

# Alternatives

TO THE HIGH COST OF LITIGATION

INTERNATIONAL INSTITUTE FOR CONFLICT PREVENTION & RESOLUTION

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## Alternatives

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TO THE HIGH COST OF LITIGATION

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## Making Sound Decisions: How to Help Your Client Evaluate Settlement Options

BY ELEANOR BARR

Imagine these two scenarios:

*Scenario 1.* A plaintiff's lawyer represents a client who has filed a sexual harassment suit against her employer. At mediation, the lawyer makes an initial demand of \$500,000. This number reflects the lawyer's assessment of his client's best-case scenario. In private, the lawyer discusses with his client the risks and uncertainties of litigation, and the possible outcomes if the case goes to trial. He tells his client that she has a "good" chance at winning on liability and a "pretty good" chance at collecting a "six-figure" damage award.

*Scenario 2.* A defense lawyer represents a corporate client who is the target of a suit filed by another company for breach of contract. At mediation, the plaintiff's initial demand is \$750,000. The defense lawyer tells her client that she believes the client will "probably lose" on liability, but that she doesn't think that plaintiff could collect "anything near" \$750,000.

Have these lawyers clearly explained to their clients the potential upsides and downsides of their cases? No, they haven't.

Sure, lawyers use words to describe potential litigation outcomes. But since words alone can be interpreted in a wide variety of ways, they often can lead to real misunderstanding. For example, when three people were asked to explain in a percentage what a "pretty good chance" of

winning means, they gave three different responses: 40%, 60%, and 75%.

In order to make sound, appropriate decisions about whether to settle or go to trial, clients need clear information that is not susceptible to that kind of potential misunderstanding.

This is where decision analysis can be very useful.

Decision analysis, also known as litigation risk analysis, can help clients evaluate multiple uncertainties in a suit, thereby helping them make better decisions about whether or not to settle a case.

Decision analysis boils down to the following three steps:

1. Determine the possible outcomes of the suit and the likelihood of their occurrence;
2. Determine the net cost or net gain with respect to each outcome; and
3. Determine whether nonmonetary factors are influencing your client's decision.

A decision tree is a simple visual way to depict this process. Building a sample decision tree will demonstrate, step by step, how this process works. For those who have math phobia—fear not! A decision tree only requires basic arithmetic and can be easily performed with some paper and a calculator.

Assume you are representing a client who is facing a suit for breach of contract.

*Step 1: Determine the possible outcomes and the likelihood of their occurrence.*

You begin the process by asking two pivotal questions: First, what are the chances of winning and the chances of losing on liability

ADR ADVOCACY

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# Sound Decision Analysis

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ity? And second, if your client loses, what damage amount would be awarded and what is the likelihood of this occurring?

In this case, you estimate that there is a 70% chance that a trier of fact will determine the contract was breached, and a 30% chance that a trier of fact will determine no breach occurred. You note the probabilities on the tree's branches, as depicted in Figure A below.

You then continue the tree from the breach branch to identify the next uncertain event: damages. Your evaluation considers the merits of the plaintiff's claim for actual as well as consequential damages.

You may decide that if damages are awarded, there are a variety of possible outcomes. If so, it is useful to organize them into ranges. For example, an evaluation of the damage range might be \$200,000 (low), \$450,000 (medium) to \$600,000 (high).

These three potential outcomes can be drawn on the damages branch. See Figure B below.

Finally, assign probabilities to these three outcomes, based on the strength of the plaintiff's damage claims, and put them on the tree, as depicted in Figure B. In this case, you believe that the plaintiff's claim for actual damages is strong but the claim for consequential damages is weak. For example, the probabilities can be depicted as a 70% chance for \$200,000, a 20% chance for \$450,000 and a 10% chance for \$600,000.

The tree is complete. Remember, decision analysis is only as good as the estimates used, so it's important to make the most realistic estimates possible.

The next step is to evaluate the outcomes.

*Step 2: Determine the Net Costs Or Net Gains to Your Client.*

To evaluate the outcomes, multiply the possible outcomes of each event by their

**Table I**

Low Range	Medium Range	High Range	Average Damage Award			
(.70 x .70 x 200,000)	+	(.70 x .20 x 450,000)	+	(.70 x .10 x 600,000)	=	\$203,000
\$98,000		63,000		42,000		

**Table II**

Average Damage Award	Estimated Attorneys Fees and Costs	Total Average Costs
\$203,000	+	\$70,000 = \$273,000

probability of occurring. For example, the value of the high range if a breach occurs would be 70% x 10% x 600,000 = \$42,000.

Then add the products of each potential outcome. See Table I above.

The \$203,000 figure is sometimes called the expected value, or from the litigator's perspective, the average amount that a trier of fact would award.

Next, estimate the litigation costs, including attorneys' fees. Assume you estimate these costs to be \$70,000. This amount should be added so that the client has a complete picture of the net result. See Table II above.

The \$273,000 amount can be characterized as the total average costs for the defendant to take the case through trial. Clearly, decision analysis does not guarantee what will happen at trial. But it provides a single number that your client can use to compare the potential costs of trial with his or her current settlement position.

If you do not want to reduce the possible outcomes of trial to a single number, then don't take this final step. You would simply diagram the tree, as outlined in this article and depicted below, with the range of possible outcomes on liability and damages. This, by itself, can help

your client evaluate settlement options by comparing them with the potential consequences of trial.

*Step 3: Determine Whether Non-Monetary Factors Are Influencing Your Client's Decision.*

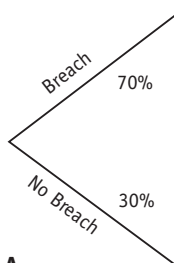
Decision analysis can be used to evaluate the non-monetary factors such as time, emotions and attitude toward risk. When helping clients evaluate settlement options, it's important to explore these intangible factors, because they may affect the client's settlement range.

These intangible factors can be quantified, and added to the decision tree using the analysis described above. But it's often just as useful for your client simply to identify these intangible factors and then determine whether or not they should play a role in increasing or decreasing his or her settlement position.

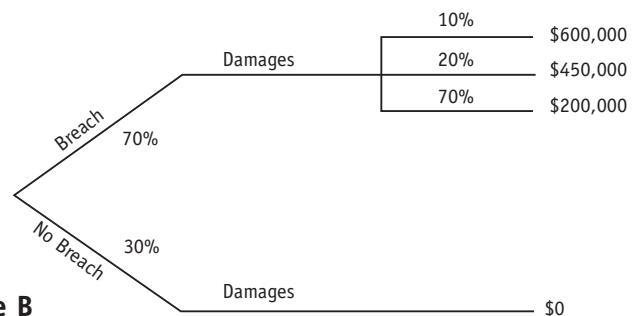
Taken together, the three steps of decision analysis help quantify the key factors, both monetary and nonmonetary, that govern good decision-making. It brings welcome clarity to a process that is inherently uncertain, and is therefore an invaluable tool for you and your client.

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**Figure A**



**Figure B**