IN DEFENSE OF COMPENSATION

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In recent years, tort victims in the U.S. have been finding it increasingly difficult to secure compensation through the legal system. This decline of compensation is the result of a decades-long campaign by corporate defendants to reshape the litigation landscape in their own favor. The most recent volley in this ongoing battle is an unprecedented, forceful attack against compensation launched by the Trump Administration. Regrettably, the inaccessibility of compensation often spells tragedy for tort victims. To justify these attacks, supporters of the anticompensation campaign utilize the economic theory of tort law to formulate forceful arguments against compensation as a general legal principle.

This Article demonstrates that the prevailing economic argument, and the legal order that follows therefrom, is based on a fundamental oversight. In particular, current economic theory fails to consider the possibility of investments by victims to shift harm to others. This Article is the first to examine the possibility of harm-shifting in the context of tort doctrine.

This additional consideration proves to be crucial for the analysis of compensation. Existing economic theory argues that compensation is "inefficient" as it annuls victims' incentive to invest in self-protection. This argument is reversed once we consider the possibility of harm-shifting. When investing to protect themselves, tort victims can pass harms on to others. Such investments are wasteful as they are designed only to redistribute harms, not to eliminate them. Therefore, compensation can actually prove beneficial precisely because it annuls victims' incentive to invest in self-protection.

Once harm-shifting investments are considered, the economic argument against compensation is overturned. The case, therefore, for compensation is stronger than economic theory currently leads us to believe, and action must be taken to reverse the trending decline of compensation.

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INTRODUCTION

An individual wronged by another is entitled to compensation for the harm suffered.[1] This is the general principle of compensation, a self-evident requisite of justice, recognized by moral philosophers at least since Aristotle.[2] Compensation aims to correct a wrong, to the degree possible, when actual repair in kind is unattainable.[3] Thus, if you suffered an injury to yourself or to your property, the least the culpable transgressor can do, morally, is to compensate you for the harm they caused.

Compensation is not only a fundamental moral principle but also an essential element of any legal system. The law defines a set of primary rights; once a primary right has been infringed upon, a secondary right for compensation follows.[4] Absent such compensation, primary rights have no meaning, as their violation bears no consequence.[5] The right for compensation must therefore be considered to underwrite all other rights.[6] From the ancient Code of Hammurabi to the modern administrative state, our societies cannot conceive of a legal system without the institution of compensation.[7]

And yet, despite its crucial importance for both morality and law, the right to compensation has suffered a series of devastating blows in recent years.[8] The structure of private litigation dictates a simple truth: compensa-

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1. Compensation is a well-established common-law principle. Livingstone v. Rawyards Coal Co. (1880) 5 App. Cas. 25 (HL) 39 (appeal taken from Scot.) ("I do not think there is any difference of opinion as to its being a general rule that, where any injury is to be compensated by damages, in settling the sum of money to be given for reparation of damages you should as nearly as possible get at that sum of money which will put the party who has been injured, or who has suffered, in the same position as he would have been in if he had not sustained the wrong for which he is now getting his compensation or reparation.").

2. On the connection between compensation and the requirements of corrective justice, see ARISTOTLE, NICOMACHEAN ETHICS bk. V, at 4–5 (W.D. Ross trans., Batoche Books 1999) (c. 350 B.C.E.); Jules L. Coleman, *Property, Wrongfulness and the Duty to Compensate*, 63 CHI.-KENT L. REV. 451, 463 (1987); Ernest J. Weinrib, *Causation and Wrongdoing*, 63 CHI.-KENT L. REV. 407, 449–50 (1987).

3. *See* Stephen A. Smith, *Duties, Liabilities, and Damages*, 125 HARV. L. REV. 1727, 1728 (2012) (explaining that compensation operates to correct a wrong by giving legal recognition to the fact a duty towards the victim was violated).

4. On the distinction between primary and secondary rights, see Joseph W. Bingham, *The Nature of Legal Rights and Duties*, 12 MICH. L. REV. 1, 12–13 (1913).

5. O.W. Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 461 (1897) (stating that the only meaning of "legal duty" is the prediction that some actions will lead to "disagreeable consequences by way of imprisonment or compulsory payment").

6. *Cf.* Ernest J. Weinrib, *Legal Formalism: On the Immanent Rationality of Law*, 97 YALE L.J. 949, 969–70 (1988) (explaining the formalist view of compensation).

7. The Code of Hammurabi, discovered in 1901, is an ancient Babylonian legal code dating back to about 2250 B.C. *See* Donald G. McNeil, *The Code of Hammurabi*, 53 A.B.A. J. 444, 444 (1967). Much of the Code consists of casuistic compensation laws detailing amounts to be paid for specific transgressions against specific types of victims. *See id.* at 445–46.

8. On the contemporary decline of compensation, see *infra* Part I.

tion is obtained only if the expected compensation amount outweighs the cost of securing it through litigation. Otherwise, victims of harm will simply never sue for compensation. Savvy repeat defendants are aware of this dynamic, and those with the requisite means have been working to systematically increase litigation costs for plaintiffs[9] as well as to limit the compensation amounts plaintiffs can be paid.[10] Increasing the costs while lowering the rewards imbalances the scale against prospective plaintiffs. This anticompensation campaign, led by powerful commercial lobbies, has been immensely successful, resulting in prohibitive costliness of lawsuits for many private plaintiffs.[11] Compensation has thus become a rarity instead of the norm: currently, only 2% of Americans injured in an accident find it worthwhile to sue for compensation.[12]

Going forward, compensation is expected to decline even further. The compensation crisis recently made national news following President Trump's declaration of a new anticompensation attack.[13] These are not empty threats: the Trump administration is currently working to block compensation suits, for the first time, as a matter of federal law. If such initiatives continue unhindered, the final defeat of compensation will soon be achieved.

To justify the anticompensation campaign, repeat defendants employ powerful normative arguments that originate in law and economics literature. According to prevailing economic theory, deterrence is the primary goal of tort law.[14] Under this paradigm, compensation carries little inde-

9. *See* Frank M. McClellan, *The Vioxx Litigation: A Critical Look at Trial Tactics, the Tort System, and the Roles of Lawyers in Mass Tort Litigation*, 57 DEPAUL L. REV. 509, 510–11 (2008) (studying litigation tactics by repeat defendants designed to drag plaintiffs into a long and costly litigation process); *cf.* AM. BAR ASS'N, PERCEPTIONS OF THE U.S. JUSTICE SYSTEM 58 (1999) (detailing survey respondents' perceptions of actions taken by defendants as designed to increase plaintiffs' litigation costs).

10. Marc Galanter, *Why the "Haves" Come Out Ahead: Speculations on the Limits of Legal Change*, 9 LAW & SOC'Y REV. 95, 97, 100 (1974) (explaining the ability and incentive of repeat defendants to invest beyond a specific case in order to change rules and institutions in their favor).

11. *See generally* Gideon Parchomovsky & Alex Stein, *Empowering Individual Plaintiffs*, 102 CORNELL L. REV. 1319 (2017) (studying the growing inability of private plaintiffs to vindicate their rights through the legal system).

12. THOMAS F. BURKE, LAWYERS, LAWSUITS, AND LEGAL RIGHTS: THE BATTLE OVER LITIGATION IN AMERICAN SOCIETY 3 (2002).

13. *See* Joanne Doroshow, *Despite Trump, Federal 'Tort Reform' Makes a Hasty Retreat*, HUFFINGTON POST (May 31, 2017), https://www.huffingtonpost.com/entry/despite-trump-federal-tort-reform-makes-a-hasty_us_592dd27fe4b075342b52c0e0; Robert Pear, *G.O.P. Bill Would Make Medical Malpractice Suits Harder to Win*, N.Y. TIMES (Apr. 15, 2017), https://www.nytimes.com/2017/04/15/us/politics/republicans-health-care-bill-medical-malpractice-suits.html; Judson Phillips, *Trump Tort Reform Threatens the 7th Amendment*, WASH. TIMES (Mar. 2, 2017), http://www.washingtontimes.com/news/2017/mar/2/trump-tort-reform-threatens-7th-amendment/.

14. *See* Richard A. Posner, *A Theory of Negligence*, 1 J. LEGAL STUD. 29, 33 (1972) (arguing liability is designed to induce the economically efficient level of precautions). For more details, see *infra* notes 156–61 and accompanying text.

pendent value; any moral justification, for example, is discounted.[15] Furthermore, economic theory emphasizes various inefficiencies generated by compensation.[16] Repeat defendants rely on economic theory to argue that the current compensation crisis is no crisis at all since compensation can be harmful just as much as it can be beneficial.[17] In fact, they argue, it might be appropriate to limit compensation even further.[18] Thus, repeat defendants and their allies justify the compensation deficit on efficiency grounds.

This Article sets out to reject the economic argument against compensation by highlighting the possibility of *harm-shifting*. This is the first scholarly work to study investments designed to shift harms in the context of tort doctrine.

To illustrate the economic argument against compensation, and this Article's rebuttal, consider the following stylized example, which follows the classic setting of conflicting land uses by two neighbors, a farmer and a rancher.[19] The farmer and the rancher both know that cattle from the ranch might trample crops in the farm, causing an estimated harm of $10,000. The most practical way to prevent this incident from happening is for the farmer, the potential victim, to invest $1,000 in order to surround the farm with a strong fence.

Under current economic theory, scholars insist that the farmer in the example should *not* be compensated here if the predicted harm befalls her. The theory dictates that the farmer is the "cheapest cost avoider,"[20] able to prevent the harm at a lower cost than the rancher.[21] It is therefore *better* if

15. John C.P. Goldberg, *Twentieth-Century Tort Theory*, 91 GEO. L.J. 513, 545 (2003) (showing that contemporary economic theory focuses exclusively on efficient deterrence as the goal of tort law).

16. *See* Robert Cooter, *Unity in Tort, Contract, and Property: The Model of Precaution*, 73 CALIF. L. REV. 1, 3–4 (1985) (showing that compensation distorts incentives to invest in precautions); Steven Shavell, *The Fundamental Divergence Between the Private and the Social Motive to Use the Legal System*, 26 J. LEGAL STUD. 575 (1997) (showing that compensation creates distorted incentives to engage in litigation). For more details, see *infra* notes 120–21 and accompanying text.

17. *See* F. Patrick Hubbard, *The Nature and Impact of the "Tort Reform" Movement*, 35 HOFSTRA L. REV. 437, 473 (2006) (describing the reliance of the tort-reform movement on the ideology and rhetoric of efficiency); Shavell, *supra* note 16, at 575, 579, 586–88.

18. *See* Shavell, *supra* note 16, at 582–84.

19. This example is most famously used by Ronald Coase. R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1, 2 (1960).

20. *See* GUIDO CALABRESI, THE COSTS OF ACCIDENTS: A LEGAL AND ECONOMIC ANALYSIS 244 (1970) (offering and developing the concept of the "cheapest cost avoider").

21. The concept of the cheapest cost avoider is closely related to the problem of the reciprocal nature of causation, as famously highlighted by Ronald Coase. Coase, *supra* note 19, at 1–3. In his seminal work, Coase showed that harms are not solely caused by injurers but also by the bipolar relationship between injurers and victims. *Id.* Coase's treatment of causation is a response to the work of Arthur Pigou. *See id.* at 28. *See generally* A.C. PIGOU, THE ECONOMICS OF WELFARE (AMS Press, Inc. 1978) (1920). More recently, Brian Simpson argued that Pigou's work is actually responsive to some of the difficulties presented by Coase. A.W. Brian Simpson, *Coase v. Pigou Reexamined*, 25 J. LEGAL STUD. 53 (1996); *see also* R.H. Coase, *Law and Economics and A.W. Brian Simpson*, 25 J. LEGAL STUD. 103 (1996); A.W. Brian Simpson, *An Addendum*, 25 J. LEGAL STUD. 99 (1996).

the farmer *cannot* secure compensation. If the farmer enjoys no promise of compensation, she will have a strong incentive to invest $1,000 in erecting the fence, thus efficiently preventing a greater harm of $10,000. This would be the most efficient prophylactic measure. Conversely, goes the economic argument, if the farmer *can* expect compensation, she is made indifferent to the harm and will therefore have no reason to invest efficiently in preventing it.[22] Thus, compensation *creates inefficiencies*. Under this view, compensation should never be granted where the victim is the cheapest cost avoider. This conclusion represents a fundamental truth for the economic analysis of tort law,[23] and it stands regardless of any intuition about justice,[24] such as the fact the cattle from the ranch trespassed into the farm, violating the farmer's property right.[25] Thus, the basic maxim of contemporary economic theory judges compensation to be unwarranted if the victim is the cheapest cost avoider.

This Article will demonstrate that the economic-theory maxim is based on a fundamental oversight and on a misleading assumption regarding the nature of the victim's investments. In the example above, the farmer is the cheapest cost avoider and can prevent the harm to herself at a low cost by erecting a fence. This cost-efficient measure, however, prevents harm *only to the farmer herself*. The rancher's cattle, their progress defeated by the farmer's new fence, can simply wander off to trample another field. In this way, the farmer's investment did not minimize the harm but merely passed it on to another victim. Extrapolating this point into a generality, we observe that victims invest to *protect themselves*, not to *minimize harms*. In other words, a victim who invests in self-protection can easily shift harms

22. This is the now classic "paradox of compensation." *See* Cooter, *supra* note 16, at 6. Compensation makes injurers internalize the harm they cause, thereby optimally deterring them. At the same time, compensation makes victims indifferent to harms, thereby annulling their incentive to invest in precautions. The term was first coined by Robert Cooter, *id.* at 3–4, following the work of Coase, Coase, *supra* note 19, and Calabresi, CALABRESI, *supra* note 20; *see also* ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 331 (6th ed. 2012). For the same problem in the context of contract law, see Steven Shavell, *Damage Measures for Breach of Contract*, 11 BELL J. ECON. 466 (1980) (showing that expectation damages can distort the incentives of the promisee).

23. For more manifestations of the paradox of compensation, see Oren Bar-Gill & Omri Ben-Shahar, *The Uneasy Case for Comparative Negligence*, 5 AM. L. & ECON. REV. 433 (2003); Giuseppe Dari-Mattiacci & Nuno Garoupa, *Least-Cost Avoidance: The Tragedy of Common Safety*, 25 J.L. ECON. & ORG. 235 (2009); Dhammika Dharmapala & Sandra A. Hoffman, *Bilateral Accidents with Intrinsically Interdependent Costs of Precaution*, 34 J. LEGAL STUD. 239 (2005); Francesco Parisi & Vincy Fon, *Comparative Causation*, 6 AM. L. & ECON. REV. 345 (2004).

24. Current economic theory insists that intuitions of fairness should never trump the requirements of efficiency. *See generally* LOUIS KAPLOW & STEVEN SHAVELL, FAIRNESS VERSUS WELFARE (2002); Louis Kaplow & Steven Shavell, *Any Non-Welfarist Method of Policy Assessment Violates the Pareto Principle*, 109 J. POL. ECON. 281 (2001); Louis Kaplow & Steven Shavell, *Fairness Versus Welfare: Notes on the Pareto Principle, Preferences, and Distributive Justice*, 32 J. LEGAL STUD. 331 (2003).

25. For a critique of this result and more details on its centrality to current economic theory, see Henry E. Smith, *Self-Help and the Nature of Property*, 1 J.L. ECON. & POL'Y 69, 72 (2005).

to others. Such investments are wasteful because they do not minimize total harm but merely redistribute harms among potential victims.

This point is crucial for the analysis of compensation. Existing economic theory argues that compensation is "inefficient" because it annuls victims' incentive to invest in efficient precautions. But this argument is erroneous. Given our understanding that investments in self-protection can themselves be wasteful by shifting harms to others rather than preventing them, compensation can, in fact, be beneficial precisely *because* it annuls victims' incentive to invest in self-protection.

To illustrate, in the example above of the farmer and the rancher, if compensation is *not* available, the farmer will indeed invest in erecting a fence. This investment is wasteful; the fence merely works to shift the harm to another victim. Conversely, if compensation *is* available, the farmer is made indifferent to the harm and will not invest to avoid it. This is a preferable result because the fence serves no useful purpose in preventing harm caused by the wandering cattle. In this way, compensation beneficially eliminates the need for potential victims to protect themselves with wasteful investments that merely shift harms to others.

This analysis reveals that the need for compensation is greater than what prevailing economic theory would have us believe. Under prevailing theory, the justification for compensation is highly contingent. In particular, whenever the victim is the cheapest cost avoider, compensation is seen to create incentives that are actually *harmful* rather than helpful.[26] From this economic-theory perspective, compensation has no general justification that is compelling, and working to improve access to compensation can create problems as much as or more than it can generate benefits.[27]

My analysis upends the economic argument, demonstrating that compensation can be justified even if the victim is the cheapest cost avoider with the ability to invest in self-protection. In fact, compensation might be justified *especially* when victims are cheapest cost avoiders. Compensation serves to protect all potential victims from harm, thus freeing individuals of the need to invest in "avoiding" harms to themselves while shifting them, wholly or partly, to others.[28]

By bringing to light this analytical about-face, this Article offers three novel contributions. First, I demonstrate that, contrary to conventional wis-

26. *See* CALABRESI *supra* note 20, at 244–50; Coase, *supra* note 19, at 2; Cooter, *supra* note 16, at 3–4.

27. *See* Shavell, *supra* note 16, at 579, 586–88.

28. To observe harm-shifting efforts, it might be necessary to take a broader view of the field in which the parties operate. Instead of analyzing only the parties to the dispute and their decisions to invest in minimizing harms, it may be necessary to consider also interactions with third parties, the flow of information between the parties, feedback over time, dynamic change, and the ability to control resources. *See generally* OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM (1985).

dom, victims' investments in self-protection are not aligned with the public policy objective of minimizing harmful effects. Current economic analysis of tort law is premised on a fundamental oversight, erroneously equating harm "avoidance" with actual minimization of harms.[29] I show that when a potential victim invests to "avoid" harm, she is doing exactly that—investing to escape it herself, not to actually minimize or prevent it.[30] This means that victims will generally invest in self-protection according to the effect of such investment on the harms they fear to suffer themselves, not according to its effect on overall levels of harm.

This contribution endeavors primarily to bridge diverse strands of literature. The wasteful nature of harm-shifting investments is a central theme in many areas of study, primarily in the criminal law and criminology literature.[31] This Article is the first to introduce these insights into the tort theory literature and to study the role of harm-shifting investments in the context of tort law.

The second contribution is conceptual. I show that, once one considers the possibility of harm-shifting, the analytical framework of the cheapest cost avoider—the most fundamental maxim of contemporary economic theory of tort law—is inverted. The basic premise of current economic theory is that, if victims are the cheapest cost avoiders, compensation is unnecessary and, in fact, harmful. If victims can cheaply prevent the harm, there is no reason to compensate them because doing so will leave no incentive for them to make efficient investments in precautions. Contrary to this conventional view, this Article demonstrates that the case for compensation can be *stronger, not weaker*, when victims are cheapest cost avoiders, able to protect themselves from harm.[32] Absent compensation, victims are driven to invest wastefully in attempts to shift harms to others. Compensation, therefore, is appropriate precisely *because* victims are cheap cost avoiders. This analysis overturns the familiar economic framework.

The third and final contribution is normative. While strong consensus exists regarding the moral justification for compensation, efficiency arguments currently run in the other direction. And, critically, it seems that the

29. *See infra* notes 156–61 and accompanying text.

30. *See infra* Part III.

31. *See, e.g.*, Robert Barr & Ken Pease, *Crime Placement, Displacement, and Deflection*, *in* 12 CRIME AND JUSTICE: A REVIEW OF RESEARCH 277 (Michael Tonry & Norval Morris eds., 1990) (showing that law enforcement efforts can displace crime rather than eliminate it, by studying different categories of crime displacement and their social effects); *see also* CRIME SPILLOVER (Simon Hakim & George F. Rengert eds., 1981); Ian Ayres & Steven D. Levitt, *Measuring Positive Externalities from Unobservable Victim Precaution: An Empirical Analysis of Lojack*, 113 Q.J. ECON. 43, 63–65 (1998); Kate J. Bowers & Shane D. Johnson, *Measuring the Geographical Displacement and Diffusion of Benefit Effects of Crime Prevention Activity*, 19 J. QUANTITATIVE CRIMINOLOGY 275 (2003).

32. *See infra* notes 175–77 and accompanying text.

efficiency-based anticompensation argument is dominating the debate.[33] Compensation can win this fight according to the economic metric only if it can be shown that it is not only "just" but also efficient. The argument I submit answers this challenge by showing that once we consider the possibility of harm-shifting, the case for compensation becomes far stronger, even on efficiency grounds.[34] This changeover has immediate policy implications; it calls for a concerted effort to reverse the decline of compensation currently favored by economic theory. Without a robust compensation regime, the legal system abandons potential victims of tortious harm to fend for themselves. I show that this generates problems since individuals protecting themselves are not considering the well-being of others and therefore invest wastefully. Compensation mitigates these deficiencies.

The Article proceeds as follows. Part I details the compensation crisis and the general decline in the ability of plaintiffs to vindicate their rights through compensation. Part II reviews the theoretical literature, focusing on the prevailing economic argument against compensation. Part III is the analytical core of the Article; it shows that the conventional economic framework of the cheapest cost avoider is overturned when we consider the harm-shifting nature of investments by potential victims. Part IV expands on the analysis in Part III to argue the normative case for compensation. This Part utilizes examples from the laws of accidents, intentional torts, and nuisance. A short conclusion follows.

I. COMPENSATION UNDER ATTACK

The ability of plaintiffs to secure compensation through the legal system is in decline. Compensation critically depends on the ability of plaintiffs to compete against defendants in court.[35] As well-organized commercial defendants grow ever more powerful, private plaintiffs stand less and less chance to vindicate their right for compensation.[36]

The cost of vindicating legal rights is a familiar theme in legal scholarship.[37] Specifically, scholars highlight the importance of the distribution of

33. *See infra* notes 146–50 and accompanying text.

34. *See infra* Part IV.

35. *See* Gideon Parchomovsky & Alex Stein, *The Relational Contingency of Rights*, 98 VA. L. REV. 1313, 1314–21 (2012) showing that the realization of an abstract right depends on the right-holder's cost of vindicating it and the challenger's cost of attacking it in court).

36. *See* Deborah L. Rhode, *Access to Justice*, 69 FORDHAM L. REV. 1785, 1785 (2001) ("Millions of Americans lack any access to the [justice] system, let alone equal access. An estimated four-fifths of the civil legal needs of the poor, and the needs of an estimated two- to three-fifths of middle-income individuals, remain unmet.").

37. *See, e.g.*, STEPHEN HOLMES & CASS R. SUNSTEIN, THE COST OF RIGHTS: WHY LIBERTY DEPENDS ON TAXES (1999) (studying the role of enforcement costs in a general philosophy of rights). For the economic analysis of this issue, see Lucian Arye Bebchuk, *Litigation and Settlement Under Imperfect Information*, 15 RAND J. ECON. 404 (1984); Steven Shavell, *Suit, Settlement, and Trial: A*

legal costs among litigants;[38] while some litigants have easy access to courts and legal services, others face great barriers on their way, financial and otherwise.[39] In the context of tort litigation, the distribution of legal costs systematically favors defendants over plaintiffs.[40] Tort litigation typically pits private plaintiffs against corporate defendants.[41] Corporate defendants, such as insurance companies, hospitals, product manufacturers, or financial institutions, tend to be well-organized, repeat litigants with ready access to litigation resources.[42] By comparison, private plaintiffs are typically one-time litigants without such easy access to the litigation system.[43]

As a general rule, all this means individual plaintiffs find it difficult to vindicate their rights for compensation.[44] What is more, these difficulties have been exacerbated in recent years by the growing wealth gap and by repeat defendants' concerted efforts to reshape the litigation landscape in their favor.[45] To illustrate this problem in greater detail, consider the following stylistic example, based on the classic polluting factory scenario.[46]

- *Example 1*: Olivia lives in an urban area not far from an industrial complex. One day, following an accident in a nearby factory, toxic waste is released into the air and causes a series of harms to Olivia. Specifically, Olivia suffers a bodily injury ($3,000), significant emotional distress ($2,000), and some damage to her home ($1,000). The total harm to Olivia is thus estimated at $6,000, and the factory, the defendant, is liable for these harms

Theoretical Analysis Under Alternative Methods for the Allocation of Legal Costs, 11 J. LEGAL STUD. 55 (1982).

38. Parchomovsky & Stein, *supra* note 35, at 1314–21 (showing that the realization of an abstract right depends on the right-holder's cost of vindicating it and the challenger's cost of attacking it in court).

39. *See id.* at 1314, 1318.

40. Parchomovsky & Stein, *supra* note 11, at 1323.

41. *See id.* at 1332–33.

42. *See* Parchomovsky & Stein, *supra* note 11, at 1323; Parchomovsky & Stein, *supra* note 35, at 1320 ("[I]n certain types of cases, the effects of asymmetric litigation costs are not randomly distributed across the population. Rather, they are systemic, favoring certain categories of litigants and disfavoring others.").

43. *See* Hubbard, *supra* note 17, at 454 ("Because defendants in tort disputes tend to have more wealth than plaintiffs, they have an advantage in the litigation." (footnote omitted)); Parchomovsky & Stein, *Empowering Individual Plaintiffs*, *supra* note 11, at 1332–33.

44. *See* Parchomovsky & Stein, *supra* note 11, at 1332–34.

45. *See* BURKE, *supra* note 12, at 3; Hubbard, *supra* note 17, at 471–72 ("Because these 'haves' know that they are repeat players on the defense side of the tort system, they have a common motive to reduce costs by reducing the amount of their potential liability in tort by changing tort law in ways that favor defendants."); Judith Resnik, *Diffusing Disputes: The Public in the Private of Arbitration, the Private in Courts, and the Erasure of Rights*, 124 YALE L.J. 2804, 2807 (2015).

46. The factory scenario is famously used by Coase, Coase, *supra* note 19, at 1, and has become the standard illustration for the injurer–victim relationship.

> as a matter of law. Yet, to enforce her right, Olivia must spend $7,000 in litigating the case.

In this example, Olivia suffers harm resulting from the factory's operations.[47] In a perfect world of zero enforcement costs, Olivia will sue the factory and receive full compensation—she will be made whole.[48] In such a world, legal rights are fully manifested in reality, and no gap in legal protection would ever exist. But the analysis changes dramatically once it integrates the cost of enforcing victims' rights. In the example above, Olivia must incur a total cost of $7,000 to vindicate her right for compensation. In this case, the suit would actually amount to a $1,000 loss for Olivia (compensation of $6,000 minus litigation costs of $7,000). Unless Olivia feels inclined to pursue justice for justice's sake and is willing to lose money in order to vindicate her rights, she is better off not suing; most plaintiffs in her position would choose this latter option.[49]

Olivia's example is not only theoretical: it is highly representative.[50] In fact, only 2% of Americans injured in an accident find it worthwhile to sue for compensation.[51] This failure to sue is not irrational; rather, it stems from the prohibitive costs of litigation.[52]

Olivia's example illustrates a fundamental truth: compensation is obtained only where the expected compensation amounts outweigh the costs of securing them through litigation.[53] This means compensation is less like-

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47. *See, e.g.*, Adams v. Cleveland-Cliffs Iron Co., 602 N.W.2d 215 (Mich. Ct. App. 1999) (complaining about dust, noise, and vibrations emanating from an iron mine); Boomer v. Atl. Cement Co., 257 N.E.2d 870 (N.Y. 1970) (complaining about dirt, smoke, and vibration emanating from cement plant); Mathewson v. Primeau, 395 P.2d 183 (Wash. 1964) (complaining about odors emanating from hog-raising operation).

48. A hypothetical world of zero enforcement costs parallels the so-called Coasean World of zero transaction costs. For important clarifications on this often-misunderstood term, see Robert C. Ellickson, *The Case for Coase and Against "Coaseanism,"* 99 YALE L.J. 611 (1989).

49. Note that the use of contingency fees does not change this result. Contingency fees can solve the plaintiff's liquidity problem by allowing the plaintiff to pay her attorney fees only in case of success in court. If, however, the cost of suit is higher than the expected compensation amount, no contingency payment will suffice to incentivize a lawyer to take the case. Similar problems persist in class actions, where potential compensation amounts are too low to properly incentivize plaintiff lawyers. *See, e.g.*, *In re* Activision Blizzard, Inc. Stockholder Litig., 124 A.3d 1025, 1070 & n.28 (Del. Ch. 2015); Alon Harel & Alex Stein, *Auctioning for Loyalty: Selection and Monitoring of Class Counsel*, 22 YALE L. & POL'Y REV. 69, 71 (2004).

50. *See* Richard L. Abel, *The Real Tort Crisis—Too* Few *Claims*, 48 OHIO ST. L.J. 443, 448–52 (1987) (surveying the literature); *cf.* David A. Hyman & Charles Silver, *Medical Malpractice Litigation and Tort Reform: It's the Incentives, Stupid*, 59 VAND. L. REV. 1085, 1088–92 (2006) (surveying the literature in the context of medical malpractice).

51. BURKE, *supra* note 12, at 3.

52. *See* Keith N. Hylton, *Litigation Costs and the Economic Theory of Tort Law*, 46 U. MIAMI L. REV. 111, 113 (1991) (explaining how the costliness of litigation can bar plaintiffs from suing).

53. Plaintiffs might be able to bypass this limitation under some circumstances, if they have some informational advantage over defendants, Lucian Arye Bebchuk, *Suing Solely to Extract a Settlement Offer*, 17 J. LEGAL STUD. 437, 448 (1988), or if their expenditure on litigation occurs in stages, Lucian Arye Bebchuk, *A New Theory Concerning the Credibility and Success of Threats to Sue*, 25 J.

ly to be obtained if (1) plaintiffs' litigation costs go up or if (2) compensation amounts go down. Unfortunately for victims of tortious conduct, recent years have seen constant trends in both these directions. Well-organized defendants are well aware of this dynamic and, through systematic efforts, are acting both to increase litigation costs for plaintiffs[54] and to limit compensation amounts.[55]

A. Rising Litigation Costs

First, consider Olivia's cost in litigating the case. In particular, why is it so expensive for Olivia (and many like her) to pursue compensation through the legal system? The answer to this question lies with the incentive of the factory, as a repeat defendant, to invest in its legal defense. Generally, the more the defendant invests in its defense, the costlier it becomes for Olivia to win her case. (The well-invested defendant can appeal decisions, submit multiple motions, etc.) Assume, for instance, that the factory invests $8,000 in a stubborn legal defense, and that is the reason Olivia's litigation costs are now prohibitively high at $7,000.[56] Of course, this situation hinges on the factory's willingness to invest the $8,000 on such legal extravagance. In theory, this form of "stubborn defense" would not be worthwhile for the factory because it would cost the factory more than its potential liability of $6,000. Therefore, the factory should be better off just compensating Olivia instead of overinvesting in litigating the case. However, this calculus changes if we consider the position of the factory as a repeat litigant. If the factory invests in a stubborn defense, making a suit unprofitable for Olivia, it signals to other potential plaintiffs that litigation against the factory is not worthwhile. Considering the great number of suits a repeat defendant, like an insurance company, expects to face, its establishing such a reputation is crucially profitable, justifying immense investment in the defense of those few cases that do end up being litigated.[57]

For exactly this reason, repeat defendants actively invest to increase plaintiffs' litigation costs. As a common practice, commercial defendants employ a variety of tactics designed to drag out trials and increase the cost

LEGAL STUD. 1, 5–9 (1996); *see also* Joseph A. Grundfest & Peter H. Huang, *The Unexpected Value of Litigation: A Real Options Perspective*, 58 STAN. L. REV. 1267, 1299–1315 (2006) (demonstrating that negative-value suits might have some value for plaintiffs if the legal regime is structured specifically to support this goal).

54. *See infra* notes 57–59 and accompanying text.

55. *See infra* notes 66–68 and accompanying text.

56. *See* Galanter, *supra* note 10 (showing that well-to-do litigants are able to achieve favorable outcomes in court).

57. *See id.* at 98–99.

of litigation.[58] As defendants advance these tactics further, this directly decreases the incentive of prospective plaintiffs to sue for compensation.

Another reason that the factory will be willing to invest to increase Olivia's litigation costs relates to economy of scale.[59] In reality, it may well be that the factory would only have to invest modestly to make Olivia's suit prohibitively costly for her. For instance, to increase Olivia's litigation costs to $7,000, the factory may only need to invest $2,000 itself. The reason for this is that the factory, as a repeat litigant, has much better access to legal services.[60] For instance, to initiate legal action, Olivia would have to gather information about possible attorneys and meet with them and negotiate the terms of their engagement. The factory, on the other hand, probably employs attorneys in house or has a standing arrangement with a large law firm. Therefore, the factory, as a repeat defendant, does not bear these search costs per case. If Olivia does find an attorney, she will typically be billed on a fixed hourly basis;[61] the factory, on the other hand, most likely pays for legal services on a more lenient retainer fee basis.[62] More generally, volume in litigation, as in many other contexts, translates into a cost advantage.[63] As repeat defendants engage routinely in similar legal procedures, they can use the same legal templates and procedures (letters, briefs, legal research, expert opinions) in multiple cases. As a result, the marginal cost of handling each individual case will steadily decline.[64] Private plaintiffs do not enjoy all these advantages. For the foregoing reasons, the factory has both the ability and the incentive to invest to increase Olivia's litigation costs.

B. Declining Compensation Amounts

As previously mentioned, plaintiffs' incentive to sue for compensation decreases not only as litigation costs rise but also as compensation amounts decline. For instance, assume that Olivia's litigation costs were "only" $5,000; in this case, she would sue the factory for an expected profit of $1,000 (compensation of $6,000 minus litigation costs of $5,000). This re-

58. *See* McClellan, *supra* note 9, at 510–11 (studying litigation tactics by repeat defendants designed to drag plaintiffs into a long and costly litigation process); *cf.* AM. BAR ASS'N, PERCEPTIONS OF THE U.S. JUSTICE SYSTEM 58 (1999) (explaining that 90% of survey respondents "strongly feel that . . . companies often wear down their opponents by dragging out the legal proceedings").

59. An economy of scale exists when the average total cost of production declines with each additional unit. N. GREGORY MANKIW, PRINCIPLES OF MICROECONOMICS 272 (6th ed. 2009).

60. *See* Galanter, *supra* note 10, at 98 (noting the economy-of-scale advantage of repeat defendants).

61. *See* Parchomovsky & Stein, *supra* note 35, at 1344.

62. *See id.*

63. *See id.* at 1344–45.

64. *Id.* at 1318, 1344.

sult changes, however, if compensation amounts are limited. Thus, assume Olivia is entitled to compensation only for pecuniary harms ($3,000 for bodily injury and $1,000 for damage to property), while nonpecuniary harms ($2,000 for emotional distress) are not compensated. Under such circumstances, the suit will constitute a loss of $1,000 for Olivia ($4,000 minus $5,000 in litigation costs), so she will most likely choose not to sue.

This circumstance is highly typical, as compensation amounts are constantly being limited as part of a broader political agenda of tort reform. These reforms aim to cap money damages as means of curbing a perceived overdeterrent effect of litigation.[65] The stated goals of this tort reform are to defend crucial industries from excessive liability and to rein in the "out-of-control" tort system.[66] Of course, this is a controversial political agenda.[67] Tort reform is supported by big business, repeat defendants who lobby legislators to limit compensation amounts with damage caps.[68] On the other hand, consumer and employee representatives lobby against these reform efforts, arguing that tort liability is not "excessive"[69]—quite the opposite: tort law is undercompensatory.[70] Similarly, various courts have held damage caps unconstitutional, mostly because of concerns of their limiting ef-

65. *See, e.g.*, Michael P. Allen, *A Survey and Some Commentary on Federal "Tort Reform,"* 39 AKRON L. REV. 909, 910 (2006) ("[A]rguments about tort reform are really arguments about restricting tort recoveries in one form or another."); Geoff Boehm, *Debunking Medical Malpractice Myths: Unraveling the False Premises Behind "Tort Reform,"* 5 YALE J. HEALTH POL'Y L. & ETHICS 357, 357–58 (2005) (explaining tort reform as an attempt to limit victims' rights through caps on damages); Rachel M. Janutis, *The Struggle Over Tort Reform and the Overlooked Legacy of the Progressives*, 39 AKRON L. REV. 943, 944 (2006) (explaining that tort reformers seek to "limit[] the availability of relief and the amount of relief in personal injury actions"); David M. Studdert et al., *Defensive Medicine Among High-Risk Specialist Physicians in a Volatile Malpractice Environment*, 293 JAMA 2609 (2005) (surveying how often physicians practice "defensive medicine" due to the threat of malpractice liability).

66. *See* Hubbard, *supra* note 17, at 469–71.

67. *See generally* Carl T. Bogus, *Introduction: Genuine Tort Reform*, 13 ROGER WILLIAMS U. L. REV. 1, 1–5 (2008) (tracking the history of the tort reform movement and noting the specific political meaning of the term); Janutis, *supra* note 65. More recently, reformers have started searching for creative ways to promote tort reform despite political opposition. *See, e.g.*, Yonathan A. Arbel & Yotam Kaplan, *Tort Reform Through the Back Door: A Critique of Law and Apologies*, 90 S. CAL. L. REV. 1199, 1199, 1211–14 (2017) (showing that commercial interests use the "'apology law' reform" to promote tort reform under a more amicable guise).

68. For more on the political context of tort reform, see Hubbard, *supra* note 17, at 470–75 (describing the political alliance between tort reformers and the U.S. Chambers of Commerce and the role of the American Tort Reform Association); Janutis, *supra* note 65, at 944–45; Paul H. Rubin, *Public Choice and Tort Reform*, 124 PUBLIC CHOICE 223, 229–31 (2005); Todd J. Zywicki, *Public Choice and Tort Reform* (George Mason Univ. Sch. of Law, Law & Econ. Working Paper No. 00-36, 2000), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=244658 (studying the role of lawyers as advocates for and against the expansion of tort liability).

69. *See* Arbel & Kaplan, *supra* note 67, at 1210–11; Hubbard, *supra* note 17, at 480.

70. *See, e.g.*, Abel, *supra* note 50, at 448–52; Myungho Paik et al., *Will Tort Reform Bend the Cost Curve? Evidence from Texas*, 9 J. EMPIR. LEGAL STUD. 173, 176–81, 209–11 (2012) (reviewing the literature and conducting an empirical analysis of the effect on costs).

fect on citizens' due process right to a trial by jury.[71] Yet, despite opposition, tort reform has made significant gains. Currently, twenty-one states have already adopted caps on noneconomic damages, while twenty-two have caps on total compensation.[72]

The debate over tort reform and the desirability of compensation is now more urgent than ever following President Trump's proposal to expand tort reform aggressively into the federal level. The President's 2018 health care budget proposal insists not only on repealing Obamacare and slashing Medicaid but also on capping compensation for severely injured tort victims.[73] If implemented, these new caps will decrease compensation amounts even more, further diminishing prospective plaintiffs' incentive to sue.[74]

C. Growing Wealth Gaps

The decline of compensation has been aggravated by widening wealth gaps between private plaintiffs and corporate defendants. The ratio of the income of an average CEO to that of an average employee illustrates this point. In the United States, this ratio increased from 20:1 in 1965 to 354:1 in 2012.[75] Quite evidently, this indicates that a private plaintiff is no match for a corporate defendant in a civil litigation.[76] The discrepancy in resources is too great.[77] Additionally, as private individuals grow poorer relative to corporate tortfeasors, they become less likely to receive high

71. *See* J. Chase Bryan et al., *Are Non-Economic Caps Constitutional?*, 80 DEF. COUNS. J. 154 (2015) (reviewing the judicial battle over the constitutionality of non-economic damage caps).

72. Ronen Avraham, Database of State Tort Law Reform Clever (5.1), THE UNIV. OF TEX. AT AUSTIN SCH. OF LAW, https://law.utexas.edu/faculty/ravraham/dstlr.php (last visited Oct. 15, 2018).

73. OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, MAJOR SAVINGS AND REFORMS: BUDGET OF THE U.S. GOVERNMENT: FISCAL YEAR 2018, at 114 (2017), https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/budget/fy2018/msar.pdf.

74. Compensation is also being blocked by the extensive use of arbitration clauses by potential repeat defendants. In a parallel move to the tort reform efforts, big businesses have successfully established an impressive ability to avoid compensating individual plaintiffs by mandating the use of private decision-making in lieu of adjudication. *See* Resnik, *supra* note 45.

75. Deborah Hargreaves, *Can We Close the Pay Gap?*, N.Y. TIMES: OPINIONATOR (Mar. 29, 2014, 2:30 PM), http://opinionator.blogs.nytimes.com/2014/03/29/can-we-close-the-pay-gap?.

76. *See* ALBERT H. CANTRIL, AM. BAR ASS'N, AGENDA FOR ACCESS: THE AMERICAN PEOPLE AND CIVIL JUSTICE 19–20 (1996); *see also* AM. BAR ASS'N, CONSORTIUM ON LEGAL SERVICES AND THE PUBLIC, LEGAL NEEDS AND CIVIL JUSTICE: A SURVEY OF AMERICANS (1994); ROY W. REESE & CAROLYN A. ELDRED, AM. BAR ASS'N, LEGAL NEEDS AMONG LOW-INCOME AND MODERATE-INCOME HOUSEHOLDS: SUMMARY OF FINDINGS FOR THE COMPREHENSIVE LEGAL NEEDS STUDY (1995).

77. *See* Rhode, *supra* note 36, at 1785–86; Robert J. Rhudy, *Comparing Legal Services to the Poor in the United States with Other Western Countries: Some Preliminary Lessons*, 5 MD. J. CONTEMP. LEGAL ISSUES 223, 237 (1994).

economic damages.[78] Again, as compensation amounts decline, it becomes more likely that compensation amounts are actually lower than an individual plaintiff's litigation costs.[79] Wealth inequality in the United States today is at historic highs,[80] with the top 1% of Americans holding nearly 50% of the wealth, the top 20% of households in the United States owning 84% of the wealth, and the bottom 40% owning only 0.3%.[81] At the same time, national spending on legal aid has been cut by a third over the last three decades.[82] In addition, the poor are generally not entitled to legal assistance in civil cases.[83] The aggregate result of these developments is that a private plaintiff's chance to secure a compensatory payment from a commercial defendant is negligible,[84] as "millions of Americans are locked out of [legal recourse] entirely."[85]

For all these reasons, compensation of victims, although a central principle of our legal system, is largely a phantom. As plaintiffs' litigation costs go up and compensation amounts go down, the ability of individuals to compete in the legal arena with corporations all but disappears, and compensation of victims becomes a distant dream instead of legal reality.

II. CURRENT THEORY: WHEN ECONOMICS & MORALITY CLASH

The compensation crisis is not the result of coincidence but rather a deliberate effort backed by strong theoretical arguments. This Part provides a

78. For the same reasons, lawyers will not want to take the cases of poor plaintiffs. *See* Catherine M. Sharkey, *Unintended Consequences of Medical Malpractice Damages Caps*, 80 N.Y.U. L. REV. 391, 489–90 (2005).

79. *Cf.* Philip L. Bartlett II, *Disparate Treatment: How Income Can Affect the Level of Employer Compliance with Employment Statutes*, 5 N.Y.U. J. LEGIS. & PUB. POL'Y 419, 430–31 (2002) (explaining that "[f]or a lawsuit to be worthwhile, the cost of litigation must be less than the expected recovery").

80. THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY 24 fig.1.1 (Arthur Goldhammer trans., Belknap Press of Harvard Univ. Press 2014) (2013).

81. Edward N. Wolff, *Household Wealth Trends in the United States, 1962 to 2016: Has Middle Class Wealth Recovered?* 44 tbl.2 (Nat'l Bureau of Econ. Research, Working Paper No. 24085, 2017), http://www.nber.org/papers/w24085.pdf; *see also* LISA A. KEISTER, WEALTH IN AMERICA (2000); EDWARD N. WOLFF, TOP HEAVY: THE INCREASING INEQUALITY OF WEALTH IN AMERICA AND WHAT CAN BE DONE ABOUT IT (2002); James B. Davies, Susanna Sandström, Anthony Shorrocks & Edward Wolff, *The Global Pattern of Household Wealth*, 21 J. INT'L DEV. 1111 (2009).

82. *See* DEBORAH L. RHODE, ACCESS TO JUSTICE 3 (2004).

83. *See id.* at 9; Earl Johnson, Jr., *Toward Equal Justice: Where the United States Stands Two Decades Later*, 5 MD. J. CONTEMP. LEGAL ISSUES 199, 201 (1994); *cf.* Richard L. Abel, *Law Without Politics: Legal Aid Under Advanced Capitalism*, 32 UCLA L. REV. 474, 475 (1985) (reviewing the rise and fall of civil legal aid).

84. *See* Alan W. Houseman, *Civil Legal Assistance for the Twenty-First Century: Achieving Equal Justice for All*, 17 YALE L. & POL'Y REV. 369, 402 (1998) (explaining that the legal services system serves no more than 20% of the needs of the population it is meant to serve).

85. RHODE, *supra* note 82, at 13; *see also* David C. Leven, *Justice for the Forgotten and Despised*, 16 TOURO L. REV. 1, 6–7 (1999) (explaining how the prison population lacks meaningful access to the justice system).

short review of this theoretical background and a summary of the prevailing economic argument against compensation.

Contemporary tort theory is divided between philosophic and economic schools of thought.[86] While philosophic theories recognize compensation as a necessary element of the tort system,[87] economic theories see no difficulty or injustice in the decline of compensation.[88] In fact, economic theory presents a forceful attack against the principle of compensation.[89] And, importantly, while philosophic theories provide a compelling account of the internal structure of tort law, economic theories—which disfavor compensation—dominate the policy debate.[90]

A. Economic Deterrence Theory

Contemporary economic theory of tort law focuses on efficient deterrence as the primary goal of the liability system.[91] Creating systems of deterrence has long been recognized as one of the central roles of the legal system generally.[92] During the second half of the 20th century, scholars

86. On the gap between functionalist and deontological theories in private law, see John C.P. Goldberg & Benjamin C. Zipursky, *Seeing Tort Law from the Internal Point of View: Holmes and Hart on Legal Duties*, 75 FORDHAM L. REV. 1563, 1563 (2006) ("[T]he most familiar divide today is that between the law-and-economics camp that focuses on efficient deterrence, and the philosophical camp that tends to focus on corrective justice."); Scott Hershovitz, *Harry Potter and the Trouble with Tort Theory*, 63 STAN. L. REV. 67, 68 (2011).

87. *See* John C.P. Goldberg & Benjamin C. Zipursky, *Torts as Wrongs*, 88 TEX. L. REV. 917, 918–19 (2010).

88. *See infra* notes 111–14 and accompanying text.

89. *See infra* note 132 and accompanying text.

90. *See infra* notes 146–54 and accompanying text.

91. In the existing economic model of liability, the focus is on deterrence as a primary policy goal. *See* Howard A. Latin, *Problem-Solving Behavior and Theories of Tort Liability*, 73 CALIF. L. REV. 677, 677 (1985) ("The most influential mode of torts analysis in recent decades has treated liability as a mechanism for social engineering in the sense that accident losses should be allocated to particular parties in order to induce efficient cost-minimizing behavior by similarly situated actors."); A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 HARV. L. REV. 869, 873 (1998) ("[T]o achieve appropriate deterrence, injurers should be made to pay for the harm their conduct generates . . . ."); Gary T. Schwartz, *Reality in the Economic Analysis of Tort Law: Does Tort Law Really Deter?*, 42 UCLA L. REV. 377, 378 (1994) ("Ever since the 1970s, the modern movement in economic analysis has been in full swing. That analysis has highlighted the deterrence function of tort law. Indeed, even in the works of mainstream scholars, deterrence has now assumed the role of a primary rationale for tort liability rules." (footnote omitted)). Shavell and David Rosenberg describe the function of litigation as its deterrent effect on the behavior of potential defendants. David Rosenberg & Steven Shavell, *A Simple Proposal to Halve Litigation Costs*, 91 VA. L. REV. 1721, 1721 (2005); *see also* STEVEN SHAVELL, FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW 391 (2004).

92. WILLIAM M. LANDES & RICHARD A. POSNER, THE ECONOMIC STRUCTURE OF TORT LAW 4 (1987) (reviewing the long history of deterrence as a primary goal of the legal system). Deterrence is also central to economic analysis quite generally, beyond the context of the compensation system. *See* WERNER Z. HIRSCH, LAW AND ECONOMICS: AN INTRODUCTORY ANALYSIS 1 (2d ed. 1988) ("[L]aws are authoritative directives that impose costs and benefits on participants in a transaction and in the process alter incentives."); THOMAS J. MICELI, THE ECONOMIC APPROACH TO LAW 1 (2004) ("The economic approach to law assumes that rational individuals view legal sanctions (monetary damages,

employed the analytical tools of microeconomics to develop deterrence theory into a comprehensive account of tort law. Prominent figures in this strand of scholarship include John Brown,[93] Guido Calabresi,[94] Ronald Coase,[95] Robert Cooter,[96] Mark Grady,[97] William Landes,[98] Richard Posner,[99] and Steven Shavell.[100]

The starting point for economic-deterrence theory is the assumption that actors operate to maximize their own wealth, while possibly neglecting to consider the well-being of others.[101] Thusly, in *Example 1* above, the factory may be indifferent to the $6,000 loss it is causing Olivia. Such loss is therefore termed a *negative externality*:[102] a harmful effect created by the economic operations of the injurer factory but borne by others.[103] If the factory is not held liable for its actions, the losses it causes are *external*, and the factory will therefore have insufficient incentive to invest in precau-

prison) as implicit prices for certain kinds of behavior, and that these prices can be set to guide these behaviors in a socially desirable direction."); Steven Shavell, *Law Versus Morality as Regulators of Conduct*, 4 AM. L. & ECON. REV. 227, 227 (2002) ("It is evident that both law and morality serve to channel our behavior. Law accomplishes this primarily through the threat of sanctions if we disobey legal rules.").

93. *See* John Prather Brown, *Toward an Economic Theory of Liability*, 2 J. LEGAL STUD. 323 (1973) (introducing the first formal economic model of tort liability).

94. *See* CALABRESI, *supra* note 20 (presenting the analytical framework of the cheapest cost avoider).

95. Coase made seminal contributions to the study of reciprocal causation, fundamental to the economic analysis of tort law. *See* Coase, *supra* note 19, at 2.

96. *See* Cooter, *supra* note 16, at 1–2 (expanding the basic principles of the economic analysis of tort law to study all areas of private law).

97. *See* Mark F. Grady, *A New Positive Economic Theory of Negligence*, 92 YALE L.J. 799 (1983) (adding uncertainty to the basic negligence model).

98. *See* William M. Landes & Richard A. Posner, *The Positive Economic Theory of Tort Law*, 15 GA. L. REV. 851, 854 (1981).

99. *See* LANDES & POSNER, *supra* note 92; Posner, *supra* note 14, at 32 (offering the famous "Hand formula," which states that the injurer has breached her duty of care if the burden of adequate precautions was lower than the expected loss (PL > B)). For a critique of Posner, and a more traditional legal approach to negligence, see Richard W. Wright, *Hand, Posner, and the Myth of the "Hand Formula,"* 4 THEORETICAL INQ. L. 145 (2003).

100. *See* Steven M. Shavell, *On Liability and Insurance*, 13 BELL J. ECON. 120 (1982) (expending the existing economic model to study its relation to liability insurance).

101. This is one of the standard assumptions of institutional economics. *See* WILLIAMSON, *supra* note 28, at 47; Oliver E. Williamson, *Transaction Cost Economics and Organization Theory*, 2 INDUS. & CORP. CHANGE 107, 114–16 (1993).

102. An externality is the effect by the action of one party on the well-being of another. SHAVELL, *supra* note 91, at 77. According to Coase, the term was first used by Samuelson. R.H. COASE, THE FIRM, THE MARKET, AND THE LAW 23 (1988). Coase suggests that the term is inaccurate, as it implies causation to be unidirectional, from an injurer to a victim, thus oversimplifying the problem and the reciprocal nature of causation. *See id.* at 23–26.

103. Contemporary economic theory of liability is heavily influenced by the study of the problem of externalities. *See, e.g.*, Coase, *supra* note 19, at 13 (discussing the problem of reciprocal causation); Landes & Posner, *supra* note 98, at 853–55 (surveying contemporary scholarship on the economic theory of liability).

tions.[104] To incentivize the factory to invest appropriately, it may be necessary to penalize it—to force it to *internalize* the negative externality.[105]

One way to penalize the factory—to internalize the negative externality—would be to obligate the factory to compensate Olivia for the harm.[106] However, compensation is not a necessary element of deterrence, and under current economic theory, deterrence is the ultimate normative goal. To create deterrence, *any* sanction against the factory should suffice, even if *not* coupled with compensation for Olivia.[107] Injurers would be equally deterred by a regulatory fine paid to the government as by civil compensation paid to victims through the legal system.[108] From a pure economic perspective, and ignoring notions of morality or justice, it should not matter whether the injurer pays the government, the victim,[109] or some other party.[110]

This means that, under economic-deterrence theory, compensation of victims is not an independent goal of the tort system.[111] In this view, compensation is only justified if it serves to appropriately deter the injurer. Considerations relating to the victim's right for compensation are of secondary importance at most.[112] To determine the desirability of compensation for the purposes of deterrence, economic theory offers the concept of the "cheapest cost avoider."[113] This concept, first offered by Calabresi, is the cornerstone of economic deterrence theory.[114] Under this analytical

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104. SHAVELL, *supra* note 91, at 93; *see also* Cooter, *supra* note 16, at 3–4.

105. *See* SHAVELL, *supra* note 91, at 101–09, 177.

106. *See* Posner, *supra* note 14, at 32.

107. *See, e.g.*, A. Mitchell Polinsky & Yeon-Koo Che, *Decoupling Liability: Optimal Incentives for Care and Litigation*, 22 RAND J. ECON. 562 (1991). For similar arguments in the context of contract law, see Robert Cooter & Ariel Porat, *Anti-Insurance*, 31 J. LEGAL STUD. 203 (2002).

108. *See* Goldberg, *supra* note 15, at 554 ("All conduct that threatens losses greater than the cost of precaution ought in principle to be deterred. Yet the deterrence machinery of the tort system kicks in only if a private victim chooses to sue. The goal of efficient deterrence might therefore be equally or better served by a system of regulatory fines. In fact, given empirical evidence suggesting that the vast majority of those with valid tort claims never bother to sue, such a system is likely preferable.").

109. *See* James J. Heckman, *The Intellectual Roots of the Law and Economics Movement*, 15 LAW & HIST. REV. 327, 328–29 (1997).

110. *See* Ehud Guttel, Alon Harel & Shay Lavie, *Torts for Non-Victims: The Case for Third-Party Litigation*, 39 U. ILL. L. REV. (forthcoming 2018) (suggesting deterrence might be improved if third parties, rather than victims of harm, are given the right to sue injurers).

111. *See* Goldberg, *supra* note 15, at 544.

112. *See id.*

113. CALABRESI, *supra* note 20, at 244.

114. Discussing Calabresi's *The Cost of Accidents*, Keith Hylton writes: "The book has had an enormous influence on the field. It would not be an exaggeration to say that modern law and economics, as we see it practiced today, had its start with Gary Becker's article on crime and Guido Calabresi's book, both products of the late 1960s." Keith N. Hylton, *Calabresi and the Intellectual History of Law and Economics*, 64 MD. L. REV. 85, 85 (2005) (footnote omitted). Calabresi's work is closely related to the problem of reciprocal causation presented by Coase. Coase's paper, *The Problem of Social Cost*, is still the most cited law review article. Fred R. Shapiro & Michelle Pearse, *The Most Cited Law Review Articles of All Time*, 110 MICH. L. REV. 1483, 1489 (2012).

framework, compensation should be granted only if the injurer is the cheapest cost avoider, that is, the party most cheaply able to prevent the harm.[115] Obligating injurers who are cheapest cost avoiders to compensate victims will assure minimization of the costs of accidents and of the costs of precautions designed to prevent accidents.[116]

This conceptualization has far-reaching implications for the way economic theories treat the problem of access to compensation. In particular, improving victims' access to compensation will not necessarily be advantageous because injurers are not always the cheapest cost avoiders. This would mean that the compensation crisis described in Part I may not be a problem at all, and definitely not one that urgently needs a solution. To see the economic argument in more detail, consider *Example 2* below, further developing the stylized example presented in the Introduction to this Article.[117]

- *Example 2*: Emma owns a farm and grows wheat for a living. Neighboring Emma's farm is a large ranch. Cattle from the ranch occasionally wander into Emma's farm, trampling crops and causing damage to property there. The expected harm from such occurrences is estimated at $5,000. The harm to Emma's farm can be prevented if Emma invests $1,000 in fencing her farm, or if the rancher invests $1,500 in fencing the ranch. If harm does occur, Emma will have to invest $6,000 in order to sue the rancher.

First, note that the suit is prohibitively costly for Emma: Emma can expect compensation of $5,000 but must incur a cost of $6,000 in order to litigate the case. Now, from an economic perspective, is this barrier to compensation even a disadvantage? In other words, is it important that we work to lower Emma's litigation costs so that she can sue the rancher?

Economists answer this question with a clear no. In the example, Emma is the cheapest cost avoider and can prevent the harm at a cost of $1,000, while the rancher can prevent it at a higher cost of $1,500. Since Emma cannot profitably sue, compensation is not available, and Emma will invest $1,000 in precautions to prevent the harm. From an economic perspective, this is the optimal result, and there is no need to address Emma's inability to secure compensation. Since Emma is the cheapest cost avoider, economic theory actually *requires* that she bear the harm and *not* be compensated.[118] In this view, the fact that the rancher's cattle encroached on

115. *See* CALABRESI, *supra* note 20, at 135–40.

116. *See id.*

117. *See* Coase, *supra* note 19, at 2–6.

118. *See* CALABRESI, *supra* note 20, at 135; Coase, *supra* note 19, at 2–6; Cooter, *supra* note 16, at 3–4.

Emma's land and harmed her property is almost immaterial and does not independently justify compensation.[119]

Consider now the possibility that we somehow manage to lower Emma's litigation costs to a reasonable $500, so that Emma no longer finds it prohibitively costly to sue the rancher after harm has occurred. Supposedly, from an access-to-compensation perspective, that would be a positive change—not so under the economic view. If we do enable Emma to profitably sue the rancher, all this can achieve is to allow Emma to secure $5,000 in compensation for her harms, which, according to economic deterrence theory, is undesirable.[120] If Emma can expect to receive this compensation, she will have less reason to invest $1,000 in erecting a fence. Instead, the rancher will be the one investing in precautions. Rather than face liability of $5,000 when harm occurs, the rancher will prefer to invest $1,500 in precautions and prevent the harm. Because the rancher is *not* the cheapest cost avoider—the harm can be more cheaply prevented by Emma at a cost of $1,000—this is an inefficient result.

In the above example, improving access to compensation actually worsened the situation. From the perspective of overall efficiency, allowing compensation would *generate* a problem here rather than solve one. Absent compensation, Emma, the cheapest cost avoider, would invest $1,000 in preventing the harm. This is the optimal result. If Emma is allowed better access to compensation, this would actually make things worse because the harm will now be prevented at a higher cost of $1,500 by the rancher. Since the rancher is not the cheapest cost avoider, improving Emma's access to legal compensation is economically inefficient.[121]

Example 2 demonstrates a fundamental truth: there is no general economic justification for improving access to compensation.[122] Therefore,

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119. For a review and discussion of possible critiques of this result, see Smith, *supra* note 25, at 71–73.

120. *See* CALABRESI, *supra* note 20, at 135–40; Shavell, *supra* note 16, at 579, 582–83.

121. The more general point is, of course, that if victims are compensated for harms, they will have no incentive to invest in preventing them. *See* Coase, *supra* note 19, at 2–6; Cooter, *supra* note 16, at 3–4.

122. This view is highly critical of existing doctrine and greatly differs from the earlier teaching of the economic analysis of tort law. Historically, law and economics drew much of its normative force from justifying existing doctrine as efficient. Early lawyer–economists knew that, in order to convince legal thinkers of the significance of efficiency to legal analysis, it would be helpful to demonstrate that the law already employs this notion. *See* RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 315–16, 713–16 (8th ed. 2011); Isaac Ehrlich & Richard A. Posner, *An Economic Analysis of Legal Rulemaking*, 3 J. LEGAL STUD. 257 (1974); George L. Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977); Paul H. Rubin, *Why Is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977). Legal thinkers are accustomed to searching for the normative principles guiding existing rules and to thinking of legal principles as normatively compelling. *See generally, e.g.*, RONALD DWORKIN, LAW'S EMPIRE (1986). Once law and economics was recognized as a legitimate form of legal argument, the attempt to explain the law based on efficiency was largely abandoned in favor of efforts to criticize and reform. *See, e.g.*, Jules Coleman, *The Normative Basis of Economic Analysis: A Critical Review of Richard Posner's* The Economics of Justice, 34 STAN. L. REV. 1105

under this view, the compensation crisis is no crisis at all. While it is true that victims are often left with no compensation for their harm, under the economic view, this is not an undesirable result. In fact, even if we are somehow able to reverse this trend, the result may actually *harm* total social welfare. This general theoretical framework is used to great effect in the campaign against compensation.[123] The core argument is that improving access to compensation is not a viable social goal in itself because compensation can be harmful just as much as it can be beneficial.[124] Since compensation is not required to deter injurers, and more often than not it also distorts the incentives of victims, there is little reason to crusade for the restoration of plaintiffs' ability to sue for compensation.[125] In fact, it might be appropriate to act to limit compensation even further.[126]

The force of the argument against compensation lies in its simplicity and general applicability. Economists use it to question the overall desirability of improving plaintiffs' access to compensation.[127] A series of works by Shavell developed the ultimate version of this argument.[128] Shavell offers a formal model in the spirit of the argument outlined above[129] and seeks to show that there is no reason to suppose that improving plaintiffs' access to compensation is generally desirable.[130] This argument has

(1982) (book review); Hylton, *supra* note 114; Francesco Parisi, *Positive, Normative and Functional Schools in Law and Economics*, 18 EUR. J.L. & ECON. 259 (2004).

123. Based on economic theory, tort reformers argue that "(1) injured persons should be required to have primary responsibility for making decisions about risk, for avoiding injury to themselves, and for insuring against that injury; (2) plaintiffs should not recover damages unless they have satisfied their responsibility to protect themselves and unless the plaintiff has clearly shown that the defendant's conduct caused the injury." Hubbard, *supra* note 17, at 473; *see also* Studdert et al., *supra* note 65, at 2617.

124. *See* Shavell, *supra* note 16, at 579, 586–88, 592. Shavell writes: "For example, a poor victim of an automobile accident might have a strong incentive to bring suit because of the amount of damages he could collect. In this situation, the contingency fee system furnishes lawyers with a financial reason to take the victim's case even though he might not be able to afford to pay legal fees in advance. Moreover, because such a suit might have a low social benefit, as I suggested, were the help of legal aid needed to bring the suit, it is hardly clear that the suit would be socially advantageous." *Id.* at 592.

125. *See* Hubbard, *supra* note 17, at 473–75.

126. *See* Shavell, *supra* note 16, at 579, 582–83.

127. *See id.* at 579, 592.

128. Shavell, *supra* note 16; Steven Shavell, *The Level of Litigation: Private Versus Social Optimality of Suit and of Settlement*, 19 INT'L REV. L. & ECON. 99 (1999); Steven Shavell, *The Social Versus the Private Incentive to Bring Suit in a Costly Legal System*, 11 J. LEGAL STUD. 333 (1982) [hereinafter Shavell, *Costly Legal System*].

129. Shavell, *Costly Legal System*, *supra* note 128, at 333–36.

130. *See* Shavell, *supra* note 16, at 579, 582–83, 592 (showing that the social benefit from compensating victims does not bear a necessary connection to the private benefit for victims). Therefore, improving access to compensation is not necessarily socially desirable. This claim explicitly goes against a rich literature advocating access to justice and supporting legal aid initiatives. *See id.*

achieved consensus in the economic analysis literature[131] and formulates a strong attack against the general idea of compensation for victims.[132]

B. Moral Tort Theory

Tort law scholarship offers a family of closely related moral-based theories. Such theories seek to explain tort law based on notions of justice and deontological right. Naturally, these offer an entirely different view on compensation. The basic premise of deontological right theories is that legal actors owe a duty not to cause certain types of harms to others.[133] For instance, one must not knowingly damage another's property. When such a duty is breached, the law intervenes by obligating transgressors to repair the resulting losses.[134] Under this view, tort law both delineates the primary duties actors owe one another and provides the legal mechanism by which the secondary duty to repair is enforced.[135] Therefore, the victim's right to compensation is fundamental to any morality-based theory of tort law.

The chief branch of deontological right theories focuses on corrective justice as the basic principle of tort law. Leading contributors in this branch of the literature include Ernest Weinrib,[136] Jules Coleman,[137] Stephen Per-

131. *See* Louis Kaplow, *Private Versus Social Costs in Bringing Suit*, 15 J. LEGAL STUD. 371, 371–72 (1986) (finding further support for Shavell's argument); *see also* Peter S. Menell, *A Note on Private Versus Social Incentives to Sue in a Costly Legal System*, 12 J. LEGAL STUD. 41 (1983) (offering exceptions to the general rule suggested by Shavell); Susan Rose-Ackerman & Mark Geistfeld, *The Divergence Between Social and Private Incentives to Sue: A Comment on Shavell, Menell, and Kaplow*, 16 J. LEGAL. STUD. 483 (1987) (integrating the models offered by Shavell, Kaplow, and Menell).

132. *See* SHAVELL, *supra* note 91, at 269 ("[T]he question of the net social desirability of the liability system is a serious one."). The debate over products liability is perhaps the clearest manifestation of the economic anticompensation argument. *See, e.g.*, Carl T. Bogus, *War on the Common Law: The Struggle at the Center of Products Liability*, 60 MO. L. REV. 1, 5 (1995) ("The literature overflows with criticism, and anyone perusing the law reviews in recent years might well come away believing that the predominant view is that products liability has been a disaster."); Keith N. Hylton, *The Law and Economics of Products Liability*, 88 NOTRE DAME L. REV. 2457, 2457–58 (2013) ("[P]roducts liability law has come in for some unusually harsh criticism in the law and economics literature of late, and much of the treatment of this area by economically-oriented legal scholars has been negative for at least a generation. . . . [Much] law and economics literature suggest[s] that products liability law is one big mistake, and perhaps should be abolished . . . ." (footnotes omitted)).

133. *See* John C.P. Goldberg, *Rights and Wrongs*, 97 MICH. L. REV. 1828, 1828–29 (1999) (reviewing ARTHUR RIPSTEIN, EQUALITY, RESPONSIBILITY, AND THE LAW (1999)).

134. *See id.*

135. *See* Jules L. Coleman, *Second Thoughts and Other First Impressions*, *in* ANALYZING LAW: NEW ESSAYS IN LEGAL THEORY 257, 302 (Brian Bix ed., 1998).

136. *See* ERNEST J. WEINRIB, THE IDEA OF PRIVATE LAW 134–36 (1995) (presenting tort law as a core case of corrective justice within the realm of private law).

137. *See* JULES L. COLEMAN, RISKS AND WRONGS (1992); Jules L. Coleman, *The Structure of Tort Law*, 97 YALE L.J. 1233, 1241 (1988) (reviewing LANDES & POSNER, *supra* note 92, and STEVEN SHAVELL, ECONOMIC ANALYSIS OF ACCIDENT LAW (1987)) (arguing that corrective justice theory best explains the bipolar structure of the tort system).

ry,[138] and Arthur Ripstein.[139] Under corrective justice theory, tort law restores the position of the plaintiff to the *status quo ante*. Under this paradigm, tort law is understood as restoring an equilibrium disturbed by the defendant's wrongful violation of the plaintiff's right.[140] In particular, the law restores the equilibrium by ordering the defendant to transfer the full value of the loss to the plaintiff.[141] This means that, under corrective justice theory, compensation of victims is a central element of private law;[142] compensation corrects wrongs and brings victims as close as possible to their original position.[143] Under this view, unlike the pure economic perspective, compensation of victims is an independent goal of tort law, not just a methodology for deterrence.

Another main branch of morality-based tort theory, promoted primarily by John Goldberg and Benjamin Zipursky, focuses on concepts of redress and civil recourse.[144] Under civil recourse theory, the quintessence of tort law lies in offering victims the power to seek redress from those who have wronged them.[145] Under this view, of course, compensation for victims is fundamental to the structure of tort law. The *raison d'être* of tort law is to enable the achievement of justice by providing opportunity for victims of a wrong to vindicate their rights.

Although morality-based theories offer unequivocal support for compensation as a general principle, their arguments seem to get lost in translation, as morality-based arguments scantly feature in the raging policy debate regarding the scope and justification for compensation.[146] This is very apparent, for instance, in the celebrated Shavell–Polinsky versus

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138. *See* Stephen R. Perry, *The Moral Foundations of Tort Law*, 77 IOWA L. REV. 449 (1992) (developing principles of reparation as the main moral foundations of tort law).

139. *See* ARTHUR RIPSTEIN, EQUALITY, RESPONSIBILITY, AND THE LAW (1999).

140. *See* Coleman, *supra* note 135, at 306.

141. The notion of corrective justice as the restoration of a normative equilibrium is traced to Aristotle. Aristotle describes corrective justice as aiming to erase a wrongful gain by a wrongdoer and a corresponding wrongful loss by a wronged victim. ARISTOTLE, *supra* note 2, bk. V at 4–5. This is achieved through a payment from the wrongdoer to the victim that simultaneously eliminates both the wrongful gain and the wrongful loss. *See id.*; Perry, *supra* note 138, at 453.

142. *See* Weinrib, *supra* note 2, at 407–08; Ernest J. Weinrib, *Corrective Justice in a Nutshell*, 52 U. TORONTO L.J. 349, 349 (2002) (explaining that corrective justice requires reparation for the wronged party). *But see* Coleman, *supra* note 2, at 464 (arguing that corrective justice provides grounds for compensation of victims but does not *require* such compensation).

143. *See* Smith, *supra* note 3, at 1730.

144. *See* John C.P. Goldberg & Benjamin C. Zipursky, *Civil Recourse Revisited*, 39 FLA. ST. U. L. REV. 341 (2011) (highlighting the differences between civil recourse theory and corrective justice theory); Goldberg & Zipursky, *supra* note 87 (arguing for a unified theory of tort law as the law of wrongs and recourse); *see also* JOHN C.P. GOLDBERG, ANTHONY J. SEBOK & BENJAMIN C. ZIPURSKY, TORT LAW: RESPONSIBILITIES AND REDRESS (3d ed. 2012).

145. Goldberg & Zipursky, *supra* note 87, at 918 (showing that tort law is best understood as an institutional attempt to empower victims of wrongs to seek redress from their wrongdoers).

146. *See* Hubbard, *supra* note 17, at 457–60 (discussing the dominance of instrumental arguments as the basis for the tort-reform debate).

Goldberg–Zipursky debate on products liability law.[147] From the economic side, Shavell and Polinsky offer a strong series of arguments against the mere existence of compensation for harms caused by defective products.[148] Goldberg and Zipursky, the leading figures of civil recourse theory, set out to provide a rebuttal.[149] However, Goldberg and Zipursky's main line of defense relies on functionalist or pragmatic arguments, rather than on their own moral theory of tort law.[150] This strongly demonstrates the dominance of functionalist economic arguments—and the relative weakness of philosophical morality—in the policy-making arena. Pure moral arguments simply do not seem to have the same weight as pragmatic ones and are therefore denied the center stage.

A main reason for the absence of morality-based theories from the policy debate is that these theories, for the most part, explicitly reject prescriptive aspirations.[151] Thus, corrective justice theory focuses on understanding tort law "from within" and regardless of its practical consequences.[152] For this theory's exponents, any investigation into the functions or goals of tort law is deemed "external" and misses the internal coherence of this field of law. In fact, Weinrib goes so far as to assert that any investigation into possible pragmatic advantages of the tort system amounts to a misunderstanding of tort law.[153] For the purposes of this Article, this is a serious limitation, since it denies the usefulness of moral arguments in determining policy. Consequently, corrective justice theory can only describe tort law for what it is, but it does not defend compensation as a socially useful practice.[154]

Against this theoretical background, this Article seeks to highlight the economic advantages of compensation as civil recourse. In other words, it

147. Products liability law is currently one of the frontlines of the anticompensation campaign. *See* Bogus, *supra* note 132, at 1; Hylton, *supra* note 132, at 2457.

148. A. Mitchell Polinsky & Steven Shavell, *The Uneasy Case for Product Liability*, 123 HARV. L. REV. 1437, 1491–92 (2010).

149. John C.P. Goldberg & Benjamin C. Zipursky, *The Easy Case for Products Liability Law: A Response to Professors Polinsky and Shavell*, 123 HARV. L. REV. 1919 (2010).

150. Thus, Goldberg and Zipursky discuss at length the "empirics of deterrence," *id.* at 1927, insurance aims of the liability system, *id.* at 1935, and the costs of law reform, *id.* at 1941–42.

151. *See, e.g.*, RIPSTEIN, *supra* note 139, at 20.

152. JULES L. COLEMAN, THE PRACTICE OF PRINCIPLE: IN DEFENSE OF A PRAGMATIST APPROACH TO LEGAL THEORY 14 (2001); Benjamin C. Zipursky, *Pragmatic Conceptualism*, 6 LEGAL THEORY 457, 482 (2000).

153. WEINRIB, *supra* note 136, at 3–6. Weinrib writes: "In this book, I will argue that, despite its current popularity, the functionalist understanding of private law is mistaken. Private law, I will claim, is to be grasped only from within and not as the juridical manifestation of a set of extrinsic purposes. If we must express this intelligibility in terms of purpose, the only thing to be said is that the purpose of private law is to be private law." *Id*. at 5 (emphasis omitted).

154. *See* WEINRIB, *supra* note 136, at 5–6, 14–16; John C.P. Goldberg, *Unloved: Tort in the Modern Legal Academy*, 55 VAND. L. REV. 1501, 1502 (2002) (explaining Weinrib's view of corrective justice).

seeks to translate into pragmatic language, and therefore into the heart of the policy debate, some of the moral intuitions that stand at the heart of morality-based theories of tort law, and civil recourse theory in particular. The general theme is that it is good and useful, and not just morally right, to allow victims of harm to seek redress from those who have harmed them.

III. THE MISSING PIECE: HARM-SHIFTING

The prevailing attack against the principle of compensation is based on a misconception of the law and a fundamental oversight. This Part demonstrates that, contrary to conventional economic wisdom, compensation for victims can be justified even when victims, rather than injurers, are the cheapest cost avoiders. The reason for this defect in the prevailing theory depends upon the way "cost avoidance" is conceptualized in the economic analysis of tort law.

Economic tort theory focuses on investments designed to *minimize* harms.[155] This focus is common to all major works in the field, including those of Guido Calabresi,[156] Richard Posner,[157] Mitchell Polinsky,[158] Daniel Rubinfeld,[159] Robert Cooter,[160] Louis Kaplow, and Steven Shavell.[161] In this framework, self-protection efforts by potential victims of harm are conceptualized as "precautions," or investments designed to minimize potential harms. The assumption here is that, when faced with the prospect of danger, the sole possible response by potential victims is to try to minimize

155. To minimize harms, individuals can invest in precautions but can also lower their levels of activity. *See* Steven Shavell, *Strict Liability Versus Negligence*, 9 J. LEGAL STUD. 1, 2 (1980). I refer to both as investments to minimize harms, as in both cases individuals incur a cost in order to effectuate lower levels of harm.

156. *See* CALABRESI, *supra* note 20, at 26 ("I take it as axiomatic that the principal function of accident law is to reduce the sum of the costs of accidents and the costs of avoiding accidents.").

157. Posner argues that liability is imposed when the actions of the injurer are socially harmful—that is, when the cost of preventing the harm is lower than the harm itself. Posner, *supra* note 14, at 32.

158. *See* A. Mitchell Polinsky & Daniel L. Rubinfeld, *The Welfare Implications of Costly Litigation for the Level of Liability*, 17 J. LEGAL STUD. 151, 151 (1988) ("The central concern of the economic theory of liability is how to induce an injurer to take the socially appropriate level of care—the level that minimizes the sum of the cost of taking care and the losses to victims.").

159. *See* Robert D. Cooter & Daniel L. Rubinfeld, *Economic Analysis of Legal Disputes and Their Resolution*, 27 J. ECON. LITERATURE 1067, 1069 (1989).

160. Cooter offers the "model of precaution," which focuses on "the direct cost of harm and the cost of precautions against it." Cooter, *supra* note 16, at 2. Cooter notes that compensation of victims might also be warranted, but this is only for considerations of equity that are separate from efficiency requirements. *See id.* at 1.

161. *See* Louis Kaplow & Steven Shavell, *Economic Analysis of Law*, *in* 3 HANDBOOK OF PUBLIC ECONOMICS 1665, 1667 (Alan J. Auerbach & Martin Feldstein eds., 2002) ("[W]e will view the primary social function of the liability system as the provision of incentives to prevent harm.").

the harm or prevent it from materializing.[162] This, however, is an unrealistic assumption, and it neglects some important aspects of the issue at hand.

When victims invest to protect themselves from harm, they care little about the total magnitude of that harm. Instead, they worry only about the share of the harm they stand to suffer. This means victims might try to avoid harms by shifting them to others, rather than by preventing them. When making any effort to escape harm, the potential victim tries only to prevent the harm to *herself*, regardless of whether the harm is actually "minimized" or prevented as opposed to suffered by a third party or borne by the injurer at a later time.

Scholars in many areas of study recognize the fact that defensive practices might shift harms rather than minimize them. In the area of criminal law, scholars devote considerable energy to the study of this possibility.[163] More generally, the notion of wasteful self-protection is central to western political philosophy. Thinkers like Thomas Hobbes, David Hume, William Blackstone, and Jeremy Bentham employ this notion to justify the individual's relinquishment of personal power to the political order.[164] In the Hobbesian state of nature, individuals enjoy no legal protection of their rights. In such a state, all resources are consumed by individuals' efforts to protect themselves.[165] Political power is necessary in order to limit this destructive dynamic,[166] and legal protection of private property has a central role in this context.[167]

These fundamental insights are also central to contemporary theory of property rights. Property law scholarship reveals how property-right protection helps lower the costs that individuals would otherwise incur in their wasteful efforts to protect themselves.[168] The main structural features and

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162. *See, e.g.*, CALABRESI, *supra* note 20, at 26–28; COOTER & ULEN, *supra* note 22, at 202; Kaplow & Shavell, *supra* note 161, at 1669, 1671.

163. *See* CRIME SPILLOVER, *supra* note 31; Barr & Pease, *supra* note 31; Bowers & Johnson, *supra* note 31.

164. *See* 1 JEREMY BENTHAM, *Principles of the Civil Code*, *in* WORKS OF JEREMY BENTHAM pt. I, chs. VII–VIII (John Bowring ed., London, Simpkin, Marshall & Co. 1843) (1776); 2 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND ch. 1 (Oxford, Clarendon Press 1766); DAVID HUME, A TREATISE OF HUMAN NATURE bk. III, pt. II, §§ II, IV (L.A. Selby-Bigge ed., Oxford, Clarendon Press 1896) (1739).

165. *See* THOMAS HOBBES, LEVIATHAN: OR THE MATTER, FORME AND POWER OF A COMMONWEALTH ECCLESIASTICALL AND CIVIL pt. I, ch. 13 (Michael Oakeshott ed., Collier Books 1962) (1651).

166. *See id.*; *see also* YORAM BARZEL, A THEORY OF THE STATE: ECONOMIC RIGHTS, LEGAL RIGHTS, AND THE SCOPE OF THE STATE (2002).

167. *See* HOBBES, *supra* note 165, ch. 14.

168. In the economic literature, the cost of protecting property is sometimes included under the broader term "transaction costs": Yoram Barzel defines transaction cost broadly as the costs of transfer, capture, and protection of rights. YORAM BARZEL, ECONOMIC ANALYSIS OF PROPERTY RIGHTS 4 (2d ed. 1997). Douglass North describes transaction costs as the general costs of doing business. *See* DOUGLASS C. NORTH, TRANSACTION COSTS, INSTITUTIONS, AND ECONOMIC PERFORMANCE 6–7 (1992). Douglass Allen describes transaction costs as any costs of establishing or maintaining property

doctrinal arrangements of property law are justified based on their ability to achieve this goal. This framework is used to explain such concepts as the *numerus clausus* principle,[169] property rule protection,[170] and the in rem nature of property rights,[171] in addition to the doctrines of first possession,[172] trespass,[173] and protection from theft.[174]

In the context of tort law, however, the possibility of harm-shifting has hitherto never been explored. Instead, a victim's self-protection efforts are always conceptualized as efforts to minimize harms, not shift them. Considering the possibility of harm-shifting in the tort context carries with it crucial implications for our understanding of efficiency within compensation regimes.

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rights. Douglass W. Allen, *Property Rights, Transaction Costs, and Coase: One More Time*, *in* COASEAN ECONOMICS: LAW AND ECONOMICS AND THE NEW INSTITUTIONAL ECONOMICS 105, 108–09 (Steven G. Medema ed., 1998). These definitions throw the study of investments to protect property into the broader framework of transaction-costs economics.

169. *See* Thomas W. Merrill & Henry E. Smith, *Optimal Standardization in the Law of Property: The* Numerus Clausus *Principle*, 110 YALE L.J. 1, 9 (2000) (suggesting the *numerus clausus* principle provides a simple set of property rights, thus lowering the cost of delineating and protecting such rights).

170. *See* Keith N. Hylton, *Property Rules and Defensive Conduct in Tort Law Theory*, J. TORT L., 2011, at 1 (studying the advantages of property rule protection in preventing the need for wasteful self-help); Henry E. Smith, *Property and Property Rules*, 79 N.Y.U. L. REV. 1719 (2004) (establishing a general advantage of property rule protection). The argument is that under liability rule protection owners will over-invest in protecting themselves, as they fear that liability payments might not capture the full value of their assets for them; this problem does not arise under property rule protection. *See id.* at 1746–48. These arguments are a response to the general skepticism in the law-and-economics literature towards property rule regimes. *See* Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972) (arguing that liability rules have an advantage when the cost of bargaining is high); Louis Kaplow & Steven Shavell, *Property Rules Versus Liability Rules: An Economic Analysis*, 109 HARV. L. REV. 713, 716–20 (1996) (arguing that property rules have no clear advantage and so their observed prevalence presents a puzzle); James E. Krier & Stewart J. Schwab, *Property Rules and Liability Rules: The Cathedral in Another Light*, 70 N.Y.U. L. REV. 440 (1995) (arguing there is no advantage for property rules even if the costs of bargaining are *low*, as the parties can transact under liability rules and property rules alike); A. Mitchell Polinsky, *Resolving Nuisance Disputes: The Simple Economics of Injunctive and Damage Remedies*, 32 STAN. L. REV. 1075, 1076–80 (1980).

171. *See* Henry E. Smith, *Property as the Law of Things*, 125 HARV. L. REV. 1691, 1706–08 (2012) (showing that in rem rights allow simple and cheap management of complex property systems and thus lower the costs of self-protection); Thomas W. Merrill & Henry E. Smith, *Making Coasean Property More Coasean*, 54 J.L. & ECON. S77 (2011); Thomas W. Merrill & Henry E. Smith, *What Happened to Property in Law and Economics?*, 111 YALE L.J. 357 (2001).

172. *See* Dean Lueck, *The Rule of First Possession and the Design of the Law*, 38 J.L. & ECON. 393 (1995) (showing that the rule of first possession can lower wasteful investments in self-protection).

173. *See* Hylton, *supra* note 170, at 2 ("[D]efensive conduct plays an important role in establishing the justification for property rules, such as trespass doctrine. . . . I show that when defensive actions are taken into account, property rules are (once again) superior to liability rules in low transaction cost settings, because they enhance social welfare by obviating costly defensive actions.").

174. *See* Richard L. Hasen & Richard H. McAdams, *The Surprisingly Complex Case Against Theft*, 17 INT'L REV. L. & ECON. 367 (1997) (showing that legal protection against theft is efficient in lowering the need for self-protection); Fred S. McChesney, *Boxed In: Economists and Benefits from Crime*, 13 INT'L REV. L. & ECON. 225 (1993). These works draw on Gordon Tullock, *The Welfare Costs of Tariffs, Monopolies, and Theft*, 5 W. ECON. J. 224 (1967).

To see the argument, consider again *Example 2* above, except this time accounting for the possibility of harm-shifting. Assume again that Emma is the cheapest cost avoider and can protect herself from the harm by investing $1,000 in fencing her farm. Now see, however, that if Emma does protect herself in this way, it does not necessarily mean the harm is minimized. To wit, if the wandering cattle are turned aside by Emma's fence, they can still wander further and trample a different field. Thus, if Emma chooses to erect her fence, the harm from the cattle does not dissipate—it shifts.

Under these circumstances, compensation for Emma is desirable from an economic perspective. Assume again that a suit will be prohibitively costly for Emma at $6,000. Since compensation is unavailable, Emma will want to prevent the harm of $5,000 to herself, and will therefore invest $1,000 to erect her fence. Although this makes sense from Emma's private perspective, this investment is socially wasteful because the cattle will simply wander off and trample another farmer's field, causing the same amount of harm they would have if Emma had taken no action. In this situation, one possibility is that Emma will invest to protect herself, and the harm will be fully shifted to another victim, resulting in a total social cost of $6,000 ($5,000 damage to the field plus Emma's $1,000 investment). A second possibility is that other potential victims will also invest in protecting themselves, so the total social cost will be, for example, $1,000 per potential victim.

Total social cost is significantly lower if compensation can profitably be obtained. Assume now we can lower Emma's litigation cost to $500 and so enable her to sue the rancher. If Emma knows she will be compensated for harms, she has no reason to invest wastefully in shifting the harm to others. Instead, the rancher will want to invest $1,500 to fence in his cattle, rather than pay compensation of $5,000 in case harm occurs. This means total social cost will be only $1,500 instead of $6,000, or $1,000 per potential victim.

It is important to note that compensation is desirable here even though Emma, the victim, is nominally the cheapest cost avoider, able to erect her fence for a mere $1,000 (as opposed to the rancher's $1,500). In fact, compensation is desirable here precisely *because* Emma is the cheapest cost avoider. Emma can cheaply invest to protect herself and "avoid" or escape the harm. But, as has been shown, such avoidance tactics can be socially wasteful, while compensation can reduce the incentive to invest in them.[175]

175. Most investments in self-protection have a mixed effect: part of the harm is minimized, and part is shifted to others. This is the reason compensation is available but also sometimes limited. Absent compensation, victims will invest in protecting themselves; some of these investments will be wasteful, as victims struggle over the distribution of harms and shift parts of the harm to others. Compensation is useful to combat this effect. Once compensation is available, however, victims may have insufficient incentive to invest in precautions that might actually minimize the harm. To combat this problem, com-

This analysis reverses the standard economic maxim. The fact that victims are able to invest to protect themselves is no longer an argument against compensation but instead serves to support it. Therefore, the case for compensation is stronger than what existing economic theory would have us believe.

This conclusion ties the economic perspective back to the fundamental insights offered by civil recourse theory. According to civil recourse theory, compensation is designed to allow victims of harm a way to vindicate their rights.[176] My analysis shows that this arrangement is not only morally justified but also efficient.[177] By denying access to compensation, the state would abandon potential tort victims to fend for themselves. Doing so would be wasteful and problematic, as individuals defending themselves have strong incentive to shift harm, merely competing with other potential victims over the distribution of the harm; in that world, there is no one trying to prevent the social harm from occurring.

IV. THE STRONGER CASE FOR COMPENSATION

The analysis in Part III provides a simple analytical point: compensation is important not only to deter injurers but also to release victims from the destructive struggle over different distributions of harms. Compensation helps relieve potential victims of the need to invest to wastefully shift harms to others. Therefore, the normative value of compensation is *greater*, not lesser, when victims are able to invest in protecting themselves.

Part IV offers some doctrinal applications of this insight. I begin by studying the cases of road accidents and intentional torts and proceed to give a more in depth account of the law of nuisance. By studying these examples, this Part presents the stronger case for compensation and drives home the theory-based argument offered in Part III.

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pensation is limited, using doctrines such as relative, contributory, or comparative fault. Thus, in those cases when victims' self-protection seems also an efficient mechanism of harm minimization, the court may limit compensation in order to incentivize victims to take such precautions.

176. *See supra* notes 145–46 and accompanying text.

177. This type of move is in line with recent calls for inclusive pragmatism, in the framework of "the New Private Law." John C.P. Goldberg, *Introduction: Pragmatism and Private Law*, 125 HARV. L. REV. 1640, 1640 n.1 (2012). Inclusive pragmatism entails a pragmatic outlook, together with a willingness to "take law seriously" and respect established legal concepts and distinctions (as opposed to viewing them as "transcendental nonsense"). *See* Yishai Blank, *The Reenchantment of Law*, 96 CORNELL L. REV. 633 (2010); *cf.* Jeremy Waldron, *"Transcendental Nonsense" and System in the Law*, 100 COLUM. L. REV. 16 (2000) (arguing that technical legal vocabulary and concepts are consistent with a functionalist approach to the law). *But see* Felix S. Cohen, *Transcendental Nonsense and the Functional Approach*, 35 COLUM. L. REV. 809 (1935) (arguing that certain established legal concepts are "transcendental nonsense").

A. Accident Law

Compensation is helpful in solving quite a prevalent problem, as wasteful investments in self-protection are ubiquitous. To illustrate this, consider the case of road accidents. Potential victims of road accidents (that is, everyone) can invest to protect themselves from expected harm. For instance, it is known that heavier vehicles are generally safer than light ones.[178] Thus, to protect themselves from harm, drivers can choose to invest in safety and purchase a bigger vehicle. However, this is not a true investment in safety. By buying a heavier vehicle, a driver can lower her *own* risk of being harmed; yet, at the same time, a heavier vehicle represents a greater danger to others.[179] This means a private investment in safety is not necessarily socially desirable; on the contrary, it may just shift harms to others, or even exacerbate them overall.[180]

In a very similar fashion, an individual can decide to drive instead of walk in order to reduce the likelihood of being struck as a vulnerable pedestrian. Again, this private precautionary measure does not actually promote overall safety. By choosing to be a motorist rather than a pedestrian or a cyclist, an individual can significantly reduce the risk to which she is exposed while simultaneously increasing the risk to others.[181] Thus, as we have seen in other contexts, an individual protecting herself can shift the harm of accidents to others. More generally, in their efforts to avoid harms, individuals try to improve their position vis-à-vis others; they place themselves as the less vulnerable participant in each possible risky interaction. By doing this, individuals redirect harms towards others. Therefore, indi-

178. Leonard Evans & Paul Wasielewski, *Serious or Fatal Driver Injury Rate Versus Car Mass in Head-On Crashes Between Cars of Similar Mass*, 19 ACCIDENT ANALYSIS & PREVENTION 119, 119, 130 (1987); Denis P. Wood, *Safety and the Car Size Effect: A Fundamental Explanation*, 29 ACCIDENT ANALYSIS & PREVENTION 139, 150 (1997).

179. It is well known that adding mass to a vehicle lowers risk to individuals in that vehicle but also increases risk for others. *See, e.g.*, G. Grime & T.P. Hutchinson, *Vehicle Mass and Driver Injury*, 22 ERGONOMICS 93, 93 (1979) (studying how adding mass to a car crashing head on into another car affects fatality risks to both drivers).

180. In fact, it has been shown that having a heavier vehicle will only lower risk from frontal collisions *between cars* and not from single-vehicle crashes. The reason for this is that having a heavier car only matters if this is relative to the mass of the other vehicle involved in the accident. If one crashes into an immobile object, the extra mass of the car provides no added protection. T.P. Hutchinson & R.W.G. Anderson, *Smaller Cars: Not To Be Feared*, 34TH AUSTRALASIAN TRANSPORT RESEARCH FORUM (2011). This means that having a heavier vehicle only reduces harm in those cases where it also shifts harm to others. In other words, this type of investment in safety is purely egoistic, only shifting harms and not actually minimizing them. *See* Leonard Evans, *Driver Injury and Fatality Risk in Two-Car Crashes Versus Mass Ratio Inferred Using Newtonian Mechanics*, 26 ACCIDENT ANALYSIS & PREVENTION 609 (1994) (finding that adding mass to a vehicle can result in an overall increase in fatality risk; that is, the added risk to other drivers outweighs the decrease in risk for the driver of the heavier car).

181. RUNE ELVIK ET AL., THE HANDBOOK OF ROAD SAFETY MEASURES 58 (2009) (showing the risk for pedestrians increases when there are fewer pedestrians on the road).

viduals' efforts to save themselves from the harm of accidents can easily result in harm-shifting. The availability of compensation can help mitigate these effects.

B. Intentional Torts

The same dynamic can be identified in the case of intentional torts, such as burglary or theft. Victims of intentional torts invest in order to deflect undesirable activity away from themselves. For instance, to protect themselves from burglars, homeowners contract with security agencies and post warning signs on their property. Yet, these measures may not actually result in the minimization or prevention of home break-ins.[182] Instead, harms may only be shifted, as burglars would simply avoid the signs and relocate their activity to unprotected properties.[183] From a social prospective, this makes the homeowners' investment a wasteful form of self-help.[184] More generally, individuals invest to make sure they are less attractive targets for tortfeasors. By definition, this means their investments make others (relatively) *more* attractive victims.

Potential victims can also make wasteful investments in protecting themselves through contracting and bargaining with potential injurers.[185] If victims and injurers are operating in a contractual relationship, they can use this relationship to allocate risk and harms among themselves.[186] While the use of these mechanisms can be efficient, it also creates opportunities for "rent seeking" as different parties compete over the distribution of harms.[187]

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182. Barr & Pease, *supra* note 31, at 287–88; *see also* Omri Ben-Shahar & Alon Harel, *Blaming the Victim: Optimal Incentives for Private Precautions Against Crime*, 11 J.L. ECON. & ORG. 434 (1995) (showing that victims' incentives to take precautions against criminal activity diverge from the social optimum).

183. For a discussion of this example, see Ayres & Levitt, *supra* note 31, at 63–65 tbl.IV, 66 tbl.V.

184. *See id.* at 64.

185. *See, e.g.*, Ernst Fehr, Oliver Hart & Christian Zehnder, *How Do Informal Agreements and Revision Shape Contractual Reference Points?*, 13 J. EUR. ECON. ASS'N 1 (2015) (comparing the strategy of *ex post* revision of simple and rigid contracts to that of complex and flexible *ex ante* contracting designed to anticipate *ex post* contingencies); Oliver Hart & John Moore, *Contracts as Reference Points*, 123 Q.J. ECON. 1 (2008).

186. Eric A. Posner, *Economic Analysis of Contract Law After Three Decades: Success or Failure?*, 112 YALE L.J. 829, 838, 843, 848–49 (2003).

187. The term *rent seeking* refers to efforts to secure gains at the expense of others. The rent-seeking literature mainly focuses on individuals' attempts to manipulate or capture regulatory mechanisms and use them to obtain a competitive advantage in a market environment. *See* GORDON TULLOCK, THE ECONOMICS OF SPECIAL PRIVILEGE AND RENT SEEKING (1989); Roger D. Congleton, *Evaluating Rent-Seeking Losses: Do the Welfare Gains of Lobbyists Count?*, 56 PUBLIC CHOICE 181 (1988); Barry J. Nalebuff & Joseph E. Stiglitz, *Prizes and Incentives: Towards a General Theory of Compensation and Competition*, 14 BELL J. ECON. 21 (1983); Stergios Skaperdas, *Restraining the Gen-*

In all these diverse contexts, compensation can be useful to reduce the need for victims' wasteful investments in self-help. Even if it does not eliminate the harm completely, compensation somewhat mitigates it, thus lowering the need for individuals to invest in shifting the harm to others. Quite generally, this means the case for compensation is stronger than what current economic theory suggests. Accordingly, the anticompensation campaign, based on economic theory, is lacking a normative justification.

C. Nuisance

This section returns to the nuisance case of the polluting factory presented in *Example 1*, only this time considering also the possibility of harm-shifting, here in the form of "Not In My Back Yard" (NIMBY) investments. Before a source of nuisance is constructed, nearby residents typically try to avert the harmful activity through NIMBY objections.[188] Naturally, this does not mean the factory disappears or will not be built. In fact, the factory may simply be moved to a different location. The very nature of NIMBY objections is that residents act selfishly; each group prefers the factory be built somewhere else and "not in my back yard."[189] Thus, each group of residents in each alternative location will invest to have the factory built near another group.[190] This means that NIMBY investments are, almost by definition, investments by potential victims to shift harms to others.

To see the effect of such investments on the analysis of compensation, consider *Example 3* below.

- *Example 3*: Prior to the construction of a factory, nearby residents consider investing in a NIMBY campaign to move the factory away from their houses. The residents can lobby against the construction of the factory, sign petitions, organize rallies, and

uine Homo Economicus*: Why the Economy Cannot Be Divorced from its Governance*, 15 ECON. & POL. 135 (2003).

188. NIMBY objections are efforts by land owners (typically residential) to prevent commercial development—a possible source of nuisance—in their area. William A. Fischel, *Why Are There NIMBYs?*, 77 LAND ECON. 144, 144–45 (2001).

189. Of course, NIMBY objections might be efficient if they help direct the nuisance to the location where it is least harmful. Yet, each group of residents has a strong incentive to invest in NIMBY objections in order to protect itself by shifting the harm to others. The overall investment may therefore easily outweigh any benefit. To provide a very simple illustration, assume the nuisance would cause a harm of *2* to the first group and a harm of *3* to the second group. The groups would invest up to *2* and *3* in NIMBY objections, respectively, and the nuisance will be located where it is less harmful: near the first group. However, the benefit of this is only *1*, while the potential cost is up to *5*. The reason for this is that the parties are investing to protect themselves, not to find the socially optimal allocation.

190. In many cases, it is difficult for owners to buy insurance against nuisance-like harms to their property, since such harms, unlike accidents, are not probabilistic events. *See* Fischel, *supra* note 188, at 145. This means owners will have a strong incentive to invest in NIMBY objections.

> so on. If the factory is eventually built, the expected harm to nearby residents is $2,000. The residents can invest $500 for a 50% chance of ridding themselves of the factory.

Consider first the residents' investment if compensation is *not* available. In this case, the residents face the possibility of a harm of $2,000 from the factory. The residents will therefore choose to invest in NIMBY objections. From the private perspective of the residents, this makes sense and will entail an overall lower cost of $1,500 for the residents (an investment of $500 plus a 50% chance of a harm of $2,000).

Indeed, the residents invest to try to banish the factory, but this does not mean the factory will not generate harm. By the nature of NIMBY objections, the residents do not object to the existence of the factory, but only to its specific proximity to them. Thus, the residents are equally happy to invest even if all this will accomplish is that the factory is relocated to harm a different group of residents in a different location. This means that, absent compensation, the total social cost is $2,500 (the harm of $2,000 to the residents in the new location plus the $500 investment by the first group to move the factory away).

Consider now the same situation, but now compensation *is* available. If compensation is available, the residents will prefer to suffer the harm of $2,000 and be compensated fully for it, entailing no loss to themselves. This situation is therefore better for the residents compared to the option of losing $500 in their NIMBY campaign (and more if their campaign is unsuccessful). Since the residents are not making NIMBY investments, the total social cost is just $2,000 (the cost of the harm) instead of $2,500 (the cost of the harm plus the residents' NIMBY investment). Compensation is therefore desirable here from an economic perspective.[191]

Note that compensation is efficient, even though the factory is not the cheapest cost avoider, and even though compensation would not incentivize the factory to increase its investment in precautions. Instead, compensation is required to protect the interests of nearby residents—those who have a property right that has been violated and who can invest to protect that right (in this case, through NIMBY objections). This illustration once again makes clear that the case for compensation is stronger than current economic theory suggests, as compensation is justified here contrary to conventional economic wisdom. This demonstrates the reversal of the familiar

191. An alternative solution would be to limit the ability of individuals to invest in NIMBY objections (rather than minimizing their incentive to do so). This is not necessarily easy, and despite efforts to minimize NIMBY objections, the cost of NIMBY-style struggles still poses a significant social problem. *See* Eli Feinerman, Israel Finkelshtain & Iddo Kan, *On a Political Solution to the NIMBY Conflict*, 94 AM. ECON. REV. 369, 369 (2004); Martin P. Sellers, *NIMBY: A Case Study in Conflict Politics*, 16 PUB. ADMIN. Q. 460 (1993).

economic framework: the case for compensation is *stronger*, not weaker, when victims are able to invest to protect themselves.

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The examples presented in this Part highlight a simple point: the case for compensation is stronger than what existing economic theory would have us believe. That is, compensation can be justified even if current deterrence theory sees no possible justification for it. Furthermore, and contrary to conventional economic wisdom, compensation actually has a greater normative value when victims are cheap cost avoiders, able to efficiently invest in protecting themselves from harm. This, in turn, means that the normative arguments of the anticompensation campaign stand on shaky grounds.

The economic anticompensation argument is false even if investments in self-protection have a *mixed effect*: partly minimizing harms and partly shifting them. It is enough that investments in self-protection have *some* harm-shifting effect to show that the case for compensation is stronger than what current economic theory portrays it to be.

CONCLUSION

The right for compensation is rapidly losing its footing in our legal system. Currently, only an insignificant minority of victims legally entitled to compensation actually sue to vindicate their rights. This new status quo is justified by economic theory that focuses on deterrence and precautions designed to minimize harms. In this framework, compensation is unnecessary for deterring injurers and also harmful in annulling victims' incentive to invest in precautions. According to this view, a regulatory fine seems an a priori superior legal mechanism, so the case for compensation is not worth pursuing.

My analysis reveals that this analytical position—and the status quo it supports—is unfounded. It is indeed true that compensation lessens the incentive of potential victims to invest in protecting themselves. However, there is no reason to generally assume this is a negative effect. To the contrary, compensation can be useful precisely *because* it frees potential victims from the need to protect themselves. Efforts of self-protection are often wasteful, as they have no direct connection to the social need for minimizing the overall magnitude of harms and often merely shift or redistribute them.

All this stresses the urgent necessity to reverse the current degeneration of compensation as a legal institution. Compensation serves an important purpose of protecting individuals as fully as practicable, considering the

legal and practical limitations. As such legal protection vanishes, self-protection takes its place. The decline of compensation means our legal system is abandoning some segments of the population to fend for themselves. This is not only morally misguided but also creates inefficiencies and distorted incentives. There is no reason to believe, as does current economic theory, that individuals fending for themselves without legal protection are acting efficiently to "minimize" harms. Instead, the threat of uncompensated harm—the absence of legal protection—can push them to invest selfishly, inefficiently, and in a way that is *more* harmful to others and to society at large.