

Coasean Blackmail: Protection Markets and Protection Rackets

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I. INTRODUCTION

This Article concerns transactions in which one party must buy “protection” by paying another not to harm him by engaging in an action the payee would otherwise be free to do. Private law often permits a party, in pursuing its own interests, to inflict incidental harm on another party without incurring any liability to compensate the loss.¹ In such cases, the vulnerable party (the “victim”) may find that the cheapest way to reduce such harm is to pay the other party (the “menace”) a bribe to forbear from the harmful action. Although such protection transactions are commonplace, it has long been recognized that some of them, such as non-disclosure agreements, are usually lawful while others, such as secrets blackmail, are not. But legal theory has struggled to rationalize the line it draws between benign bribes and criminal blackmail, between legally-approved transactions in which property owners smoothly coordinate their privileged but harm-producing activities and legally-disapproved transactions in which extortionists wring unjust profit from their victims.

This Article offers a theory of blackmail that distinguishes it from lawful bribery in a way that justifies its differential legal treatment. Under this approach, the critical difference between blackmail and bribery depends on the amount of money the menace demands for protection. Bribery compensates the menace only for the cost it incurs in forbearing from harmful activity. Blackmail exists to the extent that the amount

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1. The jurisprudential treatment of interests that receive no legal protection, under the description *damnum absque injuria*, was analyzed by Joseph William Singer, *The Legal Rights Debate in Analytical Jurisprudence from Bentham to Hohfeld*, 1982 WIS. L. REV. 975, 1041 (1982) (Legal liberty is the privilege to inflict *damnum absque injuria*). Singer concluded that the ability to freely harm another is implicit in any Hohfeldian privilege. *Id.* at 1050. Earlier analyses of the phenomenon were given in Oliver Wendell Holmes, *Privilege, Malice, and Intent*, 8 HARV. L. REV. 1, 3, 5 (1894) (arguing that whether a harmful act is legally privileged depends on many factors); Samuel D. Warren & Louis D. Brandeis, *The Right to Privacy*, 4 HARV. L. REV. 193, 197 (1890) (lamenting that mental and emotional suffering inflicted by a malicious but lawful act is *damnum absque injuria*).

demanded and paid for forbearance exceeds this cost. The “extortion premium” that a victim must pay the blackmailer constitutes unjust enrichment because it is acquired by exploiting the victim’s fear of harm that the blackmailer threatens to inflict.

Protection transactions were featured in the groundbreaking article that helped to inaugurate economic analysis of law, Ronald Coase’s *The Problem of Social Cost*.² There, Coase addressed the economic problems created when productive enterprises create harms, such as pollution, whose costs are borne by others. Economists had argued that allocative efficiency required that firms producing such externalities³ be legally required to bear their full cost. Coase disagreed. Some externalities are efficient and some are not. Whether legal treatment of an externality leads to allocative inefficiency depends on the relative values of the productive activities of the producer and its victims. To achieve efficient allocation of productive resources in the presence of externalities, Coase posited an idealized market, free from transaction costs,⁴ in which producers and their victims could take those values into account by exchanging legal entitlements to inflict harm or to be free from harm. Their exchanges would minimize the social cost of productive activities without the need for government regulation of commercial externalities.

However, Coase’s analysis overlooked one significant transaction cost that would prevent ideal markets in harm-related entitlements. Transactions in which menaces sell protection might be prohibited by the law of extortion.⁵ Moreover, the prospect of making a profit in protection markets may lead menaces to create protection rackets, in which harm-causing enterprises find it more profitable to sell protection than to engage in the productive activity that generates the harm. Although *The Problem of Social Cost* expressed no concern about this possibility, its publication launched an on-going debate about whether extortion is intrinsic to an efficient market in property rights.⁶

2. R. H. Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960) [hereinafter Coase, *The Problem of Social Cost*] reprinted in R.H. COASE, *THE FIRM, THE MARKET, AND THE LAW* 95 (1988) [hereinafter COASE, *THE FIRM, THE MARKET, AND THE LAW*].

3. COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 23–27 (explaining why he rejected the term “externality”).

4. Coase assumed that transaction costs associated with these bargains would be zero. See *Notes on The Problem of Social Cost* in COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 174–75 (noting that the term “transaction cost” was developed after publication of *The Problem of Social Cost*).

5. This Article will use “blackmail” and “extortion” synonymously, with the understanding that it does not deal with those forms of extortion in which the threatened act is itself either criminal or tortious. “Blackmail” is the more generally used term for this kind of transaction.

6. Coase, *The Problem of Social Cost* *supra* note 2, at 7–8 (discussing the risk that the rancher

Why should the law seek to prevent transactions that Coase's analysis shows to be *prima facie* beneficial? This Article offers a conception of blackmail that differentiates it from Coasean bribery and provides a theoretical basis for its legal inhibition. Under this approach, a protection transaction is a benign Coasean bribe if the victim purchases the menace's forbearance to engage in the harmful activity at a price that compensates the menace for whatever benefit it will lose by its forbearance. The same protection transaction becomes blackmail if and to the extent that the menace demands more than that amount. The extortion premium that the victim must pay represents unjust enrichment to the menace because it results from exploitation of the victim's fear of harm. Under this analysis, blackmail is thus a question of degree that varies with the size of the extortion premium demanded.

Alas, this theory does not square with the existing law of blackmail. Whether courts will treat a protection transaction as blackmail or bribery turns not on the presence or absence of unjust enrichment but on whether the exchange was induced by a menace's threat.⁷ Although the threat requirement gives the appearance of an easily-administered rule, it is often very difficult to apply and even in clear cases is both over- and under-inclusive in targeting wrongful behavior.⁸ The presence or absence of a threat is an unsatisfactory test for blackmail because the wrong lies not in threat itself or in the nature of the threatened act but in the unjust enrichment the blackmailer obtains by misuse of its power to harm the victim.

The persistent problem of Coasean blackmail illuminates a deep-seated ambivalence in moral and legal theory about the propriety of

would threaten to increase herd size just to induce the farmer to pay more); Ronald Coase, *The 1987 McCorkle Lecture: Blackmail*, 74 VA. L. REV. 655 (1988) [hereinafter "Coase, *Blackmail*"] (discussing application of *The Problem of Social Cost* to secrets blackmail). On the question of extortion, Coase's article must be considered alongside the related analyses of Harold Demsetz, *When Does the Rule of Liability Matter?*, 1 J. LEGAL STUD. 13, 24 (1972) [hereinafter "Demsetz, *When Does the Rule of Liability Matter?*"] and Harold Demsetz, *Wealth Distribution and the Ownership of Rights*, 1 J. LEGAL STUD. 223, 230–32 (1972) [hereinafter "Demsetz, *Wealth Distribution*"]. Later analyses of extortion in Coasean bargains include George Daly & J. Fred Gietz, *Externalities, Extortion, and Efficiency*, 65 AM. ECON. REV. 997 (1975); D. W. Bromley, *Externalities, Extortion, and Efficiency: Comment*, 68 AM. ECON. REV. 730 (1978); Ekkehard Schlicht, *Exploiting the Coase Mechanism: The Extortion Problem*, 49 KYKLOS 319 (1996); Wolfgang Buchholz & Christian Haslbeck, *Strategic Manipulation of Property Rights in Coasean Bargaining*, 153 J. INST. & THEORETICAL ECON. 630 (1997); Steven G. Medema, *'A Magnificent Business Prospect . . . ' the Coase Theorem, the Extortion Problem and the Creation of Coase Theorem Worlds*, 11 J. INST. ECON. 353 (2015).

7. See *infra*, Part V. Sidney W. DeLong, Symposium, *Blackmailers, Bribe Takers, and the Second Paradox*, 141 U. PENN. L. REV. 1663, 1685–86 (1993) [hereinafter "DeLong, *Second Paradox*"] (contrasting different legal treatment of identical exchanges initiated by menacers' threats and by victims' offers).

8. *Id.* at 1677–79 (considering possible efficiency-based rationales for the threat requirement).

trafficking in harm. In some contexts, profit from the exercise of monopoly leverage is accepted as a natural incident of property ownership and liberty. In other contexts, similar profit resulting from similar leverage is condemned as extortion. This Article seeks to refocus the normative debate away from the nature of the threat to the presence or absence of unjust enrichment and from concern about the harm to the victim to concern about the profit obtained by the wrongdoer.

Part II of the following discussion interprets Ronald Coase's *The Problem of Social Cost* as depicting an idealized protection market in which enterprises trade entitlements both to inflict and to be free from harms caused by their productive activities. Coase reconceived these harm-related entitlements as valuable factors of production to be traded by the enterprises that exploited them. Their reallocation increases their value and reduces social cost. But Coase's analysis of such markets had ominous implications.

Part III describes the economic and legal conditions under which Coasean bargaining can occur. Protection transactions reverse existing legal rights and privileges relating to harm-causing activities. Whether two enterprises will engage in Coasean bargaining depends on the relative values of their productive activities and the costs they impose on each other. A protection transaction is feasible whenever a privileged action will cause harm to a victim that is greater than the benefit it confers on the actor. But Coasean bargains in the real world may be prevented by transaction costs. One of those transaction costs is that the exchange may be prevented by the law of extortion.

Part IV describes the circumstances under which a protection transaction becomes extortionate. When a menace acquires leverage over a victim, it has a legal privilege to inflict harm that costs the victim more than the benefit of the harmful action to the menace. This permits the menace to demand an extortion premium that exceeds the cost it would incur in forbearing from the threatened harm. Indeed, a menace may find the sale of protection to be more profitable than the activity that causes the harm. But this form of profit is not morally justifiable. To the extent that it overcompensates the menace for its forbearance, the extortion premium constitutes unjust enrichment.

Part V contrasts this analysis with the actual law of extortion. The law condemns protection transactions initiated by a menace's threat of harm while it approves identical exchanges initiated by a victim's offer. The threat requirement makes the law of extortion both under- and over-inclusive under the proposed standard. It condemns some menaces who sell protection at a price that only compensates them for their costs of forbearance while it exonerates other menaces who demand an extortion

premium for the same protection.

Part VI compares the unjust enrichment theory with other theories of blackmail that are based on a transaction's third-party economic or social effects. Opinion is sharply divided on the economics of legalized protection markets, in part because of unanswerable empirical questions about the actual effects of laws permitting and prohibiting protection transactions. Non-economic theories have been unable to solve the paradox of blackmail by reference to the rights of the victim without reference to the blackmailer's enrichment.

Part VII applies the unjust enrichment theory of protection transactions to four commonplace situations: commercial secrets blackmail, residential spite structure blackmail, reputational blackmail, and remedial blackmail.

The Conclusion argues that the critical distinction between bribery and blackmail arises not from differences in the bargaining process that leads to a protection transaction but from the amount the victim must pay for that protection. Regardless of how they come about, Coasean bargains are not problematic if menaces merely sell forbearance at or near their cost. They become extortionate only when, through the use of leverage, the menace extracts an extortion premium that exceeds that cost. Unjust enrichment thus distinguishes protection markets from protection rackets.

II. THE PROBLEM OF SOCIAL COST.

One cannot exaggerate the jurisprudential significance of Ronald Coase's article, *The Problem of Social Cost*.⁹ Although it ostensibly addressed only the economic problem of externalities,¹⁰ in the course of its analysis it laid much of the foundation of economic analysis of law by emphasizing the many ways in which the legal system determines how the economic system functions.¹¹ *The Problem of Social Cost* caused an upheaval in the legal academy,¹² where, in the course of setting out its

9. Coase, *The Problem of Social Cost*, *supra* note 2. As of the mid-1990's, it had become the most cited article in legal periodicals. R. H. Coase, *The Problem of Social Cost: The Citations*, 71 CHI. KENT L. REV. 809, 809–10 (1996).

10. The term "externality" was coined by British economist Arthur C. Pigou in *THE ECONOMICS OF WELFARE* (1920), whose analysis Coase rejected. Coase, *The Problem of Social Cost*, *supra* note 2. Coase used the term "harmful effects" in preference to "externality" in part to avoid the connotation that had not been taken into account by producers and so could be treated like any other factor of production. COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 27.

11. RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (9th ed. 2014) ("Coase's article . . . opened a vast field of legal doctrine to fruitful economic analysis.")

12. Coase acknowledged that his analysis "has not in general commanded assent" among economists. COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 1.

simplifying assumptions, it gave the first voice to many ideas that have since become firmly fixed analytic principles.¹³ A brief, non-technical article by a non-lawyer economist thus became one of the most influential pieces of legal scholarship of the last century.¹⁴ But *The Problem of Social Cost* also revealed dramatic differences between the economic and legal perspectives on the common law. One of the most telling was in the matter of the law and economics of harm.

A. *Coasean Bargains.*

The Problem of Social Cost is in large part a standard economist's parable about how the pricing system can achieve an efficient allocation of scarce resources and maximize the social product.¹⁵ Its novelty was that, rather than describing a market for goods and services, it depicted a market in legal entitlements either to inflict or to be free from the harms that can be caused by productive activities. It was the first study to identify a producer's legal privilege to act without incurring liability for damages as a valuable factor of production,¹⁶ a property interest that can reduce the cost of production for one party even as it increases the costs of production to another.

Coase applied his approach to the problem of externalities created by productive enterprises. Economists are concerned about what happens when a producer's commercial activity imposes incidental, uncompensated costs on other producers. For example, a factory might generate pollution that imposes costs on other factories, or a railway might

13. In *The Problem of Social Cost* can be found the following ideas and concepts, all novel for their time: Law is a constraint that imposes costs on, and creates incentives for, economic activity; a legal system may be evaluated by its economic effects on social productivity; Parties trade bundles of legal rights in markets; parties will, if not prevented by transaction costs, negotiate around inefficient legal rules, including those that establish their default legal entitlements; the market will allocate legal entitlements, like other forms of property, to the persons who value them the most; harmful interactions are jointly caused by both the actor and the sufferer; incompatible uses of real property should be adjusted so as to maximize the social product; and bargains that efficiently reallocate harm-related entitlements may be prevented by transaction costs. Coase, *The Problem of Social Cost*, *supra* note 2.

14. Fred R. Shapiro & Michelle Pearse, *The Most-cited Law Review Articles of All Time*, 110 MICH. L. REV. 1483, 1489 (2012). Ironically, one of the unintended effects of *The Problem of Social Cost* was to inspire an article that contributed to the founding of the major academic competitor to Law and Economics, the Law and Society Movement. Robert C. Ellickson, *Of Coase and Cattle: Dispute Resolution Among Neighbors in Shasta County*, 38 STAN. L. REV. 623 (1986) [hereinafter Ellickson, *Of Coase and Cattle*] (empirical study showing how farmers and ranchers rely on community norms to deal with cattle trespass and that Coasean bargaining is virtually non-existent).

15. Coase, *The Problem of Social Cost*, *supra* note 2, at 1.

16. *Id.* at 6–7.

start trackside fires that harm nearby farming operations.¹⁷ If producers are not required to pay the costs of this harm, then the private benefits accruing to their owners might not equal their total (or “social”) costs, leading to a misallocation of scarce resources committed to the productive activities. At the time of *The Problem of Social Cost*, the dominant economic theory of Arthur Pigou held that, if the state did not compel producers to compensate such harms by property or tort rules, then it should regulate or tax producers of externalities by forcing them to “internalize” the cost of the externalities they created in their productive activities.¹⁸

The Problem of Social Cost is an argument that such governmental regulation is unjustified. Depending on the values of the goods and resources involved in the conflicting uses, to force the producer to pay for its damage may not lead to an efficient result¹⁹ and might lead to inefficient over-investment in less valuable, vulnerable activities. In theory, under ideal²⁰ market conditions, the parties would always negotiate to an efficient solution regardless of whether the state gave protection against the harms of productive activity. If *ex ante* harm-related property entitlements led to inefficient over- or under-production, then rational producers and those who were affected by their production would coordinate their activities by mutual agreement. When necessary, parties who suffered from the effects of externalities whose harms exceeded their benefits would bribe producers not to cause them, so that producers would

17. COASE, THE FIRM, THE MARKET, AND THE LAW, *supra* note 2, at 23–27 (discussing prevailing views of externalities and the need for government intervention). Businesses have inflicted an extensive range of harms on neighboring landowners: smoke, vile smells, noise, invasive animals, flooding, fire, crowds of people, criminal activity, noxious weeds, unsightly eyesores, and other forms of nuisance. Transactions in the modern world create their own forms of uncompensated negative externalities: ride-hailing services create traffic congestion, cell phones create hazards of distracted driving, and social media merchants contribute to widespread disinformation.

18. COASE, THE FIRM, THE MARKET, AND THE LAW, *supra* note 2, at 23–27 (summarizing prevailing views of externalities and the need for government intervention); Coase, *The Problem of Social Cost*, *supra* note 2, at 28. Whether his criticism of Pigou was apt has been seriously questioned. A. W. Brian Simpson, *Coase v. Pigou Reexamined*, 25 J. LEGAL STUD. 53, 65 (1996) (criticizing Coase for mischaracterizing Pigou’s positions); see also Herbert Hovencamp, *Perspectives on the New Regulatory Era: The Coase Theorem and Arthur Cecil Pigou*, 51 ARIZ. L. REV. 633, 633 (2009) (noting that Pigou rather than Coase first described what later became known as transaction costs).

19. Coase, *The Problem of Social Cost*, *supra* note 2, at 17–19; COASE, THE FIRM, THE MARKET, AND THE LAW, *supra* note 2, at 26 (“The ubiquitous nature of ‘externalities’ suggests to me that there is a *prima facie* case against intervention . . .”).

20. Coase based his arguments on the assumption that there would be no transaction costs to the exchanges he envisioned. He later said that the most valuable contribution of *The Problem of Social Cost* was not the Coase Theorem but his identification of transaction costs as important determinants of efficient markets and, by extension, legal policy. COASE, THE FIRM, THE MARKET, AND THE LAW, *supra* note 2, at 13.

engage in only those harm-causing activities whose value exceeded their total costs.²¹

Coase illustrated his argument with an extended example drawn from the law of cattle trespass.²² Coase's hypothetical rancher raised unfenced cattle near a neighboring farmer who raised crops. The cattle damaged²³ some of the farmer's crops, leading to the question of which party should bear this loss. Local law allocates this loss either by making the rancher liable to the farmer for the loss (the "fencing in" rule) or by the farmer having no claim for cattle damage (the "fencing out" rule).²⁴ Using assumed arithmetic values of the marginal destructive effect of adding individual cattle to the rancher's herd,²⁵ Coase showed that ranchers whose unfenced cattle damaged the crops of neighboring farmers would always enter into agreements with the farmers so as either to permit or prohibit the cattle from damaging the crop, depending on the relative economic values of cattle and crops.²⁶ By trading entitlements, the rancher and farmer could achieve an efficient solution to their conflict regardless of which fencing rule prevailed in their jurisdiction.

Unless transaction costs prevented these bargains, incompatible land uses would be coordinated by contractual exchanges rather than by property and tort law. The invisible hand of the marketplace would

21. One might question the degree to which Coase's analysis refuted the Pigovian consensus in favor of regulating or taxing externalities. Coase acknowledged that transaction costs prevented actual reallocative bargaining that would force enterprises to internalize their social cost. See Coase, *The Problem of Social Cost*, *supra* note 2, at 15–17 (instancing the collective action problems of negotiating agreements about pollution with large numbers of parties). His chief argument against Pigou's approach of using governmental regulation in such cases was that the government too faced transaction costs, including a lack of information about the costs and benefits of conflicting economic activity that would be necessary to an efficient allocation of entitlements. To force enterprises such as railways to bear all the physical costs inflicted by their activity might lead to unintended consequences, such as inefficient over-investments by those vulnerable to the harm. *Id.* In the end, however, he was forced to acknowledge that transaction costs prevented an ideal solution to the problem of externalities. *Id.* at 43.

22. Coase, *The Problem of Social Cost*, *supra* note 2, at 2–8.

23. *Id.* Coase did not describe the nature of the harm the cattle caused. Obviously, if they consumed a significant part of the crop, the farmer's claim might sound in conversion or unjust enrichment rather than trespass.

24. Coase was aware that American law favored the rancher in states with a "fencing out" rule and favored the farmer in states with a "fencing in" rule. Coase, *The Problem of Social Cost*, *supra* note 2, at 36 n.49. Pigou would presumably have favored giving the rights to the farmer in order to force the ranchers to internalize the total cost of their cattle.

25. In explaining Coase's chilly reception by economists, Oliver Williamson criticized him for using "ponderous arithmetic examples" instead of the mathematical or geometrical expressions with which economists are more familiar. Oliver E. Williamson, Book Review, *The Firm, The Market, and the Law* by R.H. Coase, 77 CAL. L. REV. 223, 229 (1989). Coase's examples are accessible to lawyers who do not speak the language of economics.

26. Coase, *The Problem of Social Cost*, *supra* note 2, at 2–8.

efficiently allocate harm-related entitlements²⁷ and the cowman and the farmer would be friends.

B. Implications.

The Problem of Social Cost is often cited for the Coase Theorem: Absent transaction costs, *ex ante* legal entitlements are irrelevant to efficient resource allocation because parties will always bargain to an efficient solution.²⁸ In fact, his point was quite the opposite: *ex ante* legal entitlements *do* matter because transaction costs often prevent reallocative bargaining. Parties usually end up with the rights and privileges that the law gives them at the outset, which may well be inefficient in light of the relative values of the resources and products of their enterprises. Yet, Coase had little faith that courts or legislators could assign ownership rights in a way that would duplicate the ideal choices the parties would have made in the absence of transaction costs, for both theoretical and practical reasons.²⁹ Because the values of resources and products are constantly changing, it is impossible even in theory to assign harm-related rights, e.g., to cattle and corn, that would always induce efficient behavior by ranchers and farmers. This year beef may be more valuable than corn. Next year corn may be more valuable than beef. Coase was also skeptical that government had the information to make the correct assignment of rights even if it had the political will to do so. Government faces its own transaction costs that prevent more efficient land use regulation.³⁰

This Article concerns some of the unstated implications of Coase's analysis. In positing a market in which victims paid menaces to forbear from harmful activity, Coase incidentally revealed that a privilege, e.g., to pollute a stream or graze a cow without legal liability for the resultant harm, not only has a *use value* for the polluter, as a factor of production, but also an *exchange value*. This exchange value rests on what is commonly called "nuisance value," or the amount of harm the act will inflict on others. If a legal privilege's nuisance value exceeds its use value, as Demsetz pointed out, a rational producer will maximize its profit by fully exploiting that nuisance value in an exchange with the victim.³¹ And

27. COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 12 ("If rights to perform certain actions can be bought and sold, they will tend to be acquired by those for whom they are most valuable either for production or enjoyment. In this process, rights will be acquired, subdivided, and combined, so as to allow those actions to be carried out which bring about that outcome which has the greatest value on the market.")

28. *Id.* at 13–15.

29. *Id.* at 26.

30. Coase, *The Problem of Social Cost*, *supra* note 2, at 18.

31. Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 24.

rational producers will invest in legally-privileged, harm-causing enterprises in order to maximize their income from protection exchanges.

When nuisance value exceeds use value, protection rackets may arise in which ranchers sell freedom-from-cows to farmers for more than they would receive selling beef to consumers; factories sell freedom-from-pollution to residents for more than they would receive by selling pollution-generating products to consumers; and blackmailers sell non-disclosure agreements to wrongdoers for more than they would receive by selling scandal to the media. The natural result of a thriving protection racket is a shift in investment from production of goods to the production of (otherwise pointless) harm (by potential blackmailers) and an increase in investments in (otherwise unnecessary) protection against the enhanced threats (by potential victims of blackmail).

Another unstated implication of *The Problem of Social Cost* is that its argument applies to relations between any two parties, not just productive enterprises. Coase confined his main analysis to harmful interactions between productive enterprises, in which the costs and benefits of their respective activities could easily be compared to determine the most efficient use of land. Business-to-business examples also validated Coase's argument that harmful interactions were reciprocal and that one of the parties would suffer "harm" under any legal regime, either by suffering from the interaction or by being prohibited from engaging in the harmful productive activity.³² Moreover, the harm resulting from the mutual interference of neighboring enterprises was easy to see as the joint product of their interaction and propinquity and not, as is usual in analysis of tort and nuisance law, the responsibility of one of them, the "tortfeasor," in injuring the other, passive victim. Thus, all of the harms instanced in his examples were incidental to some productive activity and none were the product of malice.

But some of the examples in *The Problem of Social Cost* could also be applied to non-producers or consumers. For example, Coase later acknowledged that the analysis was equally applicable to such non-commercial interactions as secrets blackmail.³³ In these cases, the disutility of the harm cannot be easily quantified and the victim's passive contribution to the interaction is notional at best. Moreover, the legally-privileged, harm-causing act itself may not be incident to any productive activity of the menace but may be engaged in solely to harm the victim.

Coase implied in his analysis of blackmail³⁴ that the state should

32. Coase, *The Problem of Social Cost*, *supra* note 2, at 2 (discussing reciprocity).

33. Coase, *Blackmail*, *supra* note 6, at 656-58.

34. *Id.*

allocate rights to the victim of secrets blackmail in order to obviate the need for costly protection transactions. But because the secrets blackmailer's threatened disclosure is legally privileged, the victim has no right to prevent it unless she can engage in a protection transaction and that transaction is often blocked by the law of extortion.

III. THE CONDITIONS FOR COASEAN BARGAINS.

A. *Vulnerability to Harm.*

Coasean bargaining in harm-related entitlements will take place only when a menace has the ability to act in a way that will cause harm to a victim without incurring a legal obligation to compensate the victim. "Harm" in this Article will refer to any unwanted experience that a party would be willing to pay to avoid or would refuse to suffer unless in return for payment. Harm includes anything that a victim perceives as damaging to his person or property, his reputation, his feelings, or his financial interests.

Under such conditions, the subject matter of a harm-related bargain consists of two antagonistic legal relationships: rights to be free from the threatened harm (correlated with duties not to inflict it) and privileges to inflict the threatened harm (correlated with the absence of rights to be free from it.) The menace and victim are always in a legal relation under which the menace either owes a duty to the victim not to harm the victim, or under which the menace is legally privileged to harm him.³⁵

Parties may adjust this harm-related relationship in exactly two ways, which for convenience will be referred to as "permission transactions" and "protection transactions." Permission transactions occur when the parties contract out of a rule making the menace legally responsible to the victim for the harm it causes. In a permission transaction, the menace obtains the victim's permission to engage in the harmful activity, as, for example, by purchasing a license, easement, waiver, or release from the victim. In the circumstances described in *The Problem of Social Cost*, a permission transaction occurred when a rancher in a fencing-in state paid a neighboring farmer to release it from liability for negligently-caused harm. The agreement gave the rancher permission to engage in cattle trespass in return for a payment that compensated the farmer for the harm to its

35. In Hohfeldian terms, a permission transaction converts a prohibition into a privilege to engage in the prohibited act, while a protection transaction extinguishes a privilege to engage in a harmful act and replaces it with a prohibition or duty not to so act. See Singer, *supra* note 1, at 1049–50.

property.³⁶

By contrast, protection transactions arise when the parties contract out of a default rule that exonerates the menace from legal responsibility for the harm. In a protection transaction, the victim pays the menace not to engage in harmful activity, as, for example, by purchasing a restrictive covenant. A protection transaction occurred when the Coasean farmer in a fencing-out state paid the rancher not to graze cattle that would harm the crop. The rancher sold protection against the harm to compensate it for its cost of forbearance to raise cattle. *The Problem of Social Cost* featured both permission and protection transactions. The problem of extortion arises only in protection transactions.

B. Leverage.

The economic incentives underlying any protection transaction depend on the expected cost of the threatened harm to the victim and the expected cost of forgoing the harmful activity to the menace. Coase repeatedly emphasized that a permission or protection transaction will occur only when it is the most cost-effective way for the parties to deal with a harmful event.³⁷ A party facing harm from another party's productive activity will suffer the cost of the harm only if it has no less costly alternative. Several adaptive strategies may be available to a victim facing potential harm. It may remove itself or its property from exposure to the harm or otherwise render itself less vulnerable. It may deter the harm by making a counter-threat. Or it may seek the cooperation of the menace by its agreement to forbear from the harm. The least costly alternative to suffering the threatened harm is the true cost of an externality to that victim.³⁸

Thus, for example, suppose a factory intermittently spews smoke into the air above a neighboring beer garden. The smoke irritates the beer garden's customers and has led to reduced patronage and loss of revenue. The beer garden's lawyer has advised that the factory is legally free to emit the smoke under local land use law and the local law of nuisance. The

36. The farmer may have chosen either to have suffered the ensuing crop loss without compensation or to have engaged in different productive activities, such as growing the crop elsewhere or growing a less-vulnerable crop.

37. See Coase, *The Problem of Social Cost*, *supra* note 2, at 3 (referring to the farmer's alternatives as including fencing as well as "the employment of dogs, herdsmen, aeroplanes, mobile radio and other means . . ."); see also Coase, *Notes on The Problem of Social Cost in COASE, THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, 175-76 (describing multiple measures either party might take).

38. See Demsetz, *When Does the Rule of Liability Matter?* *supra* note 6, at 23-24 (referring to the "next best use" to which the victim can put the land absent the menace's agreement).

factory owner has ignored requests by the owner of the beer garden to reduce smoke emissions during business hours.

The beer garden might respond to this situation in several ways. It might simply absorb the loss of revenue, which represents the *prima facie* cost of the harm. But it will explore other possibly less costly ways to mitigate the harm. It might install fans to blow the smoke away. It might enclose and air-condition the drinking area. It might eliminate the beer garden and serve only indoor restaurant customers. Each measure has its own net expense to the beer garden in comparison to the *prima facie* cost of the harm.

Other responses might approach the problem more aggressively. The beer garden might resort to a counter-threat in an attempt to increase the factory's cost of polluting to the point at which polluting was no longer profitable.³⁹ The beer garden might ask political allies to bring regulatory pressure to bear on the factory, or organize a boycott of the factory or its affiliates by the beer garden customers, or start a social media campaign against the factory.

At some point the beer garden may consider a Coasean bribe, offering to pay the factory to reduce or eliminate the smoke problem. The cost of this alternative will be the amount the factory demands plus the transaction cost of the agreement.

It would be rational for the beer garden to choose from among these alternatives the one that produced the lowest total cost in expense and revenue loss. The cost it suffers by taking the best alternative is the true cost of the externality to the beer garden and represents the most that it would offer as a bribe to the factory for its forbearance in any protection transaction. This unavoidable expense is also the measure of the "leverage" that the factory has in any such transaction with the beer garden.

If a victim's actual vulnerability to harm arises only after and because of a change in circumstances, it becomes meaningful to speak of the protection transaction as taking place either before or after that change. A menace will have no leverage in an *ex ante* transaction and will have maximum leverage in an *ex post* transaction. Absent leverage, the payment in an *ex ante* protection transaction is a bribe and will always be less than the payment in an *ex post* protection exchange. The payment in

39. Coase's analysis did not consider the counter-threat strategy. For example, the farmer might sow plants poisonous to cattle near his crops or simply steal the marauding cattle. Robert Ellickson reports that ranchers in Shasta County who repeatedly permitted their cattle to trespass in their neighbors' fields sometimes lost cattle in this way to neighbors who would kill marauding cattle. Ellickson, *Of Coase and Cattle*, *supra* note 14, at 679.

an *ex post* transaction may or may not be blackmail, however, depending on whether leverage is exploited to achieve an extortion premium.

Thus, for example:

(1) Assume that Rancher and Farmer negotiate a covenant protecting Farmer's crop before Farmer has leased land adjacent to the ranch.⁴⁰ In this *ex ante* transaction, if Rancher rejects Farmer's offer of payment, Farmer may elect to lease other land adjacent to other Ranchers.⁴¹ Neither party has leverage over the other. Rancher should accept any offer greater than the cost she incurs by providing protection by reducing or relocating her herd. If other ranchers are competing for the Farmer's business in other locations, the protection will be sold at a competitive price.

(2) Assume instead that Rancher and Farmer negotiate a protection agreement after Farmer has leased land near the ranch and planted the crop. Rancher, who is now a monopolist because of Farmer's sunk costs, can insist on any price that is smaller than the amount of unavoidable harm Rancher's cattle can inflict. So long as she bears no liability for crop damage, under these conditions, it is in Rancher's interest to increase the amount of harm her cattle will inflict.

Coase's examples from hypotheticals and nuisance cases in *The Problem of Social Cost* were all *ex post* transactions.⁴² The parties were owners or lessors of land that made them vulnerable to unavoidable harm from their neighbors. Coase and Demsetz described this economic relationship as a "bilateral monopoly" because neither owner could deal with any other party to purchase or sell protection from their harmful activities.⁴³ Each of them acknowledged that excessive payments for protection could not be demanded in the presence of competition, e.g., if multiple ranchers were offering terms to a farmer before his decision about where to raise the crop.⁴⁴

40. Unlike the situation prevailing in areas with open range land, it is presumed, as it was in *The Problem of Social Cost*, that only one rancher threatens any farmer.

41. Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 23.

42. See Coase, *The Problem of Social Cost*, *supra* note 2. In addition to the conflicts between neighboring landowners engaged in ranching and farming. *Id.* at 2–8. Coase discussed disputes involving spark-emitting railroads and adjacent land owners. *Id.* at 29–34; a noisy confectionary business and a neighboring residence used as a doctor's office. *Id.* at 8–10; a chemical factory emitting fumes that caused damage to the products of a nearby fiber manufacturer. *Id.* at 10–11; a business that piled up timber so as to block air flow from the chimney of an adjacent residence. *Id.* at 11–13; a brewer producing smelly emissions that harmed a neighboring residence. *Id.* at 14; and a smelly fish and chips restaurant harming neighboring residents. *Id.* at 21.

43. Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 23.

44. Coase, *Blackmail*, *supra* note 6, at 658 (In the case of bluff threats, since the refraining from the activity is costless to the menace, the amount the victim would have to pay in a competitive market "tend[s] towards zero."); see Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 23–24 (stating that competition among protection racketeers would cause the cost of protection to drop to the cost of private security services).

C. *Cost of Forbearance*

Assume the beer garden proposes a bribe to the factory. How much will a menace demand to forbear from the harm-causing activity? The value of the privilege to emit smoke as a factor of production to the factory is equal to the cost of the factory's least expensive alternative to doing so. Just as the beer garden has several alternatives to the harmful interaction, so does the factory. It might without incurring any cost be able to emit the smoke at times when the beer garden was unoccupied. It might employ a technological solution such as an air purification system or different mode of venting the smoke. It might employ a different, perhaps costlier, smoke-free processing method. At the extreme, it might convert the factory into a beer garden or an artist's collective, with a modest drop in revenue. The actual value of the smoke emission privilege to the factory is the lowest loss of net revenue it would experience when pursuing the least costly of these alternatives. That figure represents the factory's true cost of forbearance and represents the lowest amount it would accept voluntarily to forgo smoke pollution. But of course, the factory is not required to sell smoke abatement at this price if it can obtain more from the beer garden.

The factory's lowest cost alternative to producing smoke would also determine the amount of leverage the beer garden would have against the factory if the shoe were on the other foot and the beer garden had the power to enjoin the smoke emission. The lowest cost alternative now represents the least harm the factory will suffer if it must cease emitting smoke. It thus represents the most that the factory would pay to release the injunction in a permission transaction with the beer garden to obtain smoke emitting privileges. This amount also represents the use-value value of the harm-producing activity to the factory.⁴⁵

The alternatives available to both parties not only dictate which unilateral actions they might take when facing the prospect of harmful interaction; they also provide the basis on which the parties will negotiate protection or permission agreements with each other. These negotiations will often be costly, however, because each party lacks information about the other's true costs, which may lead to inefficient failures to agree.⁴⁶ The victim will pay a bribe to the menace equal to the cost of the menace's lowest cost alternative to the harmful activity, but only if the victim has

45. See Coase, *The Problem of Social Cost*, *supra* note 2, at 44 (noting that privileges to engage in harm producing activity are valuable factors of production).

46. Coase, *Notes on The Problem of Social Cost in COASE, THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 178 (Transaction costs might prevent exchange of information necessary to efficient Coasean bargains.).

information about this cost. The alternatives that each party might reasonably consider are idiosyncratic and generally unknown to the other party. They may turn on subjective valuation and individualized technological capacities.

D. Transaction Costs

Coase considered the most important contribution of *The Problem of Social Cost* not to be the Coase Theorem but his identification of what later became known as “transaction costs.”⁴⁷ These are all of the costs parties must incur to effect an exchange, which Coase appeared to define so broadly as to include anything that prevented an exchange from occurring. Among Coase’s greatest contributions to economic theory was his recognition that economic institutions, such as the firm, were designed to economize on transaction costs.⁴⁸

As a simplifying assumption, Coase assumed that the menace and a victim could bargain costlessly to a permission or protection transaction to show that such bargaining would efficiently allocate harm-related entitlements without the need for regulation. Although Coasean bargaining works perfectly only in the imaginary world of zero transaction costs, it also operates even in the presence of significant transaction costs so long as the parties perceive their bargaining gains to exceed those costs.⁴⁹ All of the reallocative deals arising from the nuisance and trespass cases discussed in *The Problem of Social Cost* were apparently feasible in real life.⁵⁰ Transaction costs assume significance only when the externalities are widespread, as in the pollution cases, making multi-party

47. Coase, *The Problem of Social Cost*, *supra* note 2, at 15 (referring to the need for a transactor to “discover who it is that one wishes to deal with, to inform people that one wishes to deal and on what terms, to conduct negotiations leading up to a bargain, to draw up the contract, to undertake the inspection needed to make sure that the terms of the contract are being observed, and so on”); COASE, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 6 (adopting Dahlman’s later description of transaction costs as “search and information costs, bargaining and decision costs, policing and enforcement costs” (citations omitted)); *see also id.* at 9–10, 13–15.

48. OLIVER E. WILLIAMSON, *THE ECONOMIC INSTITUTIONS OF CAPITALISM* 34 (1985) (Coase’s insight nevertheless required later identification of factors relevant to transaction cost differences.).

49. Coase, *The Problem of Social Cost*, *supra* note 2, at 15–16 (“[A] rearrangement of rights will only be undertaken when the increase in the value of production consequent upon the rearrangement is greater than the costs which would be involved in bringing it about.”).

50. Or maybe not. The fact that none of the deals were actually struck in the cited cases may imply that transaction costs *must* have prevented them, especially if transaction costs are defined as whatever-prevents-a-potential-bargain. *See* COASE, *THE FIRM, THE MARKET AND THE LAW*, *supra* note 2, at 25 (arguing against the case for prima facie government regulation of externalities, if parties have not reallocated inefficient externalities by agreement, the explanation “must be” that they were prevented from doing so by transaction costs. If government has also failed to act, it must be for the same reason.).

agreements by large numbers of indeterminate victims impossible.

Coase knew that the perfect bargaining world of zero transaction costs did not exist and that in the real world, reallocative bargains would often be prevented.⁵¹ The parties' harm-related legal entitlements *do* matter in such a world because the parties often cannot contract around them.⁵² Lawmakers⁵³ and courts⁵⁴ should make such reallocative bargaining less costly where it is possible to do and, where it is not, should assign risks to coincide with their best guess about how the parties would have agreed to allocate them.⁵⁵

But Coase was deeply skeptical about the ability of lawmakers to enact property rules that would resolve the externality problem because they lacked the information necessary to do so.⁵⁶ For one thing, a fixed set of entitlements that would be economically efficient under all conditions is impossible even in theory because of fluctuation in the market prices of goods and resources and changes in technology and culture that render productive activities obsolescent.⁵⁷ In opposition to the Pigovian strategy of regulating or taxing productive externalities, Coase demonstrated that private bargaining was the only reliable way to achieve allocative efficiency in cases of incompatible land uses. No *ex ante* legal arrangement could possibly achieve the right allocation by legislative or judicial fiat. The mix of uses that maximizes the net social product of conflicting enterprises in any particular case of incompatible productive use is determined by the contingent market values of both their products and the costs of the inputs they use as well as the constantly changing costs of alternative arrangements open to both parties.⁵⁸

Coase's analysis of transaction costs may actually have given support to Pigou's advocacy of a general rule that makes menaces liable for all harm caused to victims: It is usually easier to contract out of such a rule than it is to contract out of a contrary rule giving menaces a privilege to inflict such harm without liability. The transaction costs of permission

51. Coase, *The Problem of Social Cost*, *supra* note 2, at 15–16.

52. Coase, *Notes on the Problems of Social Cost in COASE, THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 178 (“[W]ith positive transaction costs, the law plays a crucial role in determining how resources are used.”).

53. *Id.* at 17–18.

54. *Id.* at 19.

55. See Guido Calabresi & Douglas A. Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089, 1097 n.18 (1972) (referring to the “best briber” standard).

56. COASE, THE FIRM, THE MARKET, AND THE LAW, *supra* note 2, at 19.

57. *Id.* at 18.

58. Coase, *The Problem of Social Cost*, *supra* note 2, at 40.

transactions are generally lower than those relating to protection transactions because they are easier to negotiate. A menace need only obtain permission for the exact harm it intends to generate and need not pay for more than it plans to inflict. A victim purchasing protection, however, must anticipate and buy off all potential harms that the menace may be able to inflict, e.g., by changing its activity after the bribe is paid.⁵⁹ For the law to give rights to victims instead of privileges to menaces also prevents protection rackets from arising, as argued in the next section.

IV. THE CONDITIONS FOR COASEAN BLACKMAIL.

A. *Leverage*

Because the leverage represents the most that the victim will pay to avoid the threatened harm, no potential for extortion arises if the menace's cost of forbearance is equal to or greater than this amount. No protection transaction will take place under these conditions. The potential for extortion arises only when the victim faces harm that exceeds the menace's cost of forbearing from the harmful activity.

However, the cost of forbearance may be zero or even negative, if the harm does not result from an activity that is profitable for the menace to engage in. In such a case, any payment would compensate the menace for its forbearance.

B. *The Extortion Premium*

The concepts of leverage and the cost of forbearance permit an economic definition of blackmail. Blackmail exists only when and to the extent that the menace uses its harm-causing leverage to obtain *more* than its cost of forbearance from the harm. The excess of the payment over the cost of forbearance is an extortion premium. Because the amount of this premium varies from case to case, blackmail is a question of degree.

The concept of an extortion premium is not novel. Coase argued that blackmail existed to the extent that the menace demanded more than the cost of forbearance from the threat.⁶⁰ Demsetz referred to the possibility that monopoly rents would exceed a competitive price of protection in an

59. The menace is the "best briber," the party who can least expensively bribe the other party, as described by Calabresi & Melamad, *supra* note 55, at 1097 n.18.

60. Coase, *Blackmail*, *supra* note 6, at 658 (opining that the blackmail demand is the portion of the payment that exceeds the value of the foregone activity to the blackmailer.).

extortion transaction.⁶¹ Several commentators analyzing secrets blackmail have argued that “market price” blackmail should not be illegal, where the blackmailer demands only the opportunity cost of his secrecy.⁶²

The concept of an extortion premium is also consistent with the “claim of right” defense to a criminal charge of extortion.⁶³ A victim’s threat to disclose a tortfeasor’s wrongful act is not “wrongful” within the meaning of extortion law if it is made solely to compel the tortfeasor to pay compensation or return property to which the threatener believes in good faith that she has a lawful claim. It is not blackmail to say, “If you don’t compensate me for my injury, I’m going to the police and the public and tell everyone exactly how you injured me” if the statement is made in good faith.⁶⁴ However, the defense is not available if the demand is for materially more than a good faith claim for compensation.⁶⁵ Thus, for example, if a judge driving under the influence of alcohol on the way home from a party rams into my car doing \$1,000 damage and refuses to pay for repairs, it would not be extortion for me to threaten to disclose the event to the police or the public unless the judge pays for the damage. It would be extortion for me to demand \$100,000 for my secrecy.⁶⁶ The cost of my forbearance is \$1,000. The extra \$99,000 in the second example is a measure of the harm the judge will suffer, not the value of the disclosure to the threatener.⁶⁷

61. See Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 23.

62. CHARLES FRIED, *CONTRACT AS PROMISE* 102 (2d ed. 1981) (Law should permit a journalist who sells a harmful story to its target to recover his opportunity costs in not selling to the media.); Jeffrie G. Murphy, *Blackmail: A Preliminary Inquiry*, 63 *MONIST* 156, 164–65 (1980) (opining that a potential secrets blackmailer who would otherwise sell the story to the media should be allowed to offer a right of first refusal to the victim); Joseph Scalise, Jr., Comment, *Blackmail, Legality, and Liberalism*, 74 *TUL. L. REV.* 1483, 1503 (2000) (opining that market price blackmail excites “no moral outrage”).

63. See MODEL PENAL CODE § 223.4 (AM. LAW INST. 2018) (“It is an affirmative defense to prosecution based on paragraphs (2), (3) or (4) that the property obtained by threat of accusation, exposure, lawsuit or other invocation of official action was honestly claimed as restitution or indemnification for harm done in the circumstances to which such accusation, exposure, lawsuit or other official action relates, or as compensation for property or lawful services.”).

64. See *United States v. Jackson*, 180 F.3d 55, 70–71 (2d Cir.), *rehearing at* 196 F.3d 383 (1999) (recognizing claim-of-right defense to extortion but requiring nexus between threatened disclosure and source of claim).

65. See *United States v. Jackson*, 196 F.3d 383, 388–89 (2d Cir. 1999) (holding that where the defendant had no good faith claim to amount sought and no good faith belief in a claim of right, threat to disclose out of wedlock child of famous actor was extortion and failure to instruct jury on claim of right defense was harmless error).

66. The claim of right defense also requires a nexus between the harm and the disclosure. It is extortionate to threaten the judge with disclosure of the auto accident unless she pays me money that I believe she owes me for political campaign advertising services. *Jackson*, 180 F.3d at 70–71.

67. The amount demanded has occasionally been thought relevant to the presence or absence of extortion. Coase quoted Lord Roche in *Thorne v Motor Trade Ass’n*, 1937 App. Cas. 797, 818, to the

Thus, an extortion premium may be demanded for refraining from an act that is profitable to the actor if the amount demanded exceeds that profit. Yet, under existing law, a threat is not considered to be extortionate unless the threatened activity is one that will not benefit the threatener.⁶⁸ Most analyses of blackmail stipulate that the threatened activity is one that is engaged in solely to harm the victim. But when the threatener makes a profit from its ability to harm the victim, the foregone benefit is irrelevant to the wrongfulness of the demand.

V. THE LAW OF EXTORTION.

A. *The Threat Requirement*

Both the criminal law of extortion and blackmail⁶⁹ and the contract doctrine of duress⁷⁰ require a threat as an element of the offense or tort. A threat communicates the menace's willingness to engage in the harmful act unless it is paid to refrain from it. If truthful, this information reduces the transaction costs of a protection exchange by giving the victim information about the menace's conditional intentions. A warning or an offer can communicate the same information and can have the same value in reducing the transaction costs of the exchange.

Ex post protection agreements, like other contracts, are often formed by offer and acceptance. When a victim offers money for a menace's forbearance, the exchange resembles any other purchase of valuable property and the menace who accepts this offer is blameless. But a menace who "offers" protection to a victim on the same terms may have made a "threat," with dramatically different legal consequences. Consider the

effect that the "demand of a sum extortionate in amount would . . . clearly be evidence . . . in a civil case of an intent to injure as opposed to an intent to protect trade interests and in a criminal case of the fact that the sum was demanded without reasonable or probable cause . . ." Coase, *Blackmail*, *supra* note 6, at 668.

68. MODEL PENAL CODE § 223.4(3), (7) ("A person commits theft [by extortion] if he purposefully obtains property of another by threatening to . . . (3) [expose harmful secrets]; or . . . (7) inflict any other harm which would not benefit the actor.").

69. *Id.* ("A person commits theft [by extortion] if he purposefully obtains property of another by threatening to . . . (3) [expose harmful secrets] or . . . (7) inflict any other harm that would not benefit the actor."); 18 U.S.C. § 873 (2012) (punishing anyone who receives payment "under a threat of informing" against any violation of federal law); 18 U.S.C. § 1951(b)(2) (2012) (Extortion consists of "the obtaining of property from another, with his consent, induced by wrongful use of actual or threatened force, violence, or fear, or under color of official right.").

70. RESTATEMENT (SECOND) OF CONTRACTS (AM. LAW INST. 1981) [*hereinafter* "RESTATEMENT (SECOND) CONTRACTS"] § 175(1) ("If a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim."); *Id.* at § 176(1) (stating when a threat is improper).

following pairs of examples:

1A: Upon leaving his job, an employee threatens that he will expose a secret harmful to his employer unless he is paid a sum of money. The employee thereby commits blackmail.⁷¹

1B: An employer offers severance pay to a departing employee conditioned on his agreement not to expose its harmful secrets.⁷² The resulting agreement is not unlawful and in accepting payment on these terms, the employee does not commit blackmail.

2A: An employer threatens to terminate an at-will employee unless she releases a tort claim against it. If she agrees, the employee may later avoid the release under the doctrine of duress.⁷³

2B: An at-will employee, without being threatened, offers to release a tort claim against her employer in return for a promise of continued employment. If the employer accepts the offer, the employee is bound by the release.⁷⁴

3A: During discovery a plaintiff in a products liability lawsuit obtains evidence of the defendant's potential liability to other claimants. Plaintiff threatens to publicize the evidence unless defendant agrees to an excessive settlement. Plaintiff may be guilty of extortion and the agreement is voidable because of duress.⁷⁵

71. *State v. McInnes*, 153 So.2d 854, 859 (Fla. Dist. Ct. App. 1963) (holding that employee's threat to expose employer's tax fraud constituted extortion). *See also* *Berger v. Berger*, 466 So.2d 1149, 1151 (Fla. Dist. Ct. App. 1985) (holding that husband's threat to expose wife to IRS for tax fraud constituted duress permitting her to avoid settlement agreement). This example, and the next three were cited in DeLong, *Second Paradox*, *supra* note 7, at 1685–86.

72. Such agreements have long been common. Alan E. Garfield, *Promises of Silence: Contract Law and Freedom of Speech*, 83 CORNELL L. REV. 261 (1998) (considering limits on enforceability); Julia Preston, *Laid-Off Americans, Required to Zip Lips on the Way Out*, *Grow Bolder*, N.Y. TIMES, (June 11, 2016), <https://www.nytimes.com/2016/06/12/us/laid-off-americans-required-to-zip-lips-on-way-out-grow-bolder.html> [<https://perma.cc/3DJJ-2T9M>].

73. *Mitchell v. C.C. Sanitation Co.*, 430 S.W.2d 933, 938 (Tex. Civ. App. 1968); *United States v. Smith*, 228 F. Supp. 345, 353 (E.D. La. 1964); RESTATEMENT (SECOND) CONTRACTS § 176, cmt. E, illus. 11. *See also* *Laemmar v. J. Walter Thompson Co.*, 435 F.2d 680, 682 (7th Cir. 1970) (threatening to fire at-will employees to force employees to sell their shares of employer stock might constitute duress); *Perkins Oil Co. v. Fitzgerald*, 121 S.W.2d 877, 885 (1938) (employee's release voidable where obtained by employer's threat to terminate his stepfather). *Cf.* *Simko, Inc. v. Graymar Co.*, 464 A.2d 1104, 1108 (Md. Ct. Spec. App. 1983) (non-compete agreement signed by employee under threat of firing held enforceable against competing business; no duress found); *Price v. Carmack Datsun, Inc.*, 485 N.E.2d 359, 361 (Ill. 1985) (retaliatory discharge for filing claim under employer's group health policy not tortious).

74. *See* *Reiver v. Murdoch & Walsh, P.A.*, 625 F. Supp. 998, 1013 (D. Del. 1985) (enforcing at-will employee's release of claim for bonus given in return for promise of continued employment). Such a transaction may, for example, represent the terms of the settlement of a tort claim, agreeable to and desired by both parties. RESTATEMENT (SECOND) OF CONTRACTS § 74(2), cmt. e (abandonment of claim known to be invalid is consideration if bargained for and made in signed writing).

75. *See* *State v. Harrington*, 260 A.2d 692, 700 (Vt. 1970) (holding threat to use secret

3B: During discovery a plaintiff in a products liability lawsuit obtains evidence of defendant's potential liability to many similar claims. Worried about its potential liability to other claimants, the defendant offers to pay plaintiff an excessive settlement conditioned upon plaintiff's agreement not to disclose the evidence. Plaintiff is not guilty of extortion and the agreement is enforceable.⁷⁶

4A: A landowner threatens her neighbor that, if he does not pay her, she will erect a structure on her property that will block the neighbor's valuable view. If he promises to pay her, his promise will be unenforceable if her threat is deemed to be wrongful under the doctrine of duress.⁷⁷

4B: A landowner, wanting to assure the valuable view from his property, offers to purchase an easement from his neighbor that prohibits her from erecting structures that would block his view.⁷⁸ If she agrees, his promise to pay for the easement is enforceable.

5A: A vendee seeking to be released from a land contract threatens the vendor that it will resell the land to a known polluter unless the vendor releases it from the contract. The vendee's threat constitutes duress and the release is unenforceable.⁷⁹

5B: A vendor/developer requires vendees of houses in the

information to obtain favorable settlement in divorce action constituted extortion).

76. On the public policy implications of non-disclosure agreements see Ryan M. Philp, Comment, *Silence at Our Expense: Balancing Safety and Secrecy in Non-Disclosure Agreements*, 33 SETON HALL L. REV. 845 (2003).

77. Entrepreneur Mark Zuckerberg reportedly purchased a neighbor's lot for twice its value in response to a threat to construct a house near the property line that would have a direct view into Zuckerberg's bedroom. The neighbor allegedly "offered" to sell the lot at an inflated price before construction to preserve Zuckerberg's privacy. Zuckerberg then reportedly purchased three other surrounding properties, apparently to forestall future threats. Sophie J. Evans, *Mark Zuckerberg's Fight for Bedroom Privacy: Inside Facebook Billionaire's Battle with Backdoor Neighbor Who Sold Him His California Property 'At a Discount Rate in Exchange for Entrée into Silicon Valley's Elite'*, U.K. DAILY MAIL (Feb. 10, 2015), <http://www.dailymail.co.uk/news/article-2947711/Mark-Zuckerberg-s-fight-bedroom-privacy-Inside-Facebook-billionaire-s-battle-backdoor-neighbor-sold-California-property-discount-rate-exchange-entree-Silicon-Valley-elite.html> [https://perma.cc/9ZRY-9P5K]. Such threats would constitute wrongful threats under the contract doctrine of duress. See RESTATEMENT (SECOND) OF CONTRACTS § 176 cmt. e, illus. 10 (for purposes of duress, a threat to use property in such a way would be "wrongful"). See R. NOZICK, ANARCHY, THE STATE, AND UTOPIA 84-85 (1974) (A neighbor's purchase of abstention from one who otherwise plans to erect a "monstrosity" is a productive exchange but not if the neighbor threatens to erect it just to extort a payment); A. H. Campbell, *The Anomalies of Blackmail*, 15 L. Q. REV. 382, 388 (1939) (similarly). The example assumes that the neighbor's threatened action was legally privileged, so that the landowner could not enjoin the structure as a nuisance or under the rules relating to "spite" structures.

78. See NOZICK, *supra* note 77, at 84.

79. RESTATEMENT (SECOND) CONTRACTS § 176 cmt. e, illus. 10. *Wolf v. Marlton Corp.*, 154 A.2d 625, 630 (N.J. Super. Ct. App. Div. 1959) (Vendee under real estate contract threatened to resell to "undesirable" purchasers relieved seller from duty to return down payment).

development to agree to mutual restrictive covenants not to resell to known polluters. In accepting the contracts on these terms, the vendees have not exercised duress and the agreements are enforceable.

6A: A purchasing agent threatens a sales agent that if he does not pay her, she will prevent her company from purchasing his company's products. If he pays her, then he may not be guilty of bribery and she may have committed extortion.⁸⁰

6B: On the belief that otherwise he cannot make a sale, a sales agent pays a purchasing agent to induce her to buy his company's products. Not having been threatened, the sales agent has probably committed commercial bribery and the purchasing agent's principal may recover the bribe from the sales agent in a claim for restitution.⁸¹

These protection exchanges raise problems in the areas of criminal, contract, tort, and property law. In each case, one of the parties is a menace as defined in this Article, who has a legal privilege to take some action that would inflict harm on the other party, the victim, without incurring liability to the victim for the harm. Each exchange is substantively identical, extinguishing the menace's harmful privilege in return for a payment by the victim, who pays to avoid the threatened harm. In each pair of examples, the first, legally-disfavored exchange was initiated by a threat made by the menace and the second, legally-favored exchange was initiated by an offer made by the victim. Each pair of protection agreements exemplifies a single rule: A protection exchange induced by a menace's threat is illegal while the same exchange induced by an unthreatened victim's offer is enforceable. This paradox, already identified in the law of secrets blackmail,⁸² applies to the entire range of demands for money in return for forbearing to exercise a harmful privilege in a Coasean exchange. The judicial use of the threat requirement to discriminate between blackmail and benign Coasean bargaining is ubiquitous.⁸³

80. *Kraft Gen. Foods v. Cattell*, 18 F. Supp. 2d 280, 287 (S.D.N.Y. 1998) (holding it would be a defense to a civil claim of commercial bribery if plaintiff's purchasing agent threatened seller with ruinous refusal to deal after he had become dependent on her business).

81. *Williams Elecs. Games, Inc. v. Garrity*, 366 F.3d 569, 580 (7th Cir. 2004) (holding buyer had claim of restitution against seller's agent who bribed buyer's agent to purchase goods from seller's principal, unless buyer ratified the bribe).

82. DeLong, *Second Paradox*, *supra* note 7, at 1663. See Kathryn H. Christopher, *Toward a Resolution of Blackmail's Second Paradox*, 37 ARIZ. ST. L.J. 1127, 1129 (2005) (criticizing later theories of blackmail that attempt to resolve the second paradox and arguing that the paradox should not be resolved by criminalizing the menace's acceptance of a bribe).

83. See James Lindgren, Symposium, *Theory, History, and Practice of the Bribery-Extortion Distinction*, 141 U. PA. L. REV. 1695, 1702-03 (1993) [hereinafter Lindgren, *Bribery-Extortion Distinction*] (studying the sometimes narrow distinction between bribery and extortion by public

B. The Mixed Effects of the Threat Requirement.

The ease of application of the threat requirement is illusory once one departs from unproblematic cases. Although a threat requires interpretation to distinguish it from similar expressions that convey warnings or other information, threats are notoriously difficult to interpret. What appears to a court to be a threat by a menace may be, and be accurately understood by the parties to be, only a warning and an offer. What appears to a court to be an offer of a bribe by a victim who has not been expressly threatened may be, and be accurately understood by the parties to be, submission to an implied threat by a menace, motivated by fear of harm.⁸⁴

The use of leverage to extract an extortion premium does not always require a threat. A protection exchange may be initiated by an unthreatened victim who learns of a risk posed by a potential menace and who approaches the menace seeking an agreement to forbear from the harmful action. The menace, appreciating the situation, may refuse to agree unless the victim pays a substantial amount of the cost of harm the menace may inflict if it acts.⁸⁵

The threat requirement in the law of extortion has mixed incentive effects on protection transactions, making its net economic costs and benefits uncertain.⁸⁶ Inhibiting a menace's threats will also inhibit its good faith warnings and offers to forgo a harmful action at a reasonable price. The law of extortion thus prevents the utility gains that would result from menace-initiated protection transactions.

But some efficiency gains may result from the law's prevention of threats. Without the ability to induce a protection transaction by means of a threat, potential extortionists would have less incentive to develop protection rackets. The expected profitability of engaging in harm-producing activity is reduced if the menace cannot actively induce the protection transaction and must await the offer of an unthreatened victim. Thus, while the threat requirement may inhibit some efficiency-producing protection transactions, it may make up for that loss in utility by preventing

officials and also noting the initiator of transaction irrelevant to bribery or extortion). James Lindgren disagrees that transactions initiated by the victim are not blackmail. See James Lindgren, *Blackmail: On Waste, Morals, and Ronald Coase*, 36 UCLA L. REV. 597, 603 (1988) [hereinafter Lindgren, *On Waste*] (analyzing as blackmail an employee's acceptance of another employee's bribe to keep a guilty secret). His analysis of the Hobbs Act led him to conclude that the bribery/blackmail distinction was spurious. *Id.*

84. Lindgren, *Bribery-Extortion Distinction*, *supra* note 83, at 1716–17.

85. Christopher, *supra* note 82, at 1149 (blackmailer's counter-offer).

86. Some of these points appeared in DeLong, *Second Paradox*, *supra* note 7, at 1677–78.

protection rackets. The problem is, as usual, that the empirical evidence to resolve this question is lacking.

Inhibiting threats might also inhibit bluffs in which a menace threatens to engage in a harmful act without the intention of doing so.⁸⁷ Bluffs and the possibilities of bluffs raise transaction costs of both victims and menaces, as they strive to verify threats and unmask bluffs. Because bluffs arise only when menaces make threats, and not when victims make offers, the costs of bluffing will tend to be lower when threats are inhibited by extortion law. This is especially true when a menace must make a significant investment in making a bluff threat credible.

From a non-economic, normative perspective, the threat requirement may be an essential element of extortion because we are unwilling to punish a party who merely refuses to assent to a protection transaction for any payment that is less than the extortion premium. A hold-out who does not initiate the negotiation over a protection transaction by making a threat is not an extortionist despite demanding an extortion premium. So long as the victim makes the first offer and the menace merely refuses to sell before the victim names her price, she usually escapes both legal and moral censure.⁸⁸ Deep-seated norms of property ownership give every owner an unreviewable right and privilege to refuse to sell. Harm-related entitlements are property or liberty interests and under current law it is not extortion for their owners to refuse to extinguish them except in return for a price they choose to set.

VI. A THEORY OF BLACKMAIL AS UNJUST ENRICHMENT.

A. *Unjust Enrichment*

The normative theory of blackmail advanced by this Article is that the wrongfulness of a menace's extraction of an extortion premium arises because it is obtained by threats of harm and is measured by the harm the menace can cause the victim. To profit from a wrongful threat of harm is itself wrongful and makes the recipient liable to an action for restitution.⁸⁹

87. *Id.* at 1678.

88. *But see* Eric A. Posner & E. Glen Weyl, *Property is Only Another Name for Monopoly*, 9 J. LEGAL ANALYSIS 51 (2017) (proposing a forced sale and taxing solution to gouging by holdout owners). Posner and Weyl note the inefficiencies caused by the natural monopoly created by real property ownership, and conclude, surprisingly, that "allocative efficiency and . . . efficient market economy [are] impossible in the presence of property ownership."

89. RESTATEMENT (SECOND) OF CONTRACTS § 176 (2)(a), (c) ("A threat is improper if the resulting exchange is not on fair terms, and (a) the threatened act would harm the recipient and would not significantly benefit the party making the threat . . . or (c) what is threatened is otherwise a use of

The law typically strips wrongdoers of unjust enrichment to remove the incentive from actions deemed to be socially harmful. The claim is limited to restitution of the extortion premium and does not extend to the entire payment made to the menace, because only the excess over the menace's true cost of forbearance is wrongfully obtained.

Restitution to prevent unjust enrichment rests on a normative basis that is different from that which supports compensation for injury resulting from breach of a duty. Traditionally, a party is entitled to restitution to prevent the defendant from profiting by his own wrongful act at the plaintiff's expense.⁹⁰ The measure of the remedy is the amount of benefit the defendant has enjoyed rather than the harm to the plaintiff. In some cases, plaintiff has suffered no provable harm by the defendant's wrongful action,⁹¹ yet, it is not just that the defendant retains the profit from the wrong. The wrongfulness of the blackmailer's receipt of the extortion premium does not lie in the illegality of the action the blackmailer threatens, which is assumed to be non-criminal and non-tortious. Nor is it merely the extraction of a monopolist's profit as a natural incident of property ownership. Nor does it arise merely from the making of a threat to do something harmful that one has a privilege to do. The wrongfulness is the deliberate obtaining of the portion of the payment attributable solely to the harm the blackmailer can inflict on the payer. Society has made the judgment that the blackmailer is entitled to be compensated for the cost of his forbearance, but he is not entitled to profit from the pain he can cause the victim.

The unjust enrichment analysis also addresses one of the puzzles of blackmail. How can blackmail harm the victim if the victim would prefer to make the blackmail payment rather than suffer a harm that he has no legal right to prevent? If the victim is not harmed, then why does the law prevent the transaction? The answer is that prevention of harm to the victim is not the norm that the law of blackmail should address. The prevention of unjust enrichment rests on a different footing from

power for illegitimate ends.”). *Id.* at § 376 (restitution of benefit conferred pursuant to a contract voidable because of duress); RESTATEMENT (THIRD): RESTITUTION AND UNJUST ENRICHMENT § 14 (AM. LAW INST. 2011) (transfer induced by duress, defined as coercion that is wrongful as a matter of law subject to restitution to avoid unjust enrichment).

90. RESTATEMENT (THIRD): RESTITUTION AND UNJUST ENRICHMENT § 3 (No person is permitted to profit by his own wrong).

91. *Snapp v. United States*, 444 U.S. 507, 516 (1980) (holding former CIA operative was unjustly enriched by royalties from book he published without having secured pre-publication approval required by his contract without need to show harm to government interests); *Edwards v. Lee's Adm'r*, 96 S.W.2d 1028, 1033 (Ky. 1936) (ordering restitution for profits made from subterranean trespass of which plaintiff was unaware).

prevention of harm to the victim because it focuses on preventing the blackmailer from profiting from wrongful exploitation of his privilege to harm the victim.

B. Coase and Demsetz on Blackmail.

Coase and Demsetz initially answered critics who accused Coasean bargainers of extortion by insisting that extortion is a legal, not an economic concept.⁹² What the law might label “extortion” in Coasean bargaining was, on closer analysis, simply the extraction of monopoly rents by the menace. The farmer and rancher were in a bilateral, locational monopoly because they owned⁹³ adjacent land: neither could deal with a third party on the matter of the cattle-caused crop damage. So long as the menace threatens to do only what it is otherwise lawful for it to do, the price it demands for forbearance is no more problematic than the price demanded by any other monopolist. In any event, the blackmail payment does not affect the efficient allocation of resources despite shifting wealth between the parties.⁹⁴ However, the existence of transaction costs means that the blackmail transaction can lead to wasted resources.⁹⁵

A protection transaction becomes economic extortion for Demsetz only when the threatened harmful activity has no social value, as when extortionists threaten to destroy property, or the threat is a bluff. Even in these cases, however, Demsetz strongly cautioned against regulating protection transactions as extortionate if the activity being suppressed was an activity that normally had productive value to the menace because of the risk of erroneous determination that the activity would not have had productive value in any particular case.⁹⁶

In an article written after *The Problem of Social Cost*,⁹⁷ Coase acknowledged that he had discounted the problem of extortion in harm-

92. Coase, *Blackmail*, *supra* note 6, at 656–58 (1988); Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 24 (cautioning economists that extortion and blackmail are “legal and not economic distinctions”). See also Demsetz, *Wealth Distribution*, *supra* note 6, at 230–32 (observing that “[m]any activities that seem outwardly identical to those that we identify as extortionate are perfectly legal”).

93. It is unclear whether the rancher owned the ranch land or merely had grazing rights there nor is it clear whether the farmer owned or merely leased the cropland. In all cases, the bargain was *ex post* because neither party could avoid dealing with the other for the current growing season.

94. Coase, *The Problem of Social Cost*, *supra* note 2, at 8.

95. Coase, *Blackmail*, *supra* note 6, at 671 (When transaction costs are positive “[i]t is obviously undesirable that resources should be devoted to bargaining which produces a situation no better than it was previously.”).

96. Demsetz, *When Does the Rule of Liability Matter?*, *supra* note 6, at 25.

97. Coase, *Blackmail*, *supra* note 6, at 673–74.

related bargaining between productive enterprises for two reasons. First, “extortionate” protection exchanges which result from strategic bluffs in bilateral monopolies have no impact on efficient reallocation in a world of zero transaction costs.⁹⁸ Second, the potential for “extortionate” protection or permission transactions will exist regardless of which party is assigned the harm-related entitlement.⁹⁹ In regard to secrets blackmail, Coase thought that the blackmail transaction was economically wasteful, but that its mere wastefulness was not a sufficient justification for its illegality.¹⁰⁰

C. Other Theories of Blackmail

Legal commentators have been less sanguine than Coase and Demsetz about the potential for blackmail in Coasean protection transactions. Concerned about both its legal and economic effects, they have sought to identify and distinguish extortionate transactions from the benign bribes described in *The Problem of Social Cost*. These analysts, most of whom focused on secrets blackmail rather than nuisance, have divided into two camps. Those in the larger camp argue in favor of the existing legal prohibition of blackmail, focusing their criticisms on reasons to outlaw strategic threats of harm that are made solely to exact blackmail payments.¹⁰¹ But these analysts have been forced to accept the legality of the far more common exploitation that can result from situations in which

98. Coase, *THE FIRM, THE MARKET, AND THE LAW*, *supra* note 2, at 162–63; Coase, *Blackmail*, *supra* note 6, at 671 (In the absence of transaction costs, “the payment of blackmail leaves the allocation of resources unaffected and the value of production is maximized.”).

99. Coase, *Blackmail*, *supra* note 6, at 656–57 (noting that actions undertaken solely for the purpose of being paid not to engage in them the potential exploitation of legal entitlements would exist regardless of how the law allocated them).

100. Coase, *Blackmail*, *supra* note 6, at 673–74.

101. Richard Epstein, *Blackmail, Inc.*, 50 U. Chi. L. Rev. 553, 555–57 (1983) [hereinafter Epstein, *Blackmail, Inc.*] (arguing that legalizing blackmail would foster wrongful behavior like fraud and violence); James Lindgren, *Unraveling the Paradox of Blackmail*, 84 COLUM. L. REV. 670, 670 (1984) [hereinafter Lindgren, *Unraveling the Paradox*] (arguing that blackmail is unlawful because the blackmailer exploits the rights of third parties to sanction the victim); Richard Posner, Symposium, *Blackmail, Privacy, and Freedom of Contract*, 141 U. PA. L. REV. 1817, 1820 (1993) (arguing from an economic perspective that blackmail should be unlawful because it is a coercive wealth-reducing transfer that has a sterile redistributive effect); Douglas Ginsberg & Paul Schectman, *Blackmail: An Economic Analysis of the Law* (1993) (arguing that blackmail diverts resources solely for wealth redistribution purposes); DeLong, *Second Paradox*, *supra* note 7, at 1689–91 (arguing that blackmail is made unlawful because of its social meaning rather than its economic effects). Some theorists have broadened their analyses of coercion beyond secrets blackmail. LEO KATZ, *ILL-GOTTEN GAINS*, 133–97 (1996) [hereinafter Katz, *Ill-Gotten Gains*] (extensive discussion of the paradoxes of blackmail and other forms of misbehavior from a deontological perspective); Daniel B. Kelly, *Strategic Spillovers*, 111 COLUM. L. REV. 1641 (2011) (focusing on nuisance cases, in which parties threaten to create costly, otherwise unprofitable nuisances in order to extract extortionate payments).

the menace profits from its harmful activity but sells its forbearance at a much higher price. They also must contend with transactions that are initiated and avidly sought by the victims.

A smaller group of analysts have grasped the nettle and argued that the blackmail should be legalized, so long as what is threatened is not tortious or criminal.¹⁰² Because blackmail transactions benefit both the menace and the victim, they are utility-maximizing and for that reason should be legal and enforceable.¹⁰³ If the law will not protect the victim from the menace's harmful activity, the victim should be able to purchase protection from the menace at a price the victim is willing to pay and the menace is willing to accept. These theories are economically rational but are compelled to dismiss the widespread public disapprobation of extortion as misguided or naive. They must also accept the dead weight economic loss that protection rackets create by incentivizing people to allocate scarce resources to otherwise pointless harm-causing and harm-preventing activities.

Most blackmail and extortion theories are designed to address what has been called the paradox of secrets blackmail: why is it illegal to obtain money by threatening to do what you have a legal right to do?¹⁰⁴ The paradox is admittedly perplexing. Without incurring liability, the secrets blackmailer may or may not disclose the secret; she may or may not threaten to disclose it; she may or may not agree not to disclose it; she may or may not accept a bribe not to disclose it. The only thing that she may not do is to demand money for not disclosing it. How can the blackmail exchange be wrongful if all of its elements are separately legal and if both parties prefer it to the menace's disclosure of the secret? Most theories of blackmail agree that it should be illegal and struggle to rationalize its paradox.¹⁰⁵

102. See discussion *infra* note 108.

103. *Id.*

104. For a survey of theories that address this issue, see ALAN WERTHEIMER, COERCION, 90–103 (1987) (concluding tentatively that the wrongfulness lies in the blackmailer's proposal rather than the action proposed in the threat). See also NOZICK, *supra* note 77, at 84–86 (Blackmail is wrong not because it harms the victim but because it leads to a pointless, yet costly transfer of money.).

105. Most anti-blackmail analyses are concerned with secrets blackmail and have little application to other forms of extortion. Epstein, *Blackmail, Inc.*, *supra* note 101, at 553 (arguing that legalizing blackmail would foster wrongful behavior like fraud and violence); Lindgren, *Unraveling the Paradox*, *supra* note 101, at 670 (arguing that blackmail is unlawful because the blackmailer exploits the rights of third parties to sanction the victim); Scott Altman, Symposium, *A Patchwork Theory of Blackmail*, 141 U. PA. L. REV. 1639, 1639 (1993) (arguing that no single theory explains outlawing blackmail, making the rule inherently over- and under-inclusive); DeLong, *Second Paradox*, *supra* note 7, at 1689–91 (arguing that secrets blackmail is made unlawful because of its social meaning rather than its economic effects). See generally, Leo Katz & James Lindgren, Symposium, *Blackmail: Instead of a Preface*, 141 U. PA. L. REV. 1565, 1565–89 (1993). Some

Law and economics scholars justify the prohibition of blackmail as a way of saving the economic waste that would result from widespread secrets blackmail transactions.¹⁰⁶ As one expressed it, the secrets blackmail transaction is a pointless waste of resources spent in digging up dirt just to agree to bury it again.¹⁰⁷ However, such arguments have become anachronistic in an age when both commercial and private actors are increasingly concerned with the protection of information from discovery and misuse. Given the much greater interests at stake in these efforts, it strains credulity to believe that the marginal costs of espionage and counter-espionage would increase if blackmail were legalized.

Economic arguments about the efficiency of blackmail laws are inconclusive even on their own terms. *The Problem of Social Cost* showed that protection transactions can produce exchange surplus, which would be lost if protection transactions are prevented by laws against blackmail. Outlawing blackmail is economically justifiable only if the unknowable economic waste saved by its prohibition exceeds the unknowable lost surplus from protection transactions that blackmail laws prevent.¹⁰⁸ Coase repeatedly complained about the use of “blackboard economics” that was uninformed about actual institutions that it purported to describe.¹⁰⁹ The blackboard economics of secrets blackmail analysis is completely uninformed by empirical fact.

Finally, economic arguments relating to blackmail all miss what is invisible to economics, the sense that the blackmailer has wrongfully harmed the victim.¹¹⁰ Arguments based on economic waste are an insufficient normative reason to treat blackmail as a felony.¹¹¹

Recognizing the value of Coasean protection transactions to both the menace and the victim, several theorists have argued that the law should be changed and blackmail should be legalized so long as what is threatened

theorists have broadened their analyses of coercion beyond secrets blackmail. Katz, *Ill-Gotten Gains*, *supra* note 101, at 133–97 (explaining paradoxes of blackmail and similar forms of misbehavior from a deontological perspective); Kelly, *supra* note 101, at 1645 (focusing on nuisance cases, such as the “livery stable” scam, in which parties threaten to create costly, otherwise unprofitable nuisances in order to extract extortionate payments).

106. Ginsberg & Schectman, *supra* note 101 (arguing that, where the blackmailer stands to gain nothing by the threat, legalizing blackmail would lead to wasteful investments by potential menaces and potential victims); Posner, *supra* note 101 (arguing that legalizing blackmail would lead to inefficient over-enforcement of the criminal laws against the crimes of which the blackmailer threatens to accuse the victim).

107. Ginsberg & Schectman, *supra* note 101.

108. DeLong, *Second Paradox*, *supra* note 7, at 1677–79.

109. Coase, *The Firm, the Market, and the Law*, *supra* note 2, at 28–31.

110. Coase, *Blackmail*, *supra* note 6, at 675 (referring to blackmail as “moral murder”).

111. DeLong, *Second Paradox*, *supra* note 7, at 1689.

is not itself tortious or criminal.¹¹² Walter Block has long espoused an iconoclastic, libertarian view that informational and other forms of blackmail transactions should be legal.¹¹³ Block finds that the legal prohibition of secrets blackmail is irrational, justified neither by economic nor moral reasoning. An information blackmailer threatens to do nothing that is wrongful or illegal, unlike an extortionist who threatens a victim with physical harm or property damage. The victim of a secrets blackmailer has no legal entitlement to confidentiality and is willing if not eager to pay the blackmailer's price to prevent disclosure, which would cause the victim much greater harm or loss. The ostensible beneficiaries of the law against blackmail are the victims, who are in fact harmed by legal prohibition of what may be the only way they can avoid the risk of disclosure.

The most recent defense of Coasean bargaining (although they do not use this term) has been made by Oren Bar-Gill and Omri Ben-Shahar, who apply Block's victim-centered analysis not to secrets blackmail but to commercial coercion and the contract doctrine of duress.¹¹⁴ Bar-Gill and Ben-Shahar define "credible coercion" as a demand based on a threatened harmful act that the menace is likely to carry out because the act will benefit the menace.¹¹⁵ A non-credible threat, or a bluff, is a threatened act that a menace is not likely to carry out because the act would be costly to the menace. Victims ought to be free to pay menaces to forgo credible threats because the exchange will make both parties better off than if the threat were carried out. These exchanges will be prevented if the parties

112. See Walter Block & Robert W. Gordon, *Blackmail, Extortion, and Free Speech: A Reply to Posner, Epstein, Nozick, and Lindgren*, 19 Loy. L.A. L. Rev. 37 (1985) (criticizing theories that blackmail should be illegal); Russell Hardin, Symposium, *Blackmailing for Mutual Good*, 141 U. PA. L. REV. 1787, 1794 (1993) (offering a limited endorsement of certain types of blackmail, such as plea bargains, from an institutional perspective and arguing that outlawing blackmail penalized some victims, threatened with exposure in the press); F.E. Guerra-Pujol, *The Problem of Blackmail: A Critique of Coase, and the Case for Blackmail Markets*, 5 CRIT. 1 (2012) (arguing for the creation of markets in secrets and discounting moral intuitions that blackmail is wrongful); Wolfgang Buchholz and Christian Haslbeck, *Strategic Manipulation of Property Rights in Coasean Bargaining*, 153 J. INST. & THEORETICAL ECON. 630 (1997); Medema, *supra* note 6. Making a broader argument that extortionate transactions should usually be legally enforced are Oren Bar-Gill & Omri Ben-Shahar, *Credible Coercion*, 83 TEX. L. REV. 717 (2005) [hereinafter Bar-Gill & Ben-Shahar, *Credible Coercion*]; and Oren Bar-Gill & Omri Ben-Shahar, *The Law of Duress and the Economics of Credible Threats*, 33 J. LEGAL STUD. 391 (2004) [hereinafter Bar-Gill & Ben-Shahar, *The Law of Duress*].

113. Block has written over twenty articles in this vein. Most are cited in Walter Block & Robert W. McGee, *Blackmail from A to Z: A Reply to Joseph Isebergh's "Blackmail from A to C"*, 50 MERCER L. REV. 569, 570–71 n. 2 (1999); Block & Gordon, *supra* note 112, at 37. Block disagreed with Coase's arguments in favor of outlawing blackmail. See also Hardin, *supra* note 112, at 1787 (condoning certain mutually beneficial blackmail exchanges).

114. Bar-Gill & Ben-Shahar, *Credible Coercion*, *supra* note 112, at 717; Bar-Gill & Ben-Shahar, *The Law of Duress*, *supra* note 112, at 391.

115. Bar-Gill & Ben-Shahar, *Credible Coercion*, *supra* note 112, at 718.

anticipate that they will be nullified by courts applying the law of extortion or contract duress. This dooms victims of credible threats to suffer the greater harm that they could otherwise have prevented in a protection exchange.

Again, however, this argument rests on untestable empirical assumptions. Bar-Gill and Ben-Shahar suggest that under existing law, menaces will refuse to offer their victims protection because they anticipate that victims of extortion and duress might later avoid their deals and recover their ransom payments after the threat is removed. The uncertainty of the law of duress works to the detriment of both parties by inhibiting good faith, non-exploitative, warning-offers along with threat-offers.

But are parties to a contract actually inhibited by the doctrine of duress? Consider a seller who faces unexpected cost increases and who anticipates that without a price increase, it will be forced to breach a supply contract. This seller has an economic incentive to inform the buyer and offer to perform at a higher price in an effort to minimize its liability for damages if it breaches. A rational seller will make this credible threat despite the risk that the buyer may later renege on the deal and seek avoidance under the doctrine of duress. Such threats seem to be frequently made despite the existing rules on duress that make such transactions potentially voidable. It is unlikely that law of contract duress actually inhibits a significant amount of renegotiation by parties in such cases. Nor is it likely that any utility lost as a result of such inhibiting effect is greater than the utility the duress rule *gains* by inhibiting bad faith threats or bluffs. Parties whose credible threats should be made and consented to should not be deterred by the existing law of duress because they have little to lose by the law's later operation, while those whose threats are not credible might be deterred because the expected value of their bluffs is reduced.

The chief argument, however, against the school that would legalize blackmail is that it would encourage protection rackets built around legal privileges. It may well be that extortion law creates inefficiency when producers are unable to purchase protection from other producers who inflict incidental harm as a by-product of productive activity. But that same law also removes the incentive producers may have to maximize the harm they are privileged to produce just so they can market protection from it.

More than any other theorist, Daniel Kelly has extensively analyzed the potential for protection rackets in the commercialization of threats to inflict nuisance harm and the strategic profit from forbearing from

harmful, but privileged, activity.¹¹⁶ Kelly focused on nuisance cases, in which parties threaten to create costly, otherwise unprofitable nuisances to extract extortionate payments from neighboring landowners. But his analysis is not limited to nuisances and extends to exploitation of modern environmental legislation. The profit available from what Kelly calls “strategic spillover” effects creates incentives for protection rackets, in which menaces develop the ability to inflict nuisances not because the harmful activity is directly profitable to them but for strategic reasons, *i.e.*, so that they can sell protection in return for forbearance from the harm they threaten to cause.

The unjust enrichment theory of blackmail reaches such threats. The entire payment received by a strategic blackmailer is an extortion premium because such a menace incurs no cost in forbearing from the harmful behavior. But the unjust enrichment theory also reaches threats of “non-strategic” activities that are profitable to the menace but that are nevertheless used to extract an extortion premium that exceeds their profit.

VII. THE THEORY IN ACTION

The following examples illustrate how *ex post* leverage can enable a menace to obtain an extortion premium that would have been unavailable in an equivalent *ex ante* protection transaction.

A. *Leverage in the Office: Commercial Secrets Blackmail*

A common form of commercial protection exchange involves the risk that an employee will disclose information harmful to an employer, as in the following example:

Emma was employed in a mid-level management position with SyynTech, a waste disposal and recycling company. In the course of her employment Emma learned several things about SyynTech’s business practices that would cause it legal and public relations problems if made public. Surprisingly, Emma’s contract of employment did not prevent her from disclosing this information, and none of it was a legally protectable trade secret, all of which left Emma legally free to disclose the damaging information to regulatory bodies or others.

When SyynTech experienced a downturn in its business, it terminated Emma’s employment. Consider three possible scenarios resulting from this situation.

Scenario 1: Worried that termination may lead some of its disaffected

116. Kelly, *supra* note 101, at 1642.

ex-employees to become whistle-blowers, SyynTech's management offered each of them a severance package worth \$100,000 conditioned only on their signing a legally-binding non-disclosure agreement whereby the employees agreed never to reveal any information about their jobs at SyynTech. Emma eagerly signed the agreement and received the cash.

Scenario 1 is a common form of protection exchange. In the terms used in this Article, Emma's knowledge made her a menace who was a risk to SyynTech, the potential victim. As she was under no legal constraint, Emma had a legal privilege,¹¹⁷ vis a vis SyynTech, to disclose damaging information to third parties. In some cases, exercising this privilege might be of value to her. For example, she might be able to sell her information about SyynTech's potential liabilities to a third party interested in purchasing SyynTech. To reduce the risk of disclosure, SyynTech offered to pay Emma for her silence. By accepting this offer, Emma promised to keep SyynTech's secrets, thus replacing her legal privilege to disclose with a legally-enforceable duty not to disclose. In this protection transaction, SyynTech purchased a right to confidentiality, to which it was not previously entitled, and reduced the expected cost of a business risk at a price it was willing to pay. In return, Emma extinguished her privilege to disclose and put herself under a duty of confidentiality in return for a price she was willing to accept. Both parties benefitted by changing their legal relationship. The law smiles on this type of transaction and will give it full effect in the courts.¹¹⁸

Scenario 2: When she got her termination notice, and believing that she had been treated unfairly, Emma told SyynTech that, unless she was paid \$100,000 in cash, she might "go public" with what she knew about SyynTech's "dirty secrets." Concerned about the costs of such disclosure, SyynTech agreed to pay her, but only in return for a legally-enforceable non-disclosure agreement whereby Emma promised never to reveal the harmful information. Emma eagerly signed the agreement and received the cash.

In substance the second transaction is identical to the first. As before, SyynTech sought to reduce its business risk incident to disclosure and to put Emma under a new legal obligation of confidentiality. As before, Emma sought to be compensated for giving up her legal privilege of disclosure and placing herself under a new legal duty.

117. A party such as Emma has a legal privilege to do an act if she is under no duty to SynTec to refrain from the act and SynTec would have no claim against her if she acted. See Sidney W. DeLong, *What is a Contract?*, 67 S.C. L. REV. 99 (2015).

118. It is assumed that no public policy was offended by the agreement. See Garfield, *supra* note 72, at 261.

Yet the law that smiles on the first transaction frowns on the second one. The transaction in Scenario 1 was induced by an offer from SyynTech; Scenario 2 was induced by a threat from Emma. Emma made her threat in order to receive the consideration paid by SyynTech. Under Scenario 2, Emma may have committed extortion.¹¹⁹ As a matter of civil law, SyynTech's promise to pay her is unenforceable under the doctrine of duress¹²⁰ and, if it has already paid her, SyynTech can recover the payment in restitution.¹²¹

Ethical judgment also sharply distinguishes between Emma's behavior in the two transactions. Emma has done nothing "wrong" in Scenario 1; indeed, she is not even thought of as the actor. She has helpfully acceded to SyynTech's request by accepting its offer and its money in return for submitting herself to a new duty of confidentiality. Although she may have valued her ability to disclose what she knows to third parties, she bound herself to secrecy.

But conventional ethical judgment condemns Emma's conduct in Scenario 2. As the threatener, she, not SyynTech, is the active agent while SyynTech is her victim. She has the morals of a blackmailer¹²² and has abused her privilege¹²³ of free speech.¹²⁴ Her motives are malicious and SyynTech is the victim who deserves our sympathy.

Now consider a third possibility:

Scenario 3: As part of its normal employment agreement, SyynTech required all its employees to agree at the time they were hired that they would not disclose any information about its business for a period of five years following termination of their employment for any reason. Emma willing and knowingly agreed to this term when she was hired and did not demand extra compensation for the restriction. When Emma was terminated, SyynTech did not pay her any severance pay, although it reminded her of her duty of confidentiality.

The parties' legal relationship under Scenario 3 is in most respects identical to their relationship following Scenarios 1 and 2: In all three scenarios, Emma voluntarily placed herself under a legal obligation not to disclose SyynTech's secrets in return for which SyynTech paid her consideration. The crucial legal and economic difference between

119. See *supra* note 80 and accompanying text.

120. RESTATEMENT (SECOND) OF CONTRACTS §§ 175, 176 (defining wrongful threats for purposes of duress).

121. RESTATEMENT (THIRD) OF RESTITUTION § 14(2) ("A transfer induced by duress is subject to rescission and restitution.").

122. See *infra* Part III.

123. Actually, she has abused only her privilege of speech, properly defined. See *infra* Part III.

124. See *infra* Part III.

Scenario 3 and the first two Scenarios arises solely from Emma's greater leverage in the first two scenarios. In scenario 3, Emma sold confidentiality in an *ex ante* transaction before she acquired the practical ability to harm SyynTech, i.e., before she learned its secrets. The cost of her undertaking reflected her minimal opportunity cost in binding herself to secrecy rather than the expected value of the harm that disclosure would cost SyynTech. Emma negotiated as a monopolist in the first two scenarios and in a competitive market in the third. It is not surprising that the transaction depicted in Scenario 3 is neither legally nor morally problematic, having no overtones of extortion or exploitation.

Emma obtained an extortion premium in Scenarios 1 and 2 because the price SyynTech paid for her forbearance greatly exceeded Emma's costs in forbearing. To the extent that she was aware that SyynTech was paying her out of fear of what she might do, Emma was unjustly enriched in both cases under the analysis offered here.

B. Leverage in the Neighborhood: Spite Structure Blackmail

Owners of real property may, under local law, be privileged to conduct activities or to build structures on the land in ways that impose costs on their neighbors in the form of eyesores, air or noise pollution, view blockage, water runoff, and the like. To the extent that the neighbors cannot avoid or mitigate these harms by technology or by moving away, the nuisance value of the threatened land use is a potential source of leverage in a protection exchange. The owner of the eyesore might agree to remove it at a price the neighbor is willing to pay which can approach the subjective cost that the neighbor experiences from the nuisance. Threats are rarely necessary in such situations because the neighbor is likely to make the offer when the nuisance becomes apparent.

Because of the risk of such leverage, *ex ante* real estate protection transactions are commonplace. A landowner may purchase a view easement from the owner of a neighboring parcel. The agreement will bind future owners of both parcels of land, eliminating the threat of a structure that would block the view of the victim's property. A landowner might purchase a restrictive covenant limiting other land uses that a neighbor may engage in to avoid the risk of a later extortionate transaction. *The Problem of Social Cost* illustrated several actual and potential transactions between neighbors resolving the problems of such harm.¹²⁵ In some cases, if a protection transaction is not feasible, a landowner may simply purchase the adjoining lot, perhaps reselling it to a third party

125. See Coase, *The Problem of Social Cost*, *supra* note 2.

subject to a restrictive covenant protecting both properties.

As always, the price a potential menace will demand for such protection will depend in part on whether it has leverage over the victim, which will turn on whether the transaction is *ex ante* or *ex post* in relation to the victim's vulnerability to the threatened harm. Typical *ex ante* real estate protection exchanges are the covenants and conditions agreed to by new homebuyers in a residential development. Each buyer agrees to forbear from identified land uses that would harm the value of neighboring lots. The "price" demanded for this protection is the reciprocal promise of all homebuyers and is unrelated to the value of the restriction to each buyer. The mutual abandonment of the legal privilege to engage in the full range of legally-permissible land uses is economically efficient under the standard of social cost, as measured by the net utility to each new homeowner created by the tradeoff between liberty and protection.

After a party has purchased property, its vulnerability to a neighbor's harmful land use creates leverage that can greatly increase the price it must pay for protection. Leverage is particularly common in relationships between neighboring residential homeowners in locations in which the public or private land use regulation does not prohibit building structures that harm the value of neighboring property.

The problem of extortion by spite structures has been extensively analyzed.¹²⁶ Larissa Katz has argued that an owner abuses its rights of ownership when it leverages its ability to harm another through an exercise of its rights to use its property.¹²⁷ Daniel Kelly has analyzed several instances of what he refers to as "strategic spillovers" in which land owners acquire the ability to harm other people simply to sell protection from the harm they can cause.¹²⁸ Many of these involved parties who threaten neighboring homeowners with nuisances or spite structures.¹²⁹

126. See RESTATEMENT (SECOND) CONTRACTS, §176, illus. 10 (For purposes of duress, a threat to use property in such a way would be "wrongful."); NOZICK, *supra* note 77, at 84–85 (A neighbor's purchase of abstention from one who otherwise plans to erect a "monstrosity" is a productive exchange but not if the neighbor threatens to erect it just to extort a payment.); Campbell, *supra* note 77, at 388 n.13 (similarly). The example assumes that the neighbor's threatened action was legally privileged, so that the landowner could not enjoin the structure as a nuisance or under the rules relating to "spite" structures.

127. Larissa Katz, *Spite and Extortion: A Jurisdictional Principle of Abuse of Property Right*, 122 YALE L.J. 1444 (2013). Property rights are abused when they are employed other than for their purpose, which she identifies as solving the coordination problems that attend collective use of goods. The author especially criticizes owners using property rights as "leverage" to obtain some other benefit from the victim. On the general recognition of abuse of rights in American law, see Joseph M. Perillo, *Abuse of Rights: A Pervasive Legal Concept*, 27 PAC. L.J. 37 (1995).

128. Kelly, *supra* note 101, at 1642.

129. *Id.* at 1661.

The entire payment constitutes an extortion premium in such cases because the cost of the menace's forbearance is zero, or even negative.

Some of these points are illustrated in the following example:

Scenario 1: Mark is a wealthy businessperson who purchased a lot and built a mansion on it. Mark's master bedroom is on the top floor. Vinnie then purchased an adjacent lot and told Mark that he planned to build a house near the lot line with a top floor window that would give Vinnie a direct view into Mark's bedroom. Vinnie's plans would not violate any land use regulation or contractual obligation. But before building his house, Vinnie graciously offered to sell Mark his lot at a significant markup to permit Mark to preserve his privacy. Mark bought the lot from Vinnie.¹³⁰

Vinnie had leverage over Mark because Mark had already sunk costs into building his home and his alternatives (suffering the invasion of privacy, replacing his bedroom windows with a wall, moving away) were all more costly than buying Vinnie out. On the reasonable assumption that this payment greatly exceeded the cost to Vinnie of forbearing from engaging in the harmful act, e.g., by building his house away from the lot line, Vinnie obtained an extortion premium by exercising leverage. Vinnie has committed blackmail under the standard of this Article and has been unjustly enriched by the amount by which Mark's payment exceeded the value of his lot.

Scenario 2: After the transaction with Vinnie, Mark feared that Kim, his neighbor on the other side might pose a similar threat. To forestall this risk, Mark asked Kim for a restrictive covenant that would bar both parties from building structures that would violate each other's privacy. The covenants would "run with the land" and bind future owners of both lots. Although Kim would ordinarily have agreed to such an arrangement, before she signed, she learned from Vinnie how much money Mark paid him for his lot. Kim decided that her agreement was as valuable to Mark as Vinnie's threat was. Without uttering a threat, Kim simply refused Mark's request unless he paid an amount equal to the excessive amount he paid Vinnie. Because it was the only way to secure his privacy, Mark paid Kim's demand, and she signed the agreement.

Kim also exercised leverage over Mark and profited to the same degree as Vinnie. But because she made no threat, Kim would not have committed extortion. She did nothing to justify Mark's fears of her except to refuse his offer until he met her price.

130. The hypothetical is based on news reports of a transaction between Mark Zuckerberg and Mircea Voskerician. After buying the lot from Voskerician, Zuckerberg then reportedly purchased three other surrounding properties, apparently to forestall future threats. Evans, *supra* note 77.

Kim might argue that she should not be subject to moral opprobrium either. After all, Mark was the one who asked her to sell and a property owner is entitled to ask for any price she wishes. Just because Mark is a billionaire does not give him the right to exercise eminent domain or private condemnation of Kim's property to satisfy his own desire for privacy.

However, Kim is culpable under the theory of blackmail suggested here because she has exploited her leverage over Mark to extract an extortion premium that left her unjustly enriched.

Scenario 3: Mark, Vinnie, and Kim simultaneously purchased their lots from Plutocrat Mansions, a land developer that required each buyer to sign restrictive covenants limiting construction on their lots in various ways. Although they limit the use that can be made of the lots, the covenants make the lots more valuable for residential purposes because of the mutual protection the lot owners have against each other. If Vinnie then threatened to build a non-conforming house that would violate these covenants, Mark could sue to enjoin the building.

Under the analysis here proposed, the nuisance owner who charges only its cost of complying with the neighbor's wishes is not engaging in blackmail but in a benign Coasean bribe. The owner did not obtain a blackmail premium and did not intentionally profit from the harm he was causing the neighbor. Conversely, an owner who builds a spite structure for the purpose of selling abatement to the neighbor and who charges an amount calculated by the harm the structure causes the neighbor is engaging in blackmail as here defined. But between these extremes is an enormous gray area in moral theory about trafficking in harm.

For example, assume that the offending use consists of several large trees on an unimproved lot that obstruct a very valuable ocean view from an adjacent lot on which an expensive home is being constructed. If the owner merely refuses an offer of money by the developer to remove the trees, no one would see this as blackmail. But what if the offer to pay for tree removal reaches or even exceeds the market value of the unimproved lot? If the owner of the unimproved lot is eventually paid such a sum, has he been unjustly enriched?¹³¹ What if the owner is instead operating a marginal business that detracts from the residential surroundings? Or what if he is the lone hold-out in a multi-million-dollar real estate development that depends critically on his lot? Conventional morality is ambivalent about these situations.

131. See Christopher, *supra* note 82, at 1135 (discussing the blackmail "counter-offer" to a bribe offer by the victim) (citing Murray N. Rothbard, *THE ETHICS OF LIBERTY* (1982)).

C. Leverage in the Campaign: Reputational Blackmail

In some industries, the infliction and prevention of harmful interactions can have become business as usual. The distinction between blackmail and bribery is exceedingly thin in a field of practice in which parties expend significant resources in the concealment, discovery, and disclosure of each other's harmful secrets. Witness the modern, political campaign:

Mogul and Pol are locked in a tight race for the Presidency. Gordon is a wealthy supporter of Pol and seeks campaign material adverse to Mogul. Gordon offers a reward of \$1 million for credible evidence that Mogul has engaged in money laundering in his business ventures. Sherlock is a firm that specializes in forensic and political opposition research. In response to the reward offer, after costly research, one of Sherlock's employees, Bartleby, finds and secures the sought-for evidence. Consider three scenarios:

Scenario 1: Dissatisfied with the amount of the reward that Gordon has offered, Sherlock secretly approaches Mogul and threatens to disclose the evidence to Gordon unless Mogul pays it \$1.5 million. Mogul, fearing loss of the election if the evidence is disclosed, eagerly accepts the offer and pays, receiving in return the destruction of the evidence and Sherlock's agreement never to disclose it. But after Mogul wins the election, and no longer fearing disclosure, he orders the Attorney General to prosecute Sherlock for extortion. Because Sherlock obtained money by threats to disclose Mogul's secret, it might well have incurred criminal liability for the transaction.

Scenario 2: Bartleby, the Sherlock employee who found the evidence, is a life-long friend and loyal supporter of Mogul. Without Sherlock's knowledge, Bartleby warns Mogul of his peril, but suggests that he could buy the evidence from Sherlock if he offered more than Gordon offered. Bartleby suggests that Mogul offer Sherlock \$1.5 million. Mogul thanks Bartleby for the tip and, after negotiation over the price, makes the suggested offer to Sherlock. Sherlock eagerly accepts and sells secrecy to Mogul for \$1.5 million. Because Mogul was not threatened and he initiated the transaction himself, this transaction is not extortion and should be fully enforceable on each side.

Scenario 3: Having obtained the evidence and wishing to appear fair to all concerned, Sherlock privately informs both Gordon and Mogul that it has the evidence sought by Gordon and will sell it to the highest bidder. After an auction, Mogul makes the highest bid of \$1.5 million and

Sherlock sells him the evidence.¹³² Mogul is grateful for the opportunity to buy and bury the evidence and asks for a right of first-refusal to buy any other embarrassing information Sherlock may acquire about him in the future.

These scenarios illustrate the thin line between bribery and blackmail. In all three examples, Sherlock was a menace, Mogul was a victim, and the two engaged in a protection transaction. Mogul made the payment in each case only because Sherlock made it known that otherwise it would disclose the secret to Gordon, harming Mogul's election prospects. The first transaction was initiated by Sherlock's threat, the second one by Bartleby's warning and Mogul's offer, and the third one by Sherlock's warning and offer to sell followed by Mogul's auction offer. In none of the examples was the threat a bluff: Sherlock would have benefited by \$1 million if it carried out the threat and earned the reward from Gordon.

In the first two transactions Sherlock appears to have obtained an extortion premium of \$500,000, although it is uncertain what Gordon might have paid for the information if offered the chance. In the third transaction, the auction, Sherlock appears not to have obtained an extortion premium over the cost of its forbearance (the losing bid by Mogul).¹³³ In each case, the true cost of Sherlock's forbearance to exercise the threat of disclosure to Gordon depends on how much Gordon would have bid for the evidence if given the opportunity.

D. Leverage in the Courtroom: Remedial Blackmail

A person who suffers harm can become a blackmailer herself if the law gives her a remedy that she can use against the wrongdoer. A party with a remedial right has leverage to obtain an extortion premium whenever the defendant's cost of complying with the remedy exceeds the value of the remedy to the plaintiff.¹³⁴ Thus, for example, a homeowner group that is entitled to enjoin a factory from smoke can demand for the release of the injunction more than the amount of damage than the smoke would have caused. A business that is entitled to enjoin an ex-employee

132. In his analysis of secrets blackmail, Coase assumed that the victim would always value secrecy more than the menace would value disclosure as grounds that the state should assign the right to secrecy to the victim. Coase, *Blackmail*, *supra* note 6, at 673.

133. Lindgren, *On Waste*, *supra* note 83, at 597 contains an eerily prescient hypothetical case of a fashion model who has an affair with a presidential candidate and accepts a million dollars for her silence. *Id.* at 603. Lindgren uses the example to counter economic arguments that blackmail is illegal because of wasted transaction costs, but he does not address his third-party leverage argument. *Id.*

134. Coase, *Blackmail*, *supra* note 6, at 670 (stating the payment does not represent what the menace would lose by forbearing from the threatened action).

from competition can demand for its release of the injunction more than the cost that it would suffer from this competition.

The risk of extortion by a plaintiff who wields an injunction has long been recognized.¹³⁵ An injunction is an order by a court directing the defendant to do or refrain from doing something.¹³⁶ Failure to comply constitutes civil contempt, which subjects the defendant to fine or imprisonment until it complies.¹³⁷ An injunction is awarded when the court finds that an award of damages would be inadequate to restore plaintiff to its rightful position.¹³⁸

In theory, an injunction should not be awarded if the court finds that the balance of hardships favors issuance, meaning that the plaintiff will suffer more from the enjoined act than the defendant will suffer by compliance with the injunction.¹³⁹ In some cases, the cost of compliance with the injunction may dwarf any possible damage that the plaintiff would suffer from the enjoined act. For example, a party that has recklessly constructed an unauthorized structure on the property of another may be enjoined to remove it.¹⁴⁰ Compliance with an injunction may be costly, and, while courts should balance the hardships of the parties in deciding whether to issue an injunction, it is quite possible that a party will be ordered to do something that imposes a cost that is disproportion to the harm faced by the plaintiff if it fails to comply. The plaintiff, however, has the legal power to release the defendant from the obligation to comply with an injunction if the defendant buys its consent. The plaintiff will surely demand for this release an amount that will compensate it for the

135. A. Michael Polinsky, *Resolving Nuisance Disputes: The Simple Economics of Injunctive and Damage Remedies*, 32 STAN. L. REV. 1075, 1077 (1980) (noting that the possibility of extortion exists when enforcement of the injunction would impose costs on the defendant that exceed the damage that plaintiff would suffer if the enjoined activity occurs). Richard Epstein observed that injunctions raise the hold-out problem, which is the reciprocal of the externality problem. Richard A. Epstein, *Holdouts, Externalities, and the Single Owner: One More Salute to Ronald Coase*, 36 J. LEGAL STUD. & ECON. 553, 559 (1993).

136. I DOBBS LAW OF REMEDIES § 2.1(2) (2d Ed. 1993) (Injunction is a coercive remedy enforced by threat of contempt.).

137. Coercive contempt may consist of a fine or imprisonment until the defendant obeys the order. Willful disobedience of an injunction may be punished as a crime. *Int'l Union, United Mine Workers v. Bagwell*, 512 U.S. 821, 828–29 (1994).

138. DOUGLAS LAYCOCK, *THE DEATH OF THE IRREPARABLE INJURY RULE* 22–23 (discussing the relation of irreparable injury and inadequate remedy at law) (1991).

139. I DOBBS LAW OF REMEDIES § 2.4(5).

140. *Whitlock v. Hilander Foods, Inc.*, 720 N.E.2d 307, 308–09 (Ill. App. 1999) (order reversing summary judgment and remanding to rehear the issue of removal of encroaching concrete footings at base of retaining wall despite cost); see M.T. Van Hecke, *Injunctions to Remove or Remodel Structures Erected in Violation of Building Restrictions*, 32 TEX. L. REV. 521 (1954) (finding courts more inclined to enjoin deliberate violations than inadvertent ones).

harm that the enjoined act is likely to inflict. But it may demand more.¹⁴¹

An injunction thus gives a plaintiff leverage whenever the defendant's cost of compliance exceeds the cost to the plaintiff of releasing the injunction.¹⁴² Courts alert to this risk may refuse injunctions in order not to give blackmail leverage to the plaintiff.¹⁴³ In *Carbon County Coal Co. v. Northern Indiana Public Service Co.*,¹⁴⁴ a utility repudiated a requirements contract with a coal company. Although the company was awarded its lost net income as damages for breach of the contract, it also sought an order of specific performance that would have required the utility to purchase the balance of the coal for the remaining term of the contract at the contract rate.¹⁴⁵ Affirming the trial court's refusal to grant the injunction, Judge Posner reasoned that the coal company would never actually enforce the order even if it was issued, but was instead seeking judicial leverage to demand that the utility pay a much greater sum than the actual damages for its release.¹⁴⁶

A court sought to mitigate a plaintiff's injunction leverage in a situation in which the parties were in a bilateral locational monopoly relationship in the widely-analyzed decision in *Boomer v. Atlantic Cement Co.*¹⁴⁷ A cement plant that was built at a cost of \$45 million and that employed over 300 workers was found to have constituted a nuisance to nearby residents because of pollution generated by its operation.¹⁴⁸ The court granted the plaintiffs a permanent injunction against the plant's pollution activities as a nuisance,¹⁴⁹ but permitted the defendant to buy a release of the injunction by paying a total of \$185,000 in damages to the residents, which represented the harm to their property caused by the nuisance.¹⁵⁰ This option had the effect of limiting the plaintiffs' leverage

141. Robert Ellickson, *Alternatives to Zoning: Covenants, Nuisance Rules, and Fines as Land Use Controls*, 40 U. CHI. L. REV. 681, 720–21 (1973) (noting that a court will be reluctant to enjoin a nuisance if the injunction imposes costs on the defendant that are greater than the costs of the nuisance to the plaintiff).

142. As Professor Laycock put it, “[g]ranteeing or withholding the injunction allocates the power to be unreasonable between bilateral monopolists.” DOUGLAS LAYCOCK, *MODERN AMERICAN REMEDIES* 329 (Concise 4th ed. 2012).

143. See Ellickson, *supra* note 141, at 731–32 (arguing that nuisance cases often lead to inefficient injunctions in which the costs to the defendant exceed the benefit to the plaintiff).

144. 799 F.2d 265, 267 (7th Cir. 1986).

145. *Id.* at 268.

146. *Id.* at 279 (“Probably . . . Carbon County is seeking specific performance in order to have bargaining leverage with NIPSCO, and we can think of no reason why the law should give it such leverage.”).

147. 257 N.E.2d 870 (N.Y. 1970).

148. *Id.* at 223.

149. *Id.* at 872. Its alternative was to find it liable for damages in trespass. *Id.*

150. *Id.* at 873. In effect, this permitted the plant to purchase a pollution easement for the amount

to the actual cost they suffered from the illegal land use. If instead the court had given the residents an unconditional injunction, they could have demanded an extortion premium of up to \$45 million as the price of their release of the injunction order.¹⁵¹

The courts in *Northern Indiana* and *Boomer* refused or limited injunctions to limit blackmail leverage. But after a court has issued an injunction, the plaintiff is ideally situated to extort a premium for the release without having to utter a threat, and without fear of liability for criminal extortion. It may simply refuse to release the injunction in return for a reasonable payment by the defendant.

Blackmail leverage can be wielded in injunction cases whenever the cost of complying with the injunction exceeds the value of the injunction to the plaintiff.¹⁵² And under the analysis in this Article, it is extortionate for the plaintiff to refuse to release an injunction unless paid an amount that greatly exceeds any harm to the plaintiff that the enjoined act would cause.

Although a damages judgment is not as coercive as an injunction, the leverage essential to blackmail can also arise in contracts cases whenever a party's cost of performance exceeds the value of that performance to its counter-party. This is because the plaintiff is entitled to recover as damages the cost of "cover," obtaining performance from a third party. Plaintiff has leverage to the extent that the cost of performance exceeds the value of the performance to the plaintiff. A reliable sign of this situation is that the plaintiff would not actually use the damages award to replace the breaching party's performance.

A dramatic example occurred in *Groves v. John Wunder*¹⁵³ where the lessee of a gravel pit failed to remediate the property at the end of the lease

of damages. Joel C. Dobris, *Boomer Twenty Years Later: An Introduction with Some Footnotes about Theory*, 54 ALB. L. REV. 171, 174 (1990) (suggesting that the parties always anticipated that the defendant would buy off the injunction).

151. On the economic implications of the case, see Jeff L. Lewin, *Boomer and the American Law of Nuisance: Past, Present, and Future*, 54 ALB. L. REV. 189 (1990).

152. In practice, post-award renegotiation of injunctions appears to be rare. Ward Farnsworth, *Do Parties to Nuisance Cases Bargain After Judgment? A Glimpse inside the Cathedral*, 66 U. CHI. L. REV. 373 (1999) (speculating on reasons that parties rarely buy releases from injunctions).

153. *Groves v. John Wunder Co.*, 286 N.W. 235, 241 (Minn. 1939) (holding owner's damages for the contractor's repudiation of its duty to remediate the property should be measured by the \$60,000 cost of performance rather than the \$12,000 diminution in value of plaintiff's property). *Contra* *Peevyhouse v. Garland Coal & Mining Co.*, 382 P.2d 109, 111–12 (Okla. 1962) (criticizing *Groves* and awarding only diminution of value damages instead of cost to remediate family farm at end of mineral lease). One court held that cost of completion in excess of diminution in value should be awarded only if the court determines that the plaintiff will in fact complete performance. *Advanced, Inc. v. Wilks*, 711 P.2d 524, 527 (Alaska 1985). In such a case, the plaintiff's demand for the cost of completion would not be extortionate as defined in this Article.

term as required by the contract. The lessor sought damages for breach of the remediation obligation as measured by the cost of completing the contract rather than by the diminution in value of the property caused by the breach. The evidence showed that it would have cost the defendant \$60,000 to perform the remediation, while the total value of the commercial property after remediation would have been only \$12,000.¹⁵⁴ The court approved of an award based on the cost to complete the remediation rather than on the diminution in value of the property.¹⁵⁵ This represented a nice profit for the plaintiff who had no commercial reason to expend the award on remediating the property.¹⁵⁶

It may be argued that a contractor who has such a duty should not breach the contract but should negotiate with the plaintiff for a release of the executory duty of performance by offering the plaintiff the full equivalent of performance. In *Groves*, the lessee could have offered the lessor \$12,000 for a release of the obligation to remediate the property. If indeed that sum represented the full value of performance to the lessor, it might be argued that it should have acceded to this request. But what if it demanded and received \$50,000 for the release? Under the analysis of this Article, the \$38,000 would have been an extortion premium, an example of remedial blackmail.

IV. CONCLUSION

Ironically, the primary transaction cost that prevents Coasean bargaining over harm-related legal entitlements is one that he failed to identify in *The Problem of Social Costs*: many of the bargains he proposed would be prohibited by law. In light of the presumptive utility of Coasean bargains in harm-related entitlements, legal theory must justify its prohibition of protection transactions in which victims purchase protection from harm that menaces are legally privileged to inflict. No such justification has been found. The law's prohibition of some protection transactions rests not on what is exchanged but upon whether they were initiated by a menace's threat or a victim's offer.

154. *Groves*, 286 N.W. at 241.

155. *Id.* at 238–39. The court remanded the case for a determination whether the lease actually required remediation of the sort demanded. The award in *Groves* appears to be in conflict with the rule stated in the RESTATEMENT (SECOND) CONTRACTS. It permits an award of either the diminution in the market price of the property caused by the breach (RESTATEMENT (SECOND) CONTRACTS § 348 (2)(a)) or the reasonable cost of completing performance (*Id.* at § 348 (2)(b)), but only if the cost of completion is “not clearly disproportionate to the probable loss in value to him.” *Id.*

156. Professor Dawson reports that the *Groves* parties settled for a payment of \$55,000. The plaintiff did not use the money to remediate the property. DAWSON, HARVEY, AND HENDERSON, CONTRACTS 19 (8th ed. 2003).

This Article has suggested that the difference between bribery and blackmail should lie not in the presence or absence of a threat but in the price the menace demands for protection from the harm it can inflict on the victim. Regardless of which party initiates them, Coasean bargains are not problematic so long as menaces sell forbearance at or near their cost, as did the enterprises discussed in *The Problem of Social Cost*. Coasean bargains become extortionate only when, by exercising leverage, the menace extracts an extortion premium that exceeds that cost. A menace's profit from the harm it is legally privileged to inflict enriches it unjustly and transforms protection markets into protection rackets.

But the unjust enrichment standard, while theoretically and morally defensible, is unworkable in practice in many cases. When courts lack information about a menace's true costs of forbearance, the extortion premium may be an unworkable measure of legality. In the absence of any better test, the threat requirement may at least inhibit deliberate attempts at extortion while permitting victim-initiated bribes. Over- and under-inclusiveness may be the best the law can achieve.

Like the concept of extortion, the concept of unjust enrichment is invisible to economic analysis because it rests on a moral judgment rather than a calculation of social cost. Coase realized this, perhaps better than some of his critics. Near the end of *The Problem of Social Cost*, Coase quoted fellow economist Frank Knight: "[P]roblems of welfare economics must ultimately dissolve into a study of aesthetics and morals."¹⁵⁷ The ethical quandaries posed by trafficking in harm cannot be resolved by appeals to efficiency alone.

157. Coase, *The Problem of Social Cost*, *supra* note 2, at 43. Concerning the difficulty of establishing clear legal definitions of blackmail, he also confessed that "It would be a sad day if all the answers had to be given by economists." Coase, *Blackmail*, *supra* note 6, at 676.