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COMMENTARY

***203** SETTLEMENT PSYCHOLOGY: WHEN DECISION-MAKING PROCESSES FAIL

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Most cases settle, and the job of a litigator is increasingly becoming a process of using judgment and making decisions to bring about a settlement.

The litigator performs two roles, advocate and counselor, and in each role, the litigator uses judgment and makes decisions. As an advocate, the lawyer strategizes about the case, collects and preserves evidence, and negotiates on behalf of the client. As a counselor, the lawyer gives cost estimates, odds of prevailing, and odds of the probability of various desired and undesired outcomes.

Clients have good reason to expect that their lawyers will make these judgment calls and decisions in a consistent and well-reasoned manner. But at each phase of the litigation/settlement process, pervasive psychological traps may impede lawyers' ability to make decisions that effectively maximize client values. This article describes a few of the most well-established psychological phenomena that occur during the litigation/settlement process. Hopefully, by understanding more of the psychology of lawyering, ***213** litigators can give more consistent and better reasoned advice to their clients.

This commentary breaks the litigation/settlement process into four phases and discusses applicable psychology. The phases are:

(1) initial case intake and preliminary evaluation of the case's strength;

(2) the discovery process--information gathering and the evaluation of the strength of the information gathered;

(3) evaluating potential settlements; and

(4) the actual negotiation of settlements--presenting and evaluating offers, and trying to get the other side to accept your offer.

PHASE ONE: INITIAL INTAKE AND PRELIMINARY EVALUATION

Four psychological biases that affect lawyers' abilities to make good estimates are Availability, Anchoring, Perspective Bias and Positive Illusions.

Why we form initial estimates that favor our side--Availability and Anchoring: The most common way to form an estimate of the value of something unknown is to compare it to the value of something known. If a person wants to know what her house is worth, she may look to the price at which a similar house sold recently. So it is with litigation.

When clients describe cases and ask for estimates of strength and value, the lawyers try to recall cases that relate to the one described by the client. Unfortunately, the cases that come to mind do so because they are memorable and relatively unusual, not because they are run-of-the-mill. Thus, when a client describes his tort case against a restaurant, his lawyer is likely to flash for a moment on the McDonald's coffee cup case. When the client describes a sexual harassment claim, the lawyer might think of any of a number of such cases recently in the news. When the lawyer compares his or her client's case to a notorious case, he or she distorts its value as a result of the Availability heuristic. The attorney, like all people, doesn't have the memory to retain every bit of information that comes before him or her, so the mind selects the most vivid to remember. The vividness of the image or the ease with which it can be recalled distorts its representativeness. This is why people tend to believe, incorrectly, that there is more annual rainfall in Seattle than in northern Georgia, that shark attacks lead to more deaths than falling airplane parts, or that murder is more common than suicide.

Of course, a good lawyer understands that the case the client described is not the McDonald's coffee cup case. She understands that this client's case is probably worth less than that one, so she adjusts from the McDonald's verdict downward. The question is whether she adjusts far enough. Research suggests that she will not adjust sufficiently because of something called the Anchoring effect: that decision makers will become anchored on reference points with highly attenuated or even nonexistent links to the decision at hand. For example, people--many with legal training--have been asked questions such as, "What are the odds that the temperature in San Francisco is higher or lower today than 578 degrees?"

Of course, everyone says the odds are 100% that the temperature is lower than 578 degrees. But when they are then asked to estimate the true San Francisco temperature, their estimates are invariably higher than the true temperature. When asked the likelihood that the temperature is higher than 1,000 degrees below zero, they answer 100%. If then asked the true temperature, the distortion is toward the low side. Of course, these temperatures are absurdities and are entirely unrelated to the true temperature of any place on this planet. Nevertheless, they affect the responses given. Thus, when a lawyer recalls a notorious case like McDonald's Corp.'s for torts, Mitsubishi Motor Corp. or Baker & McKenzie for sexual harassment, or some locally notorious case after a client has begun to recount the facts of his case, rest assured that it has a distorting effect on the lawyer's initial case evaluation. When availability causes a case to pop to mind as comparable, the odds are that the mind will anchor on it and insufficiently adjust.

The best cure is to check base rates. Checking a database of awards in the local jurisdiction will yield a better estimate of case value than will reliance on experience and adjustment from seemingly comparable cases. Data always trumps intuition.

Why we think we always win--Perspective Biases and Positive Illusions: The mere fact that the client hires a particular lawyer often triggers a "bias of perspective" exacerbated by "positive illusions."

***214** Perspective biases cause lawyers to overestimate the rightness of their side, and also to feel more confidence in their assessments. In one well- known experiment, each of four groups of subjects was given one of several different packets of information. Members of group one received plaintiff's information only, and these people were told that they were representing the plaintiff. Members of group two received only the defendant's information and were told that they were representing the defendant. Each of these groups was informed that other information existed--namely, the other side's information and some background information--but that they, as the plaintiff or defendant, would not receive that information.

Group three received both sides' information and group four received both sides and background information. These two groups were not assigned roles as plaintiff or defendant.

Each group was asked to estimate the plaintiff's odds of winning and to indicate their confidence in their prediction. Groups three and four estimated that plaintiff's chances were about 50/50, while group one plaintiffs viewed themselves as having a very strong chance of winning and group two defendants viewed the plaintiff's chances as poor. In addition, the plaintiffs and defendants (the people who received the least information) were more confident in their assessments than the neutral groups, suggesting that people fail to take into account the existence of information that they know exists but that they do not have.

Thus, when a client comes to his lawyer's office and tells his or her side of the case, the lawyer may know that there is another side of the story and may try to withhold evaluation until he or she hears it, but experiments indicate that the lawyer will form an opinion favorable to the client and be more confident in that opinion than the lawyer would be if he or she were not a partisan.

Perspective biases are reinforced by positive illusions -- unrealistic optimism, exaggerated perceptions of personal control and inflated positive views of the self. For example, people tend to overestimate the probability that their predictions and answers to trivia questions are correct. There are a great many studies that indicate lawyer overconfidence. One study, conducted at a recent American Bar Association meeting, found that on average lawyers rated themselves in at least the top 80th percentile on such qualities as ability to predict the outcome of a case, honesty, negotiation skills and cooperativeness. This high degree of self-regard leads to an inflated sense of the value of a case.

These biases are difficult to correct, but if the goal is a realistic estimate of case value, lawyers should realize that their healthy self-images may lead to distorted images of how much a case is worth, and how likely they are to win. Finding a brutally honest colleague to act as "devil's advocate" may be a worthwhile investment of time.

PHASE TWO: DISCOVERY

The next four principles, "Biased Assimilation," "Confirmation Bias," the "Certainty Effect," and the principle of "Commitment and Consistency," occur primarily during discovery.

Why discovery makes us overconfident--Biased Assimilation and Confirmation Biases: Operating in tandem, assimilation biases and confirmation biases distort both the search for information and the valuation of information found.

As the lawyer begins discovery, he or she has a theory of the case--a plan of attack or defense that is discussed with the client. As the attorney gathers cases and information, he or she sorts the information into three categories: helpful, harmful or neutral. The psychology of biased assimilation suggests this lawyer will interpret cases and evidence in a way that supports the conclusion he or she wants, whether the information actually supports that conclusion or not. If the information is favorable, he or she will overweight its relevance and applicability. If the information is harmful, the attorney may concede that it is harmful but will underweight its harmful effects. If the information is neutral, he or she will tend to see it as marginally helpful.

Finally, if the information contains information that is part helpful and part harmful, the attorney will tend to overweight the helpful parts and underweight the harmful parts, concluding that the information is of net positive value. This often causes a distortion in the valuation of the evidence. If both sides have done this, the case may be difficult to settle.

Moreover, experienced attorneys rarely start case research by canvassing the entire legal literature to determine the state of the law and the relative power of all of the related areas of law. It would be hard to justify billing too many hours doing general research. Instead, the lawyers try to go straight to research directly bearing on their clients' cases. They are biased and have incentives in favor of confirming that which they already believe to be true.

The same, of course, is true of lawyers processing cases. When they hope a proposition is true (e.g., a theory of liability or a defense), they will see supporting information as strong and negating information as weak. This is biased assimilation. Furthermore, because they tend to look for and find corroborating information first, their theories tend to be mentally reinforced. This is a confirmation bias.

In order to reduce the negative effects of these biases, it may make some sense to think about the "anti-thesis" before doing research. ***215** Ask yourself what the case looks like to the other client, and consider doing a little bit of research into their case-in-chief before starting your own. If you think about your research as rebutting their case (as opposed to building yours), you may retain a view of the case closer to the one that a neutral judge or juror might hold. If you can have such a neutral view, you will be more likely to settle earlier for an amount that would approximate an average verdict.

Why we spend too much for information--the Certainty Effect: As attorneys approach the

middle of the discovery process they face decisions whether to gather more information on a particular point or to spend the time and money on another aspect of the case or another case.

The certainty effect suggests that when people already have a great deal of information about an issue, they will spend more resources to establish that point than is warranted by the prospective value of the new information. Studies of decision making have found that increasing the probability of winning a prize by a fixed amount, say 5%, has more impact on people when it changes the probability from 95% to 100%, than when it changes the probability from 25% to 30% or 65% to 70%. Stated another way, people are willing to pay a premium to change a high probability into a certainty. The certainty effect may cause lawyers who are "pretty sure" that they have uncovered all information to spend more in the search for information than is warranted by the value of the information uncovered.

Why it costs so much to "stay the course"--Commitment and Consistency: Discovery exacerbates a tendency to escalate commitment to initial courses of action. The concept of "sunk costs" causes people who have invested in a course of action to make economically irrational choices to promote their desired outcome. A powerful example of this is known as the "dollar-bill auction," where an auctioneer auctions off an amount of money. Twenty dollars usually works well. The rules are simple--the high bid gets the money, but the second highest bidder must also pay the amount of their last bid. Many people in the room hope to buy the bill for something less than $20, and so they bid readily. Typically, the auction starts at a very low amount, and zooms up from there. Once one bidder has bid $10 and this bidder is outbid, the auctioneer is assured of a profit.

As the amount approaches the item's face value, the number of bidders usually winnows to two. As one bids $18, the other faces the sure loss of his or her last bid, so he or she bids $19. The $18 bidder faces a sure loss so he or she bids higher than $19. At some point, one of the bidders realizes that breaking even is better than losing $19 or more, so he or she bids $20.

The other bidder then bids more than the $20 face value, because a bid of $21 results in a loss of $1, whereas concession results in a loss of $19 or more. Thus, the "winning" bid is generally higher than the value of the auctioned item.

Recently, a colleague told the author that a $1 auction produced a winning bid of $6.50, and a second highest bid of $6--a net loss for the players of more than 1,100%. The only auction winners are the auctioneer and those audience members who didn't bid at all. Those who committed to a course of action escalate their commitment, and make choices consistent with that initial commitment--even if the original commitment turns out to have been unwise.

When discovery resembles a dollar-bill auction, the litigants often invest far more in information exchange than the value of the claim. It is the attorney's job to advise their clients, as they embark on a course of discovery, to be wary of the dangers of commitment and its attendant invitation to irrationally escalate that commitment.

PHASE THREE: A JUST AND FAIR SETTLEMENT

Once discovery is complete and the lawyer wishes to engage in a conversation with the other side, he or she needs to know what a fair settlement is to persuade the other side to say "yes," or the settlement will not occur. He or she needs to find the bargaining range, and while the lawyer wants to end up closer to the end favorable to the client, the attorney needs to be sure that the offers do not alienate the other side and cause negotiations to terminate or stall. The "Fixed-Pie Bias," however, may impede his or her path to rational calculation of the bargaining range, and a "Self-Interested Choice of Norms" may make calculation of a fair offer difficult.

Why we see the world as zero-sum--the myth of the Fixed Pie: The legal system turns most client desires and needs into monetary units. Pain and suffering is measured in dollars, as are the negative effects of illegal discrimination, loss of consortium, and many other values that have no conventional market value. This tendency of converting all intangible and tangible needs of the litigant into dollars and cents may have the unfortunate side-effect of turning negotiations into distributive tugs of war, even when client interests are poorly served by this type of bargaining.

Rather than making gains from trade, negotiators see every dollar as part of a zero-sum payout; they assume that the mythical negotiation "pie" is of fixed size. Studies show that negotiators tend to believe that the other party's interests are diametrically opposed to their own. This faulty perception is remarkably resistant to information which disconfirms the truth of this belief. Indeed, laboratory studies have shown that people waste resources unnecessarily in battling over the conflicting interests while ignoring shared and differing ones. Anecdotal evidence confirms these laboratory results. The classic book "Getting to Yes," by Roger Fisher, William Ury and Bruce Patton, notes that ***216** "the assumption of a fixed pie" inhibits the bargaining range by drawing the bargaining range along one competitive vector, rather than seeing negotiation as a chance to satisfy multiple interests in ways that allocate value where it is most highly valued.

As a practical matter, the attorney defending a case of wrongful discharge may engage in an unproductive exchange of dollar offers with the plaintiff, and the negotiations may be costly and still result in an unbridgeable gap between the parties' offers. If the defendant could ferret out the plaintiff's interests, he or she might offer an apology, a recommendation for future employment, a confidentiality agreement, or other such considerations, and the resulting dollar amount that would need to change hands might be one agreeable to both sides. In return, the plaintiff might offer insight into ways the company might change practices or policies that would lessen the likelihood of similar lawsuits in the future.

The best way to combat the fixed-pie bias is to approach negotiations with as creative and open a mind as possible. Look for ways to trade complementary interests. Embrace differences in interests, risk attitudes, or perceptions to enlarge the range of acceptable bargains. Moving away from established patterns may feel risky, but the failure to change may cause breakdowns of negotiations that should have resulted in mutually beneficial settlements.

Why we can't be fair--Self-Interested Choice of Norms: Not only do negotiators have a hard time seeing the bargaining range consisting of multiple and differing interests, they also experience a great deal of difficulty determining a fair division of that range. Decision makers frequently invoke ostensibly neutral principles or practices as negotiation norms that they

propose should govern the distribution of the benefits of a bargain, i.e., equality, need, past precedent, or custom.

Studies show that people tend to choose norms of fairness in a highly self- interested manner. While the voting structures "majority rule" or "two-thirds rules" are each ostensibly neutral, once the voters are counted and the person holding the election knows what the vote tally will be, the choice of a voting rule is outcome-predictive, and no longer neutral. So it is with fairness norms.

Powerful people prefer equity norms whereas less powerful people favor equality norms. People elect between local norms and national norms, depending on which produces an outcome they prefer. People are overly sensitive to relative vs. absolute pay-outs and to legal entitlements. A decision maker will make judgments about a deal's fairness based on what the other side gets out of it, even though the opponents' payout should be irrelevant to them. Even if they get what they requested out of a settlement, they may reject the proposed settlement because they feel that the other side benefits too much or does not feel the appropriate degree of pain.

Fairness also may be a function of wealth. An individual likely will feel more pleasure from a split that is $5,000 in his or her favor than does a corporation. Conversely, a company needs a larger percentage of the split to feel any sense of gain. The poorer party favors norms that equalize the disparity, while the richer party focuses on relative utility.

Furthermore, if a person thinks about fairness when they feel that they are "owed" because the other party has impinged upon a legal entitlement of theirs, a 50/50 or ostensibly "fair distribution" will not seem or feel fair.

People tend to reject offers if they feel that they are being treated unfairly. This is true even when accepting the offer would leave them better off. Empirical experiments, often called "dictator games" or "ultimatum games" have illustrated this point. In such games, one player is authorized to propose a particular split of a sum of money between himself or herself and a second player. If the second player accepts the split, each keeps the portion of the split named by the first player. If the second player rejects the split, no one gets any money. In situations in which the sum to be split is $100, and the split offered is 90/10, the second player usually rejects the split. Presumably, if the second player was asked "Would you like $10, no strings attached?" or if the amount to be split was $20 and the offer was for $10, they would gladly take the $10--but they reject the net wealth increase of $10 in the 90/10 split because it violates their norms of fairness.

Some examples of fairness norms that cause problems in a legal conflict are illustrated by the wrongful discharge scenario mentioned above. Imagine that the former employee is suing a multinational corporation, alleging that the discharge was in retaliation of a complaint about some questionable behavior on the part of one of the company's vice presidents.

The company responds that the discharge is easily justified for business reasons and was not retaliatory. The employee may believe that she deserves $200,000 and the company may believe that the appropriate settlement figure is $100,000. If they litigate to conclusion, they each expect to spend an additional $50,000. There is a large range of settlement figures that leave both sides

better off than litigating the case to conclusion.

If the offer to settle is exactly in the middle, the difference is equally split and the bargain is set at $150,000. Objectively, the settlement would be fair, but if the large corporation wronged the individual somehow (perhaps by illegally discriminating against her), a 50/50 split may not be fair. Fairness would require that more than half of the benefit of the bargain flow to the wronged party.

***217** Of course, both disputants may believe that the other party is in the wrong, and each may then believe that they are entitled to more than half the benefit. In addition, as a result of difference in size, they may value the money differently, each believing that their relative size requires a split in their favor.

The best prescription for overcoming problems related to a search for fairness may be to try to craft a settlement that allocates items in the bargaining range in a way that makes each party feel that they got the better deal, and to abandon the idea that a "fair" split will be mutually acceptable. Because "fair" is in the eye of the beholder, it may be impossible to find an agreeable fairness norm between disputants.

PHASE FOUR: NEGOTIATING

The process of exchanging offers and ideas with the other side is a complex and rich area for exploration of the psychology of settlement. Three areas of particular interest are "Framing," related to the making of offers, "Reactive Devaluation," related to the other side's offers, and "Social Influence" tactics, related to getting the other side to agree.

Why we fail to treat similar offers in similar ways--Framing: Not all offers are alike, but some only differ in the way that they are phrased. Empirical studies of attorneys suggest that particular phrasings, or "framings," can affect a lawyer's willingness to accept an offer. Experimental and real-world data demonstrate that losses have more impact on choices than do equivalent gains. For example, most people think that a 50% chance of gaining $100 is not sufficient to compensate for a 50% chance of losing $100. In fact, people typically need a 50% chance of gaining $200 or $300 to offset the 50% chance of losing $100.

The theory further asserts that decision makers are risk averse when faced with medium-to-high probability gains and risk seeking when faced with medium- to-high probability losses. By framing a settlement offer as a gain and the trial as a risk, the person making the offer may increase his chances of getting the offer accepted, relative to a framing in which the settlement is seen as partial compensation for a loss and a trial as a risky way to perhaps eliminate the whole loss. Furthermore, the tendency to think of gains and losses so differently may lead to a heightened aggressiveness when the bargaining is viewed as an attempt to minimize losses rather than maximize gains.

Why we don't like their offers--Reactive Devaluation: When an attorney receives an offer from the other side, his or her impression of the offer--and indeed, the client's impression--will be

influenced to some degree by her relationship to the person making the offer. In particular, if the attorney's dealings with the other side have been difficult, the attorney may view any offer with a great deal of suspicion. Sometimes the relationship impedes impartial evaluation of an offer, causing a negotiator to reject an offer from an adversary that she should have accepted. This tendency, known as reactive devaluation, is a tendency to evaluate proposals less favorably after they have been offered by one's adversary.

In one study conducted during the days of apartheid, researchers asked students at a college their opinions of two university plans for divestment from South Africa. The first called for timed divestment, the second for an immediate divestment. Some students preferred the first plan and others liked the second. After the initial ratings, each student was told that the university chose the other plan, and the students were asked to rate the plans again. The results were dramatic: Students rated the university plan less positively than they had initially rated it after the university picked a plan they had chosen. They also rated the alternative plan more positively after learning that the university had not chosen it. These results were consistent, no matter which plan a student chose initially.

Certainly, the same sort of reaction attends offers from opponents in legal negotiations. If they are the "enemy," then their offers are discounted, even if the offer contains the things that were initially considered desirable.

How people manipulate each other--tools of Social Influence: Notwithstanding the aforementioned obstacles, people do make deals. They manage, somehow, to persuade the other side to accept offers. They use tools of social influence. The psychological literature ontopics related to persuasion is abundant--and as yet has been rarely adapted over to legal settings. A handful of the best- known tools of social influence are scarcity, authority, liking, social proof, and reciprocation. These are familiar, so the descriptions are brief.

Scarcity is the extra boost of desire one feels for something that will disappear after deadlines pass, opportunities disappear, or something becomes unavailable. Experience suggests that "exploding offers" are accepted more often than offers that ostensibly don't expire.

Authority captures the ways in which the trappings of authority promote certain behaviors. Stanley Milgrom's famous experiments showed that when an experimenter ordered subjects to administer painful electrical shocks to innocent people, that the subjects' willingness to cause pain in others was correlated with the trappings of authority of the experimenter. If ***218** the experimenter wore a white lab coat and other "scientific" emoluments, the subjects were more willing to obey the cruel commands. These experiments stand as a "shocking" reminder of the lengths to which people will go to please or placate someone perceived to be an authority figure.

Liking is somewhat the opposite of reactive devaluation. Naturally, people think more kindly of offers made by people they like, but this may not always yield the best results for a client.

Social proof is the tendency to confirm the rightness of choices or actions by reference to observations of others in similar settings. People view a behavior as correct in a given situation to the degree that they see others performing it. Sometimes following the pack will yield a good

result, but in other circumstances, this method of choice may result in a lemming-like march over a cliff.

Finally, the tendency to reciprocate should not be underestimated. Even uninvited favors and gifts leave people with a sense of indebtedness. In negotiation, there is a strong norm that the recipient of a concession from the other side should make a concession of her own, even if the initial offer from the other side was extreme and the concession not particularly meaningful. The tendency to reciprocate is not in itself problematic, but when the person on the receiving side reciprocates a relatively trivial concession with a more meaningful one, such as a significant reduction of an already-reasonable request, she may be committing a negotiation error.

Lawyers, like all professionals, aspire to make rational decisions and to maximize their clients' outcomes. However, all decision makers, including lawyers, depart from the rational path to best outcomes. Fortunately, psychologists have shown that some of these departures are systematic, and by understanding that they exist and seeing how they operate, decision makers might be able to avoid or overcome the obstacles to best outcomes. For lawyers who settle the vast majority of the cases they handle on behalf of millions of people--many of whom are emotionally engaged in the conflictand rely on their lawyers for advice--this is an area of study of enormous importance. There are no simple answers for how to handle all of this psychology, but that is as it should be--the lawyer's mind is a complicated place.

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