp. 9-13).

As a result, the concept of capital does not end up doing much work for Pistor. Indeed, what this book is really about is best-described by its subtitle: This is a book about how the law creates (or more precisely, affects) wealth and inequality (and other features of economies). But that is not surprising, nor novel. While the book does contain some innovative arguments along those lines, they are sparse.

Pistor lays out her strategy in the first chapter of the book. She says that contract law, property rights, collateral, trusts, corporate law, and bankruptcy law “code” assets

and transform them into (or out of) capital. They do this by bestowing (or revoking) four attributes: *priority*, which ranks competing claims to assets (e.g. when a firm goes bankrupt, bondholders typically have priority over shareholders on the firm's assets); *durability* (which "extends priority claims in time" (p. 3)); *universality* (which "extends them in space"); and *convertibility* (i.e. creditors' ability to transform their claims into cash).

Chapter 2 ("Coding Land") is mostly a history of property rights. Pistor discusses the Belizean Maya's struggle to secure a property right to the land on which their people traditionally worked and lived. She also provides a perspicuous explanation of trusts (one of the six aforementioned "modules" which allegedly code capital).

Chapter 3 ("Cloning Legal Persons") considers corporate personhood by way of (yet another) "institutional autopsy" of Lehman Brothers and its 2007 collapse. Pistor also discusses how corporations relocate their finances and operations to take advantage of favorable regulatory environments. Obviously, capital gets affected by such arrangements. If a jurisdiction taxes capital income, for example, that disincentivizes capital investment there. But this chapter is really *about* corporate personhood and jurisdiction shopping (among other things). It is not about the ramifications of these practices for capital.

Chapter 4 (“Minting Debt”) begins with the claim that “if there is one asset that defines capitalism, it is debt” (p. 77). Pistor relates the history of CMLTI 2006-NC2, a mortgage-backed security which collapsed during the 2007-2008 financial crisis for the typical reasons: imprudent buyers, rapacious lenders, corrupt rating agencies, incompetent regulators. She then discusses the 1998 collapse of Long-Term Capital Management, the Nobel Prize winner-led hedge fund which misjudged the risk of sovereign default in Asia and Russia.

Pistor concludes that “debt . . . is coded in law and ultimately relies on the state to back it up. States should realize this and keep the inflation of private money under control” (p. 107). To be sure, debt—how it is defined, used, recovered, *etc.*—depends critically on the law. But because this chapter is mostly history (including *descriptions* of how various securities were assembled and sold), the arguments given are superficial.

I was left wondering: *How* have these debt securities transformed our economy? Do they serve any productive purpose? Have they, for example, increased the typical American’s access to credit? Or is that just self-serving Wall Street spin? What has been their distributional impact? Have they made the poor poorer? How have they affected the efficiency of our economy? The book would have benefitted from less history and more engagement with questions like these.

Chapter 5 (“Enclosing Nature’s Code”) discusses intellectual property. Chapter 6 (“A Code for the Globe”) discusses globalization. Chapter 7 (“The Masters of the

Code”) “take[s] a closer look at the lawyers, the rise of the legal profession, and its impact on the coding of capital in different legal systems” (p. 159).

Although there are interesting moments in all these chapters, my core complaints persist. Many portions within have little or nothing to do with capital. (Those addressing, *e.g.*, elitism in the legal profession (pp. 162-63); “poison pill” defenses to hostile takeovers (pp. 163-64); and comparative differences in legal practice (p. 169*ff.*.)

Some of Pistor’s claims are platitudinous (“bankruptcy is where life and death decisions are made and where losses must be accounted for” (p. 144)); others are indecipherable (“economists have discovered that capital is not a thing, but a quality, although most don’t know it yet” (p. 115)). Further, Pistor leaves obvious objections to her claims unanswered.

She says, for example, that “even the citizens of England and New York State, the jurisdictions where the legal code for global capital is forged, have little say, because most of the activities take place in private law offices, not public legislatures and no longer even in courts” (p. 133). This is dubious. Lawyers do not make the law. Lawyers contend with the law as it is written by the people (through their elected representatives) and interpreted by the courts. *Pace* Pistor, lawyers do not “constantly make new legal rights from old cloth” (p. 169). Or at least, Pistor needed to buttress her claims with rigorous support.

Chapter 8 (“A New Code?”) argues that just as “law is code”, “code is law” (p. 183). Here, “code” refers, literally, to computer code. Blockchain technology, “smart contracts” (“a generic computer program that codes legal contracts in digits” (p. 187)), digital property rights, “digital firms”, and cryptocurrency are all discussed at length.

The ninth, final chapter (“Capital Rules by Law”) serves both to conclude the book and offer economic and legal prescriptions. Pistor sees two options for fixing contemporary capitalism: *radical markets*, which “subordinat[e] all decisions and, one might add, all values, to the price mechanism”, thereby producing an “efficient allocation of resources” (p. 231). Or, in the alternative, following Christoph Menke’s (2015) lead and denying rights (as we currently understand them) a foundational place in our economy. Although I would have liked a more nuanced account of these views (which are fringe), and of their normative competitors, this should not be considered a weakness of the book.¹ Indeed, with the exception of this chapter, Pistor wisely avoids controversial moral matters in *The Code of Capital*. This is appropriate in light of the book’s aspiration: *explaining* the deep and essential link between capital and the law.

Had Pistor executed the argumentative plan laid out in the introduction, this aspiration might have been fulfilled. But Pistor’s six modules (bankruptcy law, *etc.*) are

¹ E.g. even setting aside the possibility that the price mechanism will fail to reach an efficient equilibrium, few philosophers or welfare economists think that efficiency (*i.e.* maximizing the economic surplus) is the appropriate moral goal. Consequentialist-minded scholars think, rather, that we should maximize *utility* (and so redistribute from the rich to the poor, even if this introduces inefficiency into the market).

only superficially connected to capital in the chapters that follow. And the four alleged attributes of capital (universality, *etc.*) go unexplored, conceptually. The problem with *The Code of Capital* is simple: It lacks focused and rigorous arguments in favor of its thesis.

The book does have its uses. It serviceably introduces features of the law (*e.g.* trusts) which are interesting in their own right and which doubtless have ramifications for economic production and distribution. But Pistor leaves it to the reader to surmise what these ramifications are. The capital-law link remains obscure.

REFERENCE

Menke, C. 2015. *Kritik der Rechte*. Berlin: Suhrkamp Verlag.

BIOGRAPHY

Thomas Mulligan is a Visiting Scholar at Georgetown University. A political philosopher, most of his research addresses economic justice or group decision-making. He is the author of a number of journal articles and a monograph, *Justice and the Meritocratic State* (2018, Routledge).