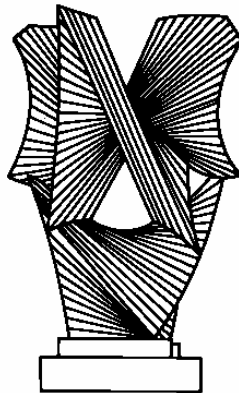


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EXPANDING RESTITUTION: LIABILITY FOR UNREQUESTED BENEFITS

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EXPANDING RESTITUTION: LIABILITY FOR UNREQUESTED BENEFITS

*Ariel Porat**

Suppose Owner can improve his property at a cost of 15, thereby creating benefits of 10 for himself and 10 for his Neighbors. Since each Neighbor expects to reap the benefits regardless of whether she pays Owner or not for this enhancement, all Neighbors may refuse to share the burden and the welfare enhancing activity will not take place. This paper advocates correcting this failure by recognizing an Expanded Duty of Restitution (“EDR”) that obligates recipients of benefits, under certain, well-defined conditions, to compensate benefactors for unrequested benefits voluntarily conferred upon them.

Part I of the paper compares the law’s approach to harm cases with its treatment of benefit cases and offers a novel explanation as to why injurers are commonly allowed to create risks and internalize the resulting harms, while benefactors are not entitled to internalize the unrequested benefits they create. This explanation derives from the different types of obstacles that may preclude reaching agreements between injurers and victims, on the one side, and between benefactors and recipients of benefits on the other.

By elucidating the differences between harm and benefit cases, and notwithstanding the explanation offered in Part I, the paper proceeds in Part II to advocate recognition of an Expanded Duty of Restitution. Here, the framework of the duty is outlined, and a wide range of examples is presented to illustrate in which cases such a duty would be warranted.

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INTRODUCTION

When people promote their own interests, they often create negative or positive effects for other people's interests, without the latter's consent. Economists refer to these effects as "negative externalities"—the harms injurers cause to victims—and "positive externalities"—the benefits benefactors confer upon the recipients of those benefits (hereinafter "recipients"). Ideally, from an economic perspective, both the negative and positive effects should be internalized by those who produce them, for with full internalization, injurers and benefactors alike will behave efficiently. In actuality, however, whereas the law requires that injurers

bear the harms they create (or wrongfully create), benefactors are seldom entitled to recover for benefits they voluntarily confer upon recipients without the latter's consent. The claim made in this paper is that the law's stance on this matter and, particularly, its completely diverging treatment of negative and positive externalities are not justified. Therefore, recognition of an Expanded Duty of Restitution ("EDR") is called for, under which, when certain conditions are met, recipients should compensate benefactors for the benefits they obtain due to the voluntary acts of the benefactors, even when there was no agreement between the two on the matter (hereinafter "unrequested-benefits cases").

To concretize this claim, let us consider Example 1 ("Construction Example"), where Owner contemplates constructing a building on his land at a cost of 15. The building is expected to yield a benefit of 10 to Owner and a benefit of another 10 to Neighbors. Owner could try convincing Neighbors to pay him 5 or more for constructing the building, and if he succeeds and the construction takes place, a net social gain of 5 (20-15) will be created. However, the transaction costs between Owner and Neighbors, which are typically the result of free-riding in such cases, could be prohibitively high, making the reaching of any agreement between the parties implausible. Specifically, each and every Neighbor could refuse to pay for the construction, knowing that he or she would be able to personally reap the benefits of the construction work without paying anything to Owner, thereby free-riding on Owner's and other Neighbors' investments. Failing to raise enough money from Neighbors, Owner will decide not to construct the building even though the project is cost-justified. The result would be different were Owner entitled to recover from Neighbors more than 5, with or without their consent. The law, however, refrains (except in very limited categories of cases) from imposing such a duty of restitution for *unrequested* benefits *voluntarily* conferred. In so doing, it fails to recognize an internalization of benefits principle, which could facilitate efficiency in numerous sets of circumstances.

In tort law, a problem very similar to the one illustrated by Example 1 arises, but it is resolved in a different manner. As is well-known, injurers are commonly not required by tort law to secure their victims' consent prior to the creation of risk, but once harm has occurred, they are often required to compensate them for their losses. Thus, if an injurer derives a benefit of 10 from his injurious activity but exposes his victim to expected wrongful harm of 5, the injurer will often be entitled to con-

tinue his activity so long as he bears the resulting harm.¹ Tort law, like restitution law, allows injurers to unilaterally affect people's interests, but, unlike restitution law, combines this with an internalization of harms (or wrongful harms) principle, thus facilitating efficiency.

Arguably, a uniform legal approach would allow unilateral creation of harms and benefits and mandate in both that their creators internalize them. The question that then emerges is why the law treats the two cases differently. Surprisingly, this basic and important query has received very little attention from legal writers.² A non-economic approach could find no particular interest in responding to this question, with the a-priori assumption that harm cases and benefit cases share very little in common.³ An economic approach would find the law's treatment far more puzzling.

Part I of the paper contrasts the law's approach to harm cases with its treatment of benefit cases. After a short overview of the respective branches of restitution law and tort law, this Part discusses several possible justifications for the diverging approach to internalization of harms and benefits, showing that these arguments fail to explain the absence of an EDR. Part I also raises the question of the law's differential treatment of benefits conferred incidentally to the causing of harm and benefits conferred when no harm occurs, with the result that, in the former, the wrongdoer is entitled to a credit for the benefits he created whereas, in the latter, no such credit is allowed.

The final section of Part I proposes an explanation for the law's differentiation between harm and benefit cases. *First*, it explains that given the creation of risks by injurers and the high transaction costs between injurers and victims, internalization of the resulting harms—or wrongful

¹ It seems that this example is possible under a strict liability rule rather than a negligence rule, since under the latter, when the costs of precautions are higher than the expected harm, liability is not imposed. But in fact, under a negligence rule as well, liability is often imposed even when the full prevention of what is considered by the law to be a wrongful harm is prohibitively high. Thus, the only way to achieve full prevention of the wrongful harms of driving is to avoid the activity altogether; this fact in itself, however, does not convince courts to release drivers from tort liability. See in greater detail *infra*.

² For a major exception, see Saul Levmore, *Explaining Restitution*, 71 VA. L. REV. 65 (1985) (justifying the law's different approaches to harm and benefit cases).

³ Daniel Friedmann, *Unjust Enrichment, Pursuance of Self-Interest, and the Limits of Free Riding*, 36 LOYOLA L. REV. 831 (2003) (arguing that the negative aspect of freedom of contract entails that the recipient of unsolicited benefits be under no duty to pay for them); Scott Hershovitz, *Two Models of Tort (and Takings)*, 92 VA. L. REV. 1147, 1160 (2006) (arguing that "there is an underlying moral asymmetry between harms and benefits" and that "it is perfectly intelligible that the institution which redresses the harms that we inflict on one another is more robust than the institution which allows recapture of the benefits that we confer on one another").

harms—by injurers is most crucial, as otherwise they would have no reason to restrict their injurious activities. There is no parallel concern in benefits cases. *Second*, this section argues that the real puzzle is, therefore, not why, when risks and benefits are created, the law treats the two cases differently. Rather, what is puzzling is why, *to begin with*, the law allows injurers to force transactions on victims who are entitled not to be injured, by creating risks for them and then compensating them for any resulting harms, yet at the same time, benefactors are not allowed to similarly force transactions on recipients by conferring benefits upon them and recovering for those benefits. The solution offered to this seeming inconsistency is that harm cases give rise to a unique problem that does not emerge in benefit cases, which manifests in cases where entitlements are allocated to victims. If, in such cases, injurers were not routinely allowed to create risks for victims without the latter's consent and compensate them if harm materializes, then each and every potential victim would have veto power over the injurious activity. This would result in many beneficial activities being stymied. *Benefit cases do not raise a similar risk*, since no recipient has a similar power to veto beneficial activities. Of course, in many cases, the fact that benefactors are prevented from recovering from recipients for the unrequested benefits they create for the latter leads to a free-riding problem, which results in some beneficial activities not taking place. But this free-riding concern is not comparable in seriousness to the veto power problem inherent to harm cases.

Part II proceeds to develop a new concept of an EDR based on the comparison between harm and benefits cases, on the one hand, and that between benefits conferred incidentally to causing harm and benefits conferred without causing harm, on the other hand. Under this concept, recipients are obligated to compensate benefactors for benefits voluntarily conferred upon them even though they have not consented to either receive or pay for those benefits. The recognition of a duty of this sort will be warranted when: the market, the public authority, or the parties through consensual transaction are incapable of creating the benefit in question themselves; the risk of over-evaluation of the benefits is low; and the costs of proving the benefits and collecting the restitutionary damages are not so high as to make the enforcement of the duty inefficient. In order to reduce the risk of over-evaluation, the measure of recovery should typically be the lower of two measures—either the indisputable benefit gained by the recipients or their relative share of the costs of producing the benefit. Although this Part outlines the framework of the remedy available to recipients and proposes several mechanisms for reducing the risk of recipients' paying in excess of the true benefits

they obtained, it leaves many details open for further inquiry and consideration.

The adoption of an EDR as conceptualized and advocated in this paper will result in a substantial extension of the categories of restitution for unrequested benefits currently recognized by the law. Whereas, presently, such a duty is recognized only (or almost only) when a benefactor protected or preserved existing entitlements, the EDR proposed here applies also to instances in which new entitlements were created. Moreover, whereas, presently, a duty of restitution is limited solely (or almost solely) to cases where there is a preexisting or other close relationship among the parties, the EDR in this paper applies also to cases in which such a relationship does not exist. Consequently, the adoption of an EDR will render a dramatic change in the law and, more importantly, a substantial improvement in current incentives to create benefits.

I. THE BENEFIT CASE VERSUS THE HARM CASE

A. *Unrequested Benefits under Restitution Law*

When a benefactor *voluntarily* confers benefits *at the recipient's request*, the contract between the benefactor and recipient typically regulates the rights and duties of the two sides.⁴ However, when a recipient secures benefits by way of wrongful behavior on her part and those benefits are consequently *non-voluntarily conferred*, the law of restitution often mandates the disgorgement of the ill-gotten benefits to the non-voluntary benefactor.⁵ In contrast, when benefits are *voluntarily* conferred but *not at the recipient's request*, the law does not impose any duty of restitution on the recipient and she is allowed to keep the benefits at no cost to her.⁶ This rule, whose abolishment is called for in this paper, has certain exceptions. The next paragraphs present a short overview of the main categories of those exceptional cases and their underlying rationales.

⁴ But sometimes the contract is unenforceable, and restitution law prevails. *See, e.g.*, Restatement of the Law (Third) Restitution and Unjust Enrichment §§ 31-37 (Tentative Draft No. 4, Mar. 31, 2004); 2 GEORGE E. PALMER, LAW OF RESTITUTION 2-8 (1978); DAN D. DOBBS, LAW OF REMEDIES: DAMAGES, EQUITY, RESTITUTION 856-57 (2d ed. 1993).

⁵ For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment §§ 2, 13, 14 (Tentative Draft No. 1, Mar. 31, 2000); PALMER, *supra* note 4, ch. 2; DOBBS, *supra* note 4, §§ 5.18, 6.1, 9.3.

⁶ Such cases are also referred to as "self-interested intervention" cases, Restatement of the Law (Third) Restitution and Unjust Enrichment § 23 (Tentative Draft No. 2, Apr. 1, 2002).

The *first category* of exceptions is rescue cases. It includes all those instances where the benefactor has acted to protect the recipient's life, health, property, or other economic interest when the latter's consent could not be obtained due to the emergency nature of the circumstances. In cases of property or other economic interest, the law allows the benefactor to recover a reasonable charge for his beneficial actions. In cases of protecting life or health, the law allows such recovery only when the services granted were professional, as when a doctor provides First Aid to an unconscious bystander.⁷

A *second category* relates to cases in which one party has performed all or part of an obligation when he and a second party are jointly and severally liable to a third party. Based on a theory of restitution, the law allows the first party to recover from the second party in the amount of the latter's relative share of the obligation, even if he did not consent to the first party's performance on his behalf. This extends to cases in which there are no preexisting relations between the joint obligors, for example, two wrongdoers who separately cause inseparable harm for which they are jointly and severally liable towards the victim.⁸ Resembling this second category of cases are instances of "equitable subrogation," where one party performs an obligation towards a third party, thereby discharging a second party from performing his *separate* obligation towards the same third party.⁹

In cases falling under a *third category* of exceptions, the benefactor, due to an innocent mistake (or other defect of will, such as fraud or duress), pays money to or creates a non-monetary benefit for the recipient.

⁷ See, e.g., *Cotnam v. Wisdom*, 83 Ark. 601, 104 S.W. 164 (1907) (a doctor who performed emergency surgery on an unconscious injured passerby was awarded restitutionary damages for his services). For an overview, see PALMER, *supra* note 4, at 374-77; DOBBS, *supra* note 4, at 374; Restatement of the Law (Third) Restitution and Unjust Enrichment §§ 20-21 (Tentative Draft No. 2, Apr. 1, 2002). For a critical analysis of the law with strong support for a broader duty of restitution, see Hanoch Dagan, *In Defense of the Good Samaritan*, 97 MICH. L. REV. 1152 (1999).

⁸ See, e.g., *Medical Protective Co. v. Groce, Locke & Hebdon*, 814 S.W.2d 124 (Tex. App.1991) (permitting an obligor who settled with the creditor to recover indemnity from another obligor). For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 25 (Tentative Draft No. 2, Apr. 1, 2002); PALMER, *supra* note 4, at 400-02; Friedmann, *supra* note 3, at 852-54; HANOCH DAGAN, *THE LAW AND ETHICS OF RESTITUTION* 126-27 (2004); Levmore, *supra* note 2, at 100.

⁹ See, e.g., *Ford v. United States*, 115 Ct. Cl. 793, 88 F. Supp. 263 (1950) (U.S. military authorities that compensated a victim of a crime committed by a U.S. soldier were entitled to recover the amount from the soldier's confiscated money). For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 26 (Tentative Draft No. 2, Apr. 1, 2002); DOBBS, *supra* note 4, § 4.3(4).

Under certain conditions, the benefactor is entitled to recover the benefits that are thus transferred to the recipient.¹⁰

A *fourth category* of cases encompasses those instances in which one party protects or preserves an interest he shares with another party, thereby benefiting the latter without her prior consent to pay for this benefit. A common example is a co-owner of property who incurs expenses to maintain or protect it, thereby benefiting the other co-owners. Generally, under a theory of restitution, the co-owner who bears the costs can recover from the others in the amount of their relative shares.¹¹

A *fifth and final category* of cases deals with common funds that are obtained through legal proceedings initiated by one party (or her attorney) but to which a group of people are entitled. Under certain conditions, the initiator of the legal proceedings is entitled to collect from the other fund recipients their relative shares in the expenses he incurred in the process, even if they refused to back his efforts at the outset.¹² An illustration is the case of an heir who initiates legal proceedings and ends up increasing the estate's value, to the benefit of the other heirs as well.¹³

¹⁰ See, e.g., *Challenge Air Transport, Inc. v. Transportes Aereos Nacionales, S.A.*, 520 So. 2d 323 (Fla. App. 1988) (an airline carrying passengers with tickets issued by another airline, when mistakenly believing a reimbursement agreement to exist between the two, may recover under certain conditions from the issuing airline). For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment §§9-10 (Tentative Draft No. 1, Mar. 31, 2000); Palmer, *supra* note 4, ch. 11; DOBBS, *supra* note 4, ch. 11. It could be argued that, strictly speaking, the benefits in this category of cases cannot be classified as having been *voluntarily* conferred, since there was a defect in the benefactor's volition. See Restatement of the Law (Third) Restitution and Unjust Enrichment § 23 cmt. b (Tentative Draft No. 2, Apr. 1, 2002).

¹¹ See, e.g., *United Carolina Bank v. Caroprop, Ltd.*, 316 S.C. 1, 446 S.E.2d 415 (1994) (when one co-tenant stops paying his share of taxes and mortgage payments, other co-tenants may pay his share and recover from him). For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 24 (Tentative Draft No. 2, Apr. 1, 2002); PALMER, *supra* note 4, § 10.7(c); Friedmann, *supra* note 3, at 855-58; DAGAN, *supra* note 8, at 125-26; Levmore, *supra* note 2, at 100-01.

¹² For an overview, see John P. Dawson, *Lawyers and Involuntary Clients: Attorney Fees from Funds*, 87 HARV. L. REV. 1597 (1974) [hereinafter Dawson, *Attorney Fees*]; John P. Dawson, *Lawyers and Involuntary Clients in Public Interest Litigation*, 88 HARV. L. REV. 849 (1975); Levmore, *supra* note 2, at 95-99. Note that the section 23, comment b, of the Restatement of the Law (Third) Restitution and Unjust Enrichment (Tentative Draft No. 2, Apr. 1, 2002) allows recovery in cases where "the benefit is a money payment," thereby substantially broadening the "common funds" category of cases.

¹³ Restatement of the Law (Third) Restitution and Unjust Enrichment § 30 (Tentative Draft No. 4, Mar. 31, 2004); PALMER, *supra* note 4, at 420-21; Friedmann, *supra* note 3, at 858-61 (discussing cases of co-heirs when an indemnity claim was allowed and cases in which it was denied). See also *Feick v. Fleener*, 653 F.2d 69 (2d Cir. 1981) (heirs who hired a lawyer who represented them successfully and enlarged the amount they received were denied restitution from other beneficiaries of the lawyer's actions). Class actions are

Another category of cases, which I will mention only briefly, relates to cases where the benefactor, without any duty on his or her part to do so, performs the recipient's duty without the latter's consent, to the benefit of a third party or to promote a societal interest.¹⁴ The motivation for allowing recovery in these types of cases is principally the advancement of a third party's (as opposed to benefactor's or recipient's) interests, however, and therefore is less relevant to the discussion in this paper.

From this short overview of the five categories of exceptions, it arises that, in most cases, there are three necessary—but not sufficient—conditions for imposing a duty of restitution on a recipient for unrequested benefits: reaching an agreement prior to the conferral of the benefit was unfeasible; the benefactor was pursuing his own interests while the benefit to the other party was incidental; and the benefactor protected or preserved existing entitlements and did not create new ones. Both the case-law and commentary have raised as an additional condition for recovery of unrequested benefits the existence of a "proximity of interests," "closeness of interests," or "community of interests" between the parties.¹⁵

We can now proceed to a more detailed examination of the first three conditions and brief consideration of the additional condition.

The unfeasibility of reaching an agreement is a central feature of all five categories of exceptional cases. In the *first category* (rescue cases), reaching an agreement is impossible due to the emergency circum-

also aimed, inter alia, at surmounting the high transaction costs among potential plaintiffs. *See, e.g.,* Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 809 (1985) ("[class actions] may permit the plaintiffs to pool claims which would be uneconomical to litigate individually"). Moreover some courts have granted fee awards to plaintiffs who enforced the law through their legal actions to the benefit of others, thereby helping parties to overcome a free-riding problem. *See infra* note 16 and text accompanying it. Lastly, allowing derivative actions by shareholders and obliging the firm to cover the derivative plaintiff's litigation costs also mediates a free-riding problem. *See* Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 19-20 (1991) ("[M]embers of the plaintiff class in a large class action or shareholder's derivative suit often have claims so small that the litigation is a matter of relative unimportance to them. Even though the claims in the aggregate may be very large, the small size of the individual claims creates enormous free-rider effects"); *Mills v. Elec. Auto-Lite Co.*, 396 U.S. 375, 395, 24 L. Ed. 2d 593, 90 S. Ct. 616 (1970) (stating that because shareholder derivative suits are brought on behalf of the corporation, courts reason that the corporation should pay for any benefit it receives as a result of the suit).

¹⁴ *See, e.g.,* Estate of Cleveland, 837 S.W.2d 68 (Tenn. Ct. App. 1992). For an overview, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 22 (Tentative Draft No. 2, Apr. 1, 2002); PALMER, *supra* note 4, at 405-06; Friedmann, *supra* note 3, at 854-55.

¹⁵ *See* Restatement of the Law (Third) Restitution and Unjust Enrichment § 30 cmt d. (Tentative Draft No. 4, Mar. 31, 2004); Friedmann, *supra* note 3, at 856-58.

stances. In the *third category* (mistake), the benefactor is not aware of the fact that he has conferred a benefit upon the recipient at no cost to the latter, and therefore he should not be expected to have reached an agreement with respect to it. In the *fourth* (protecting common interests) and *fifth categories* (common funds), the inability to reach an agreement prior to the conferral of the benefit stems from free-riding. In both types of cases, recipients might be tempted to free-ride on the benefactor's investment, seeking to gain the benefit created by him or her without paying for it. Thus, the recipients' refusal to pay for the benefit in these categories is often strategic in nature and not motivated by their true preferences.¹⁶ The *second category* of cases (performing a joint obligation and "equitable subrogation") seems to reflect a different notion, unrelated to the difficulties in reaching an agreement. Here, the entitlement of the obligor who performed the obligation to recover from the other obligor the latter's relative share is aimed at stripping the creditor of the power to arbitrarily choose from amongst co-obligors to bear the ultimate burden of performing the obligation. This explanation, however, does not make difficulty in reaching an agreement irrelevant as a factor impacting the law in this matter. Imagine a legal rule that conditions entitlement to recover for the obligor who performed the obligation on the consent of the other obligor to performance. Such a stipulation would encourage obligors to strategically refuse to give their consent to obligors who are willing to perform, when they realize that the latter are unwilling to infringe the law by not performing the obligation. The power of one obligor to perform the obligation and recover from the other obligor, regardless of prior consent to the performance, reduces the extortion power of the latter over the former and overcomes the impediments to the parties' reaching an agreement.

There is a straightforward rationale for making implausibility of reaching an agreement (or, in economic terms, high transaction costs) a requirement for imposing a restitution duty. Absent this condition, conferring unrequested benefits would replace market transactions. In practical terms, then, this condition mandates that, whenever a consensual transaction is plausible, the benefactor should not be able to take the restitution path.

The second condition for imposing a duty of restitution is that *pursuit of the benefactor's self-interests was the goal with the benefit to the recipient incidental*. Most of the categories implicitly recognize this condition, the exception being the rescue category. Under this condition,

¹⁶ An alternative justification for a duty of restitution to apply in some of these cases is the savings in time and effort necessary for securing the consent of all recipients to each and every expenditure, even the smallest ones. See, for instance, court decisions awarding restitution to co-owners who made reasonable expenditures maintaining the property in divided ownership without the consent of all co-owners, *United Carolina Bank*, 316 S.C. 1, 446 S.E.2d 415 (1994).

the benefactor must also be a recipient and not just an intervener. In all the categories that meet this condition, the law equips the benefactor with a practical tool to advance his own interests at reasonable cost; the absence of an entitlement to recovery from his co-recipients would hinder his ability to pursue his interests. However, when the benefactor is not a co-recipient and his only interest is to profit by creating benefits for others and, in fact, even when he is motivated by pure altruism, he is required to shoulder all his costs (the exception being rescue cases). To illustrate, a person who has maintained other people's property without their consent to pay for the costs of his efforts would not be able to recover those costs, whereas a co-owner in the same circumstances would be so entitled.

The third condition is that *the benefactor protected or preserved existing entitlements, rather than creating new ones*. A co-owner (fourth category) would be able to recover maintenance expenses from other co-owners, but not expenses incurred for improving the property (even though it is sometimes difficult to distinguish between the two). Similarly, a person who increased the value of another person's property would not be able to recover his expenses. However, incurred expenses are recoverable if the benefactor saved the property from demolition, in certain circumstances (the first category). Also, a possible reading of fifth category cases (common funds) is that the benefactor did not actually create a new asset but, rather, initiated the proceedings that enabled the preservation of his and the co-recipients' pre-existing entitlements.¹⁷ Due to its unique features, the third category (mistakes) is the sole exception to the protection and preservation condition.

The rationales of the second and third conditions are less obvious than that underlying the first condition. Clearly, the former two conditions limit the range of cases where a person can create a benefit for others and then charge them. The requirement that the benefactor be a recipient who is motivated by his own interests and the accrual of benefits to others is incidental (second condition) prevents the emergence of an extensive practice of sellers' providing benefits through avenues other than market transactions. Further on, I explain why this practice could pose a risk that the law would seek to avoid.¹⁸ The requirement of protection and preservation of existing entitlements (third condition) reflects the law's preference for maintaining the status quo over a broader principle of maximizing utility. I will criticize this requirement and propose its

¹⁷ For the view that the distinction between creating and preserving a fund is tenuous, see Friedmann, *supra* note 3, at 860.

¹⁸ See *infra* Part II.D.

abandonment.¹⁹ For present purposes, it suffices to note that it is not always clear whether the third condition focuses on protection and preservation of the benefactor's entitlement or that of the recipient.²⁰ Interestingly, in most of the categories of cases, the benefactor's acts clearly protected and preserved both.

The additional condition sometimes mentioned in the case-law and commentary is the requirement of proximity of interests between the parties. Presumably, this condition would be satisfied in some of the cases included in the second category of exceptions (performing a joint obligation and "equitable subrogation"), the fourth category (protecting common interests), and the fifth (common funds). But the term "proximity of interests" is an ambiguous one and cannot fully encompass the complexity of the issue of restitution for unrequested benefits. Indeed, were this term to point to the existence of a contractual relationship among the parties, the rationale of the additional condition would have been to allow a duty of restitution as a default rule that the parties can opt out of if they wish. Under this interpretation, the enforcement of a duty of restitution would not infringe on recipients' autonomy²¹ any more than any other default rule that the parties are free to reject.

The EDR advocated in this paper is certainly not limited to cases where a contractual relationship or other "proximity of interests" exists. On the contrary, the main appeal of the EDR derives from the parties' inability to regulate their relationship through contract due to high transaction costs.

B. Liability Rules in Tort Law

In sharp contrast to restitution law, which only rarely allows recovery for benefits voluntarily conferred on recipients without their consent, tort law routinely permits injurers to create risks without their victims' consent and to bear the harms (or wrongful harms) that consequently materialize. The result is that, while injurers can force transactions on victims ("get injured and get paid"), benefactors cannot force transactions on recipients ("receive a benefit and pay for it").

The Calabresi & Melamed seminal article distinguishing between how entitlements are allocated by the law and how the law protects those entitlements can shed light on tort law's allowing such coerced transac-

¹⁹ See *infra* Part II.F.

²⁰ See PALMER, *supra* note 4, at 362-63 (discussing two categories of cases: those in which the person seeking restitution acted primarily to protect the interests of the defendant and those in which he sought primarily to protect his own interests), and the discussion *infra* Part II.F.

²¹ For the discussion on recipient's autonomy, see *infra* Part I.C.1.

tions.²² According to the Calabresi & Melamed argument, the law uses principally either a property rule or a liability rule to protect entitlements:²³ protection under the former means that the owner of the entitlement has the exclusive right to choose to forego his entitlement; protection under a liability rule means that someone else can deprive the owner of his entitlement but with the accompanying obligation to compensate the owner for the value of the entitlement and for any other ensuing losses. The main factor in the choice between property rule and liability rule is the magnitude of the transaction costs between the parties. If they are low, a property rule is preferable to a liability rule and vice versa if they are high.²⁴ The law's choice of a liability rule to protect the victim's entitlement constitutes authorization to injurers to force transactions on victims.

Let us consider why high transaction costs constitute a valid reason for the law to allow transactions to be forced on victims. Under Coase's famous theorem, when transaction costs are zero, efficiency is achieved regardless of the initial allocation of entitlements.²⁵ Thus, if the victim is entitled not to be injured but the expected benefit to the injurer from the injurious activity exceeds the expected harm to the victim from that activity, the parties will reach an agreement that will allow the injurious activity to occur. However, when transaction costs are high, there is a risk that the parties will not be able to reach such an agreement; under a property rule regime, efficiency might therefore not be achieved. A liability rule could be the solution: the injurer has the choice whether to inflict harm on the victim and pay damages or refrain from his injurious activity; since he internalizes both the benefits and costs of the activity, his choice will be an efficient one.

Tort law and, in particular, accident law can be understood as comprising sets of liability rules. Of course, injurers are often entitled to create risks without being liable for the resulting harms. Negligence law, for example, leaves victims uncompensated whenever the harm was due to no fault of the injurer. But more relevant to our discussion is the fact that injurers are very often entitled to create risks alongside a duty to compensate victims for their accompanying losses. For example, in a no-

²² Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972).

²³ A third way, which will not be discussed here, is protection by an inalienability rule, under which the owner of the entitlement cannot transfer it. *See id.*

²⁴ Liability rules have their drawbacks, and therefore, when transaction costs are low, property rules are preferable. The main disadvantage to liability rules are the risks of over- and under-evaluation of harms. *See infra* note 40 and accompanying text.

²⁵ Ronald H. Coase, *The Problem of Social Cost*, 3 J. L. ECON. 1 (1960).

fault legal regime, drivers are entitled to create risks by their driving without their victims' permission, but, at the same time, are required to compensate them for the resulting harms. This appears to be liability rule protection for victims' entitlement not to be injured. If, instead, the entitlement were protected by a property rule, drivers would never be able to drive because of the very high transaction costs that would preclude reaching agreements with potential victims. A negligence rule further complicates matters, for victims are entitled not to be *negligently* injured. Yet, in order to ensure maximum protection for the entitlement, as is achieved by a property rule, injurers should be prevented from creating negligent risks. This is never the case. Rather, injurers are permitted to create risks but are liable for harm they cause through their negligence. Arguably, this seems to indicate that a negligence rule in fact represents a type of liability rule. An alternative classification of the rule of negligence, and perhaps of other rules governing accident cases, is as a compensation, rather than liability, rule. Under this alternative, the limitations of the protection offered to potential victims of an accident stem from practical enforcement difficulties and do not reflect permission to injurers to create risks and bear the costs of resulting harms.²⁶ Specifically, since, in most such cases, it is virtually impossible to enjoin an injurer *ex ante* from negligently creating risks, the best the law can do is impose an *ex-post* duty of compensation when negligence is the cause of the harm. In short, when the victim is entitled to compensation for his losses, it is not because the injurer has a *right* to create risks accompanied by a duty of compensation, but, rather, because he did *not* have such a right to begin with.

Regardless, tort law very often allows injurers to create risks and bear the costs of the consequent harms. This is true also under a negligence-based legal regime, where the law "authorizes" injurers—*de facto* if not *de jure*—to negligently create risks toward victims without their prior consent. With regard to many activities, authorization to create risks is tantamount to authorizing *negligently* creating risks, since negligence is unavoidable in those activities. Driving a car is one typical example: Obviously, no driver can avoid being negligent from time to time. Therefore, a negligence-based legal regime that allows drivers to drive their cars without securing their victims' prior consent in fact recognizes that many victims will be injured through negligent driving even

²⁶ For such an argument, see Jules L. Coleman & Jody Kraus, *Rethinking the Theory of Legal Rights*, 96 YALE L.J. 1335 (1986); Benjamin C. Zipursky, *Rights, Wrongs, and Recourse in the Law of Torts*, 51 VANDERBILT L. REV. 1, 55-70 (1998). For the argument that risk creation will respect the victim's rights only if the injurer expects to compensate the victim in the amount prescribed by their hypothetical agreement at the time of risk-creation, see Mark A. Geistfeld, *Punitive Damages, Retribution, and Due Process*, 81 SO. CAL. L. REV. (forthcoming 2008).

though they have never agreed to be exposed to the risks. Thus, tort law permits injurers to force transactions on victims. The economic interpretation for this is that absent this permission, many beneficial activities would not take place due to high transaction costs between injurers and victims.²⁷

A similar logic applies to benefit cases. High transaction costs prevent agreements between benefactors and recipients, which could have enabled many efficient activities that would otherwise not occur. Permitting benefactors to force transactions on recipients when transaction costs are high could be as good and efficient a solution in benefit cases as in harm cases. Yet restitution law has not taken this path. The next section discusses some possible reasons for this divergence in approaches.

C. Possible Reasons for Not Recognizing an Expanded Duty of Restitution

1. Infringing on the Recipient's Autonomy

A prominent possible reason against recognizing an EDR is that it could infringe on recipients' autonomy, for under such a duty, they would be required to pay for benefits they never sought to buy. Arguably, it violates their right "to be left alone" as well as sharply clashing with the basic principle of freedom of contract, in that it allows benefactors to impose an exchange on recipients.²⁸

Several responses can be offered to this autonomy concern. *First*, the EDR proposed here would be limited solely to those cases in which a market transaction is not a practical option and where the risk of over-evaluation of the benefits to the recipient is very small.²⁹ When these conditions are met, applying the EDR would typically be consistent with the parties' will. To illustrate, consider a case in which the benefactor created a wholly monetary benefit. Here, imposing a duty of restitution on the recipients would hardly contradict their will, since after transferring part of the benefit to the benefactor, they will clearly be in a better position than the benefactor not created the benefit. The same holds for other types of cases when it is certain that the recipients were willing to pay for the benefit in question and are required to pay no more than the

²⁷ ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS* 102-06 (3d ed. 2000); RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* § 3.10 (6th ed. 2003).

²⁸ For this argument, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 23 cmt. b (Tentative Draft No. 2, Apr. 1, 2002); Friedmann, *supra* note 3, at 846-47.

²⁹ See *infra* Parts II.B., D.

monetary value of this benefit to them. Finally, when the recipients are firms, businesses, or other wealth maximizers, it can often be assumed that the objective value of the benefit is identical, or at least very close, to the value the recipients actually ascribe to it. Here, too, all recipients will be better off if an EDR applies, and adopting it would be consistent with their will.

Second, from a comparison of benefit cases with harm cases, it arises that the law's failure to recognize an EDR cannot be *solely* due to the threat to recipients' autonomy. Tort law by (*de facto*) allowing injurers to impose transactions on victims who are entitled not to be injured infringes on the latter's autonomy far more severely than an EDR could. Tort law enables injurers to inflict bodily and property injury on victims and obliges the injurers to compensate the victims for their wrongful losses. These losses are measured by objective criteria, and victims are often not fully compensated. The infringement of the autonomy of a pedestrian who lost his arm in a road accident due to a driver's negligence and who is compensated according to objective criteria is incomparable to an infringement of the autonomy of a recipient who is required to pay for a benefit he gained from a benefactor's activity.

Third, limiting people's autonomy by obliging them to pay for unrequested benefits is very common in contexts similar to those in which the EDR would apply. Public authorities create public goods on a daily basis and charge the recipients through taxes. Accordingly, an EDR can be conceived of as the privatization of the public authority's power to produce public goods and collect payment for them.³⁰ The counterargument to this would be that the power to levy taxes is the prerogative of the public authority and delegating it to private entities infringes on basic principles of democracy. I address this argument further on.³¹

In sum, the goal of an EDR is to enhance people's welfare by freeing them from situations they do not wish to be in. Indeed, when the law allows coerced exchanges only when there is a barrier to a consensual transaction (high transaction costs) and there is a strong presumption of the recipients' will in favor of the exchange (the risk of over-evaluation of benefits is very small), recognizing an EDR promotes, rather than infringes on, recipient autonomy.

2. *Undermining Markets*

Another possible reason for not recognizing an EDR is that it would discourage market transactions: sellers and providers of services would force exchanges on buyers and avoid consensual transactions. The co-

³⁰ See *infra* Part II.E.

³¹ See *infra* Part I.C.6.

erced exchanges could consequently often be inefficient ones,³² resulting in inefficient resource allocation.³³

This objection to an EDR loses force if the EDR is limited solely to cases in which a market transaction is not a practical option. Indeed, the EDR proposed in this paper is thus restricted to cases in which transaction costs preclude consensual transactions, either between the benefactor and recipient or between the recipient and third parties.³⁴

A variation of the argument that an EDR could undermine markets is that its recognition would create disincentives to develop markets where they do not exist. Sellers would always prefer—so the argument goes—the alternative route of non-consensual transaction to a market transaction. This concern should be given serious consideration when shaping the EDR. As I will argue below,³⁵ awarding restitutionary damages for the benefits conferred below the objective value of the benefits—sometimes far below—would guarantee adequate incentives for sellers to develop markets for the sale of goods and services instead of forcing them on buyers.

3. Over-Evaluation of Benefits and Ex-Post Inefficiency

Another possible reason for not adopting an EDR is the risk of over-evaluating the benefits to the recipients, which would result in the creation of benefits even when this is not cost-justified.³⁶ This objection holds even when a market transaction is not a viable option. To illustrate this problem, let us return to the Construction Example, where Owner expects to garner a benefit of 10 from constructing a building at a cost of 15 and Neighbors expect a benefit of 10 as well. Under these circumstances, an EDR would allow Owner to recover from Neighbors more than 5 and induce him to efficiently construct the building. But assume now that the actual benefit to Neighbors is less than 5, but the court

³² POSNER, *supra* note 27, at 135-36 (explaining the denial of restitution of unrequested benefits except in life rescuing cases).

³³ Levmore, *supra* note 2, at 79-82 (claiming that the denial of restitution to intervening providers encourages a complex, thick market, which is required for enabling efficient resource allocation).

³⁴ *See infra* Part II.A.

³⁵ *See infra* Part II.B.

³⁶ DAGAN, *supra* note 8, at 139-48 (discussing the recipient's subjective devaluation of the conferred benefit); Levmore, *supra* note 2, at 69-72 (claiming that the law may be seen as normally disallowing restitution claims because of valuation difficulties).

evaluates it as 10. Here, the application of an EDR would incentivize Owner to construct the building even though it is not cost-justified.³⁷

One variation of the over-evaluation problem could be the result of *lost opportunities*. Suppose that, in Example 1, one of the Neighbors could have created a benefit that is a substitute for the benefit created by Owner, and assume that that benefit could have been greater than the benefit created by Owner. If Owner were able to recover in the amount of the benefit he actually created, he would create the benefit even if someone else could have achieved this better.

Another variation of the over-evaluation problem is the *liquidity* problem, which relates to the point in time when the recipient is required to compensate the benefactor for her benefits. Thus, if the recipient is an owner of property and the benefit she accrued is an increase in her property's market value, she can convincingly argue that obliging her to compensate the benefactor for this benefit will force her to take a loan, to sell the land, or to use other resources differently from what she would prefer.³⁸

But the risk of over-evaluation does not pose a convincing challenge to recognizing an expanded duty of restitution.

First, inaccuracy in awarding damages is typically not considered by the law to be a compelling reason against recognizing liability rules in tort law, and it is not clear why the law's stance should differ with respect to benefit cases. Under tort law, therefore, injurers compensate victims for harms, as measured by objective criteria. Consequently, damages paid by injurers are often higher or lower than the precise harms incurred by victims, due to discrepancies between the value victims ascribe to their life, health, and property and the value the law assigns them.³⁹ Over- and under-evaluation of victims' harms result in over- and under-compensation of victims, which makes injurers inefficiently create too low and too high risks, respectively. Unlike benefit cases, in harm cases, *under-evaluation* presents the main concern in considering whether to allow injurers to unilaterally create risks and compensate victims for the resulting harms (liability rule) or to condition

³⁷ Under-evaluation of the benefits could also raise efficiency concerns, but this concern, as important as it may be, is not relevant to our discussion since it raises no hurdle for the argument for recognizing an EDR. See discussion *infra* Part II.B.

³⁸ Cf. DAGAN, *supra* note 8, at 141 (describing the duty of restitution of unrequested benefits as an obligation to exchange money for nonmonetary values without an opportunity to refuse the exchange). See also Levmore, *supra* note 2, at 74-79, who detaches the misevaluation argument from another argument, according to which even if the recipient is required to pay no more than the value of the benefit, because people's decisions to spend money depend on their wealth, a duty of restitution might force some recipients to spend their money in a way that deviates from their preferences. Levmore calls this latter argument the "Wealth Dependency" argument.

³⁹ Calabresi & Melamed, *supra* note 22, at 1108.

the risk-creation upon victim consent (property rule).⁴⁰ This concern, however, is not considered by tort law to be strong enough to preclude liability rules.

Second, and more importantly, in both harm and benefit cases, the concerns of *under-* and *over-*evaluation, respectively, can be easily mitigated. In harm cases, courts could award higher damages than what objective criteria dictate and take the opposite route in benefit cases. Consequently, victims and recipients alike would not be exposed to the risk of being forced into inefficient transactions that, from their perspective, are less desirable than what they would have opted for given the choice. Thus, in the Construction Example, the court could award recovery of 6 even if it were to measure the benefit at 10. Note that distributive justice considerations could also justify such mitigation.⁴¹

Part II.B. will discuss various mechanisms for reducing the risk of over-evaluation that can also mitigate the lost opportunities and liquidity problems. For present purposes, it should be noted only that the measure of recovery under an EDR would be the lower of two amounts: the indisputable benefit obtained by the recipient and his relative share of the reasonable costs of producing that benefit. This will ensure minimal risk of over-evaluation.

4. *Costs of Proof and Collection*

If the costs of enforcing a duty of restitution will typically exceed its benefits, then it can be forcefully maintained that such a duty would not be welfare-enhancing.⁴²

Admittedly, the enforcement costs in benefit cases can be expected to pose a greater barrier to recovery than in harm cases, mainly in situations in which there are numerous benefactors and victims. This stems from the fact that the potential plaintiffs in harm cases are the victims, who possess *more* information than injurers about their losses,⁴³ whereas in benefit cases, the potential plaintiffs are the benefactors, who possess *less* information than the recipients about the latter's benefits. Thus, in

⁴⁰ Over-evaluation can also lead to inefficient outcomes since it can prevent many of injurers' beneficial activities from taking place. But those inefficiencies would not be eliminated if risk-creation were contingent on victims' consent.

⁴¹ See *infra* note 80 *infra* and accompanying text.

⁴² Compare this argument with the one made by Donald Wittman, *Liability for Harm or Restitution for Benefits?*, 13 J. LEG. STUD. 57 (1984), according to which the choice between encouraging actors to create benefits by sanctions and by subsidies should depend to a great extent on the litigation costs entailed by each method.

⁴³ STEVEN SHAVELL, FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW 578-81 (2004) (arguing that the reason the entitlement to collect damages for harm done is allocated to victims and not the state is that the former have better information about their harms).

harm cases, when there is one injurer and many victims, it is relatively easy to locate the injurer, bring a suit against him, prove the harm suffered by each victim, and subsequently collect damages. In contrast, enforcement will be a much harder task for the benefactor in benefit cases. The recipients will have good reason to hide as well as to understate their benefits, and at times, the benefactor will not be able to collect anything from them.

A second argument supporting a distinction between harm and benefit cases on enforcement costs grounds is that the volume of litigation in benefit cases, were an EDR recognized, would far exceed the litigation in harm cases under a rule of negligence, even if we assume, counterfactually, that proving harms and benefits and collecting damages for them in both types of cases are of equal difficulty. In fact, with full enforcement of the law and absent court or injurer error, in equilibrium, under a rule of negligence, no harms are caused negligently, when harms caused non-negligently are not recoverable.⁴⁴ Consequently, no claims are brought against anybody. In contrast, if a duty of restitution were recognized in benefit cases, the benefactors would create more and more benefits and would be repeated plaintiffs for recovery from their recipients.⁴⁵

These two arguments warrant closer scrutiny. The second argument implicitly assumes that most claims are brought when liability exists, for in the absence of liability, there are no grounds for a court suit. In fact, in an ideal world, with full enforcement of the law and no court, injurer *or* benefactor error, claims would never be brought in either harm or benefit cases. In such a world, there would be no disputes between parties regarding liability, but there also would be no disputes over the amount of damages to be paid by defendants to plaintiffs. In contrast, in our non-ideal world, however, both liability and damages are controverted; it is an empirical matter and hard to predict whether an EDR would trigger more or less litigation than triggered by a negligence rule (not to mention a strict liability rule).

⁴⁴ Injurers will not behave negligently because if they do, their expected liability will be higher than the precautions they could have taken to avoid liability. This is a simple application of the Hand Rule, *see* POSNER, *supra* note 27, § 6.1 (describing and explaining the Learned Hand Rule).

⁴⁵ This argument is inspired by a different argument made by GEUSEPPE DARI-MATTIACCI, *NEGATIVE LIABILITY* (George Mason Law & Econ. Research Paper No. 03-29, 2003), available at <http://ssrn.com/abstract=422961>, as part of an endeavor to explain why a duty of restitution, which he calls "negative liability," is so rare. Dari-Mattiacci argues that under a rule of negligence, it is sufficient for the law to have one sanction at its disposal, since in equilibrium, there is no negligence and the sanction is never implemented. In contrast, in benefit cases, the "sanction," or, more accurately, the subsidy, should be implemented again and again, whenever a benefit is created by one person for another person.

The first argument is more compelling. A possible response could be that so long as proof and collection costs are fully internalized by benefactors, there is no reason why they should not be allowed to decide for themselves whether or not to enforce recipients' duty of restitution, rather than rejecting such a duty from the outset. This response is weak if a substantial proportion of the costs are borne either by the state, in providing a judicial system and other enforcement mechanisms, or by defendants when they win on the merits in a suit against them but are not fully compensated for their litigation costs. This concern would be serious were a major part of the benefit cases to involve minor benefits. In such cases, an EDR would be either superfluous—if the benefactor were to internalize most of the enforcement costs, he or she would not enforce—or, even worse, detrimental—if the benefactor were to externalize most of the enforcement costs, he or she would create the minor benefits even when it is not cost-justified to do so.

5. Miscalculation of Benefits and Ex-Ante Inefficiency

In a recent (unpublished) paper, Bar-Gill & Bebchuk show why a market operating under a restitution rule, where sellers provide goods and services without buyers⁴⁶ consent but are entitled to recover the value of the benefits, will probably not survive. According to their thesis, when courts are imperfectly informed about the value of goods and services, a restitution rule will induce excessive entry of low-quality sellers and excessive exit of low-valuation buyers.⁴⁷ Court adjustment of the value estimate upwards to reflect the exit of low-valuation buyers will induce the exit of more buyers, and the market could thus completely unravel.⁴⁸

Bar-Gill & Bebchuk's argument is limited by its own terms to situations in which transaction costs are low and consensual exchange is possible. Therefore their argument does not apply to the cases for which the EDR presented here is designed, where transaction costs are high and consensual exchange is not an option. In these latter cases, there is no room to argue that, from a comparative perspective, creation of benefits

⁴⁶ The terms "seller" and "buyer" are metaphorical, since in fact, no sale is involved in providing goods without the other party's consent.

⁴⁷ OREN BAR-GILL & LUCIAN A. BEBCHUK, CONSENT AND EXCHANGE (NBER Working Paper No. 13267, 2007), available at <http://www.nber.org/papers/w13267.pdf>.

⁴⁸ Note that the Bar-Gill & Bebchuk argument applies even if court errors are unbiased, meaning that the incidence of errors in over-evaluation and under-evaluation of benefits is symmetrical, *see id.* at 10 n.6.

is better achieved through the market than through the imposition of a duty of restitution.⁴⁹

Furthermore, Bar-Gill & Bebchuk's claim is persuasive mainly in those situations in which benefactors compete among themselves for the production of the benefits in question. In contrast, an EDR would typically apply to cases in which no such competition exists and when only one benefactor is (or a very few are) likely to produce the benefit. One main reason for this is that, under this EDR, benefactors would never be paid beyond the costs of producing the benefits, and therefore it would be undertaken only by benefactors with a self-interest in their production. *Lastly*, Bar-Gill & Bebchuk's argument does not apply when there is no risk of misevaluation of benefits. In such cases, an EDR should present no efficiency concern.

6. *The Role of the Public Authority*

The benefits the EDR is chiefly aimed at producing are characterized as public goods.⁵⁰ One of the traditional roles of public authorities is to either produce such goods or enable their production when the market fails to do so.⁵¹ Therefore, it can be asserted, there is no need for an EDR.⁵² Moreover, allowing private entities to recover from recipients for the benefits the former produced contradicts a basic tenet of democracy, that only the elected body or its authorized representatives are empowered to levy taxes on citizens in order to finance the production of public goods.⁵³

⁴⁹ Note that also in markets of consensual transactions, courts and buyers are often imperfectly informed about the value of goods and services, and some of the outcomes, similar to those anticipated by Bar-Gill & Bebchuk under a restitution rule, could obtain. In particular, when buyers lack information about product quality, they will assume the worst, which may cause the market to unravel. This is known as "the market for lemons" problem. See George Akerlof, *The Market for Lemons: Quality Uncertainty and the Market Mechanism*, 84 Q. J. ECON. 488 (1970).

⁵⁰ Pure public goods are characterized by the inability to exclude people from consuming them ("non-excludability") and by the inability of one person's consumption to detract from or prevent another person's consumption ("non-rivalry"). See JOSEPH E. STIGLITZ, *ECONOMICS OF THE PUBLIC SECTOR* 128-29 (3d ed. 2000).

⁵¹ See Paul Samuelson, *The Pure Theory of Public Expenditure*, 36 R. ECON. & STAT. 387 (1954); Paul Samuelson, *Diagrammatic Exposition of a Theory of Public Expenditure*, 37 R. ECON. & STAT. 350 (1955) (discussing the market's ability to provide public goods); Paul Samuelson, *Aspects of Public Expenditure Theories*, 40 REV. ECON. & STAT. 332 (1958) (same); STIGLITZ, *supra* note 50, 129 (explaining how non-excludability and non-rivalry result in market failure).

⁵² It seems that this is a generally acceptable argument amongst the reporters of the Restatement of the Law (Third) Restitution and Unjust Enrichment § 23 cmt b. (Tentative Draft No. 2, Apr. 1, 2002).

⁵³ See *supra* note 31 and accompanying text.

A short digression to tort law will help to understand why this argument is deficient. It can be argued in the context of tort law as well that, instead of imposing liability on injurers and letting them decide if and how to create risks, the state should always regulate their behavior in a centralized way, leaving no room for free choice with respect to risk-creation. However, regulations are not free of flaws. On the one hand, when, under a liability regime, injurers are expected to externalize costs or benefits, regulation could work better than liability. Yet on the other hand, political constraints, in some cases, and prohibitive costs, in others, undermine the feasibility of efficient regulation.⁵⁴ But more relevant to our purposes is the fact that, very often, the individual possesses better information than the state about the costs and benefits of her behavior. If, in such situations, she also internalizes all or most of those costs and benefits, she may be better suited to bring her behavior to its optimal level. Liability, and not regulation, could be a better solution in such cases.

The same argument holds with respect to public goods. On many occasions, the public authority is better suited than individuals to produce the public good or to finance its production, either due to superior information or because individuals may externalize costs if production is left in their hands. But this is not to say that, under certain conditions and for many types of public goods, individuals are not the better producers. In these latter situations, to be discussed in Part II, an EDR is essential.

Lastly, the argument that an EDR, by allowing, in practice, private entities to levy taxes, is counter to basic tenets of democracy, is misplaced. First, this objection falters if the "tax" is not greater than the benefit to the recipients and the EDR therefore has no redistribution effects.⁵⁵ Second, as discussed in Part II, there are safeguard mechanisms (licensing by the public authority and voting by the potential recipients) that can further mitigate this democracy concern.⁵⁶

D. Benefits Incidental to Harms

In contrast to its rejection of an EDR, the law admits "the tort exception." This exception relates to cases in which restoring a tort victim to

⁵⁴ GUIDO CALABRESI, *THE COSTS OF ACCIDENTS: A LEGAL AND ECONOMIC ANALYSIS* 68-129 (1970) (discussing the pros and cons of market deterrence and collective deterrence as a mean to reduce accident costs); POSNER, *supra* note 27, § 23.2 (discussing the advantages of private enforcement in torts and contracts over public enforcement in criminal law).

⁵⁵ J.A. Mirrlees, *An Exploration in the Theory of Optimum Income Taxation*, 38 *REV. ECON. STUD.* 175 (1971) (discussing principles and methods of optimum income tax).

⁵⁶ See *infra* note 92 and accompanying text; see also *infra* Part II.E.

his *ex-ante* position will place him, from an *economic* point of view, in a better position than what he would have occupied had he not been injured. In many such cases, courts deduct the value of the enhancement from the damages amount and award the balance. The question that arises, then, is why are *wrongdoers* entitled, under the tort exception, to charge victims for benefits forced upon them, yet in other benefit cases, the benefactors are not entitled to similarly do so? As will shortly be shown, most of the possible reasons against recognizing an EDR collapse in the context of the tort exception.⁵⁷

Consider the following illustration of the tort exception: Driver A negligently hits Driver B's car. Driver B expends 100 in replacing the broken parts with new ones, since used parts are not available on the market. With the addition of the new parts, the value of B's car increases by 20 relative to its value prior to the accident. Most courts will allow recovery of 80 (100-20) only, meaning that B is forced to improve his car and A is permitted to charge him for the resulting benefit.⁵⁸

⁵⁷ Sometimes the same act will injure some and benefit others. Efficiency requires internalization of both types of effects. See Israel Gilead, *Tort Law Internalization: The Gap Between Private Loss and Social Cost*, 17 INT'L REV. L. & ECON. 589 (1997) (indicating costs and benefits that are typically not internalized by injurers). Thus, in takings, the public authority will act efficiently only if it internalizes both the negative and positive externalities of the takings. For this latter argument, see Avraham Bell & Gideon Parchomovsky, *Givings*, 111 YALE L.J. 547 (2001). In other cases, while wrongfully creating risks, injurers often reduce risks either to the victim who suffers the actual resulting harm or to third parties. For the argument that the latter risks should be taken into account by courts in awarding damages and on the substantial effects it should have on the measure of damages, see Ariel Porat, *Offsetting Risks*, 106 MICH. L. REV. 243 (2007). See, e.g., *New York State Elec. & Gas Corp. v. Fischer*, 24 A.D.2d 683, 261 N.Y.S.2d 310 (1965) (reducing recovery for damaged property by depreciation rate); see also DOBBS, *supra* note 4, § 3.8. Another example is based on *United States v. Fifty Acres*, 469 U.S. 24 (1984), a takings case decided by the U.S. Supreme Court, where the federal government had condemned property used by the city of Duncanville as a landfill. As opposed to the market value of the condemned property of \$225,000, the municipality spent \$723,000 to acquire a substitute facility. A cheaper facility, it was assumed, had not been available. The Court refused to award the municipality \$723,000, allowing recovery only in the amount of \$225,000. As a consequence, the municipality was forced to improve its property, pay for this improvement, and allocate much more resources than it had intended on garbage disposal. In other cases, the injury itself, not the restoration, creates benefits, which are deducted from damages under the "Offsetting Benefits Rule." For the rule and its exceptions, see 1 DAN B. DOBBS, *LAW OF REMEDIES* § 3.8, at 372-79 (2d ed. 1993); *University of Ariz. Health Sciences Ctr. v. Superior Court*, 136 Ariz. 579, 667 P.2d 1294 (1983) (in wrongful conception cases, offsetting benefits rule allows the jury to decide when child-rearing costs exceed the benefits and allow plaintiff to recover the difference between the costs and the benefits). In yet other cases, the injurer, while injuring the victim, saves the latter from the risk of other harms. See Porat, *supra* note 57. The *infra* discussion of the tort exception is generally applicable to all such cases as well.

Some of the objections to an EDR discussed in the previous section apply to the tort exception as well, such as that referring to the risk of over-evaluation of benefits and the *ex-post* inefficiencies that could result.⁵⁹ In the context of the tort exception, the concern is that over-evaluated benefits would be deducted from the damages, meaning that the injurer would pay for less than the true social costs of his wrongdoing. As a consequence, victims would be under-compensated and injurers under-deterred. To illustrate using the previous example, if the benefit Driver B garnered from the installation of new parts in his car was only 10, deducting 20 would result in excessively low damages. However, no-deduction is not without its flaws, leading to over-compensation of victims and over-deterrence of injurers. The optimal solution would be to seek the best estimate possible of benefits and deduct them from the damages awarded.

This discussion reveals some important differences between the tort exception and the general case of voluntary conferral of benefits. These divergences can explain the law's differing approach to the two types of cases. *First*, in the tort exception cases, courts cannot sidestep the complex task of evaluating harms. In pursuing accuracy, they simply cannot ignore benefits conferred on victims. In contrast, in the general case of benefits, courts are not required to evaluate harms, and dealing with benefits as such is probably not considered essential. *Second*, market-based arguments⁶⁰ that could operate against recognizing a wide duty of restitution are irrelevant in the tort exception context. Specifically, the assertion that, in many circumstances, the benefactor, or others, could create the benefit in question by consensual transaction and therefore a restitution duty should not be recognized is completely inapplicable to the tort exception. In the latter case, the harm and benefit are concurrent, and just as injurers are not expected to secure their victims' consent prior to creating risks for them, so are they not expected to achieve their victims' consent to pay for benefits that emerge from restoring them to their *ex-ante* positions. *Third*, the concern relating to proof and collection costs,⁶¹ which has appeal in the context of the general case of benefits, is much less persuasive in the tort exception context. In the latter, charging the victim for his benefits is accomplished through a process of evaluation of losses that takes place in any event. The incremental costs of proving benefits in addition to harms are thus often negligible. *Fourth* and finally, one possible reason for not recognizing an EDR is that it is the role of the public authority—not individuals—to provide and finance

⁵⁹ See *supra* Part I.C.3.

⁶⁰ See *supra* Part I.C.2.

⁶¹ See *supra* Part I.C.4.

public goods, thereby preventing free-riding.⁶² This objection is completely irrelevant to the tort exception. In fact, the transaction costs that undermine any possibility of securing a victim's consent to pay for the benefits he obtains through restoration are typically not the result of free-riding, and the public authority is therefore unable to eliminate them.

The comparison between the general case of benefits and the tort exception demonstrates that there is no inconsistency in a legal system refraining from recognizing an EDR but willing to allow deduction of benefits from damages. Moreover, this sheds light on the major obstacles to recognizing an EDR.

E. Harms versus Benefits—Holdout versus Free-Riding

Given creation of risks by injurers and given the high transaction costs between injurers and victims, which preclude agreement between them, injurer internalization of the resulting harms—or wrongful harms—is most crucial, especially when regulating the risks is impractical. For without regulation or internalization, there would be no restriction whatsoever on injurers' harmful activities. And without restriction, injurers would be completely indifferent to causing harms: even a small expected benefit would induce them to create huge losses for others. For this reason, the law only rarely allows injurers to *negligently* create harm without an accompanying duty of compensation. No parallel risk exists in the case of benefits. Many beneficial activities will take place even without internalization of benefits, since often the benefits the benefactor expects to derive from his beneficial activity are great enough to provide him with sufficient incentive to produce that benefit even if not compensated by the recipients.

But this does not answer what seems to be the crucial question in our discussion: why the law, *from the outset*, allows injurers to force transactions on victims who are entitled not to be injured, by creating risks for them and compensating them for the resulting harms, yet, at the same time, disallows benefactors to force transactions on recipients by conferring benefits upon them and recovering for those benefits. Both the analysis of the various objections to an EDR and the comparison of the general case of benefits and the tort exception seem to suggest that when neither the market nor the public authority is capable of efficiently creating the benefits in question, when the risk of over-evaluation is not substantial, and when proof and collection costs are not prohibitively high, a similar efficiency rationale holds in benefit and harm cases for allowing actors to unilaterally impact others' interests and internalize the

⁶² See *supra* Part I.C.6.

resulting benefits or harms. I will now show that this conclusion is misguided: the need for a liability rule—in Calabresi & Melamed's terms—is, in fact, more acute in harm cases than in benefit cases. In particular, whereas in harm cases, liability rules typically solve a holdout problem, in benefit cases, it is a free-riding problem that is typically mitigated. As will be argued below, efficiency is impaired far more by holdout problems than by free-riding.⁶³

Suppose that tort law were to not recognize liability rules. In such a world, the law would allocate to victims an entitlement not to be injured or, alternatively, an entitlement to injurers to create risks without an accompanying duty of compensation, and it would protect those entitlements with property rules. In some cases, the law would likely opt for the former option and, in others, for the latter. Let us consider now these two options and compare them with parallel options that are applicable to benefit cases.

1. Harms (Victims Have the Entitlement Not to Be Injured) versus Benefits

Let us first contrast benefit cases in which beneficiaries have an entitlement not to pay for unrequested benefits with harm cases where victims have an entitlement not to be injured, with both entitlements protected by a property rule. This means that injurers and benefactors are not allowed to force transactions on victims and recipients, respectively.

The prohibitively high transaction costs between injurers and victims, especially in cases with numerous victims, would prevent injurers from securing victims' consent to be exposed to risks of harm regardless of whether efficiency requires it. As a result, many of the modern activities of our society, like driving cars or manufacturing products, would be paralyzed, even if their benefits far exceed their costs. Indeed, one could argue that even under a property rule, injurers would proceed with their injurious activities and compensate victims for the resulting harms (or wrongful harms). But for our purposes, this is mere semantics: it is hard to imagine the modern world without a rule that *in practice* allows the creation of risks accompanied by a duty of compensation (whether conditioned on the injurer's wrongdoing or not).⁶⁴

Fortunately, in the real world, victims' entitlements are often protected by liability rules. Injurers are often entitled to create risks but while liable for their victims' losses. Sometimes this liability extends to

⁶³ For a comparison between holdout and free-riding, indicating that sometimes free-riding is a more severe obstacle to efficiency than holdout, see Lloyd Cohen, *Holdouts and Free Riders*, 20 J. LEG. STUD. 351 (1991).

⁶⁴ See *supra* note 22 and accompanying text.

any harm that they cause and, other times, only to wrongful harms. Either way, allowing injurers to *force transactions on victims* by unilaterally creating risks for them and then bearing all or a substantial proportion of the costs associated with those risks is essential for the occurrence of many important activities in modern society.

A liability rule is not as crucial in benefit cases as in harm cases. Indeed, society operates quite well without an EDR, and public goods are created on a regular basis. This may sound like a rather weak argument: we see the world we do have, and cannot see the world we do not have but could exist were an EDR adopted! But the divergence in extent of need for liability rules in harm and benefit cases is not just an empirical observation. The next paragraphs outline a crucial difference between two types of transaction costs: the one type existing between injurers and victims when victims are entitled not to be injured and the other between benefactors and recipients when benefactors are not entitled to recovery for unrequested benefits they voluntarily conferred upon recipients.

In harm cases, when victims are entitled not to be injured and this entitlement is protected by a property rule, each victim enjoys veto power over the potentially injurious activity. This power means that every potential injurer *should* obtain the consent of *all* potential victims prior to subjecting them to risk of harm. In contrast, in benefit cases where recipients are not liable for benefits voluntarily conferred upon them, the potential benefactor should *not* obtain the consent of *all* potential recipients prior to creating the benefit and, consequently, none of those recipients has veto power over the beneficial activity. There are two important ramifications to this difference between harm and benefit cases. The first is relevant regardless of whether victims and recipients behave strategically and is mostly applicable to cases of numerous victims and recipients; the second is relevant only when strategic behavior occurs and is applicable to all cases with more than one victim or recipient. *These* two ramifications fairly account for most cases in practice.

Assume an injurer with 1000 potential victims who are all entitled not to be injured and are protected by property rules. Assume also that the benefits of the injurious activity exceed its costs. Since, by definition, each potential victim has the power to veto the injurer's activity, the injurer should reach all of them and negotiate an agreement with each one. But even when victims express their true preferences and do not behave strategically, it will be impossible to reach *all* victims. Moreover, the injurer who starts reaching the victims can never know whether he will be able to reach all of them and knows that negotiating with "only" 999 of the 1000 would be both very costly and insufficient. Most injurers will thus abandon the negotiation attempt from the outset, and efficiency will not be achieved.

Now assume a benefactor with 1000 potential recipients who are not liable for benefits conferred upon them. Assume also that the benefits of the benefactor's activity exceed its costs. Finally, assume that an EDR is not recognized. Here, by definition, no one enjoys any veto power. Consequently, for the beneficial activity to be worthwhile for the benefactor, it would be often more than enough for him to reach 900, 800, or perhaps even 500 of the recipients and convince them to share in the costs. Assuming recipients do not behave strategically, in many cases, the beneficial activity will take place regardless.

This is not to say that the high transaction costs of reaching the recipients and collecting payments from them could not obstruct efficient creation of benefits. Indeed, the central claim of this paper is that often such a risk does in fact exist. But regardless, there seems to be a more pressing need for a liability rule in harm cases than in benefit cases.

The *second ramification* of the difference between harm and benefit cases arises only when strategic behavior occurs. In such cases, however, the difference between harm and benefit cases is apparent even when there are only a small number of victims and recipients.

Assume an injurer with five potential victims who are entitled not to be injured and are protected by a property rule. Assume also that the benefits of the injurious activity exceed its costs. Since, by definition, each potential victim wields veto power over the activity, the injurer should reach all victims and negotiate an agreement with each. Reaching all five victims could be relatively easy. Reaching an agreement with them, however, could be very hard due to holdouts: armed with veto power, each victim has incentive to holdout and extort the injurer. Since all victims share the same powers and incentives, the injurer would find it very difficult, sometimes impossible, to reach an agreement with them even when the benefits of his activity far exceed its costs. And the greater the number of victims, the more acute this holdout problem.

Now assume a benefactor with five potential recipients who are not liable for benefits conferred upon them. Assume also that the benefits of the benefactor's activity exceed its costs. Finally, assume that an EDR is not recognized. Even though the recipients in this case have no veto power, each has the power and incentive to refuse to pay for the benefits and free-ride on the benefactor's investment. Since all recipients have the same powers and incentives, the benefactor would not be able to reach an agreement with them even when the benefits produced by him are far greater than the costs of production.

In both harm and benefit cases, victims and recipients are likely not to be driven by their true preferences. In both cases, recognition of a liability rule is justified by the severe risk of strategic behavior, where the reasons for this behavior are not identical but the outcomes arguably are.

Under closer scrutiny, however, this conclusion seems to be wrong. Assume, for the moment, that four victims and four recipients in each group, respectively, are motivated solely by their true preferences, while only one victim and one recipient behave strategically. Under this scenario, in the absence of liability rules, the veto power of the strategically-acting victim will typically be far more detrimental than the free-riding power of the strategically-acting recipient. This is because the strategic victim can veto the entire activity, whereas the recipient can only refuse to pay his share of the costs of creating the benefit.

It could be argued that this difference between the two cases is a fallacy: if only one victim uses his veto power, the injurer will negotiate with him and reach agreement, and the efficient outcome will be achieved. But it is precisely here that the distinction between harm and benefit cases lies: the injurer will be willing to invest far greater resources in negotiating with the strategically-acting victim than the benefactor will with the strategically-acting recipient. The reason for this is that, in the context of the injurer and victim, the entire surplus of the injurious activity is at stake, whereas in the context of the benefactor and recipient, only the benefit that the latter can derive from the beneficial activity is at stake.

Indeed, strategic behavior is a genuine threat. If it is prevalent, the holdout and free-riding problems will lead to similar severe outcomes. In the real world, however, victims as well as recipients sometimes behave strategically and sometimes act only (or mainly) on their true preferences.⁶⁵ In this world, holdouts constitute a more detrimental problem than free-riding, with a corresponding variation in urgency in overcoming these two phenomena through a liability rule.⁶⁶

⁶⁵ For experiments that show that the free-riding problem does not always preclude cooperation, see Gary J. Miller, *The Impact of Economics on Contemporary Political Science*, 35 J. ECON. LIT. 1173, 1179-83 (1997); John D. Ledyard, *Public Goods: A Survey of Experimental Research*, in HANDBOOK OF EXPERIMENTAL ECONOMICS 111 (John H. Kagel & Alvin E. Roth eds., 1995). For the argument that rational actors would cooperate and not free-ride, see ROBERT NOZICK, *THE NATURE OF RATIONALITY* 50-55 (1993). For the argument that repeat players will tend not to free-ride, see David M. Kreps et al., *Rational Cooperation in the Finitely Repeated Prisoner's Dilemma*, 27 J. ECON. THEORY 245 (1982); Robert M. Axelrod, *The Emergence of Cooperation among Egoists*, 75 AM. POL. SCI. REV. 306 (1981). Identification with the group can also prevent free-riding, see Ernst Fehr & Urs Fischbacher, *Why Social Preferences Matter—The Impact of Non-Selfish Motives on Competition, Cooperation and Incentives*, 112 ECON. J. 478 (2002). Daphna Lewinsohn-Zamir has argued that the main reason for people's reluctance to take part in financing public goods is not their desire to free-ride but, rather, their belief that others will do so, Daphna Lewinsohn-Zamir, *Consumer Preferences, Citizen Preferences, and the Provision of Public Goods*, 108 YALE L.J. 377 (1998).

⁶⁶ For the argument that allowing developers to exercise *eminent domain* powers only after negotiations with owners resolves the holdout problem, see Thomas J. Miceli & Kathleen Segerson, *A Bargaining Model of Holdouts and Takings*, 9 AM. L. ECON. REV. 160 (2007). It seems that a liability rule does not solve the holdout problem but, rather,

2. Harms (*Injurers Have the Entitlement to Injure*) versus Benefits

Harm cases do not, by nature, present a veto-power problem, nor do benefit cases inherently raise a free-riding problem; rather these obstacles are the result of the prevailing allocation of entitlements in society. The previous section discussed cases where victims have entitlements protected by a property rule not to be injured and therefore have veto power over the injurious activity. But suppose a different allocation of entitlements, under which injurers are allowed to create risks without bearing liability for resulting harms and the entitlements protected by a property rule. If the costs of the injurious activity exceed its benefits so that stopping it would be efficient, the parties will find it difficult to reach an agreement with the injurer to that effect, not because of the victims' veto power, but due to free-riding. Specifically, even if it is in the interest of all the victims that the injurious activity come to a halt, many will refuse to share in the burden of compensating the injurer for stopping the activity, motivated by the desire to free-ride on the investments of other victims. But, as explained above, this is "just" a free-riding problem, and exactly as in benefit cases, here, as well, it is not as detrimental an impediment to reaching an agreement between the parties as posed by veto power in the hands of victims.

More relevant to this discussion, however, is the fact that the law fails to cure this free-riding problem *exactly as it fails to cure the free-riding problem in benefit cases*.⁶⁷ The law is consistent, therefore, in ig-

merely changes the identity of the person creating the problem. Thus, in instances of one injurer and one victim and where the victim has an entitlement, protected by a property rule, not to be injured, the victim has the power to holdout (by refusing to permit the injurious activity unless he or she is well paid). If, instead, the injurer's entitlement is protected by a liability rule, he or she, in turn, has the power to holdout (by refusing to stop the injurious activity unless well paid). But the situations discussed in this Section are different. I have assumed all along that, in a typical harm case, there is one injurer but many victims. In such cases, the holdout problem is severe because there are many actors, not just one, who can holdout. Therefore, the move from "property rule protection for the victim's entitlement" to "liability rule protection for that entitlement" also represents a move from a situation in which "many victims can holdout" to a situation in which "many victims can free-ride." This latter move is a desirable one since the holdout problem is more severe than the free-riding one. A similar analysis applies to benefit cases.

⁶⁷ In allocating the entitlement to injurers, the law could offer a liability rule under which victims could stop injurers from harming them but would have to compensate them for the resulting costs. Such a liability rule was proposed by Calabresi & Melamed, *supra* note 22, at 1115-18, which they entitled "Rule four." But in our example, such a liability rule would not be of much assistance, since even if injurers were to be required to halt their activities and be compensated upon victim demand, free-riding would still be an obstacle to agreement amongst potential victims. Specifically, each victim would have an

noring the free-riding problem in both harm and benefit cases. Consequently, in the above example it is likely that the injurer would create risks even if this is inefficient, and no potential victim would stop him. Note that an EDR could remedy the problem, by allowing a victim who acted to stop the inefficient injurious activity to recover part of his costs from victims who benefited from his actions. This will be elaborated on elsewhere in the paper.⁶⁸

Let us proceed to consider the validity of the assumption that benefit cases present *only* a free-riding problem. A veto power problem could arise in such cases were the law to grant potential recipients the entitlement to force benefactors to create benefits for them and were this entitlement protected with a property rule. Under such a legal regime, if the costs of the beneficial activity were to exceed its benefits so that its cessation would be efficient, the benefactor who would try to arrive at an agreement with the recipients to halt the activity would face the difficult hurdle of their veto power (each recipient could veto the agreement). But allocation of this type of entitlement to many recipients of one benefactor is a very rare, perhaps implausible, phenomenon in the private law sphere.⁶⁹

The distinction between harm cases and benefit cases can now be summarized as follows. In harm cases, a veto power problem arises when the entitlement is allocated to victims, and a free-riding problem arises when it is allocated to injurers. In benefit cases, only a free-riding problem arises. The law provides a liability rule to remedy the veto power problem but does not do so for the free-riding problem in either harm or benefit cases. This seems to make sense, since veto power is more severe an impediment to agreements than free-riding. Still, free-riding can also block efficient outcomes, making an EDR a good solution in benefit (and some harm) cases. The EDR laid out in the next Part of this paper is motivated by this possibility.

II. CONSTRUCTING AN EXPANDED DUTY OF RESTITUTION

We concluded Part I with the claim that an Expanded Duty of Restitution in benefit cases is less essential for welfare enhancement than a

incentive to free-ride on other victims' investments, refusing to share with them the costs of compensating the injurer for halting his activity.

⁶⁸ *Infra* Part II.A (discussion of Example 2).

⁶⁹ This phenomenon is, however, common in the public law sphere, where public authorities are often obliged by law to produce public goods for groups of people. In such cases, each person belonging to the given group is entitled to force the authority to produce the benefit. It could be argued, though, that under certain circumstances, the public authority should be allowed to refrain from producing the public good, while bearing the resulting harms to all potential recipients (including expectation damages). Such a liability rule would prevent any possible holdout problem.

liability rule is in harm cases. This is not to say that recognizing an EDR is not essential: in fact under certain conditions, it is most crucial. Drawing on the objections to an EDR and on the comparison between the general case of benefits and the tort exception, presented in Part I, this Part will now set forth a framework for recognizing an EDR, under which five cumulative conditions must be met:

1. Transaction costs must preclude securing recipients' consent to pay for the benefits conferred upon them.
2. The risk of over-evaluation of the benefits is not so high as to undermine the efficiency of the restitution duty or to substantially infringe on recipients' autonomy.
3. Proof and collection costs are not high relative to the value of the benefits conferred and therefore do not weaken the efficiency of enforcing the duty.
4. The benefits will not be created by the market.
5. The benefits will not be created by a public authority.

Recovery under the proposed EDR would be limited to the lower of the two measures: either the recipient's indisputable benefit or the recipient's relative share in the reasonable costs of producing the benefit. Furthermore, postponing payment would sometimes be necessary for reducing the burden to the recipients. Finally, under certain circumstances, licensing and voting mechanisms could be used as a precondition for the application of the EDR.

Even though theoretically possible, it would be unrealistic to apply the EDR on a case-by-case basis. Instead, it should be developed in categories of cases where the five above conditions are typically met. The cases most suitable to the EDR, as will be shown throughout this Part, are those in which the value of the recipients' property is enhanced and where the recipients receive monetary benefits, although applying the duty in other contexts is not excluded.

In addition to analyzing all five conditions, the following discussion will also consider different means for reducing the risk of overburdening recipients. The final section will address the question of whether there is place in the framework of the EDR for any of the conditions currently prevailing in the existing restitution doctrine.

A. Transaction Costs

As explained, free-riding is a common obstacle to efficient creation of benefits when no duty of restitution applies.⁷⁰ The Construction Ex-

⁷⁰ Restatement of the Law (Third) Restitution and Unjust Enrichment § 23 cmt. b (Tentative Draft No. 2, Apr. 1, 2002) (explaining that the protection commonly afforded to property rights and contractual liberty (by denying restitution) comes at an important

ample is illustrative: Some Neighbors may refuse to share Owner's costs, hoping to free-ride on his and other Neighbors' investments. As a result, the construction work will not take place.⁷¹ Example 2 below represents another typical case in which free-riding subverts efficient creation of benefits.

Example 2. Stopping an Interference. X creates an interference to residents. A, one of the residents, pays X to cease his interfering activity or, alternatively, takes costly precautions to remove the cause of the interference, or, alternatively, sues X in court, where an injunction to stop the interference is issued against X. A's successful efforts result in an increase in the market value of all the residents' houses and apartments. Should A be entitled to recover from the other residents at least part of her reasonable costs?⁷²

Assuming A's costs exceed her benefits, she will not make the necessary effort at stopping the interference even if this would be welfare-enhancing, unless she is able to collect from the other residents at least part of her costs. Due to the difficulty in reaching all the residents and the accompanying free-riding problem, collection would be very difficult. A duty of restitution could solve the problem here, assuming the other conditions discussed below are satisfied.

If the interference in this example is illegal, the question will be whether A should recover from the recipients or from the enforcement agency that failed to stop the illegal interference, if at all. This issue will be elaborated on below.⁷³ A possible variation on Example 2 would be that X, the creator of the interference, voluntarily and under no legal duty, stops or reduces it, bearing costs in so doing. Would X be entitled to recover from the residents in these circumstances? The risk of applying an EDR in such a case is that risk creators will be tempted to inefficiently increase risks to the maximum legally permissible level and

cost: the invitation to strategic behavior and free-riding); DAGAN, *supra* note 8, at 130-39 (arguing that the rationale for allowing recovery for unrequested benefits under prevailing restitution law is to avoid free-riding); Friedmann, *supra* note 3, at 846 (mentioning free-riding as an obstacle to efficient creation of benefits). See also *Consol. Edison Co. of N.Y., Inc. v. Bodman*, 370 U.S. App. D.C. 359, 445 F.3d 438 (2006) ("courts have found it sensible to apply the unjust enrichment principle ... because doing so answers a potential free-rider problem").

⁷¹ *Cf. Green Tree Estates v. Furstenberg*, 21 Wis.2d 199, 124 N.W. 2d 90 (Wis. 1963) (developer who made improvements for its own benefit and for benefit of local residents was denied restitution).

⁷² *Cf. Ulmer v. Farnsworth*, 80 Me. 500, 15 A. 65 (Me. 1888) (restitution denied to owner of a flooded quarry who drained it to his own and neighboring quarry owner's benefit).

⁷³ *Infra* Part II.E.

then later reduce it and charge recipients accordingly.⁷⁴ But this risk is usually not real: if benefactors are compensated for no more than their costs, they will gain nothing from such a maneuver. To illustrate, suppose X legally increases the risk by 10 and later reduces it at a cost of 1; since he can recover no more than 1, he will have no incentive to increase the risk from the outset.

In contrast to Example 2, which involves stopping interference to recipients' property and, as such, can be characterized as protecting the existing entitlements of the recipients and benefactor, the next example entails the creation of new entitlements.

Example 3. Changing Zoning Plans. In a certain neighborhood, building more than four floors in apartment buildings is prohibited. A, the owner of a fourth-floor apartment, spends a substantial sum of money on convincing the zoning authorities to change the zoning plans and permit adding a fifth floor. As a result—in addition to the increase in market value of A's apartment—the market value of another twenty fourth-floor apartments increases by 10%, with no one in a worse-off position. Should A be entitled to any reimbursement for his costs from the owners of the other fourth-floor apartments?

As in Example 2, free-riding can, in Example 3, hinder the reaching of an agreement between A and the other apartment-owners prior to his incurring of costs. This example can be seen as analogous to the common fund category of cases, where the fund creator is entitled to collect from the recipients their relative share in the expenses he incurred.⁷⁵ In both scenarios, the benefactor acts across from a public authority (the court and the zoning authority, respectively), and his or her successful efforts yield a considerable and measurable benefit to a group of people. The difference between the two cases is that, in common fund cases, unlike in Example 3, the benefit is monetary. This divergence *in itself*⁷⁶ should not change the outcome, however: in both cases, applying an EDR could be the only practical way of resolving the free-riding problem.

Another case where an individual causes the creation of benefits to other people by triggering a public authority to act is the plaintiff who wins a claim in a high instance court and thereby benefits many other litigants, present and future, who will win their cases under the legal

⁷⁴ In the original version of Example 2 as well, one could imagine collusion between A and X, where X would increase risks and, subsequently, in line with A's demands and payment, agree to stop creating or reduce those risks.

⁷⁵ See *supra* Part I.A.

⁷⁶ But the over-evaluation problem can make a difference here. See *infra* Part II.B.

precedent set in his case⁷⁷ It seems, however, unwarranted to allow the plaintiff to recover from all recipients in this case, even if an adequate solution to the free-riding problem: the group of recipients is indefinite and the cumulative gains of its members do not necessarily represent the social good created by the court decision.⁷⁸

Example 4, below, illustrates cases in which a benefactor acts to protect her own and other people's interests in their bodily integrity and property.

Example 4. The Security Firm. A lives in a small neighborhood with thirty residential homes that is substantially threatened by crime. Posting a guard at each house is too costly. The most desirable option both for residents and from the social perspective is to hire the services of a security firm to patrol the streets at night. After failing to reach agreement among the residents on the matter, A hires a security firm. The threat to the neighborhood decreases significantly, as do the residents' insurance premiums. Should A be reimbursed by the residents for part of her costs?

While prevailing restitution law recognizes rescuers' entitlement to recover from those they rescued in emergency circumstances,⁷⁹ it fails to solve the free-riding problem that may prevent a group of people from acting in concert to protect themselves against risk of injury, as in Example 4. Applying an EDR in the Example and allowing A to recover from the residents their relative share of the reasonable costs of hiring the security firm could be a practical solution to the problem.

B. Over-Evaluation of Benefits and Its Mitigation

A duty of restitution should not be recognized when there is a substantial likelihood that the so-called recipients did not actually gain any benefit from the so-called beneficial activity. Indeed, it would seem that with an expanded duty of restitution, the risk of under-evaluation of benefits poses the same threat to efficiency as does over-evaluation. But in fact, there are good reasons for preferring under-evaluation to over-

⁷⁷ See *Sprague v. Ticonic Nat'l Bank*, 307 U.S. 161 (1939) (plaintiff awarded reasonable attorney's fee and litigation expenses, when, by virtue of stare decisis, fourteen other claimants, who were not parties to the litigation, could recover from the defendant). See also the discussion in Dawson, *Attorney Fees*, *supra* note 12, at 1610-12.

⁷⁸ Furthermore, if the winning party is entitled to recover for the positive externality, then consistency requires that the losing party have the same entitlement; after all, were it not for the losing party's stubborn insistence on litigating, the positive externalities would never have been created!

⁷⁹ See *supra* Part I.A.

evaluation. *First*, allocating the risk of error to benefactors is justified by distributive justice: the benefactor is the active party who has promoted his own interests and affected those of others, whereas the recipient is the passive party being affected without his consent by the benefactor.⁸⁰ Therefore, the risk of over-evaluation (which is borne by the recipient) should be reduced to a minimum even if at the expense of increasing the risk of under-evaluation (which is borne by the benefactor). *Second*, under-evaluation of benefits mitigates the concern that an EDR will infringe on the recipient's autonomy.⁸¹ *Third*, under-evaluation creates an incentive for benefactors to engage in a market transaction when plausible. Indeed, the inability to create the benefits through the market is one of the conditions for a duty of restitution to arise.⁸² Limiting damages to a low measure of recovery is a safeguard against benefactors' intentionally avoiding the market and then later convincing the court that a consensual transaction was not an option. It also provides incentives to develop markets for creating the benefits in question, when such markets do not exist.⁸³

A practical way of reducing the risk of over-evaluation is to impose a duty on recipients to compensate benefactors by the lower of two measures: either the indisputable benefits the recipients gained from the beneficial activity or the *reasonable* costs of producing those benefits.⁸⁴ In some cases, those costs should include a quantum meruit fee⁸⁵ and even a premium for the risk the benefactor took upon himself in producing the benefits. That would be essential especially in cases where there was an *ex ante* risk that the benefactor would fail to produce the eventual benefits and have to bear the costs. Of course, limiting recovery to reasonable costs has its own costs.⁸⁶ But as previously explained, the risk of over-evaluation is more troubling and therefore should be minimized.

⁸⁰ For an argument that distributive considerations favor the victim over the wrongdoer and for possible applications of this argument, see Stephen R. Perry, *The Moral Foundations of Tort Law*, 77 IOWA L. REV. 449 (1992). This could justify a preference of over-evaluation to under-evaluation in tort law.

⁸¹ See *supra* Part I.C.1.

⁸² See *infra* Part II. D.

⁸³ See *supra* Part I.C.2.

⁸⁴ For use of the latter measure, see Restatement of the Law (Third) Restitution and Unjust Enrichment § 24 cmt. e (Tentative Draft No. 2, Apr. 1, 2002); PALMER, *supra* note 4, at 429 ("In some cases the value of the benefit has been measured by ... the cost of the improvement.").

⁸⁵ Cf. DOBBS, *supra* note 4, at 237-38 (explaining the quantum meruit measure of damages).

⁸⁶ Thus if Owner in Example 1 can choose between two uses of his land, and one is more beneficial to him than the other but less beneficial to Neighbors, under a rule that allows him to recover reasonable costs only, he would choose the first use even if the total bene-

Furthermore, in measuring the indisputable benefits and the reasonable costs of their production, courts should also take into account *lost opportunities*.⁸⁷ In particular, they should give weight to the possibility that somebody else, even the benefactor himself, could have produced an alternative benefit that would have been greater than that actually produced or created at lower cost. For this reason, the benefactor should recover no more than his *reasonable*—rather than actual—costs. Thus, if more than one person can produce the benefit, each of the potential producers should be certain enough before acting that he can do so in the most efficient way.⁸⁸

Finally, when the benefit is an increase in the market value of recipients' property, it could be appropriate to allow them to delay payment for the benefit until its materialization in the form of profits from the sale of the property. This will overcome *the liquidity problem*.⁸⁹ To secure the benefactor's interest, a lien could be imposed on the enhanced property,⁹⁰

fit to him and Neighbors from the second use would be greater. A rule allowing Owner to recover at least some of Neighbors' benefits could prevent this inefficient outcome.

⁸⁷ See *supra* Part I.C.3.

⁸⁸ Alternatively, when there are many potential benefactors, a licensing mechanism can be used. See *infra* note 91 and accompanying text. In class actions, a parallel question arises when there are many candidates for the class action plaintiff and only one can be chosen. See JOHN J. COUND, JACK H. FRIEDENTHAL, ARTHUR R. MILLER & JOHN E. SEXTON, CIVIL PROCEDURE CASES AND MATERIALS 707-08 (6th ed. 1993). (describing a situation where several members of a class want to be affirmed as class representatives).

⁸⁹ DOBBS, *supra* note 4, at 249-50 (describing courts' discretion to impose equitable lien to prevent unjust enrichment). See also *Kelley v. Acker*, 216 Ark. 867, 228 S.W.2d 49 (Ark. 1950) ("Under the equitable rules above announced, appellee was entitled to be subrogated to the extent of the principal of the mortgage debt which she paid for the benefit of [the appellant] ... and the Chancellor correctly held that she was entitled to a lien on the proceeds of the partition sale to the extent of such payment."); *Graham v. Inlow*, 302 Ark. 414, 790 S.W.2d 428 (Ark. 1990) ("It is well settled that a tenant in common has the right to make improvements on the land without the consent of his cotenants; and, although he has no lien on the land for the value of his improvements, he will be indemnified for them, in a proceeding in equity to partition the land between himself and cotenants, either by having the part upon which the improvements are located allotted to him or by having compensation for them, if thrown into the common mass.").

⁹⁰ See PALMER, *supra* note 4, § 1.5(a) (explaining how equitable lien is used to protect plaintiff rights); cf. Restatement of the Law (Third) Restitution and Unjust Enrichment § 24 cmt. e (Tentative Draft No. 2, Apr. 1, 2002) ("Where a claimant has made expenditures to protect an interest in common property, the basic requirement that a liability in restitution not prejudice an innocent defendant (§49) is frequently observed by limiting the remedy in restitution to subrogation or equitable lien."); *Application of Mach*, 71 S.D. 460, 25 N.W.2d 881 (S.D. 1947) (equitable lien in circumstances of performance of another's duty); *Bennett v. Bennett*, 84 Miss. 493, 36 So. 452 (Miss. 1904) (a tenant in common is entitled to a lien on the shares of his co-tenants in the land for taxes paid by him beyond his proportionate share and for any sum due him for improvements or rent from his co-tenants).

and a market will likely develop in which firms buy from benefactors their interests in the property for immediate payment.

To illustrate how the risk of over-evaluation can be mitigated, let us return to Examples 1-3 (Construction, Stopping an Interference, and Changing Zoning Plans). In all three, a defined group of recipients gained benefits through the benefactor's activity and the benefit manifested itself in an increase in the market value of their property. This increase can easily be verified and sets a limit to the benefactor's recovery. Another limit is the recipients' share of the reasonable costs of producing the benefit. Both limitations reduce the risk of over-evaluation to a minimum. To avoid the liquidity problem, the recipients should have a choice between paying the benefactor immediately or placing a lien on their property in his favor. Furthermore, in Example 3 (Changing Zoning Plans), a quantum meruit fee for the benefactor should be a component in the costs, as perhaps should a modest premium for the risk of failure he took upon himself. Finally, in all three examples, the possibility that someone else could have provided the same benefit or its substitute at lower cost should also be taken into account in determining the recovery amount.

Applying the EDR in all three examples could be much trickier were there were no reliable objective criteria to evaluate the benefits or were the benefits more controversial. Thus, in Example 1 (Construction), had Owner constructed a park and it failed to influence the market value of Neighbors' property, the risk of over-evaluation of their benefits would be very high, justifying the non-application of an EDR. In contrast, the EDR would easily apply in all three scenarios were all recipients wealth-maximizers, such as commercial firms or other businesses. In such a case, the risk of benefit over-evaluation would be minimal, since typically this type of recipient lacks any idiosyncratic preferences or values. To illustrate, were all recipients property owners who lease apartments and offices to customers and the beneficial activity enables them to increase the rent and earn more, evaluating their benefits would be a simple task.

Similarly, Example 4 (The Security Firm), even though it does not involve enhancement of property value, should also not raise any insurmountable evaluation hurdles. If a decline in insurance premiums subsequent to the hiring of a security firm can be reasonably attributed to the firm's activity and that decline is in an equal or higher amount than the recipients' relative share of the reasonable costs of hiring the firm, there should be no difficulty recovering those costs under an EDR.

Two mechanisms can further reduce the risk of over-evaluation, although they should be resorted to only in exceptional cases. *The first mechanism is licensing.* This mechanism is suitable for cases in which

there is a substantial risk of over-evaluation and the recipients are likely to be required to make a large payment for the benefits they received. Under these conditions, the law should allow an EDR only with prior authorization from the public authority. In addition to reducing the over-evaluation risk, licensing could also mitigate the concern that public goods be produced—or their production controlled—by public authorities only.⁹¹ *The second mechanism is voting.* Condition the application of an EDR on recipients' advance vote in favor of production of the benefits can reduce the risk of over-evaluation and mitigate the autonomy concern as well.⁹² The problem with this mechanism, however, is that it could trigger a free-riding problem, in that there is the risk of recipients' making their vote conditional on their paying less than others to the benefactor. A secret vote could presumably counter this problem, but the mechanism could be objectionable on other grounds.

C. Proof and Collection Costs

When proof and collection are costly and the benefits gained by each recipient are low, the enforcement of an EDR is not cost-justified. More precisely, if benefactors internalize all enforcement costs, the duty becomes superfluous; if they do not internalize them, it could even be detrimental to efficiency.⁹³

Generally, proof and collection costs increase and the practical significance of a duty of restitution decreases when the benefits spread across many recipients, non-uniformly allocated and are of a low average value. Thus, in Example 1 (Construction), an EDR would not be cost-justified were there thousands of Neighbors and the benefit for each small and varying across individuals. In contrast, when the group of recipients is defined and the benefits relatively high, with each individual's share easily verified, recognizing an EDR will be warranted. Examples 1 to 4 fall into the latter category.

D. The Market

Sometimes, even when the parties cannot reach an agreement due to high transaction costs, there are still market mechanisms that facilitate the creation of the particular benefit. When such mechanisms are a realistic option, a duty of restitution should not be applied.

Consider a variation of Example 1 (Construction) in which Owner constructed a park on his land and thereby benefited Neighbors who can visit and enjoy the park. A free-riding problem arguably does not arise in

⁹¹ See *supra* Part I.C.6.

⁹² See *supra* Part I.B.

⁹³ See *supra* Part I.C.4.

this case or, alternatively, if one does, it is resolvable. For example, Owner can charge a fee for using the park and thereby collect reimbursement, all or in part, for his costs. If this is a realistic option, an EDR should not be applied. However, this can be a very costly—and inefficient—process due to the many users and many more instances of use on a daily basis.⁹⁴ Imposing a duty of restitution on Neighbors and charging them the lower amount of the indisputable increase in the market value of their property or their relative share of the costs of constructing the park could be far more practical.

Occasionally, legislatures create institutions that facilitate market solutions to free-riding. A good example is the patent registration afforded inventors under intellectual property law. The ability to collect a fee from users of their inventions through the market protects patent holders from free-riders, resulting in sufficient incentives for inventors to invent.

But market mechanism argument is not of unlimited applicability. Presumably, with respect to some of the examples discussed in the paper, it can be argued that were the recipients willing to allow the creation of the given benefit, they could organize in such a way so as to enable its production. For example, they could all live in a condominium or in a Business Improvement District,⁹⁵ which would enable the hiring of the security firm as in Example 4. Thus—the argument goes—the recipients should not be forced to pay for benefits they have *chosen* not to have. But this argument overlooks an important point. Many recipients, while preferring not to live in condominiums or to be involved in similar associations, will at the same time be willing to receive the benefits that an EDR would facilitate. An EDR provides recipients with an *ad hoc* solution, which is often more suited to their needs and preferences than an institutional solution.

Should an EDR be applied in cases where the benefactor would have produced the benefit regardless of whether he could recover? In an ideal world absent any enforcement costs or over-evaluation risk, a general principle of internalization of benefits would be warranted. This princi-

⁹⁴ Note also that after constructing the park, the investment in its construction is a sunk and fixed cost. In a perfectly competitive market, the price competing parks charge would not reflect the fixed costs of construction; in fact they would be zero, assuming the marginal cost of giving each additional person access to the park is negligible. Competition, however, is seldom expected to be perfect. Specifically, since there are no identical substitutes for A's park, he would probably have the ability to charge Neighbors a positive price even if all of his costs are fixed and sunk. *See, e.g.*, JEAN TIROLE, *THE THEORY OF INDUSTRIAL ORGANIZATION* 280 (1988) (showing formally how, in the case of competition amongst a small number of firms that do not provide perfect substitutes, prices remain above the cost of supplying the marginal unit). A detailed discussion of this issue is beyond the scope of this paper.

⁹⁵ *See infra* note 104 and accompanying text.

ple would provide benefactors with efficient incentives not only to take steps to produce a certain benefit but also to choose efficient levels of benefit-producing activities.⁹⁶ In the non-ideal world, however, if certain benefits are expected to be created in any event, an EDR is less crucial. Note, however, that an EDR works in categories of cases and not on a case-by-case basis. Therefore, only in cases in which benefactors *typically* expect great enough benefits to cause them to create those benefits regardless of later recovery, an EDR becomes less essential.

E. The Public Authority

Often, the public authority is the most suitable actor for enabling the production of public goods when the market fails to do so. But as explained earlier, there are a considerable number of situations in which individuals are better suited to this task,⁹⁷ and in those situations, an EDR could be a viable solution. In cases where there is real concern that an EDR would burden recipients with large payments, a licensing mechanism should be considered.⁹⁸ The next sections discuss three factors that, combined, yield the "best producer of the public good."

1. Information

The question of whether it is necessary to produce a certain public good can be very complex. Sometimes the authority possesses more information on the matter than individuals, while at other times the reverse is true.⁹⁹ Indeed, even when individuals have greater information, they could attempt to convey this information to the public authority and try to convince it either to produce the public good or finance it. But the authority will not necessarily be convinced. Among other things, it may suspect that individuals would prefer overproduction of public goods, especially when they do not internalize all the costs of production. Alternatively, the authority could take a different stance from individuals regarding the need for a particular public good.¹⁰⁰ Either way, in such

⁹⁶ Cf. STIGLITZ, *supra* note 50, at 131 (explaining how a benefactor who expects to gain a large benefit from a public good will produce it, but not in the efficient quantity).

⁹⁷ See *supra* Part I.C.6.

⁹⁸ See *supra* Part II.B.

⁹⁹ See GARETH D. MILES, PUBLIC ECONOMICS 311 (1995) ("One aspect of public goods that prevents the government making efficient decisions is the government's lack of knowledge of households' preferences and willingness to pay for public goods.").

¹⁰⁰ There could be different views on the necessary conditions for justifying the production of public goods by the authorities. For a thoughtful discussion, see Barak Medina, "Economic Constitution," *Privatization and Public Finance: A Framework for Judicial Review of Economic Policy*, in ZAMIR BOOK ON LAW, SOCIETY AND POLITICS 583 (Yoav Dotan & Ariel Bendor eds., 2005) (Hebrew) (arguing that the public good theory is not

cases, an EDR could encourage individuals to both produce and finance the public good in question.

Thus, in Example 1 (Construction), Owner could know much more than the authority whether the construction work is beneficial to him and to Neighbors; the same is true with respect to Example 2 (Stopping Interference). In the latter example, if the interference is illegal, the public authority has both the information and obligation to enforce the law. But this notwithstanding, if the authority fails to act, the individual who takes upon herself to step in should be able to recover her costs from the recipients of the benefit, since otherwise no one will act in the circumstances. There is an alternative route for resolving the problem in such cases, namely, that the individual who accrued expenses doing what the authority should have done be entitled to recover those expenses from the authority itself. Some courts have granted fee awards to plaintiffs who enforced the law through their legal actions to the benefit of others.¹⁰¹

2. *Negative Externalities*

One troubling issue related to the production of public goods is the negative externalities that can result from this.¹⁰² When creating public goods could result in externalization of costs, the public authority, and not individuals, is more suitable a producer.

To illustrate this negative externalities concern, let us return to Example 3 (Changing Zoning Plans). Recall that, in this Example, permitting the addition of a fifth floor to apartment buildings creates substantial benefits for owners of fourth-floor apartments. Suppose, now, that some of the residents living in the neighborhood will incur costs due to the zoning plans change. Under these circumstances, an individual who can recover from the winners but is not liable to the losers will have inefficiently excessive incentives to induce the authority to change the zoning plans and allow the construction of a fifth floor in apartment buildings. Indeed, if the authority is persuaded to change the zoning plans, it can be reasonably assumed that the benefits of the change likely

value-free, but rather depends on the normative considerations underlying the authorities' goals).

¹⁰¹ See Scott J. Jordan, *Awarding Attorney's Fee to Environmental Plaintiffs Under a Private Attorney General Theory*, 14 B.C. ENVTL. AFF. L. REV. 287 (1987) (discussing those cases and supporting them). Class actions are another mechanism by which the problem can be solved.

¹⁰² See JOHN G. HEAD, *PUBLIC GOODS AND SOCIAL WELFARE* 184-210 (1974) (discussing externalities and their relevance to the theory of public goods).

exceed the costs. Still, the true social benefit in this case cannot be claimed to equal the sum of the benefits garnered by all winners, since the losers' costs should be factored into the calculations. However, as long as the measure of recovery is limited to the costs spent by A, the benefactor, to persuade the authority to change the zoning plans, the risk of excessively crediting him is rather small, and thus recognizing an EDR can be justified.

3. Finance

Suppose that Example 4 (Security Firm) transpires in a wealthy neighborhood in New York. The Residents ask the municipality to send police patrols to their neighborhood at night. Even though such an activity would be clearly welfare-enhancing, the City of New York refuses to do so due to limited resources. In fact, due to the City's budgetary limitations, improving security in the wealthy neighborhood would be at the expense of more valuable activities elsewhere and therefore would be welfare-reducing.¹⁰³ One possible system of taxation could, in fact, be to allow the City to levy taxes only on those who are expected to directly benefit from the improved security and then use the money for the police patrols. But this is quite a rare practice¹⁰⁴ and usually not a viable option. An EDR could be a practical solution.

¹⁰³ It has been argued that there should be less willingness on the part of the authorities to produce public goods that are consumed by high-income earners. This argument was raised with respect to activities for the preservation of the environment, *see* Richard J. Lazarus, *Pursuing "Environmental Justice": The Distributional Effects of Environmental Protection*, 87 NW. U. L. REV. 787 (1993).

¹⁰⁴ A similar practice is the creation of a "business improvement district" ("BID"). A BID is a public-private partnership in which property and business owners of a defined area elect to make a collective contribution to the maintenance, development, and marketing/promotion of their commercial district. BIDs require legislative authorization from the local government representing the BID initiators seeking to establish the district. They typically provide services such as street and sidewalk maintenance, public safety officers, park and open space maintenance, marketing, capital improvements, and various development projects. The services provided by BIDs supplement the services already provided by the municipality. BIDs are funded through special assessments collected from the property owners in the defined boundaries of the district. Like a property tax, the assessment is levied on the property owners who can, if the property lease allows, pass it on to their tenants. For further details, see the website of The Los Angeles Downtown Center Business Improvement District, <http://www.downtownla.com>, and Downtown DC BID, <http://www.downtowndc.org>.

F. Preserving and Pursuing the Benefactor's Interests

In cases of unrequested benefits, there are three conditions to a duty of restitution arising under prevailing law.¹⁰⁵ Should these conditions be preserved in the EDR framework set forth in this paper?

One central condition, *high transaction costs* between the parties, remains intact also in the EDR framework proposed here. In contrast, the condition of *protecting and preserving existing entitlements*, as opposed to creating new ones, should be abandoned. There are two possible rationales for this condition: the first rationale is consistent with the understanding that the condition focuses on the benefactor, and the second rationale correlates with a different interpretation, that the recipient is the focus. *Under the first rationale*, the *benefactor's* interest in protecting and preserving *his* existing entitlements warrants greater support from the law than his interest in creating new entitlements, especially when there is a risk that the recipients' entitlements could be adversely affected by the new entitlements. But if there are satisfactory ways to ensure that the recipient will not be adversely affected—as the conditions for recognizing an EDR imply—then maintaining a distinction between protecting and preserving existing entitlements, on the one hand, and creating new ones, on the other, does not make any sense. *Under the second rationale*, only when the *recipient's* entitlements were protected or preserved by the benefactor is it safe to assume that he actually benefited from the benefactor's acts. If, instead, new entitlements were created for the recipient, there is a risk that obligating him to compensate the benefactor for what he received would place him in a worse-off position. But here, again, if all the conditions for an EDR are met, this risk is minimal.

The third condition for a duty of restitution to arise under prevailing law is that *the benefactor pursued his own interests* and only incidentally created benefits for others. Under this condition, the benefactor himself must also be a recipient and not just an intervener who is interested in being paid for the benefits he created. This condition excludes cases where the benefactor is a merchant or was otherwise motivated by simply a desire to get paid. When benefactors are merchants, competition among them could arguably make the application of an EDR very complex.

The five conditions for an EDR to be applied will typically be sufficient for reducing the risk that many benefactors will compete over producing the benefits. But more importantly, since an EDR would allow benefactors to recover from recipients no more than their relative share

¹⁰⁵ See *supra* Part I.A.

of the *reasonable* costs of producing the benefits (which are determined taking into account alternative ways of production), only benefactors with a self-interest in creating the particular benefits, as well as the ability to produce them efficiently, will have incentive to create them in the first place.

CONCLUSIONS

This paper has considered the issue of how the law should deal with positive externalities. The central claim advanced here has been that the existing categories of restitution law dealing with voluntary conferral of unrequested benefits should be replaced with a consolidated, principled approach to restitution.

By way of comparing harm cases with benefit cases, on the one hand, and cases of benefit incidental to harm with pure benefit cases, on the other, the paper has proposed five conditions that should be met to give rise to a duty of restitution: transaction costs are high enough so as to preclude securing recipients' consent to pay for the unrequested benefits; the risk of over-evaluation of the benefits is not so high as to undermine the efficiency of the restitution duty or to substantially infringe on recipients' autonomy; the proof and collection costs are not so high, relative to the value of the benefits, so as to make enforcing the duty inefficient; the benefits cannot be created by the market; and the benefits will not be created by the public authority. The proposed EDR is much broader than the duty of restitution currently recognized by the law. In particular, recognizing an EDR as set forth here would enable recovery under restitution law even when benefactors create new entitlements and do not merely preserve existing ones and even when no "proximity of interests" exists among the parties involved.

Due to space constraints, the paper developed only the principal parameters of its proposed EDR. It was argued that two caps should be set to recovery under an EDR: the amount of the indisputable benefits conferred on recipients and the reasonable costs of producing the benefit (with or without a quantum meruit fee and a risk premium). Moreover, it was also suggested that when the benefit is an increase in the market value of the recipient's property, the recipient should have a choice between paying the benefactor when the benefit is created or deferring payment until the increased value is realized in profits. Finally, in exceptional cases it was recommended to consider using licensing and voting mechanisms before applying an EDR.¹⁰⁶

¹⁰⁶ Extending the duty of restitution as proposed here can be expected to trigger the development of at least six rules for handling benefit cases, although only the second and

The paper argued that an EDR should be developed in categories of cases where the proposed five conditions are typically met. It seems that the application of an EDR is most suitable when the benefits are wholly monetary or an enhancement of property value. When the recipients are wealth-maximizers, the argument for an EDR has even greater appeal-
ing.

Recognizing a general duty of restitution would not substitute other mechanisms for producing public goods, mainly those used by the public authorities. Instead, an EDR would be just one more mechanism supplementing existing ones. It holds the potential for changing people's incentives to create benefits for themselves as well as for others. And of course, the motivation for writing this paper is the belief that such change would be desirable.

third rules were comprehensively discussed in this paper. These six rules are as follows: (1) A benefactor is free to create a given benefit but is not entitled to any recovery from the recipients. (2) A benefactor is free to create a given benefit and is entitled to recovery from the recipients in the amount of their relative share of his reasonable costs. (3) A benefactor is free to create a given benefit and is entitled to recovery from the recipients in the amount of their benefit. (4) Recipients are entitled to the creation of a given benefit and are not liable towards the benefactor. (5) Recipients are entitled to the creation of a given benefit, but are liable in the amount of their relative share of his reasonable costs. (6) Recipients are entitled to the creation of a given benefit, but are liable in the amount of the benefit.

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