At the Table: The First Course — Demands and Offers

By Robert A. Creo

Previous columns have addressed the lawyer's identity and reputation and explored self-awareness, perpetual learning, professional growth through civic service, persuasion and emotion — specifically, fear and anxiety — and the preparation and self-control necessary for engaging at the bargaining table. This column focuses on making and responding to initial proposals and negotiation strategies.

Deciding and Negotiating

Research has proven that humans are hard-wired with certain defaults affecting processing information, judgment and decision-making. Most decisions we make — and how we act upon them — are subject to some form of unconscious bias. This field of study is usually referred to as cognitive psychology or cognitive science. Cognitive science as a separate discipline was introduced by professors Daniel Kahneman and Amos Tversky in 1972 with the study of what they called cognitive bias. Cognitive biases are tendencies to think in certain ways that can lead to systematic deviations from a standard of rationality or good judgment. Their work gave rise to the field of behavioral economics, with Kahneman sharing a Nobel Prize in economic science in 2002 and receiving a Presidential Medal of Freedom in 2013.

Demands and Offers

Lawyers traditionally start bargaining with a specific proposal from the plaintiff/claimant called a demand. This makes sense historically since the plaintiff has initiated the action and must plead relief. This has evolved in most jurisdictions from stating a specific dollar amount to a plea for specific elements or classes of damages.

In the evaluation and adjustment of claims, it is typical to take a micro or segmented approach by assigning a range of value to each element of potential exposure. Although insurance carriers and risk managers will reserve an amount for potential liability early in the case, as required by law or policy, most defendants do not initiate bargaining by making the first offer. This is true despite the fact that the science of cognitive bias supports making the first proposal in any litigation or transaction in order to anchor the bargaining on your end of the spectrum.

The psychological process at play here is called anchoring (or focalism by researchers), which describes the human tendency to rely too heavily on the first piece of information offered (the anchor) when making decisions. During evaluation and decision-making, anchoring occurs when individuals or groups use an initial piece of information to make subsequent judgments. Once an anchor is set, other judgments are made by adjusting away from that anchor, and there is a bias toward interpreting other information around the anchor. This can be restated as the power of first impressions. It is more difficult to erase/dislodge information or an opinion as compared to writing on a blank slate.

Most direct negotiations start with a demand and involve an auction model where a demand is made and then an offer, followed by a series of reductions in demands and increases in offers.

Strategies, Techniques and Tactics

My experience, consistent with the science, is that the benefit of anchoring a negotiation is lost if the initial proposal is extreme or beyond the pale of any possible outcome. Demands should not be outliers in the sense that they are off the bell curve of probability by being in the flat line of reasonable expectations drawn at the end of the proverbial curve. It is recommended, however, that a demand be formulated that is close to the edge of the flat line while remaining inside the curve. In other words, claimants can demand their best or highest verdict potential, but not more. Defendants wisely ignore or otherwise do not respond to extreme demands. This should result in the anchoring effect being reduced or eliminated. Obviously, if there are benchmarks of verdicts or public settlements of or deals in comparable matters, this provides the rationale for the best-case demand. If a plaintiff, because of time pressure or other legitimate considerations, wants to jumpstart the negotiations, the signal of a lower demand will be easily read and reacted to by the defense. Negotiators are more likely to have a shorter negotiation dance under these circumstances.

The defense, in response to an unrealistic or extreme demand, usually attempts to send a message by refusing to make a proposal or low-balling with a nominal offer. Impasse is often quickly reached as parties decline to bid against themselves. In litigated matters, often the parties resort to mediation or judicially supervised settlement conferences when demands and initial offers bring matters to a standstill. In transactions, one party may walk away or find alternatives to the deal.

page 58

from page 57

Asymmetry in the nature of the parties and dynamics does not permit the defense to go below zero with an offer unless there is a viable counterclaim. A small-number offer, closer to zero, without any basis in fact, including nuisance value or avoidance of transaction costs, usually is met with a comment by counsel that the defendant is now insulting the plaintiff. Low-balling with laypeople is usually counterproductive and further polarizes the parties, causing the plaintiff to dig in to an unrealistic starting position.

My experience recommends that an offer made in response to an unrealistic demand should carry an express disclaimer that it is not in response to the amount of the demand. The offer should delineate objective factors that support it. It should not be a low-ball proposal or a message intended to show resolve or strength since these are rarely effective if the offerer has a sincere interest in ending the matter. It should be an amount that is inside the comfort level of the defense, yet could be near a reasonable place to settle the case.

The zone of possible agreement (ZOPA) is an abstraction intended to identify a range of numbers or potential overlap between the parties' final positions in a negotiation or sales transaction. Both parties are willing to make a deal within this range. This zone may be defined by comparable prior matters or created ad hoc by the parties based upon a mix of objective and subjective factors. Others may characterize this as reaching the fair market value of a matter based upon a willing buyer and a willing seller in an arms-length transaction. Many times counsel signal to each other informally these parameters or otherwise carve out the turf in oral communications to lay a framework for a ZOPA. Many times the client is not listening to the reasonable recommendations of his or her own counsel, so ignoring the demand moves the process forward toward resolution.

When the reasonable offer intended to reach the ZOPA is communicated in response to the unrealistic demand, it should be made expressly clear that it is not related to the demand and is not made as a response but as an offer independent of the demand. A calm and confident explanation why the demand is an outlier and being ignored for practical purposes should accompany the offer as a preamble. The goal is for the defense offer now to anchor the negotiations and to obtain a response that is closer to the ZOPA. If the demand is lowered substantially, most likely outside the ZOPA yet closer to its boundary, then an action can continue. If this invitation is rejected by only a marginal reduction in the demand, then the defense should break off negotiations and walk.

Some rules of thumb and appropriate tactics are based upon some general expectations:

1. Most negotiations should follow a monotone concessionary pattern that involves larger moves at the beginning, with each successive move being a smaller step by the party. It avoids sending mixed messages and creates a consistent and more predictable pattern. For example, demands could be reduced as follows: Initial demand, $1 million; concession 1, $750,000; concession 2, $550,000; concession 3, $400,000; concession 4, $300,000; concession 5, $250,000 and settlement. Concessions amounts, in descending monotone order: $250,000, $200,000, $150,000, $100,000 and $50,000. Each step is progressively smaller without an erratic pattern such as move 1, $50,000; move 2, $250,000; move 3, $100,000; move 4, $150,000; and final move, $200,000.

2. Once both parties are in or near the ZOPA, bargaining tends to move to the midpoint of the demand and offer.

3. Once you offer to split the difference, you will never obtain more and you have expressed one number you will now accept. The other side can take advantage of this by rejecting the split and offering to split between your new number and their last number. For example, the demand is now $40,000 and the last move an offer of

TAKEAWAYS

- Making the first economic proposal should be advantageous.
- Initial positions should be at the edge of the best possible outcome.
- Bargaining concessions should not be random, and monotone patterns are common.
- Identify a zone of possible agreement (ZOPA) and plan the bargaining to meet a comfortable goal within it.
- Once in or near the ZOPA, bargaining tends to the midpoint.

$20,000. Plaintiff wants to cut to the chase by proposing to split the delta at $30,000. It is a no-lose proposition for the defense to counter by rejecting the $30,000 and offering to split the difference between $20,000 and $30,000 at $25,000. An observer in the room now knows the plaintiff will take $30,000, the defense will pay $25,000 and the case is almost certain to settle between $25,000 and $30,000. The plaintiff can dig in at $30,000 and risk impasse or counter with a number between $27,500 and $29,000. My experience is that counsel banter back and forth until a number is reached. ⚖

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