AMERICAN BANKRUPTCY INSTITUTE

# 2019 Southeast Bankruptcy Workshop

*Skills Track*

# Mediation Strategies in Chapter 11


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CONCURRENT SESSION

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# EMOTION and MEDIATION

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## TRIGGER POINTS IN MEDIATION

- Money dispute
- Power
- Fraud
- Lying
- Breach of agreements/contracts
- Feeling of victimization
- Need to win/impress/be appreciated
- Frustration
- Arrogance/ aggression
  - Client
  - Attorney….opposing of course!

# Overview

1. Introduction
   - Anger, frustration and other emotions in mediation
   - Anger is visible emotion but other emotions are underneath
2. The angry/emotional decision maker – the relationship between appraisal, cognition and anger
3. Developing a "toolkit" to manage emotion
4. Harvard Negotiation project
5. Fisher and Schapiro: using emotions in negotiation
6. Dealing with one's own anger
7. Techniques: "I" messages, diffusing, active listening, CARS, EARS and BIFF
8. Conclusion-role of Mediator
9. References

# Whose emotion?

- Parties
- Attorneys
- Mediator

# 5 Critical Core Concerns That are Basic to all Humans

Harvard Mediation Project/ "Beyond Reason"

Emotions are not rational!

the underlying motivations: Emotions have unique and powerful influence on negotiation & results

1. Appreciation
2. Affiliation
3. Autonomy
4. Status
5. Role

# Critical Core Concerns

- Appreciation—find the merits in the other person's point of view; ask individual to try acting as the impartial mediator; refrain from judging whose side is right or wrong
- Affiliation—individuals need to feel some personal connection to others
- Autonomy—individuals want to preserve if not enhance their autonomy
- Status—individuals want to have their status acknowledged
- Role—individuals want to occupy a fulfilling role within the negotiation

# Emotions--Unique Thought Processes

- Emotion related cognition interrupts ongoing cognitive processes (attention, memory, judgment)
- Sadness: Situational forces seen as more responsible for ambiguous events rather than another person (anger)
- Guilt and Shame: negative events associated with the belief that oneself is responsible
- Fear and anxiety: If an individual feels uncertain or lacks confidence about the cause of negative events
- Anger: others at fault

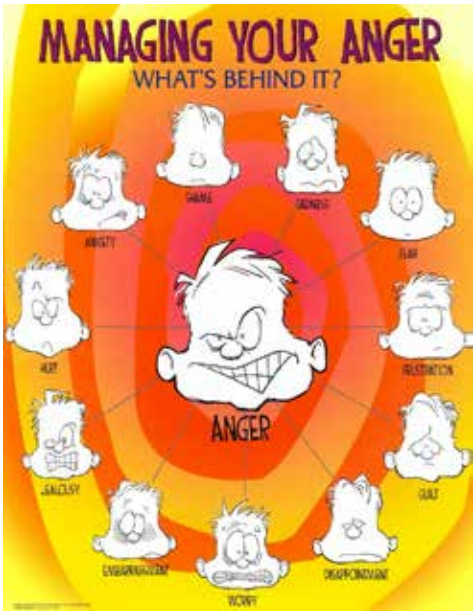
Lerner & Tiedens

# The Appraisal-Tendency Framework

- To understand effects of specific emotions on judgment and decision making
- Specific emotions lead to unique cognitive and motivational properties
- Each are expressed biologically and behaviorally

"Portrait of the Angry Decision Maker: How Appraisal Tendencies Shape Anger's Influence on Cognition," Lerner and Tiedens, Journal of Behavioral Decision Making, 19: 115-137 (2006)

# Underlying Motivations




- Anger is the tip of the iceberg, that is, anger is a feeling with hidden deeper emotions
- By examining situations (triggers) that cause anger, it becomes clear that the underlying feelings are hurt, anxiety, shame, frustration, feeling of victimization, etc.
- Anger and other intense emotions are associated with bodily reactions, such as, rise in heartbeat and blood pressure, gritting one's teeth, clenching one's fists, becoming tense, sweating, grimacing, feeling a knot in one's stomach, etc.
- **When emotion is high, cognition is low**

- Rice, S.

# Anger Has Unique Effect On

- Outcome: What people think
- Process: How people think

- Impact on:
  - Judgment
  - Decision making
- Influences perceptions, beliefs, ideas, reasoning, and ultimately choices

# Anger

- Anger is one of the most frequently experienced emotions
- Anger has an infusive potential: it carries forward from past situations to unrelated judgments and decisions

- Anger associated with:
  - The sense that self, or someone close to self, has been offended or injured
  - Anger is associated with a sense of certainty or confidence: optimism
  - Anger is associated with the belief that another person was responsible: blame
  - Anger is associated with the notion that the aggrieved has power to do something about this: control

# Outcome : What Think

- Tendency to attribute blame to another
- Tendency to respond more punitively
- Optimistic judgment and increased risk taking
- Increases sense of control and certainty
- Indiscriminatively punitive
- Anger and happiness produce similar levels of optimism about self; not necessarily realistic
- Eager to act
- Thinking, processing impaired

# Process : How Think

- They think they will prevail
- Triggers a bias toward seeing the self as powerful and capable
- Angry decision-makers typically process information in trial-and-error, non-systematic ways, without considering alternative options
- If thinking lacks careful analysis, they are likely to make quick decisions, related to sense of certainty and optimism
- These distorted appraisals may hinder ability to use objectivity and rationality

# Fear- opposing perceptual lens vs. anger

- pessimistic expectations as to the likelihood they will succeed in the future
  - "I'll be victimized."
  - "I will come out on the bad end."
- Fear
  - Associated with decreased problem solving
  - Decreased processing speed
  - Decreased short term memory
  - Becoming more immobilized

# Emotion specific physiology

## adaptive biological processes

- Emotions regulate stress responses in specific adaptive ways

- Fight (anger) or flight (fear) response - immediate
  - response to a perceived harmful event, attack, or threat
  - Adrenalin and nor-adrenalin released by adrenal cortex
  - Cardiovascular and other changes

- Cortisol, a hormone produced by adrenal cortex
  - "stress hormone" – slower process
  - Increases blood pressure and blood sugar
- Anger leads to increased cortisol : mobilizes energy/confrontation
- Fear leads to decreased cortisol: withdrawal/avoidance

# Appraisal Theory Summary

- To understand the impact of specific emotions on judgment
- If reach an impasse in negotiations, step back and look at these factors
- Emotions carry with motivational properties that can carry over into judgments and decisions
- Emotions not only can arise from certain cognitive approaches but can also give rise to cognitive predispositions to appraise future events

# Is Anger a Negative or Positive

- Feel can control a situation and change it
- Feel can conquer opponents and obstacles
- Triggers careless thought
- Anger may be especially exhilarating when revenge anticipated (schadenfreude)
- Exhilaration may portend negative consequences
- Rush and optimism may lead to unwise choices, violence and aggression
- Effects on cognition-processing, memory, problem solving

# When is Anger Good?

from obstacle to productive force


- Anger can be beneficial when expressed constructively: focus on problem solving
- Anger/assertiveness can be constructive whereas aggression is destructive
- Anger can be the impetus for social change
- Anger can improve work and social relationships: catharsis
- Constructive anger expression allows for both parties to express their feelings/grievances
- Constructive anger promotes ultimate solving of a problem

# Developing a toolbox

- Interest based negotiations
- Harnessing emotion for constructive purposes
- The work of Bill Eddy, J.D., LCSW
  - EAR, CARS, BIFF
- Dealing with one's own anger; self-calming
- Talking and negotiating tips
  - Use of "I messages"
  - Diffusing the other person's anger
  - Active Listening

# Harvard Negotiation Project

5 Rules:

1. Separate the people from the problem—think of engaging the other person as a partner in the solution to the problem using their input to help arrive at a resolution; not "us" against "them" but "us" against "it"
2. Don't bargain over positions—focus on the goal and various ways to obtain it; gives more options for arriving at a solution
3. Focus on interests rather than positions—look for ways to achieve goals/interests without having a specific position
   - "what want:" position
   - "why want it:" interest
4. Invent options for mutual gain—examine each other's interests to come up with options in which both parties gain
5. Insist on using objective criteria—e.g., some industry standard in business negotiations or developmental needs in family disputes.

## "Beyond Reason: Using Emotions as You Negotiate"

Roger Fisher and Daniel Shapiro/Harvard Negotiation Project

- Using emotions as a positive force in negotiation/mediation
- A model which attempts to harness the ubiquitous human feelings in ways that are constructive to agreement
- Assist in building rapport
- Aids in creating a positive environment for agreement

## Dealing with One's Own Anger

- To effectively interact with other people one must learn how to manage one's own anger
- Anger interferes with effective problem-solving unless it is dealt with
- Anger is associated with an adrenaline rush such that the response is both psychological and physiological: fight or flight response
- Even when anger feels justified or righteous, it works against a person's own best interests because it impairs the ability to negotiate effectively
- Use self calming mechanisms and techniques to reduce the adrenaline rush and enhance the ability to think clearly and problem solve effectively
- Develop compassion rather than reciprocal anger by recognizing that anger is a person's best shot at getting their needs met

Rice, S.

# Self Calming Mechanisms:

## Relaxation Response as Antidote to Fight or Flight

- Counting to 10
- Taking deep breaths
- Taking a walk/changing environment/take a break to regroup and refresh
- Venting
- Meditating, imagery and other relaxation techniques
- Humor
- Cognitive reframing/cognitive restructuring
- Better communication—listen and respond before reacting
- Problem solving

Rice, S.

# As said by…

- "When angry, count to 10 before you speak; if very angry, a hundred"

  Thomas Jefferson

- "When angry, count to 10 before you speak; if very angry, swear."

  Mark Twain

- "If you are patient in one moment of anger, you will escape 100 days of sorrow."

  Chinese Proverb

- "He who angers you, conquers you."

  Elizabeth Kenny

Cited in Fisher and Shapiro

# Talking and Negotiating:

## Alternative to Fight or Flight

- Use of "I messages"
- Diffusing the other person's anger
- Active/empathic Listening
- Reframing
- Validation
- Non-verbal
- Use of apologies

# "I-Messages"

- Technique to confront a problem behavior/situation to:
  - enhance the chance you will be accurately heard
  - without making the other person defensive
- Takes extra work and energy
- Focus on a specific piece of behavior that is problematic rather than the individual
- Does not resolve the conflict, but is a way to open up the problem-solving process
- Operating assumption: when there is a problem, it is shared by both participants
- Letting go of the concept of fault frees up both to be involved and invested in finding solutions

Rice, S.

# Examples of "I" statements

- " When… " Describe the behavior objectively, not the motive
- "The effects are... " Describe how the behavior impacts you
- "I feel..." State feelings in a positive way related to a goal
- "I'd prefer... Propose a small ask
- "The consequences will be…" Explain the appreciation or the negative consequences around the behavior
- "What's your reaction..." What did they understand, do they have an alternative, how do they feel or think

# Diffusing Anger

## 5 steps

1. Listen—pay attention to both the words and feelings expressed by the other side without interrupting; people stop venting when they believe you are listening because they want a reaction from you
2. Acknowledge the anger— "I can see that you are really upset", and without any judgment
3. Apologize—shows genuine sympathy for someone's pain without taking responsibility for causing it
4. Agree with the truth—acknowledge the other person's perspective is legitimate, to de-escalate the situation and enhance problem-solving, without having to agree with it
5. Invite discussion—this respects the feeling of the other person and allows for a regaining of cognitive abilities by reducing anger; this engages the other person as an ally and refrains from blame or accusation

Rice, S.

# Don'ts in Diffusing Anger

- Don't debate the facts
- Don't ask "why" questions
- Don't jump to conclusions
- Don't rush
- Don't use sarcasm
- Don't criticize and blame
- Don't impose your value judgments
- Don't nag and preach
- Don't counterpunch
- Don't take a statement at face value

Rice, S

# Active Listening: verbal and nonverbal responses

- Posture—convey ease and attentiveness, not intrusion or relaxation
- Facial expression—no criticism or judgment; be engaged, nod
- Eye contact—a balanced position in which eye contact is maintained
- Words—
  - Let person talk…until done
  - Don't interrupt
  - listen for meaning
  - repeat and reframe…first
  - Respond nondefensively…next

# Bill Eddy, LCSW, Esq.

www.highconflictinstitute.com

- "You are not responsible for the outcome."
- "It's not about you."
- "Don't work harder than your clients."
- "It's another dilemma for the parties to resolve"
- "That is, be aware of your own emotional contributions to the impasse."

- High conflict mediation strategies
  - Bonding
  - Structuring
  - Reality testing
  - Consequences

# EAR method

Bill Eddy

- Empathy – build bond
  - build relationship and trust
  - Empathy does not mean agreement
  - They distort information and need reality testing
- Attention-
  - emotional clients need more attention, repeat and repeat
  - Emotional clients need more structure to avoid slipping into their distracting emotions
- Respect –
  - show nonverbally and verbally: lean in, nod
  - Give emotional client time to vent

# E.A.R. statements

- BONDING
  - "I can empathize with…
    - how difficult this process is for you."
    - how important these decisions are to you."
  - "I really respect the efforts you have made to present a thoughtful proposal."
  - Use nonverbal – nodding, leaning in
- STRUCTURING
  - Provide structure around making a proposal
  - Ask them to respond:
    - "Yes, no, or I'll think about it"
    - If they argue, blame, focus on the past, don't criticize but repeat, "So, what's your proposal?"

# Reality testing/ Consequences

- Distortions with high emotionality present impossible issues
- Avoid appearance of taking sides
  - "You might be right! You have a dilemma!"
- Educate about realities and consequences
  - External consequences, policies, law
  - Self-defeating

- "You might be right: I've seen cases where one side was hiding money; I've seen cases where one person thought the other was hiding money and they were not. Here are your options:"
  - Stop mediation and do thorough discovery
  - Do some discovery and return to mediation
  - Continue the mediation and accept the uncertainty."

# CARS METHOD

How to calm down high conflict person:

- CONNECTING with empathy, attention and respect (E.A.R.)
- ANALYZING alternatives or choices
- RESPONDING to misinformation
- SETTING LIMITS on inappropriate behavior

Bill Eddy, LCSW, Esq.

# CARS with High Conflict Persons

- Calm HCP's emotion by forming a brief positive connection
- Reduces blame or attacking back
- Enhances their ability to access their problem-solving skills for a while
- Soothes HCP's unconscious defenses
- Calms their fear
- Mediator is perceived more as an ally in solving an objective problem

# BIFF Response

HOW TO RESPOND TO HOSTILE EMAILS:

- BRIEF- keep your response brief
- INFORMATIVE- correct inaccurate statements
- FRIENDLY- best way to end the conflict
- FIRM- non-threatening, clear and confident statements

Bill Eddy, LCSW, Esq.

# The Role of Mediator

- Prepare; learn about trigger points/emotions
- Create a safe environment
- Model appropriate behavior
- Encourage others to talk about their anger in a constructive manner
- Use empathic listening
- Guide people to rephrase or reframe their issues and concerns constructively
- EAR, CARS, BIFF

# THE END

- Use these concepts as a goal/framework
- Conditions where they won't work:
  - too angry
  - too rigid
  - feel too unsafe
  - unable to participate meaningfully- impaired (substance abuse, mental illness, personality disorder)

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# NEGOTIATING THE SETTLEMENT OF A LAWSUIT

**A Presentation for the American Bankruptcy Institute's Southeast Conference in Amelia Island**

**July 18-21, 2019**

**C. Edward Dobbs**
**Parker, Hudson, Rainer & Dobbs LLP**
**Atlanta, Georgia**

# NEGOTIATING THE SETTLEMENT OF A LAWSUIT

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# NEGOTIATING THE SETTLEMENT OF A LAWSUIT

**C. Edward Dobbs**
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## I. Overview of Settlements

A. Some Statistics

1. A report of the Association of Trial Lawyers of America, with a research date of April 28, 2013, found that the annual cost to the U.S. economy for civil lawsuits is $233 billion; the average compensation payout for personal injury lawsuits is $60,000; the percentage of punitive damages awards won by plaintiffs is 6%; and the average award in a punitive damage lawsuit is $50,000.

2. According to the same report, the percentage of tort lawsuits won by the plaintiff is 48% -- with the percent of cases won in bench trials being 54% and the percent of cases won in jury trials being 46%. It is likely that the 52% of tort plaintiffs who lost their cases were steadfast in their belief that they had meritorious claims.

3. Since 1960, there has been a marked decline in trial rates, and summary judgment has been identified as contributing to that decline. See Marc Galanter, "The Vanishing Trial: An Examination of Trials and Related Matters in Federal and State Courts," 1 J. EMPIRICAL LEGAL STUD. 459 (2004). Several empirical studies have found an increase in the use of summary judgment motions and an increase in civil case terminations through the use of summary judgment practice as opposed to trial. *See* Theodore Eisenberg & Charlotte Lanvers, "Summary Judgment Rates Over Time, Across Case Categories, and Across Districts: An Empirical Study of Three Large Federal Districts," Cornell Law School Research Paper No. 08-022, prepared for The First International Conference on Empirical Studies of Judicial Systems (May 28, 2008 draft), at 1-4 (noting a 2007 study that concluded that in fiscal year 2006, about 4% of federal cases were terminated by summary judgment).

B. The Law Favors Settlement

1. It has long been the policy of the courts to encourage the settlement of litigation. *See* Stephen McG. Bundy, "The Policy in

Favor of Settlement in an Adversary System," 44 HASTINGS L. J. 1 (1992). This policy has been spawned in part by congestion in the nation's courts and is also the product of the belief of some that "a bad settlement is almost always better than a good trial." In re Warner Communications Sec., Litig., 618 F. Supp. 735, 740 (S.D.N.Y. 1985), *aff'd*, 798 F.2d 35 (2d Cir. 1986).

2. It is the strong policy in most jurisdictions for parties to attempt to settle their differences. *See, e.g*., SEC v. Citigroup Global Markets, Inc., 752 F.3d 285 (2d Cir. 2014) (reversing district court's refusal to approve a settlement because the defendant declined to acknowledge culpability); In re Syncor ERISA Litig., 516 F. 3d 1095, 1101 (9th Cir. 2008) (noting the "strong judicial policy that favors settlements, particularly where complex class action litigation is concerned.); LNV Corp. v. Studle, 743 S.E.2d 578 (Ga. App. 2013); Pickett v. Holland Am. Line-Westours, Inc., 35 P.3d 351 (Wash. 2001), *cert. denied*, 536 U.S. 941 (2002).

C. Most Cases Settle

1. Irrespective of the time or scope of studies on the subject, it is clear that the overwhelming number of civil litigation matters ultimately settle. *See* James C. Duff, ADMIN. OFFICE OF THE U.S. COURTS, JUDICIAL BUSINESS OF THE UNITED STATES COURTS: 2010 ANNUAL REPORT OF THE DIRECTOR 172 (2011) (stating that of some 309,000 civil cases in federal courts terminated during a 12-month period ending in 2010, approximately 1.1% of them were terminated by trial, after taking into account both the granting of dispositive motions and settlements reached by the parties).

2. Some early studies have concluded that only 7% of cases filed in federal courts are decided by a judge or a jury. *See* Marc Galanter & Mia Cahill, "Most Cases Settled: Judicial Promotion and Regulation of Settlements," 46 STAN. L. REV. 1339, 1340 n. 2 (1994). Other early studies, looking at both federal and state settlement rates, indicate that only 5% of all civil cases are ultimately decided by a judge or jury. *See* Susan C. Del Pesco & Richard K. Herrmann, "The Second Face of Toxic Tort Litigation: Claims for Insurance Coverage," 2 WIDENER L. SYMP. J. 205, 219 (1997). *See also*, Brian J. Ostrom & Neal v. Kauder, EXAMINING THE WORK OF STATE COURTS, 1996: A NATIONAL PERSPECTIVE FROM THE COURTS STATISTICS PROJECT, at 11, National Center for State Courts (1997) (noting that less than 3% of civil cases reach a trial verdict and less than 1% of all civil dispositions are through jury trials).

3. These statistics do not mean that the balance of the cases that are not resolved at trial are settled. Some may be the subject of dispositive motions and others may simply be voluntarily dismissed with or without prejudice by the plaintiff. *See* Theodore Eisenberg and Charlotte Lanvers, "What is the Settlement Rate and Why Should We Care?" SIXTH JOURNAL OF EMPIRICAL LEGAL STUDIES, Issue 1, 111-146 (March 2009).

## II. When to "Talk Settlement"

A. Any Time is a Good Time

1. Settlement discussions can be initiated at any time -- after an overt threat of litigation, but before its commencement; at any time after commencement, but prior to trial; after trial and before the jury or judge returns a verdict or judgment; or after entry of a judgment and during the pendency of an appeal. The choice is rarely between settlement and litigation, but rather the point in time when it becomes appropriate in the eyes of the parties to attempt to resolve their differences by agreement.

2. Some may be concerned that initiating settlement discussions is a sign of weakness. Hence, some counsel are reticent to be the one to suggest a settlement dialogue. That may explain why so many cases settle "on the courthouse steps," when counsel and parties more soberly assess their case and believe that broaching the topic of settlement is less likely to be misconstrued as a lack of resolve.

3. A court's intervention may facilitate settlement discussions among the parties. The court may refer the parties' dispute to a court-connected mediation program. Some courts have the power to refer cases to mediation, but cannot order parties to resolve their difference in mediation. *See* Dept. of Transp. v. City of Atlanta, 380 S.E.2d 265 (Ga. 1989). In addition, the court may require a settlement conference with the parties, either pursuant to Rule 16 of the Federal Rules of Civil Procedure in the case of a lawsuit pending in federal court or a corresponding state statute or rule in the case of a lawsuit pending in state court.

B. Settlement Talks Prior to Litigation

1. The parties may undertake settlement discussions prior to commencing a suit or arbitration because they are contractually required to do so, or to engage in formal mediation. Courts have unhesitantly enforced agreements to mediate by requiring mediation prior to arbitration. *See, e.g.*, Clarke's Allied, Inc. v. Rail Source Fuel, LLC, 2012 WL 6161565 (E.D. Tex. Dec. 11, 2012). The Commercial Rules of the American Arbitration Association now

require mediation as precursor to binding arbitration in matters involving $75,000 or more, unless the parties to the arbitration opt out of the mediation requirement. *See* AAA Commercial Arbitration Rule 9.

2. In some cases, the parties may elect to undertake mediation prior to the commencement of a lawsuit. A risk of doing so is that the parties may lack essential information for informed bargaining. *See* Dwight Golann, SHARING A MEDIATOR'S POWERS: EFFECTIVE ADVOCACY IN SETTLEMENT at 132 (American Bar Association 2013) (citing an American Bar Association study in which 81% of mediation users expressed the belief that the best time to mediate is after "critical," but before full, discovery is completed).

3. Putative plaintiffs should make certain that the applicable statute of limitations or repose will not run during the period that settlement discussions are being held. To ensure that an approaching limitations period does not bar pursuit of a claim if settlement is not achieved, the plaintiff might insist upon the execution of a so-called tolling agreement that extends the bar date during the period of settlement discussions and typically an additional period (say, 60 days) thereafter.

C. Post-Commencement Settlement Talks

1. After the commencement of a lawsuit, the court may require a settlement conference overseen by the trial judge.

2. Settlement discussions may be required as a result of a court-ordered mediation.

3. The parties may voluntarily undertake to mediate their dispute, either as part of or separate from the court's mediation program. The parties often undertake settlement discussions without the aid of a mediator.

D. Factors Prompting Settlement Discussions

1. If the anticipated source of recovery for the plaintiff is an insurance policy covering the claim, both the plaintiff and the defendant may be desirous of settling early on so that policy coverage is not depleted by legal fees incurred in the defense of the litigation.

2. If a litigant makes an offer of judgment or settlement pursuant to Rule 68 of the Federal Rules of Civil Procedure ("FRCP") or

pursuant to an equivalent state rule, counsel for the offeree may be wary of the consequences of rejecting such an offer.

3. The filing of a dispositive motion, such as a motion to dismiss, for judgment on the pleadings, or for summary judgment, may refocus a litigant's attention upon the strength and value of its case, as well as the likelihood (and consequences) of the motion being granted.

4. An approaching trial date often has a sobering effect upon parties and their counsel. As noted English writer, Samuel Johnson, is supposed to have said, "Nothing concentrates one's mind so much as the realization that one is going to be hanged in the morning."

5. From the perspective of a defendant, the risk of imposition of punitive or treble damages may provide ample incentive for it to make settlement concessions.

6. The specter of substantial litigation costs (particularly in discovery, where most costs are typically incurred) may coax otherwise reluctant litigants to the settlement table. However, "sunk costs" resulting from significant past litigation activity may be an obstacle to settlement.

7. If one party has been awarded preliminary equitable relief, such as a temporary restraining order or preliminary injunction, a counterparty, for whom "time is of the essence," may opt for a settlement resolution.

8. A defendant's concern for reputational issues that may flow from the commencement and vigorous prosecution of a suit, such as one involving allegations of fraud, mismanagement, unethical conduct, or discrimination may lure a defendant to the settlement table.

9. If a judgment for the plaintiff in the amount requested would threaten the ongoing viability of the defendant organization, the defendant may be prepared to make significant concessions to buy peace.

## III. Disputes Difficult to Settle

A. Lack of Information

1. Although an early initiation of settlement discussions can save parties significant investments of time and expense in the litigation, a disadvantage exists when a party lacks information that is essential to informed bargaining. Lack of information often centers around evidence of damages and the absence of expert reports calculating lost profits or other damages.

2. Litigation attorneys are often obsessed with "leaving no stone unturned" in the discovery process. The desire to find the proverbial "smoking gun" can result in parties feeling unprepared to negotiate when they have not undertaken some discovery. Like some physicians who prescribe every conceivable diagnostic tests, counsel may worry that the failure to discover a "smoking gun" that is found to exist after trial or settlement can lead to malpractice claims. As a result, an inordinate amount of time and expense is often devoted to a wide-ranging discovery process by both sides.

3. Parties desirous of a settlement should be prepared to exchange documents and other information that may assist case evaluation by the other side and informed bargaining, particularly where that information is otherwise freely discoverable in litigation.

B. Strong Emotions of Parties

1. Fear, anger and other emotions of a party may cloud thinking and ultimately become a barrier to settlement.

2. Fearful people usually have pessimistic risk assessments, tend to make risk-averse choices, feel vulnerable and not in control, and rarely see an upside to compromise.

3. Anger may surface when a party feels that it has been mistreated by the opponent, either prior to or during the course of the litigation. Through litigation, a party may seek vindication and validation from a judge or jury of the party's "aggrieved status" or confirmation that the party is "blameless" and recognition that the opponent is culpable.

4. The surfacing of anger or other strong emotions in the course of a settlement conference can elicit a similar response from an opposing party and frustrate the goal of settlement discussions.

5. In a recent mediation, the plaintiffs, who claimed to have been defrauded into making investments in the defendant corporation by allegedly false representations of the defendant officers and directors, rejected substantial settlement offers from the individual defendants because, after giving effect to the settlement, the individual defendants would still possess some (though nominal) assets. Anger and the desire for revenge were motivating factors, as the aggregate settlement amount would have still left the plaintiffs with substantial losses.

C. Desire to Establish a Favorable Precedent

1. Settlement prospects are severely diminished when one party's primary motivation is to overturn an adverse ruling that may have an impact beyond the case at hand or to establish a favorable precedent for ongoing business reasons. This motivation is frequently encountered in dealing with governmental agencies that wish to establish a favorable precedent in various jurisdictions throughout the country and view settlement as thwarting that goal.

2. To be weighed against the desire for a favorable precedent is the prospect that an adverse ruling or unfavorable precedent may lead to an untenable business environment for a party or the prospects for significant future litigation based on the adverse ruling.

D. Litigating on "Principle" or for Public Vindication

1. A party may be litigating on "principle" rather than economics or other practical realities. However, parties often confuse a desire for retribution with a desire for "justice" and therefore believe they are negotiating out of principle when in truth vengeance is their real motivation. For example, a defendant may feel that the claim asserted against it is frivolous and will not "knuckle under" to a settlement solely for the purpose of defraying defense costs -- "I would rather pay my lawyer to teach you a lesson than pay the same amount as 'ransom money' to you!"

2. When a party seeks public vindication, as might occur when significant press coverage has intimated that the party has been guilty of wrongdoing, settlement will rarely achieve the party's desired litigation goal.

3. Those bargaining from a position of principle or for public vindication may grow weary of the fight if they have significantly underestimated the necessary investment of time and expense establishing the principle or achieving vindication.

E. Justice and Fairness

1. Although lawyers and lay persons often refer to the "justice system" and the dispensation of "justice" by courts, there is little agreement on what a just result would be in a given civil dispute or how the interests of justice are served by a particular dispute resolution.

2. In negotiating the settlement of a lawsuit, many parties are motivated by a sense of entitlement to "justice" and "fair" treatment. At times, justice and fairness in their minds means that

they receive the same or substantially the same treatment that others in the justice system receive in what they perceive to be similar circumstances. For example, if multiple co-obligors are sued on the same instrument and several of them settle, a remaining defendant in settlement negotiations will surely want to know, for "fairness" sake, at what price each co-defendant settled.

3. This desire for equality of treatment may extend to settling defendants who have been told of settlement results achieved by other defendants in unrelated, but similar, litigation brought by the same plaintiff. The anecdotal evidence may be a more significant influencing factor in the negotiations than the particular facts and merits of the defendant's case.

4. Plaintiffs, too, in their quest for "justice" and "fair" treatment are influenced by reported recoveries in similar cases. The recoveries in those cases become the benchmark against which the plaintiff assesses the fairness of settlement offers made to it. One can see how outlier recoveries, such as that in the McDonald's hot coffee case, can have an anchoring effect on plaintiffs and create unrealistic expectations.

F. Involvement of Multiple Parties

1. The larger the number of parties involved in a dispute, the more difficult it may be to orchestrate an acceptable "global" result.

2. This is especially true when multiple parties are not aligned and have significant adverse interests. For example, there may be a claim prosecuted by a party against multiple defendants who are alleged to be jointly and severally liable but who have differing defenses and potential cross-claims against one another, as well as rights of contribution and reimbursement. The defendants may have a common interest in defeating the plaintiff's claim, but conflicting interests in apportioning fault and damages. In these types of disputes, it may be very difficult to settle with one defendant without settling with all of the other defendants.

G. Inequality of Bargaining Power

1. When there is a substantial inequality of bargaining power among the parties, the party in the superior position may feel that a "scorched earth policy" in the litigation will wear down the weaker opponent.

2. Inequality may result from a variety of factors, including a party's relative lack of financial resources, a party's time constraints in

obtaining dispute resolution, or reputational issues that are significant for a party to preserve.

3. When a plaintiff having a superior position is also motivated by a desire for revenge, settlement prospects may be dim. Indeed, it may prove difficult to coax the plaintiff to participate in a settlement conference.

H. Disagreements over Interpretation of Law

1. When the primary impediment to a negotiated resolution is a disagreement over the law, its interpretation, or its application to the facts, a settlement may be difficult to reach.

2. The party believing that it has the better legal position may view the outcome of litigation as a chance to "win it all." Settlement prospects becomes even more remote when the counterpart holds the same view of its case.

3. When a case may be disposed of as a matter of law, parties confidant in their legal positions will usually file dispositive motions and may be content to await a ruling before engaging in serious settlement discussions.

4. Unlike fact-based disputes, where the outcome may turn on the credibility of witnesses or the persuasiveness of expert testimony, a law-based controversy can often be resolved on briefs and without undue expense.

I. Contingency Fee Arrangements

1. When a plaintiff's counsel has taken a case on a contingency fee basis, the plaintiff may feel that it has no real "skin in the game," other than reimbursable out-of-pocket expenses incurred by counsel and the plaintiff's time and emotional investment in the case.

2. Plaintiff's attorney may view the case as having a potential "jackpot" outcome and be disinclined to recommend settlement absent an unrealistically high settlement payout.

3. Counsel may be unduly influenced by the economics of the case, depending upon whether counsel has the case on a contingency fee or an hourly fee arrangement. Thus, a contingency fee plaintiff's counsel may view with disfavor settlement proposals that entail a substitution of non-monetary consideration, in whole or in part, for a lump sum settlement payment.

J. Third-Party Litigation Funding

1. A plaintiff may have obtained third-party funding for the case and ceded significant authority over settlement of the dispute to the litigation funder.

2. Opposing counsel should inquire whether a third-party funding arrangement exists before entering into settlement discussions. If a funding arrangement exists, the defendant should condition its participation in settlement discussions upon the active participation of the litigation funder.

3. On occasion, the existence of litigation funding can actually facilitate a settlement. A litigation funder normally is free of many of the biases affecting the case assessment and decision-making of parties and their counsel and may be more objective, rational, free of emotion, sophisticated in risk assessment, and economically (rather than emotionally) driven in determining when and at what level to settle a dispute.

4. Because litigation funders may take a collateral assignment of the cause of action and proceeds realized from trial or settlement as security for their funding or acquire a percentage ownership interest in the claim, counsel for the defendant should be certain to obtain the litigation funder's consent to the settlement and to disburse settlement proceeds pursuant to mutual agreement of the litigation funder and the plaintiff.

K. Defendant Pleads Poverty

1. In many cases, the defendant may not have the financial resources to pay a judgment against it for even a fraction of the amount sought to be recovered.

2. A defendant who "pleads poverty" may attempt to use lack of financial resources and the possibility of bankruptcy to its advantage in the settlement negotiations. The plaintiff, on the other hand, will usually insist upon some evidence of the defendant's financial wherewithal, with a warranty of accuracy of disclosures regarding such financial condition in the settlement agreement as a condition to the effectiveness of any claim releases.

3. The defendant will understandably be reluctant to disclose the nature, extent and location of its assets unless and until the parties are within a zone of settlement, negotiated based upon an assumed financial ability to pay and to be backed up later with proof of the defendant's financial worth.

4. A rational claimant will have to give careful consideration to the possibility of the defendant's bankruptcy if a sizeable judgment is awarded in the plaintiff's favor. In a bankruptcy of a defendant who is rendered insolvent by a judgment, the plaintiff's ratable share of distributions from the insolvent estate may be less, and payable over a longer period of time, than could be achieved in a settlement.

5. If the settlement amount that the defendant is able or willing to pay is nominal in relation to the amount of the plaintiff's claim, and if the claim arises from acts or inactions of the defendant that would make the claim nondischargeable in the defendant's bankruptcy (*see* 11 U.S.C. §§ 523(a) & 727)), the plaintiff may be disincentivized to settle for such a small amount and may opt instead to "punish" the defendant by pursuing a nondischargeability proceeding in the defendant's ultimate bankruptcy.

L. Saving Face

1. A client representative may have made decisions or taken actions that have led to the dispute and that, with the benefit of hindsight, were ill-advised. In such a situation, the client representative may need to "save face" within his or her organization, may view the litigation as an opportunity to vindicate the representative's decisions or actions, or cover up wrong-doing, and may resist any settlement that suggests an error or omission on the representative's part.

2. When an attorney believes that a client representative may be too implicated in the operative facts of the dispute and too emotionally invested in the controversy, counsel might suggest that another representative within the client organization attend the settlement conference, either in lieu of or together with the involved representative.

3. Similarly, an attorney may have been overly aggressive and optimistic in the attorney's initial evaluation of the merits of the client's case to persuade the client to hire the attorney. The client may have sent strong signals to the attorney that the client wanted a "warrior" attorney who "bought into" the client's assessment of the merits and would zealously champion the client's cause. In those instances, it may be difficult for the attorney to modify the original case evaluation, lest the attorney be perceived by the client as lacking "fire in the belly."

M. Inexperienced Counsel

1. Inexperienced litigation counsel may offer irrational settlement advice to clients due to minimal exposure to actual trial of cases, less appreciation for trial risks, an overly optimistic case evaluation, and an inability to handicap trial outcomes.

2. Inexperience may also manifest itself by an attorney's substantial underestimation of the costs and delay of litigation.

3. On other occasions, lawyers lacking experience may be anxious to gain trial experience and "make a name" for themselves through the case and therefore discourage settlement. Of course, the reverse is true and some lawyers may be too eager to settle for fear that a trial will reveal their inexperience and inadequacies.

N. Pure Money Cases

1. If a dispute involves solely the payment of money by one side to the other, the settlement is said to involve a "zero sum game" (a dollar received minus a dollar paid = 0). The plaintiff's gain is a loss for the defendant, dollar-for-dollar, and vice versa. The parties regard the "settlement pie" as fixed.

2. In a pure money dispute, each side evaluates the settlement based solely on monetary considerations, such as the time value of money, the net gain or loss after factoring in the cost of litigation, the magnitude of the potential recovery (*e.g.*, the possibility of treble or punitive damage award), and the likelihood of success on the merits. If each side has a starkly different case evaluation, and neither side is sufficiently incentivized to settle, the dispute will likely linger in court until a dispositive motion is granted or denied (thereby perhaps sobering a party's case evaluation), newly discovered evidence reveals previously unknown strengths or weaknesses in a party's case, or litigation costs spiral out of control.

3. To be contrasted with pure money disputes are those in which the parties have other interests and needs at stake. This is often the case when a dispute involves parties who hope to continue a past business relationship with one another that is threatened by the dispute. Suppose, for example, a dispute arises between a franchisor and franchisee, both of whom hope to continue their relationship after the dispute is resolved. The collateral damage to the relationship that would occur through ongoing litigation may be ameliorated by settlement. Even when an ongoing business relationship is not foreseeable, the parties may need to address non-economic issues, such as public apologies or retractions, the

negotiation of cross-licenses in intellectual property disputes, or cooperation in an orderly dissolution of a joint business enterprise.

4. Litigation is generally about the recovery of money -- who pays and how much. Litigation rarely lends itself to the reconciliation of non-monetary interests and needs of the parties. Courts are ill-equipped to fashion remedies that address all of the needs and interests of parties to a dispute. Because lawyers are advocates in this litigation arena, they may fail to ferret out the needs and interests of a client beyond monetary considerations. Thus, while litigation may be framed in terms of a monetary recovery by the plaintiff from the defendant, there may be other interests and needs of the parties which can (and should) be addressed and the satisfaction of which will facilitate resolution of the controversy.

> For example, the author mediated a dispute between two owners of a highly successful business, which, when initially formed, did not provide a mechanism for one owner to buy out the other in the event of a disagreement. Unless the parties mutually agreed upon a buy-out of the shares of the putative defendant by the putative plaintiff, the only way of reconciling their differences would be through a dissolution of the successful business, a result that neither party desired. The putative defendant placed an unrealistically high value on his shares, stating that he did not want to be bought out and, if the putative plaintiff wanted to acquire his shares, the plaintiff would have to pay the defendant's exorbitant price. Underlying the dispute, however, were significant personal issues that had arisen between the parties. A resolution of those issues was essential to a resolution of their dispute (which allowed the putative plaintiff to have full control of company operations while permitting the putative defendant to retain some economic interest in the continued success of the venture).

## IV. Case Evaluation and Preparing for Settlement

### A. Elements of Case Evaluation

1. The basic elements of case evaluation include, for the plaintiff, whether the claim will survive a motion to dismiss, survive a summary judgment motion, prevail at trial, withstand an appeal, and be collectible. Additional factors to be considered include the cost of the litigation to the client and the expected timeline from start to finish. Counsel must obtain a firm grasp of all applicable principles of law, including affirmative defenses, possible counterclaims, and offsets.

2. Counsel should take into account the existence (or absence) of supporting documentary evidence, credible witnesses for a claim or defense, and potential judge/juror biases for or against the client (*e.g.*, large bank suing "hapless" consumer); realistically assess the strengths of the opposite side's case; review past experiences of counsel (or colleagues) before the judge assigned to the case; consider the characteristics of the jury pool from which a jury may be selected; and factor in the sophistication and experience of the adversary's counsel in trying cases.

3. Suppose a plaintiff's trial counsel handicaps the risk of surviving a motion to dismiss, surviving a motion for summary judgment, and prevailing at trial at 60:40, in favor of the plaintiff. Mathematically, the odds of an ultimate favorable outcome for the plaintiff is 22% (.6×.6×.6 = .216). If counsel predicts a 90% likelihood of prevailing, the odds of a favorable outcome for the plaintiff is 73% (.9×.9×.9 = .729). If the plaintiff's estimated recovery at trial is $1,000,000, the handicapped recovery would be $220,000 or $730,000, depending upon which of the foregoing percentages is used, less legal fees and other expenses (assume $250,000), for a net handicapped recovery of ($30,000) or $480,000, again depending upon the percentage. *See* Robert B. Calihan, John R. Dent, & Marc B. Victor, "The Role of Risk Analysis in Dispute and Litigation Management," presented at the American Bar Association 27th Annual Forum on Franchising, October 6 - 8, 2004 (2004 American Bar Association).

4. In case assessments, counsel should be mindful of studies that reveal the magnitude of errors made by litigants in unsuccessful settlement negotiation, based upon an analysis of 2,054 contested litigation matters in which the parties conducted settlement negotiations, rejected the adverse party's settlement proposal, and proceeded to trial. *See* Randall L. Kaiser, Martin A. Asher & Blakeley B. McShane, "Let's Not Make a Deal: An Empirical Study of Decision Making in Unsuccessful Settlement Negotiations," 5 JOURNAL OF EMPIRICAL LEGAL STUDIES, Issue 3, at 407 - 645 (September 2008).

5. The cost of the litigation will clearly have to be part of the analysis in case assessment. What rational business person would knowingly commit to spend an estimated $1 million in four years of litigation to recover the same amount of money from a defendant on a contract claim?

B. Difficulty of Objective Evaluation

1. Much of the outcome of litigation depends upon a number of variables beyond the control of counsel, including the relative

expertise of adversary counsel in trial matters, the identity and predilections of the judge, the make-up (age, race, sex, religion, and financial status) of the jury, the availability and credibility of witnesses, the presence or absence of potentially damning documents, and the relative "likability" of the client or client representative. Failure to acknowledge these variables is often the result of unconscious biases that infect our analysis (discussed below).

2. As a result, forecasting litigation outcomes is inherently risky and precise outcomes are usually unpredictable. Trial counsel can control what jurors see and hear, but not what they perceive. Counsel for McDonald's Restaurants no doubt was shocked when a jury in Albuquerque, New Mexico, returned a $2.9 million award ($2.7 million being punitive damages) to a customer of the restaurant chain who spilled coffee on herself after purchasing the coffee at a drive-thru. *See* "McDonald's Cup of Scalding Coffee: $2.9 Million Award", CHI. TRIB., August 18, 1994, p. 1. The trial judge later reduced the final verdict to $640,000 and the parties ultimately settled for a confidential amount before an appeal was decided. *See* Liebeck v. McDonald's Restaurants, 1995 WL 360309 (N.M. Dist. Ct. August 18, 1994).

3. A plaintiff may point to sizeable verdicts rendered in cases having similar facts to those supporting the plaintiff's claim, but without focusing on the facts in those cases that may significantly differentiate them from the facts of the plaintiff's claim. Counsel for a party may recall a similar case handled in the past with a favorable result and, without considering unique aspects of the case (including witness credibility) that would explain in part the favorable result achieved, cite that experience as precedent for predicting a similar outcome in the case at hand.

4. It is not uncommon for lawyers on opposite sides of the fence in litigation to handicap their respective chances of success at better than 50%. If both lawyers are seasoned trial attorneys, with relatively the same level of experience, the fact that the sum of their predictions exceeds 100% can only be explained by perspective biases that cloud their analyses.

5. Counsel for a party will often have a more optimistic view of the outcome of litigation than would a neutral evaluator, having access to the facts and arguments from both sides. *See* Richard Birke & Craig R. Fox, "Psychological Principles in Negotiating Civil Settlements," 4:1 HARV. NEGOTIATION L. REV. 1, 13 - 14 (1999).

C. Prepare the Client for Settlement

1. Remind the client that settlement entails giving up something that it thinks it deserves and allowing an adversary to gain something that the client believes is an undeserved windfall for the adversary.

2. It is important for institutional clients to select an appropriate representative for the settlement conference -- ideally someone without emotional involvement in the case, but having an understanding of the underlying facts and basic legal principles and possessing adequate authority to negotiate a settlement.

3. The client (or client representative) must be encouraged to put aside emotional baggage, to the extent possible.

4. Counsel should have an honest discussion with the client regarding the time that it will take to get to a trial of the case, the reasonable prospects of the court granting a dispositive motion in the client's favor, the anticipated cost of litigation, and the additional delays and costs from an appeal. Rarely will experienced counsel forecast the outcome of litigation as "It's a slam-dunk" or "It's a sure thing." Instead, counsel typically will use words of hedging, such as "more likely than not" or "we have a solid chance of prevailing at trial, but the outcome will depend on how persuasive our expert is."

5. Perhaps the most difficult part of the preparation will be to discuss with the client an honest evaluation of the merits of the claims or defenses, the strengths and weaknesses of the client's case, the strengths and weaknesses of the adversary's claims or defenses, problems of proof (including the credibility of witnesses), and counsel's experience with cases of a similar nature before the same judge or jurors drawn from the same jury pool.

6. Plaintiff's counsel should discuss with the client the collectability of a judgment, including the potential for a bankruptcy of the defendant if a sizeable judgment is rendered.

7. Counsel should explore with the client the needs and interests of the adversary that will have to be addressed for a settlement to be reached, including non-economic considerations, such as confidentiality, saving face, an apology, reputational concerns, or the restructuring or repairing of an ongoing business relationship.

8. Similarly, the client and counsel should identify all non-economic considerations of the client that will need to be woven into any settlement. It can sour settlement prospects if, after a settlement in principle has been reached, a party introduces new issues of a non-

economic nature that were not identified prior to or during the settlement conference.

9. Counsel should develop with the client a game plan for settlement negotiations, including who makes the first offer and the likely reaction of the adversary to opening proposals or counter-proposals. At the same time, litigants should be mindful of the need to be flexible in order to react thoughtfully to new information gleaned from the settlement negotiations. In addition, when the client has multiple "wants" (some of which may have to be sacrificed in the negotiation process), counsel and client should attempt to prioritize those wants and be prepared to concede some in exchange for a concession by the opponent to a higher priority want of the client.

10. Client and counsel should discuss their BATNA -- best alternative to a negotiated agreement.[1] In determining their BATNA, counsel and parties should weigh settlement proposals against the probability of success in the litigation, the cost of litigation, emotional and time commitment to the litigation process (in the case of the plaintiff), the collectability of a judgment, and reputational issues.

11. Counsel should discuss with the client how best to address potential barriers to a settlement (such as anger of a counterpart or lack of information that either the client or the other side may need to conclude a settlement agreement).

12. While there may be some justification for withholding production of documents or summaries of testimony (including expert witness testimony) that are unknown to an adversary, the attorney should carefully consider (and discuss with the client) the potential benefits that may accrue in settlement discussions through disclosure of such information.

D. Self-Preparation by Counsel

1. Counsel should be fully informed regarding the facts, documents and applicable legal principles. An attorney who appears to be well prepared and conversant with the facts and law has credibility in a negotiation and can more readily persuade both an opponent and its counsel on the strength of positions advanced.

[1] The term "BATNA" was coined by Roger Fisher and William Ury of the Harvard Program on Negotiation in a series of books beginning with Getting to Yes: Negotiating Agreement Without Giving In, first published in 1981 and re-issued in 1991 with an additional authorship credit to Bruce Patton.

2. If either the parties or counsel have not dealt with one another, it can be beneficial to perform due diligence about the individual client (or client representative) on the other side as well as information about the adversary's counsel. Counsel who have dealt with one another before in the successful conclusion of a case may have a better working relationship and one more conducive to working collaboratively to reach a settlement.

3. Counsel should assess whether the client is risk-averse and motivated to settle or risk-tolerant and less motivated to settle. Risk-averse parties typically come to the table more readily than a risk-tolerant litigant. Risk-aversion is prevalent when the size of a potential judgment can threaten the very existence of the client organization. *See* Janet Cooper Alexander, "Do the Merits Matter? A Study of Settlements in Securities Class Actions," 43 STAN. L. REV. 497, 532 (1991).

4. Counsel should prepare a checklist of items to be included in a definitive settlement agreement, in term sheet format, and review the terms with the client to make sure that all material terms of a settlement have been identified and addressed. The term sheet may come in handy at the settlement conference when parties are reaching closure and the term sheet, updated with the current negotiated points, can be quickly generated for review by the adverse party.

## V. Confidentiality and Privileges

A. Importance of Confidentiality

1. To promote candor and to maximize the effectiveness of settlement discussions, parties and counsel must be comfortable that their actions and statements during the bargaining session will remain confidential and not be discoverable or admissible in evidence. *See* In re County of Los Angeles, 223 F.3d 990 (9th Cir. 2000); Lake Utopia Paper Ltd. v. Connelly Containers, Inc., 608 F.2d 928 (2d Cir. 1979), cert denied, 444 U.S. 1076 (1980).

2. Parties to settlement discussions, whether undertaken with or without the intervention of a neutral facilitator, are concerned both with external and internal confidentiality. The former refers to a party's maintaining confidentiality of settlement communications with respect to non-participants and the latter refers to a neutral (such as a mediator) not sharing with any party confidential information obtained from another party in the course of a mediation conference.

B. Sources of Confidentiality Requirements

1. Sources of confidentiality commitments and obligations include local rules of the court, mediation orders entered by the court in party-initiated or court-connected mediations, evidentiary rules and statutory provisions applicable in a particular state, the Federal Rules of Evidence, ethical rules applicable to attorneys, and agreements of parties entered into in connection with a mediation or independent settlement discussions.

2. Pending the adoption by Congress of confidentiality rules applicable to mediations under the under The Alternative Dispute Resolution Act of 1998, 28 U.S.C. §§ 651 *et seq.*, each district court is directed under the Act (28 U.S.C. § 652(d)) to provide, by local rule, for the confidentiality of all ADR resolution processes and to prohibit disclosure of confidential dispute resolution communications. *See, e.g.*, Oregon Local Bankruptcy Rule 9019-1(e)(2) (making FRE Rule 408 applicable to mediations and barring parties from relying on or introducing "as evidence in connection with any arbitration, judicial, or other proceeding the existence of or any aspect of the mediation effort, including, but not limited to," the views expressed or suggestions made by another party regarding settlement of the dispute, admissions made by another party in the course of the mediation, and proposals made or views expressed by the mediator).

C. Federal Rule of Evidence 408

1. Statements made during settlement conferences and mediations in federal court cases enjoy protection under Rule 408 of the Federal Rules of Evidence, which is expressly recognized in many local rules applicable to mediation communications. *See, e.g.*, N.D. Fla. Local Rule 9019-2(g)(3). *See also*, FRCP Rule 68 (evidence of an unaccepted offer of judgment is not admissible except in a proceeding to determine cost) and Rule 7068 of the Rules of Bankruptcy Procedure (which makes FRCP Rule 68 applicable in bankruptcy cases).

2. FRE Rule 408, however, is a rule of evidence and courts are divided on whether and when discovery of otherwise inadmissible settlement terms and communications may be appropriate. *Compare* Hasbrouck v. BankAmerica Housing Services, 187 F.R.D. 453, 461 (N.D.N.Y. 1999), *aff'd*, 190 F.R.D. 42 (N.D.N.Y. 1999) (discovery not allowed), and Allen County v. Reilly Indus., 197 F.R.D. 352, 353 (N.D. Ohio 2000) (noting that supposed facts revealed from settlement discussions may be misleading due to party posturing, exaggeration and assumption of facts as true for purposes of settlement discussions) *with* Morse/Diesel, Inc. v.

Fidelity & Deposit Co. of Maryland, 122 F.R.D. 447, 449 (S.D.N.Y. 1988) (rejecting an absolute bar against discovery). *See also* Bottaro v. Hatton Assoc., 96 F.R.D. 158, 160 (E.D.N.Y. 1982) (applying a heightened standard to allow discovery of settlement terms). *Contra*, In re Initial Public Offering Sec. Litig., 2004 WL 60290 at *5 (S.D.N.Y. 2004) (court allowed discovery and found heightened standard not permitted by the Federal Rules of Civil Procedure).

D. Uniform Mediation Act

1. The Uniform Mediation Act, promulgated in August 2001 by the National Conference of Commissioners on Uniform State Laws, in conjunction with other groups that included the Section on Dispute Resolution of the American Bar Association, has been approved for adoption by some 12 states and the District of Columbia.

2. The Act establishes an evidentiary privilege for mediation communications, applicable to both parties and the mediator.

E. Confidentiality Agreements

1. Parties to mediations and non-mediated settlement discussions often enter into pre-negotiation agreements by which each agrees that information disclosed during the course of settlement discussions are confidential and not admissible in evidence, unless documents produced or matters discussed in the mediation are otherwise subject to discovery.

2. It is an open question in some jurisdictions whether settlement discussions pursuant to a confidentiality agreement remain confidential and exempt from discovery by non-parties to the settlement.

F. Exemptions from Confidentiality

1. Despite confidentiality provisions in local rules, rules of evidence, bankruptcy court orders, and party agreements, the exemption of settlement discussions from discovery or use at trial is far from absolute.

2. Information otherwise discoverable or admissible does not become exempt from discovery or inadmissible simply because the information was used by a party in mediation. *See, e.g.*, Uniform Mediation Act § 6(b); FRE Rule 408.

3. Settlement discussions may be admissible to impeach testimony of a party, to disclose or prevent the commission of a crime, or to prevent "manifest injustice" that would result from non-disclosure. *See* In re Teligent, Inc., 640 F.3d 53 (2d Cir. 2011); In re Grand Jury Subpoena, 148 F.3d 487 (5th Cir. 1993); In re Anonymous, 283 F.3d 627 (4th Cir. 2002). Some courts have allowed discovery of matters occurring in a mediation to facilitate enforcement or interpretation of a settlement agreement. *See, e.g.*, Wilson v. Wilson, 653 S. E.2d 702 (Ga. 2007) (where one party challenged enforceability of settlement agreement based upon alleged incapacity to contract, mediator was permitted to testify concerning general impression that parties had mental capacity to mediate and reach settlement). *Accord*, Uniform Mediation Act §6(b)(2).

4. In addition, FRE Rule 408 may not prohibit the introduction in a criminal case of statements or conduct during compromise negotiations regarding a civil dispute by a government regulatory, investigative, or enforcement agency. *See, e.g.*, U.S. v. Prewitt, 34 F.3d 436, 439 (7th Cir. 1994) (admissions of fault made in settlement of civil securities enforcement action admissible in subsequent criminal action for mail fraud). Nor does the rule bar evidence of a settlement when offered to prove a breach of a settlement agreement. *See* Cates v. Morgan Portable Bldg. Corp., 708 F.2d 683 (7th Cir. 1985).

5. Confidentiality of settlement communications may be waived by all of the parties, if the waiver is voluntary and intentional or results from an authorized disclosure of settlement communications. *See* Uniform Mediation Act § 5(a)-(b), comment 1. However, the protections of FRE Rule 408 cannot be waived unilaterally as the rule is intended to safeguard both parties from having the fact of negotiation disclosed to a jury. *See* Pierce v. F. R. Tripler & Co., 955 F. 2d 820, 828 (2d Cir. 1992).

G. Sanctions for Confidentiality Breaches

1. Breaches of confidentiality commitments may result in the imposition of sanctions by a court or an action by an injured party for violation of a confidentiality agreement.

2. Courts are particularly inclined to level sanctions for confidentiality breaches in a mediation context. *See, e.g.*, Hand v. Walnut Valley Sailing Club, 475 Fed. Appx. 277 (10th Cir. 2012) (affirming district court's dismissal with prejudice of plaintiff's complaint as sanctioned for plaintiff's breach of mediation confidentiality).

## VI. Some Psychological Issues in Bargaining

A. The Conflict Spiral

1. The so-called "conflict spiral" is the tendency of a conflict to escalate when the disputants resort to heavy-handed tactics in their negotiations. For a thorough discussion of the conflict spiral and an alternative approach to settlement discussions, *see* Gary Friedman & Jack Himmelstein, CHALLENGING CONFLICT: MEDIATION THROUGH UNDERSTANDING (American Bar Association 2008).

2. When conciliatory tactics fail to achieve a desired end, a negotiator may move to hard bargaining, threats, or unflattering characterizations of a counterpart's stance, with the counterpart escalating its response and with the escalation continuing on each side until one side prevails or gives up trying.

3. Litigation attorneys are trained to be combative, and "war" analogies in litigation are common. Unfortunately, some litigators are unable to put aside their sword and shield and assume the role of a negotiator looking for a "win win" position that will foster dispute resolution.

4. In settlement negotiations, litigation counsel often attempt to justify the merits of their side's offer, or argue the lack of merit of a counterpart's proposal, by a confrontational recitation of the manifold ways in which counsel will bludgeon the counterpart into submission in the litigation if a settlement is not achieved. Attempts to settle through intimidation and threats rarely work with sophisticated counsel and parties.

5. A litigious stance typically begets a litigious response, with the conflict elevated, rather than tempered through negotiation.

B. The Optimism Bias

1. Most people have an overly optimistic view of their chances to beat the odds -- in life, gambling, work . . . and litigation. While mathematically impossible, well over 90% of college professors believed that they were above average in performance and almost 75% of adults surveyed believed that they would live beyond the average life span for their generation. *See* P. Cross, "Not *Can* But *Will* Teaching Be Improved," 17 NEW DIRECTIONS FOR HIGHER EDUCATION 1 (1977). An addiction to gambling can be explained in part by the gambler's conviction that he or she will surely beat the odds and, with one more quarter in the slot, will ultimately hit the jackpot. While smokers may realize that they are

susceptible to lung cancer, most are convinced that they are less likely to contract the disease than other smokers.

2. The optimism bias taints our ability to detect weaknesses in our case and the possibility of an adverse result. An excess of optimism affects not only litigants but also their counsel, as studies have shown. *See generally*, Tali Sharot, THE OPTIMISM BIAS (Pantheon 2012).

3. Trial attorneys are notoriously passionate advocates of their causes, which can make them inaccurate forecasters of litigation outcomes. Counsel's view of a case may be significantly colored by the belief that counsel's persuasive powers will carry the day for the client against all odds. This tendency to overestimate one's abilities is sometimes referred to as the "egocentric bias." *See* Jennifer K. Robbennolt & Jean R. Sternlight, PSYCHOLOGY FOR LAWYERS, at 70–71 (ABS 2012).

4. When counsel is overly optimistic in an assessment and evaluation of the strengths and weaknesses of the client's case, counsel may unduly influence the client to fix a settlement range that is unrealistically high. *See* Richard Birke & Craig R. Fox, "Psychological Principles in Negotiating Civil Settlements," for HARV. NEGOT. L. REV. 1, 15 (1999).

5. Even when told of the bias, litigants tend to believe that it infects the other side and that they are bias free.

C. Reactive Devaluation

1. Reactive devaluation is the tendency of a party to value the content of a proposal less favorably if it is advanced by an opponent.

2. Reactive devaluation is quite prevalent in settlement discussions involving parties with an intense dislike of one another. Each side may view a proposal from an opponent with suspicion and as likely entailing a loss for it and a windfall for the opponent.

3. Building sufficient trust to counter reactive devaluation may be extremely difficult. The use of a skilled mediator, through whom proposals are funneled, can be helpful in facilitating settlement negotiations.

4. In the absence of a mediator, parties may seek to circumvent reactive devaluation by channeling proposals through a business associate or intermediary. Moreover, when attorneys collaborate with one another regarding the contours of a proposal and discuss the outlines of a proposal with their respective clients, their clients

may feel that the proposal is actually one that they fashioned rather than one emanating solely from the adversary. *See* Jennifer K. Robbennolt & Jean R. Sternlight, PSYCHOLOGY FOR LAWYERS at 274 – 275 (ABA 2012).

D. Anchoring

1. Anchoring refers to the tendency of a party to rely on, and be unduly influenced by, an initial (and often) irrelevant data point.

2. The anchor often influences later decisions by prompting a bargainer to make adjustments in perspective and bargaining in relation to the anchor and to assess options based upon their degree of deviation from the anchor.

3. Research reveals that information provided prior to, or at the beginning of, negotiations can influence a negotiator's initial offer, aspiration level, bottom line, and guestimates of an opponent's bottom line.

E. Reciprocity

1. Parties tend to reciprocate by repaying, in kind, what an opponent has conceded. A natural human impulse in most societies is to return a favor—if I open the door for you, then further down the hallway, you are apt to open the next door for me.

2. In settlement negotiations, parties make concessions with the expectation that the counterpart will respond in kind. When a concession is made and it is not reciprocated by a counterpart, the party making the concession may believe that it is being called upon to make additional concessions and therefore "bid against" itself.

3. A party can elicit a reciprocal response often by highlighting significant concessions that it has already made for the other side.

F. Assimilation (or Confirmation) Bias

1. We find it difficult to divorce ourselves from common biases that tend to color our analyses. Part of the difficulty in pegging the "worth" of a case is the presence of what is often referred to as "assimilation bias."

2. That bias results in a person assimilating and evaluating facts that tend to support his or her position and overlooking, or significantly discounting the relevance of, facts that do not support the position. *See* Robert Birke & Craig R. Fox, "Psychology Principles in

Negotiating Civil Settlements," 4 HARV. NEGOT. L. REV. 1, 26-28 1999).

3. Lawyers, as advocates, tend to "buy in" to their client's cause and, through discovery, seek information that confirms or supports their client's position while often ignoring discovered items that may lend support to the opponent's position.

G. Framing and Loss Aversion

1. Framing affects the manner in which individuals may perceive a particular decision based upon how it is presented to them for consideration or "framed." Trial lawyers are particularly adept at framing.

2. At times, issues may be framed in a way to suggest that the choices of a counterpart are limited to one of two options, which may serve up what is often referred to as a "false choice" by concealing other options that may be equally available.

3. When a choice is framed as a certain gain versus the prospect of a higher potential gain, most people elect the certain gain over a gamble. When, however, the choice is framed as a loss, most people would risk the possibility of a greater loss than incur a certain loss in a lesser sum.

4. "Loss aversion" refers to the tendency of some people to prefer avoiding losses over the acquisition of gains. The pain of loss impacts people differently than gaining the same thing in equal measure. For many people, an *initial gain* is not as fulfilling as an *additional gain*, whereas an *initial loss* is not as painful as an *additional loss*. *See generally*, Deepak Malhotra & Max Bazerman, "Psychological Influence in Negotiation: An Introduction Long Overdue," revised and resubmitted to the JOURNAL OF MANAGEMENT (January 8, 2008).

H. Sunk Cost Bias

1. So-called "sunk cost bias" induces us at times not to walk away from a case or a transaction after having invested significant resources in it, even though additional investments may not lead to a recovery of costs already incurred.

2. A decision whether to invest additional resources typically should not be influenced previously incurred costs if an objective analysis would suggest that recovery of those costs is doubtful.

3. Bargainers need to be mindful of the fact that some losses are best forgotten and cutting losses may be the optimal approach.

I. Social Proof

1. Social proof prompts us to look at what others are doing or thinking in order to determine our own conducts or thoughts.

2. Social proof is the theory behind "laugh tracks" on television and is a driving force behind fashion trends.

3. Social proof creeps into negotiation behavior when we are told the amount of money that others were compensated for a similar injury or paid in settlement of a preference claim. Social proof often is couched in terms of what is a "market" convention in the drafting of a particular provision in a document.

4. Being told that something is customary and the norm appeals to our desire not to be outside of the mainstream and to have a social norm or reference point. Thus, litigants may be persuaded to settle a case based upon what they understand other cases of a similar nature have settled for in the past.

J. Inner Voices

1. We all have an inner voice (silent verbal thinking).

2. Your inner voice talks to you all day long -- sometimes it rehearses a closing argument, or a response to points made by a counterpart in conversation; at times it simply verbalizes what you are seeing or experiencing ("This cake is delicious"); on occasion it serves as our conscience; and it may help us make decisions based on intuition formed from a subconscious rapid processing of information and perceptions.

3. When listening to others, consciously endeavor to suppress your inner voice. When attempting to make a difficult choice, sometimes it pays to listen to your inner voice -- "follow your gut."

4. Be mindful that your adversary's inner voice is speaking to him/her and may at times impede active listening to what you are saying. It sometimes is helpful to ask the counterpart to a conversation whether he/she heard you and ask whether there are any questions.

## VII. Bargaining Tips

A. What is a Settlement Negotiation?

1. A settlement negotiation is a process by which two sides alternate making concessions to one another until a deal can be reached.

2. The parties in entering into a settlement negotiation should understand that concessions must be made by each side.

B. Build Rapport

1. Building rapport enhances the quality of interaction through face-to-face contact and can facilitate agreement.

2. We tend to like and agree with those who share interests, friends, hobbies, goals, names, colleges, law schools, military service, or birthdays. If we build rapport with a counterpart, they have an inclination to like and agree with us.

3. Rapport often results from prior, satisfactory relationships between parties or counsel. We tend to trust those with whom we have had past satisfactory experiences.

C. Have a Strategy

1. As earlier noted, it is important for parties to prepare a strategy for the settlement negotiations, with an end game in mind, rather than ad-libbing during the settlement conference.

2. Parties must be flexible and prepared to alter that strategy as new perspectives are gained from the settlement conference.

3. A rational party will elect to settle or continue with the litigation by comparing the value of the two alternatives at any point in time, factoring in to the decision the net gain expected to be achieved under each approach -- in other words, a BATNA analysis.

D. The First Offer Conundrum

1. Conventional wisdom posits that the side making the first offer is at a disadvantage because it tips the counterpart off to the first offeror's bargaining range and ultimate expectations for a settlement.

2. Some studies demonstrate that the side making the first offer may actually have an advantage in many negotiations. That advantage results from the fact that the first offer often has an "anchoring" effect in the negotiations and sets the negotiating bar in favor of

the offeror. *See* Jennifer K. Robbennolt & Jean R. Sternlight, PSYCHOLOGY FOR LAWYERS at 273-274 (ABA 2012). If the plaintiff makes the first offer and it is high, the defendant often makes an upward adjustment to its settlement range. The reverse is true when the defendant makes the offer and it is quite low in the eyes of the plaintiff.

3. On the other hand, the party making the second offer is afforded an opportunity to define where the midpoint of the negotiation may lie and the point at which the offeror is signaling to be within its zone of settlement. *See* Richard Birke & Craig R. Fox, "Psychological Principles in Negotiating Civil Settlements," for HARV. NEGOT. L. REV. 1, 41 (1999). Thus, if the initial offer from the defendant is $1 million and a counterpart (the plaintiff) desires to settle for $3 million, the counterpart should counter at $5 million. Experience confirms that parties frequently try to settle in the mid-range of their bid/ask.

4. A "process impasse" can result when the parties argue over which side should make the first offer. The plaintiff often states that it has made it first offer in the complaint, although realistically that is not an offer of settlement but simply defines the outer limits of the demand. The defendant often counters that the plaintiff should make the first offer as it is the plaintiff that must come down from the demand in its complaint.

E. Identify the Adversary's Decision-Influencers

1. Counsel may have a view, based upon prior interaction with an opponent in the litigation, whether the opponent or its counsel is the primary influencer on whether the matter will settle or continue in litigation. Passive clients who can be overwhelmed by the litigation may rely heavily upon counsel's advice and essentially cede decision-making to counsel. In other cases, a sophisticated adversary may be the one calling the shots, while certainly taking into account counsel's legal advice.

2. Knowing who are the key "influencers" will assist a party in formulating proposals and the manner in which the proposals are conveyed. For example, if an attorney is the primary influencer, counsel for the other side may communicate settlement proposals in legal constructs and terms. On the other hand, when the client is firmly in control of decision-making, proposals may be fashioned in business constructs and terms.

3. When there are multiple influencers, including multiple counsel present at the settlement conference for a counterpart, a party may attempt to ascertain which of the influencers will be the most

receptive to settlement and less inclined to hold fast to entrenched positions.

F. Refrain from Taking Offense at an Offer

1. Settlement negotiations often bog down at an early stage when one side believes that the initial offer was made in bad faith -- a "low ball" offer from the defendant or a "ridiculously and unrealistically high number" from the plaintiff. Settlement negotiations often are in peril after the initial offer, when the offeree exclaims "That offer is ridiculous and is in bad faith - one more offer like that and we are out of here!"

2. Sophisticated bargainers understand that no side puts its best offer on the table at the outset, as otherwise each party could conduct a one offer/counteroffer negotiation by a simple exchange of e-mails.

3. Each side must understand that settlement proposals are part of a process by which each side seeks to "feel out" the other, endeavoring to ascertain a bargaining range and the possibility of reaching a zone of settlement.

4. It is not necessarily the content of an offer that should be troubling to the offeree, but rather the point in time when offers ceased to be forthcoming from a counterpart or the rate of movement signals that a counterpart is in its zone of settlement - a zone that is not shared by the offeree. Negotiators should bear in mind that movement in negotiations begets movement, and movement by both sides represents progress that often leads to agreement.

G. Offer as a Communication

1. Each offer from a counterpart carries with it a clue as to the end game that that offeror seeks. Each side seeks to conceal from the other its "end game," while trying to discover the counterpart's end game.

2. An offer perceived to be unrealistically low will likely attract a counterproposal that is unrealistically high, with the party making the responsive proposal likely signaling its displeasure with the size or nature of the opponent's proposal.

3. As the incremental amount in the plaintiff's settlement demands decreases and incremental increases in the defendant's settlement offers lessen, both sides are communicating to the other that they are running out of dry powder.

4. An offer/proposal should be accompanied by an explanation for it. For example, a defendant might seek to justify a dollar amount lower than the plaintiff's last settlement demand by saying "While we may disagree on the issue of liability, your side has offered no evidence to substantiate the level of damages that you claim and our expert at trial will firmly support our position."

5. At times, communications between the parties to justify their positions are designed to focus an adversary's attention on the consequences of rejecting what the other side believes to be a reasonable offer.

   For example, "While your client may believe that his case is worth at least $5 million, our offer of to settle for $1.5 million is quite reasonable when one considers that the case is not likely to be tried sooner than two years from now, the cost of preparing for trial on each side may well exceed $500,000, and your case may rise or fall on the credibility of a witness whose integrity is open to question."

6. Advising a counterpart that a proposal, or some aspect of it, is non-negotiable or the "final offer" can be a bad negotiating tactic unless the non-negotiable point or final offer has been fully considered and is, indeed, the proposer's bottom line. Otherwise, a retraction of a purported non-negotiable point is injurious to the credibility of the bargainer and encourages a more aggressive posture by the opponent.

H. Highlight Progress

1. At different junctures in a settlement negotiation, the parties may reach a temporary impasse. The impasse may result from weariness, frustration, or indecision.

2. At each temporary impasse, one party should summarize the progress made to date. By highlighting the progress that has been made, the parties can see that their investment has paid dividends and they may become psychologically and emotionally vested in concluding a deal.

3. It is often helpful for a party to summarize significant concessions that it has made so that the other party does not feel that it, alone, is sacrificing value for the sake of settlement.

I. Do Not Demonize the Opponent

1. It is commonplace for a party to view itself as representing "the forces of light" and the opponent as representing "the forces of

darkness," and to demonize both the conduct and motives of the opponent and its agents.

2. This tendency is reinforced when it is perceived that the opponent is being unreasonable and engaging in hard bargaining. In truth, the opponent may simply believe that its position is well-founded and that significant concessions by it are unwarranted.

3. Mediators often find it helpful to have each side articulate to the mediator, in private, the best arguments available to the other side as well as weaknesses in their own case. By articulating the opponent's best case, a party may come to realize that an opponent's claim or defense may have some merit and jury appeal.

4. To overcome a counterpart's viewing a party as evil, it is helpful for each party's proposal to be accompanied by a rational explanation and an acknowledgment that, despite the strength of the party's convictions, there are litigation risks on each side and some merit to each party's position. This is especially true in cases where non-economic interests are present and the needs and interests of a counterpart are clearly legitimate. Acknowledging legitimacy of a party's needs and interests will help the party to overcome the perspective that the opponent is evil and unreasonable.

5. Remember, we tend to judge ourselves by our motives (despite the consequences of our actions), but at the same time judge others solely by their deeds (without regard to their true intentions).

J. Don't "Cut to the Chase" Too Quickly

1. Inexperienced, and typically impatient, bargainors often advocate that the parties "cut to the chase" early on in the negotiation process by revealing their best numbers. The term "cut to the chase" is believed to be derived from movie-makers in earlier times, when the director would direct the production crew to shift filming to the chase scene, often appearing at the end of the movie.

2. Sophisticated bargainors understand that the negotiation of a settlement is a process that takes time and patience, as each party seeks to identify a counterpart's needs and interests, risk-aversion or risk-tolerance, zone of settlement, and case evaluation. If getting to the bottom line quickly were the goal, negotiations could be accomplished by two emails, the first with a "take it or leave it" offer from the plaintiff and the second with an acceptance or rejection by the defendant. The process would be efficient and cost-effective, but likely unproductive.

3. The settlement of a lawsuit is orchestrated by human beings, not robots (at least not yet), and entails a mix of intelligence, negotiating skills, persuasiveness, and analytics, liberally seasoned with an understanding of human emotions.

K. Pay Attention to Body Language

1. There is often a conflict between a party's words and his or her body language. It is perhaps an everyday occurrence in America when one spouse, in the heat of argument with the other spouse, utters a denial through gritted teeth and pursed lips, "I am not mad."

2. The innermost thoughts of a person are often unconsciously communicated through the language of the body – the eyes, mouth, hands and overall posture.

3. Changes in speech patterns, posture fidgeting, and demonstrative hand gestures are often keys to the thoughts of a party.

4. Attention to body language can provide clues to the thoughts of an adversary and also the adversary's emotional state of mind -- nervous, apprehensive, fearful, bored, angry (red in the face, or fists clenched), or resigned.

## VIII. Settlement Agreements

A. Enforceability of Settlements

1. To be enforceable, a settlement agreement must be definite and certain in its terms and must satisfy the same requirements for formation and enforceability as any other contract, including the requirement that there be an acceptance of the terms, adequate consideration, and a meeting of the minds on all essential terms.

2. Oral settlement agreements have been enforced by a number of courts. *See, e.g.*, Winston v. Mediafare Entertainment Corp., 777 F. 2d 78, 80 (2d Cir. 1985) (factors used in determining whether oral settlement is binding include whether there was an express reservation of right not to be bound absent a writing, whether there has been partial performance, whether all material terms have been agreed upon, and whether the agreement is the type of contract usually committed to in writing). Courts typically will attempt to determine whether the parties intended to enter into a binding agreement.

3. The requirement of a written agreement can be satisfied through an exchange of emails or correspondence between the parties or

counsel setting forth the terms of the settlement, unless the settlement is expressly conditioned upon the execution of a written settlement agreement. *See, e.g.*, Remark, LLC v. Adell Broadcasting Corp., 702 F. 3d 280 (6th Cir. 2012); Anderson v. Kaiser Gypsum Co., 134 Wash. App. 1038 (Wash. App. 2006) (exchange of e-mails created binding settlement agreement before formal settlement agreement was even prepared).

4. Under the laws of some states, an attorney has apparent authority to enter into a settlement agreement that binds the client and that authority is plenary unless the authority is limited by the client and that limitation is communicated to the opposing party. *See, e.g.*, Kinan v. Cohen, 268 F. 3d 27 (1st Cir. 2001); Anderson v. Atlanta Indep. School District, 742 S.E.2d 524 (Ga. App. 2013).

B. Content of Agreement

1. The agreement should spell out clearly the scope of matters to be settled.

2. The settlement consideration should be detailed, including any cash consideration to be paid, method and timing of cash payments, and non-cash consideration forming part of the settlement.

3. One of the more controversial sections of a settlement agreement is the scope of releases or covenants not to sue that are to be exchanged by the parties as part of the settlement, the date of and conditions to effectiveness of the releases, and exemptions from the release or covenant not to sue (such as enforcement of the settlement agreement).

4. Although confessions of judgment are not enforceable in some jurisdictions, they may be enforceable in others (such as New York) and may be prudent to obtain as part of the settlement. As an alternative, the party should consider the possible use of a consent judgment to be filed as part of the settlement in the pending lawsuit, with the settlement terms annexed, or a so-called "pocket" judgment to be filed in the lawsuit if settlement consideration is not performed in accordance with the terms of the settlement agreement.

5. The settlement agreement typically will contain representations and warranties of the parties, as well as acknowledgments that the parties were represented by counsel (if that is the case) and are entering into the settlement agreement knowingly and voluntarily.

6. A condition to a settlement agreement in a bankruptcy case may be the entry of an order granting a Bankruptcy Rule 9019 motion or confirmation of a plan that contains a so-called "bar order." The order operates to bar certain parties (often including non-settling parties to pending litigation) from pursuing claims against a settling defendant to the extent that those claims were released by the debtor or trustee pursuant to the settlement agreement or plan or are claims for contribution or indemnity arising out of or based upon the released claims. Although bar orders remain controversial, they have often been approved by the courts in appropriate cases. *See, e.g.*, In re Munford, 97 F. 3d 449 (11th Cir. 1996) bar order that prevented non-settling defendants from pursuing contribution claims against the settling defendant was upheld).

C. Confidential Settlements

1. The issue of confidentiality of a settlement agreement may arise in a variety of contexts, including the settling party's desire to maintain the confidentiality of information that was used in the course of settlement negotiations or to maintain confidentiality of certain settlement terms. The extent to which confidentiality will be honored by a court may depend upon whether court approval for the settlement is required.

2. If court approval for the settlement is not required, the parties may desire to include confidentiality provisions so that the settlement itself, and settlement consideration, remain confidential. It is not clear whether a court will in every instance extend privacy protection to confidential settlement agreements. *See, e.g.*, Hinshaw, Winkler, Draa, Marsh & Still v. Super. Ct., 51 Cal. App. 4th 233 (1996) (where the court held, as a matter of first impression, that confidential settlement agreements are entitled to privacy protection given the strong public policy favoring settlements and placing the burden on the requesting party to show a "compelling" interest to overturn that privacy).

3. Confidential settlement agreements in federal courts, to the extent not requiring court approval, are often protected from disclosure by the issuance of a protective order upon a showing of good cause. *See, e.g.*, Phillips *ex rel* Estates of Byrd v. General Motors Corp., 307 F.3d 1206, 1212 (9th Cir. 2002). *But see* Grumman Aerospace Corp. v. Titanium Metals Corp. of America, 91 F.R.D. 84 (E.D.N.Y. 1981) (allowing discovery of confidential settlement agreement).

4. Settlements in bankruptcy, however, require court approval pursuant to Bankruptcy Rule 9019 (and, according to some courts, pursuant to Section 363 of the Bankruptcy Code). In circumstances

where confidentiality is requested by a party as a condition to the settlement, the scope of confidentiality typically must be quite narrow in order to provide enough information to interested parties to determine whether the settlement is in the best interest of the estate. Accordingly, the parties seeking confidentiality will be called upon to present evidence to rebut the presumption of public access to judicial records. *See, e.g.*, In re Oldco M Corp., 466 B.R. 234 (Bankr. S.D.N.Y. 2012) (liquidating trustee and counterparty to settlement agreement failed to show basis for sealing proposed settlement, although certain financial information could be redacted).

5. Moreover, Section 107 of the Bankruptcy Code provides that, with limited exceptions, "a paper filed in case under this title and the dockets of a bankruptcy court are public records and open examination by an entity at reasonable times without charge." The presumption of open inspection of court filings codified in Section 107(a) evinces a strong congressional desire to "preserve the public's right of access to judicial records in bankruptcy proceedings." *See* In re Orion Pictures Corp., 21 F. 3d 24, 26 (9th Cir. 1994). However, the public's right of access is not absolute and, as provided in Section 107(b) of the Bankruptcy Code as well as in Bankruptcy Rule 9018, there may be limited circumstances where preserving confidentiality of certain settlement terms may be appropriate. *See, e.g.*, In re Dana Corp., 412 B.R. 53 (S.D.N.Y. 2008).

## IX. Some Bankruptcy Considerations

A. Settlement Payment as Voidable Preference

1. Section 547 of the Bankruptcy Code provides that a payment made by an insolvent debtor within 90 days of the debtor's bankruptcy (or, in the case of an insider, within one year of the date of bankruptcy) to a creditor on account of an antecedent debt owed to that creditor may be voidable as a preference, unless a defense to preference avoidance under Section 547(c) of the Bankruptcy Code exists.

2. Typically, a plaintiff will have few, if any, defenses to a payment made by an insolvent defendant within 90 days of the insolvent defendant's bankruptcy. If a preferential payment is recovered in the defendant's bankruptcy, the plaintiff will have a claim against the defendant in the amount of the recovery (*see* 11 U.S.C. § 502(h)), together with any other amounts owed at the time of bankruptcy by the defendant to the plaintiff.

3. If the plaintiff compromises the amount of a liquidated claim in order to reach a settlement with a financially distressed defendant, and the amount paid to the plaintiff is recovered in the defendant's subsequent bankruptcy, the plaintiff's claim in bankruptcy will be for the settled amount rather than the full amount of the liquidated claim. Accordingly, when compromising a liquidated claim against a financially distressed defendant (such as a claim on a promissory note or guaranty), some plaintiffs structure the settlement to provide for a discharge of the claim only if the discounted amount is paid in accordance with the settlement terms and no bankruptcy of the defendant occurs within 91 days after the last payment on the discounted amount.

B. Settlement Payment as Fraudulent Obligation

1. Transfers that are intentionally or constructively fraudulent as to creditors of the transferor may be avoided under applicable state law or pursuant to the provisions of Section 548 of the Bankruptcy Code.

2. A payment or other transfer of property in settlement of a claim may be found to be fraudulent as to creditors of the transferor if the transfer is made by a non-obligated party (such as a relative of or an entity affiliated with the defendant) and the effect of the payment or transfer is to impact adversely upon the solvency, debt paying ability, or capital adequacy of the transferor.

3. A plaintiff's agreement to settle a viable claim at a significant discount when the plaintiff is (or is thereby rendered) insolvent may be avoided (and release is given by the plaintiff to the settling defendant vitiated) as a constructively fraudulent transfer. Such a settlement might occur when the plaintiff is disadvantaged in bargaining power and is in significant need of a cash infusion from a settlement, without regard to the value of the released claim.

C. Possible Liability of Counsel

1. Under Section 550 of the Bankruptcy Code, a transfer that is avoided under one of the avoidance sections of the Bankruptcy Code (such as Sections 544, 545, 547, 548, 549 or 553(b)) may be recovered from (a) the initial transferee of the transfer or the entity "for whose benefit" the transfer was made or (b) any "immediate" or "mediate" transfer transferee of the initial transferee. 11 U.S.C. § 550(a).

2. If an attorney receives a settlement payment from an insolvent defendant for the benefit of the attorney's client (the plaintiff), there is a risk that the transfer may be subject to recovery both

from the attorney as the "initial transferee" and the client as a successor transferee.

3. However, in most instances, the attorney may avail himself or herself of the so-called "mere conduit theory," pursuant to which a party who is receiving an otherwise preferential payment for immediate transmission to the actual creditor is not liable under Section 550(a), as long as the attorney does not exercise any control over the funds and acts in good faith. *See* In re Harwell, 628 F.3d 1312 (11th Cir. 2010) (material issue of fact as to whether attorney was mere conduit with respect to settlement funds paid into attorneys' trust account when attorney alleged to be involved in fraudulent scheme); In re Jackson, 436 B.R. 29 (E.D. Mich. 2010) (law firm was conduit, and not initial transferee, of garnishment proceeds received in trust account but was "immediate transferee" to extent of payment of fees); In re S&W International Food Specialties, Inc., 362 B.R. 36 (Bankr. N.D. Ga. 2006) (closing attorney acted as mere conduit and was not initial transferee of fraudulent conveyance); In re Spinnaker Industries, Inc., 328 B.R. 755 (Bankr. S.D. Ohio 2005) (law firm was conduit as to proceeds of preferential settlement payment). However, if the attorney deducts from the settlement payment any amounts owed by the client as attorney's fees, the mere conduit theory may not be a viable defense to the extent of the deduction. *See* In re Florida Manufacturing & Distribution, 484 B.R. 847 (Bankr. S.D. Fla. 2012) (credit counseling company was "initial transferee," and not just mere conduit, as to amounts company applied from payments received from Chapter 7 debtor to pay company's monthly service fees); In re Moon, 385 B.R. 541 (Bankr. S.D.N.Y. 2008) (with respect to settlement proceeds paid into attorneys' trust account, attorney was "initial transferee" as to amount of proceeds constituting attorneys' contingency fee); In re Imperial Corp. of America, 114 B.R. 115 (Bankr. S.D. Cal. 1992) (at the very least, material issue of fact as to whether law firm was "transferee" or conduit as to proceeds of settlement paid to firm for its fees). *But see* In re Cargo Transportation Services, Inc., 502 B.R. 875 (Bankr. M.D. Fla. 2013) (law firm was mere conduit of settlement proceeds, even as to amount ultimately paid to law firm from proceeds as contingency fee, when settlement proceeds initially deposited in trust account and then transferred to debtor and contingency fee was paid in accordance with court order).

D. Dischargeability of Settlement in Bankruptcy

1. If the full settlement payment is not made prior to bankruptcy, or is made and the amount of any pre-bankruptcy payment is recovered as an avoidable preference, the amount owed to the

plaintiff may be subject to discharge in the defendant's bankruptcy case, to the extent that the defendant is otherwise entitled to a discharge under the particular chapter of the Bankruptcy Code in which the bankruptcy case is commenced.

2. If the plaintiff's claim is not subject to discharge, such as a claim for actual fraud perpetrated by the defendant (*see* 11 U.S.C. § 523(a)(2)), and the plaintiff gives the defendant a release of claims as part of the settlement consideration, there is some concern that the unpaid amount of the plaintiff's claim in bankruptcy may be subject to discharge.

3. However, in Archer v. Warner, 538 U.S. 314 (2003), the United States Supreme Court held that the balance owing under the settlement of a state law fraud claim can be non-dischargeable as a debt for money obtained by fraud under Section 523(a)(2) of the Bankruptcy Code.

> In Archer, the debtor entered into a settlement of a state law fraud claim pursuant to which the debtor executed a promissory note for the settlement amount, the creditor released any claims against the debtor other than the amount owing under the promissory note, and the creditor dismissed the state court litigation with prejudice. When the debtor failed to make any payment under the promissory note, the creditor brought another state court action to enforce the settlement, and the debtor filed for bankruptcy. The debtor contended that the settlement agreement constituted a novation and that any amount owing under that agreement was dischargeable in the bankruptcy case, and the bankruptcy court, district court and Fourth Circuit Court of Appeals agreed. The Supreme Court, however, relying upon Brown v. Felsen, 442 U.S. 127 (1979), reversed, concluding that the bankruptcy court can look behind the settlement to determine if the debt arises out of an underlying fraud. *But see* In re Sager, 2014 WL 2565839 (Bankr. E.D. Pa. 2014) (bankruptcy court, without citing Archer, rules that plaintiff who settled with defendant held a contract claim and lacked a viable basis to contest dischargeability of $1.05 million judgment, apparently concluding that the court could not look behind the settlement agreement to determine if the underlying claims were non-dischargeable) (appeal pending).