Psychological Impact of Scrutiny on Contingent Fee Attorney Effort

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VII. STATISTICAL APPENDIX

I. INTRODUCTION

The use of economics has been pervasive in the analysis of litigation.1 This theory when applied to methods of compensating litigators has produced strong implications for attorney behavior and client welfare.2 The contingent fee arrangement enhances judicial access by shifting the risk of loss to attorneys, and aligns an attorney’s interests with his client’s by giving the attorney a stake in case outcomes.3 Perhaps due to these benefits, the contingent fee has become the most pervasive form of financing litigation for plaintiffs in personal injury cases.4 However, the alignment of interests is imperfect.5 According to economics theory, an attorney

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3 The impact of attorney fees on the attorney-client relationship has received as much attention from the bar and commentators as any other aspect of litigation. See, e.g., LESTER BRICKMAN ET AL., RETHINKING CONTINGENCY FEES (1994) (arguing that contingent fee attorneys are overpaid and client welfare suffers as a result); Kevin M. Clermont & John D. Curriuan, Improving on the Contingent Fee, 63 CORNELL L. REV. 529 (1978) (providing a theoretical analysis that predicts that contingent fee attorneys invest less in case preparation than is optimal for clients); Thomas J. Miceli & Kathleen Segerson, Contingent Fees for Lawyers: Their Impact on Litigation and Accident Prevention, 20 J. LEGAL STUD. 382 (1991) (arguing that contingent fee arrangements do not provide incentives to take due care); Terry Thomason, Are Attorneys Paid What They're Worth? Contingent Fees and the Settlement Process, 20 J. LEGAL STUD. 187 (1991) (arguing that in certain types of cases clients are better off without representation than with contingent fee attorney representation). For a history of U.S. legal fee arrangements, see John Leubsdoet, Toward a History of the American Rule on Attorney Fee Recovery, 47 LAW & CONTEMP. PROB. 9 (1984).

4 See Miceli & Segerson, supra note 2, at 381.

5 Estimates are that in excess of 95 percent of personal injury cases are taken on a contingent fee basis. Note, Settling for Less: Applying Law and Economics to Poor People, 107 HARV. L. REV. 442, 448 n.23 (1993) (citing JAMES S. KAKALIK & NICHOLAS M. PACE, COSTS AND COMPENSATION PAID IN TORT LITIGATION 37 (1986)).

6 See Clermont & Curriuan, supra note 2, at 536 ("In sum, neither the certain hourly fee nor the contingent percentage fee can align fully the economic interests of lawyer and client.").
has an incentive to shirk (perform less work than his client prefers) in preparing cases because he receives only a fraction of the client's return. Hence, if we accept the economic assumption that actors behave in the selfish, selfinterested fashion known as utility-maximization, an attorney stops investing time and resources in a case when his return is maximized, an event that occurs before the client's return is maximized. Thus, economics suggests that the judicial access that the contingent fee arrangement provides comes at a high price.

Although quite elegant, the economic theory of contingent fee behavior fails to account for at least two psychological phenomena that can cause deviations from economic predictions. First, attorneys are susceptible to face-saving behavior which is the psychological desire to avoid embarrassment, appearing foolish or being wrong. Secondly, attorneys are subject to escalating commitment. This phenomenon occurs when an individual increases his investment to often irrational levels in a failing or risky course of action because to cease such investments is equivalent to admitting failure. These prevalent behaviors are well documented in the psychology literature. An individual frequently validates his actions by increasing investment in the relevant activity in order to avoid prospective failure and an accompanying loss of status. For example, when put on hold, an individual often refuses to hang up even though the wait is unacceptably long. At this point, the caller often continues investing time in the phone call because hanging up would be a tacit admission that he wasted time by holding too long. In such situations the loss of status is personal due to the confirmation that the caller made an incorrect decision. As a result, the caller may find that he must validate the increased investment, leading to yet greater investments in the failing enterprise. In other words the longer the caller stays on hold the harder it is to terminate the phone call due to his ever-increasing time investment. If attorneys fall into this cycle of rationalization and augmented investment, then the shirking implications of economic theory may not apply to those contingent fee cases.

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6 Utility is a concept that generally applies to preference rankings. When used with maximization, it typically refers to a measure of satisfaction, welfare, happiness or even pleasure. See ROBERT COOTER & THOMAS ULENI, LAW AND ECONOMICS 22-23 (1988). Thus, a utility maximizer is someone who tries to maximize his level of satisfaction.


10 See infra notes 73-78 and accompanying text.
In this article, I develop a theory that addresses the paradox of why some contingent fee attorneys shirk while others work hard. I posit that the presence of critical scrutiny, which has been identified as promoting escalating commitment in other settings, promotes similar behavior in high stakes litigation. The escalation literature identifies scrutiny from a critical audience as one of the factors that increase the probability that an individual succumbs to the entrapping effects of escalation and face-saving behavior. An additional factor contributing to escalation is the existence of a competitive environment. I argue that almost all litigation is competitive, and most high-stakes and high profile cases are subject to scrutiny that is evaluative or critical in nature. Thus, it is likely that contingent fee attorneys are more prone to escalating commitment in high stakes and high profile cases. Thus, while contingent fee attorneys in low stakes cases are likely to shirk due to the relative anonymity under which they toil, attorneys in high stakes cases who are subjected to critical scrutiny are likely to work in excess of the levels that economic theory predicts.

In Part II, I begin the analysis with a review of three economic models of contingent fee attorney behavior. Economics has modeled contingent fee attorneys as selfish utility-maximizers, competitive firms, and agents in principal-agent

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11 Bert R. Brown, Saving Face, in NEGOTIATION: READINGS, EXERCISES, AND CASES 308, 313 (Roy J. Lewicki et al. eds., 1993).

12 See BROCKNER & RUBIN, supra note 8, at 58-65.

13 The level of scrutiny increases with the notoriety of the case. Coverage can range from minor newspaper articles to heavy electronic media coverage in the most famous cases. See John F. Onion, Jr., Mass Media's Impact on Litigation: A Judge's Perspective, 14 REV. LITIG. 585 (1995) (discussing the media's fascination with high profile criminal cases). This media attention also applies to civil cases. See, e.g., Robert C. Weaver, Jr., Sixth Amendment At Peril: The Media Frenzy Surrounding the Tonya Harding Cases, 4 KAN. J.L. & PUB. POL'Y 53 (1995); JAMES B. STEWART, DEN OF THIEVES (1991) (examining the case of the disgraced, former Wall Street Financier Michael Milken); PETER TRUELL & LARRY GURWIN, FALSE PROFITS: THE INSIDE STORY OF BCCI, THE WORLD'S MOST CORRUPT FINANCIAL EMPIRE (1992) (discussing the indictment of former Presidential Cabinet secretary Clark Clifford for involvement in the BCCI scandal); Owesly J. Smith, The Heat Over McDonald's Coffee, SAN FRANCISCO CHRONICLE, June 19, 1995 at A19 (recounting the story of Stella Liebeck, the 79-year-old grandmother, who received a multi-million dollar judgment against McDonalds after receiving third-degree burns from split hot coffee). Noting the entry of a 24-hour cable network known as Court TV devoted exclusively to broadcasting and analyzing trials, one commentator observed that the media coverage and outlets for such coverage, "has jumped by a startling amount." Jonathan M. Moses, Legal Spin Control: Ethics And Advocacy In The Court Of Public Opinion 95 COLUM. L. REV. 1811, 1812 n.5 (1995).

14 The media does not simply cover trials, it dissect and criticizes them. As the attorney for figure skater Tonya Harding in her "knee breaking" conspiracy case observed, "press coverage is almost uniformly cynical. In my judgment, there seems to be less and less distinction between editorializing and news reporting." Weaver, supra note 13, at 57. See also infra notes 59-61 and accompanying text.


16 See Patricia M. Danzon, Contingent Fees for Personal Injury Litigation, 14 BELL J. ECON. 213,
Although providing valuable insights about contingent fee attorney behavior, the models do not provide an explanation for why contingent fee attorneys do not either all shirk or all work diligently. In Part III, I argue that the answer to this question is that in certain cases attorneys are especially susceptible to the psychological dynamics of escalation. Specifically, attorneys are pressured by highly critical scrutiny in high stakes and high profile cases. The pressure from this scrutiny increases the probability that attorneys escalate their commitment. In Part IV, I describe an experiment that I conducted to test the implications of escalation theory for contingent fee attorney behavior. These experimental results, although not definitive, provide unequivocal support for the susceptibility of attorneys to escalating commitment. In Part V, I consider the theory’s implications. In particular, I examine the implications of face-saving and escalating commitment on reform measures designed to increase client returns at the expense of shirking attorneys. Finally, I conclude that proposals that increase the allowable contingent percentage based on the stage of litigation may be counterproductive by encouraging escalating commitment. Instead, graduated fee limits are more likely to achieve the desired redistribution with fewer pitfalls, whereas more invasive proposals may curtail the accessibility of the judicial system in low-to-moderate-stakes cases.

II. ECONOMIC MODELS OF CONTINGENT FEE BEHAVIOR

This section examines economic models of contingent fee behavior. These analyses treated the contingent fee attorney as a utility maximizer, a competitive firm, or as an agent of his client-principal. The implications of each of these models are strikingly different, yet all fail to fully capture the differences in contingent fee behaviors.

A. Utility Maximization

Schwartz and Mitchell provided the first formal economic critique of contingent fee arrangements. They assumed that 1) attorneys’ actions are independent of defendants’ actions, 2) attorneys are self-interested utility maximizers, and 3)
clients’ expected returns increase with attorney effort at a decreasing rate. The initial assumption means that the contingent fee attorney does not have to worry about the defense attorney’s decisions or case. Thus, whether the plaintiff’s attorney faces an incompetent adversary or an experienced, diligent, Order-of-the-Coif, top of the class law school graduate, he makes the same litigation decisions. Although this assumption is rather unrealistic, its primary purpose is to simplify the analysis. The second assumption means that an attorney takes an action if and only if it increases his return relative to the opportunity costs\(^2\) of taking the action. There is no charity or self-sacrifice in the model, and attorneys definitely do not put clients’ interests before their own. In its most extreme form, the assumption suggests that an attorney will refuse to take an action that would increase his client’s return by one million dollars if the action would reduce the attorney’s return by one dollar.\(^3\)

The third and final assumption, although not as controversial, is significant in that it suggests that clients are better off with more attorney effort rather than less. Additional effort may not increase a client’s expected return in every case, but when averaged over many cases clients benefit from the effort. Moreover, the assumption indicates that initial effort is more productive than supplemental effort. Clearly initial acts such as filing the case, arranging to have a defendant served, and appearing at all court proceedings are critical. Failure to take these actions insures almost certain defeat, whereas performing these actions gives a client a positive probability of obtaining a significant settlement or winning. However, there are limits to the benefits of additional effort. The strongest witness to testify on an issue usually has greater probative impact than the tenth or eleventh strongest witness. Eventually an additional witness used to prove the same point adds virtually nothing to a client’s case. The same logic applies to case authority. Using a few authorities to support an argument may be quite powerful. However, at some point an additional authority increases the strength of the argument less than the previously used authority. This decreasing-returns assumption is key to the shirking implication of the utility-maximization model.

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\(^1\) Economic actors are influenced by the decisions and actions of other economic actors. See generally David M. Kreps, Game Theory and Economic Modeling (1990); Douglas G. Baird et al., Game Theory and the Law (1994).

\(^2\) Schwartz and Mitchell assume that the attorney can receive a fixed wage per hour working elsewhere. See Schwartz & Mitchell, supra note 15, at 1127-1128. Therefore, the profit received from the case is the return in excess of the opportunity wage of devoting effort elsewhere.

\(^3\) Opportunity costs are the economic costs of a forgone alternative action. For example, when an individual attends law school, he pays tuition and forgoes the income he would have received from working. Hence, his opportunity costs after the first year of law school include his alternative annual salary, tuition plus the return on that amount had he invested it. See Cooter & Ulen, supra note 6 at 35. An attorney’s opportunity costs include the return he could have received by investing his time in alternative cases. Thus, if it is possible for a contingent fee attorney who spends 100 hours on a case to take other cases with an hourly fee of $100 per hour, the attorney’s opportunity costs are $10,000.

\(^4\) But see Stephen Pearlstein, The Economist as Ebenezer Scrooge, WASH. POST, August 25, 1994, at B9 (reviewing research that suggests that the selfish and uncooperative behavior, integral assumptions of microeconomic theory, may be learned or acquired behaviors).
In deciding whether to increase his effort, a utility-maximizing contingent fee attorney compares the increase in his personal expected return to the cost of undertaking additional effort.\(^{24}\) An attorney increases his effort if and only if the added benefit exceeds the added cost. The problem is that an attorney's personal expected return is less than the client's expected return. In other words, a contingent fee attorney receives some fraction or percentage of his client's return.\(^{25}\) This fractional share coupled with decreasing returns to effort causes an attorney's marginal increase in expected return due to additional effort to be less than the overall increase in his client's expected return. Hence, the marginal increase in expected return that an attorney compares to his marginal costs is less than the total increase in expected return. An attorney, in essence, undervalues the benefits of additional effort and, accordingly, declines to take actions whose total expected benefits exceed attorney costs.\(^{26}\) This undervaluation leads to the attorney exerting less effort than plaintiffs would choose to maximize their net returns.

To illustrate, suppose that you can assign numerical values to five possible actions that an attorney can take to improve his case prospects. For simplicity, each action has an identical cost of 12 using the same measurement units as expected benefits. The expected benefit of each of the actions from most beneficial to least is 60, 45, 30, 15, and 6. A hypothetical hourly fee attorney, whose interests are perfectly aligned with the plaintiff's, performs all but the last action.\(^{27}\) Each of the four most beneficial actions provides a net positive expected benefit of at least three. The plaintiff rejects only the last action, with a gross expected benefit of 6 and a net return of -6.

A contingent fee attorney views this choice set quite differently. A contingent fee attorney, receiving one-third of the plaintiff's total litigation return, perceives these five actions as providing him with personal expected benefits of 20, 15, 10, 5, and 2. When weighed against his costs of 12 per action, the utility-maximizing attorney performs only the two most beneficial actions: the two whose benefits exceed the attorney's marginal costs. Each of the three least beneficial actions leaves the attorney with a personal return of at best negative two. Thus, in our example, the utility-maximizing attorney performs only two actions, half the

\(^{24}\) An expected value, whether utility, benefit, return or cost, is the sum of the probabilities of each possible outcome times the value of each of those outcomes. See COOTER & ULEN, supra note 6, at 56. Hence, if there are two possible returns, the first with a one-third probability and the second with a two-thirds probability, the expected return is one-third times the first return plus two-thirds times the second return.

\(^{25}\) This contingent percentage is typically one-third, although, there can be a wide variance. One commentator stated that fees range from 25%-40%. Richard M. Bimholz, The Validity and Propriety of Contingent Fee Controls, 37 UCLA L. REV. 949 (1990). Other commentators have indicated that fees can range up to 50%. See LESTER BRICKMAN ET AL., supra note 2, at 13.

\(^{26}\) For detailed analyses of this argument, See Clermont & Currivan, supra note 2, at 543-546 (providing a graphical analysis); Danzon, supra note 16, at 215 (providing a mathematical analysis).

\(^{27}\) The choice of a hypothetical hourly fee attorney with perfectly aligned interests is the baseline used in other analyses. See, e.g., Clermont & Currivan, supra note 2; Danzon, supra note 16. The benefit of this baseline is that it the attorney becomes a mere conduit of the plaintiff's interests.
actions that the plaintiff prefers that he perform. The implications of the utility-maximization model is that a plaintiff might reap a net positive return from the attorney questioning six or seven witnesses, whereas a contingent fee attorney would be willing to question at most four or five witnesses. Hence, attorneys provide suboptimal representation under contingent fee arrangements. \(^{28}\)

B. The Competitive Model of Attorney Behavior

With limited barriers to entry and a plethora of attorneys, one would expect the legal services market to be perfectly competitive. \(^{29}\) Many contingent fee attorneys make real economic profits, and there is little indication that they discount their services. \(^{30}\) This characteristic suggests that there is limited competition in the market for attorney services. However, Professor Danzon notes in her study that there can be competition without price discounts. \(^{31}\) In order to compete for future cases without offering discounts, a competitive attorney must choose actions that distinguish his practice from the practices of competitors.

The following exposition tracks Danzon's competitive model. Quality as well as price is typically used to differentiate products from those of competitors. \(^{32}\) This dimension is available to attorneys as well. Whereas price is the most common dimension on which firms compete, attorneys are more likely to use quality to distinguish their services. An attorney can discount his contingent percentage to attract clients. However, a plaintiff with a strong claim might be reticent to accept such discounts unless he is convinced that the attorney is willing and able to provide

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\(^{28}\) The actual conflict between contingent attorney and client is actually greater than Schwartz and Mitchell suggested because the contingent fee client incurs no costs, and therefore, cannot have interests aligned with a contingent fee attorney who incurs costs. Hence, the contingent fee client faces a zero marginal cost of effort, and therefore, prefers his attorney to work until the marginal return of additional effort is zero. However, such an outcome is no more optimal than that produced by the contingent fee attorney's decision because the costs of performing marginal actions far exceed their costs. This analysis carefully avoids the issue of social optimality because of the complexity of this issue. A true consideration of optimality not only would include attorney's costs and client benefits but externalities such as the cost of the publicly provided judiciary and the impact of erroneous decisions on precedent creation and behavior. See GORDON TULLOCK, TRIALS ON TRIAL 5, 14-15 (1980). Tullock argues that social optimality is achieved when all litigation costs are minimized and decision accuracy is maximized. Instead of addressing social optimality, I instead adopt the \textit{de facto} standard in fee research maximizing the client's welfare net the hourly fee value of attorney effort. See Clermont & Currivan, \textit{supra} note 2, at 543; Danzon, \textit{supra} note 16, at 214-215.

\(^{29}\) A market is perfectly competitive when there are so many sellers that all sellers accept the given market price and receive zero economic profits. Clearly there are attorneys who make substantial economic profits. See DEREK BOK, THE COST OF TALENT, 139-140 (1993) (asserting that contingent fees have made some attorneys millionaires).

\(^{30}\) \textit{See} Danzon, \textit{supra} note 16, at 214.

\(^{31}\) \textit{See id.}

high quality representation. A discounted contingent fee is no bargain if the attorney is unable to bargain effectively for a fair settlement. In a case that settles for a million dollars, a one-third reduction in a thirty percent contingency might initially save the plaintiff $100,000. However, if a more skilled attorney could have obtained a $2 million settlement, then the plaintiff is worse off by $600,000. Therefore, given the wide differences in outcome that may be attributed to the attorney’s ability, many plaintiffs, especially those in high stakes cases, are likely to be more concerned about the quality of the representation rather than price. Therefore, establishing a reputation as a provider of high quality legal representation is likely to be a more effective strategy for maximizing long-term returns. If an attorney develops a reputation for putting his own interests ahead of his client’s, then he is not likely to compete well for cases with high expected returns. Without such cases, the attorney’s practice is unlikely to thrive. His practice will consist of weak and marginal cases or cases with low expected returns. The attorney is likely to draw poor and unsophisticated clients who either have trouble obtaining the services of attorneys with better reputations, or who do not search for high quality representation.

Although obtaining clients in this manner may occasionally garner a large return

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33 Second-tier liberal arts colleges termed this paradox the "Chivas Regal" effect during the tuition run-up of the 1980s. These colleges found that reduced or discounted tuition actually lowered applications rather than increasing them. Prospective students used the lower tuition of such institutions as a signal of inferior quality rather than a signal of a bargain. Hence, instead of increasing the yield of top students, the lower tuition actually left the schools with less high quality students than the high tuition. Morning Edition: College Costs Rise - More Slowly (National Public Radio broadcast, April 21, 1997) (Transcript no. 97042106-210).

Analogously, rather than attracting clients, fee discounts may signal clients that the quality of the attorney's representation is lacking. With limited information about attorney ability, plaintiffs are likely to search for alternative information to serve as proxies for attorney ability. Under certain conditions, the discount may signal plaintiffs that the discounting attorney is unlikely to provide high quality service. Although any attorney can charge the going contingent rate or high rates, high quality attorneys will not give discounts. The value of their representation is high, and their costs may be higher as well reflecting the incremental investment they put into representing clients. As a result their costs are likely to be higher making it infeasible to give discounts. Therefore, an attorney who offers a discount signals to the plaintiff that costs are low, or that he is not yet established. The low cost may be indicative of substandard effort, whereas an attorney who is not established may not have the experience necessary to provide high quality service. In either case, the discount signals the plaintiff that he is unlikely to find high quality representation with the discounting attorney. For a discussion of the informational value of signaling see Tirole, supra note 32, at 118-21.

34 Under a 30% contingent fee arrangement, the client receives $700,000 of the $1 million settlement or $800,000 after the discount. In the undiscounted case that yields $2 million the client receives $1.4 million. Therefore, the client by choosing the more expensive attorney gains $600,000. This example raises intriguing implications for recent debates about contingent fee arrangements. Many commentators have expressed dismay at the exorbitant imputed hourly fee rate of some contingent fee attorneys. See, e.g., Lester Brickman, Contingent Fees Without Contingencies: Hamlet Without the Prince of Denmark? 37 UCLA L. REV. 29, 76 n.186 (1989); Brickman, et al., supra note 2, at 55 n.24; J. Golden, The Million-Dollar Lawyers 64-65 (1978); Warden, Should a Lawyer Make $10,000 an Hour? STUDENT LAW., Apr. 1981, at 21-23. However, perhaps a better question is whether the value added by the attorney exceeds additional fees. An attorney who increases client's net return by $600,000 in exchange for an addition $300,000 in fees may be worth a $100,000 imputed hourly fee.

for the attorney, an attorney who fails to establish a reputation for providing high quality representation is unlikely to consistently attract the most lucrative cases.

In order to establish a reputation as a high quality provider of legal services, an attorney must put forth effort that exceeds that of the utility-maximizing attorney. However, if all or many attorneys adopt this strategy, an attorney would have to exert still more effort in order to distinguish his practice. Any attorney who establishes a reputation for investing more effort and money in his cases than all other attorneys is likely to have a competitive advantage over other attorneys vying for the same cases. Establishing such a reputation is extremely difficult. In a competitive environment, all participating attorneys have an incentive to match or exceed other attorneys' case investments. This game of outspending competitors has its limits. An attorney must avoid bankrupting his practice by investing excessively in cases. Therefore, the most that any attorney invests in a case is an amount that gives him an expected return of zero.\textsuperscript{36} In a perfectly competitive environment, this amount is also the lowest amount invested.\textsuperscript{37} If the attorney invests less, then other attorneys outbid him for the best cases leaving the under-investing attorney marginal cases only. Hence, in equilibrium, all attorneys invest at an effort level that leaves them with zero-profit returns. Under these conditions, the competitive contingent fee attorney exerts the same level of effort that the hypothetical interests-aligned attorney chooses.\textsuperscript{38} Thus, under the competitive model, contingent fee attorneys maximize client welfare.

C. The Agency Model of Attorney Behavior

Neither the utility-maximization nor the competitive model completely describes contingent fee attorney behavior. The utility-maximization model provides a good explanation of attorney behavior in low stakes litigation but fails to describe the behavior of elite, 'superstar' attorneys who specialize in high-stakes liability cases. These attorneys invest enormous resources in their cases and often obtain substantial judgments and settlements as a result of their efforts.\textsuperscript{39} Undoubtedly,

\textsuperscript{36} For an illustration of the misfortunes that may befall an attorney who fails to heed bankruptcy constraint and overinvests in a case see id.

\textsuperscript{37} See Danzon, supra note 16.

\textsuperscript{38} See id. The benefit of using the hypothetical interests-aligned attorney as the baseline is that the attorney becomes a mere conduit for the plaintiff's interests.

\textsuperscript{39} Others have recognized that contingent fee attorneys who successfully differentiated their services can obtain above average fees for their services. In decrying this phenomenon, former Harvard Law School Dean Derek Bok stated:

There are famous plaintiffs' attorneys who preside over a stable of associates and succeed, year in and year out, in earning incomes of more than $1 million. Because of their reputation, these attorneys are asked to take many more cases than they can handle. As a result, they can pick and choose more carefully and hence confine their efforts to claims that are likely to produce big verdicts or generous settlements. In this way, they can exploit the rigid contingent fee structure and reap huge rewards for the effort they expend.
utility-maximizing behavior in response to withering defense efforts by deep-pocketed corporations is unlikely to produce the large court awards that have prompted popular calls for tort reform. On the other hand, the competitive model provides a better description of attorney behavior in high-stakes cases. Attorneys behaving competitively are more likely to match and, perhaps, exceed the investment of deep-pocketed defense teams. However, the persistence of attorneys who provide inadequate representation is clearly inconsistent with the competitive model. The competitive model also fails to explain how a contingent fee attorney profits from his efforts. The model predicts that competing attorneys will bid profits to zero by increasing their work effort. Yet a small but significant percentage of contingent fee attorneys obtain substantial positive returns from their efforts. The persistence of such success is inconsistent with competition. Hence, whereas each model provides descriptive power for certain cases, neither model satisfactorily explains the full range of contingent fee attorney involvement.

The agency model provides an alternative description of contingent fee behavior by recognizing that the structure of the attorney-client relationship as well as case characteristics influence attorney behavior. Under agency theory, the attor-

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**Bok, supra** note 29, 139-40, as quoted in Brickman et al., supra note 2, at 56 n.26. What Bok does not consider in his denunciation is the benefit that plaintiffs receive from hiring these high priced attorneys.

**40** I discuss some of these proposed reforms below. See infra Part V.B.


**42** One of the criticisms of the contingent fee arrangement is that attorneys profit excessively, often receiving case returns that are disproportionately large relative to case risk, and annual incomes that exceed those of their hourly fee counterparts. Professor Brickman has illuminated this point in several articles. See Lester Brickman, On the Relevance of the Admissibility of Scientific Evidence: Tort System Outcomes are Principally Determined by Lawyer's Rates of Return, 15 CARDOZO L. REV. 1755, 1773-74 nn.57-60 (1994) (citing hourly fee rates of return for contingent fee attorneys of $30,000-$50,000 per hour); Brickman, supra note 34, at 102-03 (From the perspective of a plaintiff seeking to sell a claim on a contingent fee basis, "lawyers have been instrumental in creating a tort system which overcompensates lawyers, undercompensates many claimants, and creates barriers to nonlawyer competition in the claims invoking process."); Brickman et al., supra note 2, at 15.

**43** Agency is a common law concept. In recent years economists have explicated and modeled the complex cost and incentive issues associated with agency in contract. See, e.g., Eugene Fama, Agency Problems and the Theory of the Firm, 88 J. POL. ECON. 288 (1980); Sanford J. Grossman & Oliver D. Hart, An Analysis of the Principal-Agent Problem, 51 ECONOMETRICA 7 (1983); Bengt Holmstrom, Moral Hazard and Observability, 10 BELL J. ECON. 74 (1979); Steven Shavell, Risk Sharing and Incentives in the Principal and Agent Relationship, 10 BELL J. ECON. 55 (1979). Business management scholars have augmented the work of economists by applying agency principles to management studies. See, e.g., S. Baiman, Agency Research in Managerial Accounting: A Second Look, 15 ACCT. ORG. & SOC'Y. 341 (1990); R. E. Hoskisson & M. A. Hitt, Antecedents and Performance Outcomes of Diversification: A Review and Critique of Theoretical Perspec-
ney acts as agent for his client-principal in litigation. The attorney's utility depends on the size of his expected return from the case and how hard he has to work to get it. Agency assumes, quite reasonably, that the attorney prefers to make as much money as possible but strongly dislikes working hard. The attorney accepts the case provided its expected return exceeds the return he can obtain from employing his efforts in his best alternative activity. The return from this activity is called his reservation wage. Under the simplest agency model, the agent's effort choice is binary; he either shirks or works hard.\textsuperscript{44} The client is better off if the attorney works hard. Hence, there is an inherent conflict of interest between attorney and client. Therefore, the client's task within the context of contingent fee arrangements is to enter into a feasible contract with the attorney that elicits hard work.

This exercise is no simple task because attorneys prefer to shirk rather than work hard. In a perfect world, the client executes a contract under which he pays his attorney \( x \) if he shirks and \( x+d \) if he works hard choosing \( d \) to be sufficiently greater than \( x \) to elicit hard work. The problem with this strategy is that the attorney's effort is unobservable. If the client could monitor his attorney's efforts then he could implement the strategy. However, monitoring is neither practical nor feasible. It is unlikely that any attorney would agree to the constant monitoring required to insure hard work. Even if the client could conceivably monitor the attorney, he typically does not have the expertise to assess his attorney's behavior. An unsophisticated client does not know whether the attorney has researched the issues adequately, deposed all necessary witnesses, or discovered all relevant evidence.\textsuperscript{46} Therefore, although the client's interest is effort, he must base the contract on an observable proxy.

A common effort proxy identified in economics textbooks is the outcome or, for litigation, the case return.\textsuperscript{46} Assume, for the moment, that litigation has a binary outcome, the plaintiff either wins or loses.\textsuperscript{47} Depending on the probabilities

\textsuperscript{44} For a fairly elementary exposition of the agency problem that utilizes a binary choice space, see David M. Kreps, A Course in Microeconomic Theory, 578-583 (1990).

\textsuperscript{45} See Deborah L. Rhode, Ethical Perspectives on Legal Practice, 37 Stan. L. Rev. 589, 635 (1985) (noting that clients are not always in a position to monitor attorney actions). The attorney is likely to exert substantial influence on litigation decisions regardless of the level of monitoring due to his superior experience and legal expertise. Hence, the attorney has the power to make decisions in the attorney's favor, and not the plaintiff's, by persuading the plaintiff that the action is in the plaintiff's best interests. See Bimholz, supra note 25, at 955.

\textsuperscript{46} See Kreps, supra note 44.

\textsuperscript{47} This binary assumption has been the basis of a significant debate in the law and economics literature. Priest and Klein's now famous prediction that plaintiff's win 50% of trials implicitly assumes a binary outcome. George L. Priest & Benjamin Klein, The Selection of Disputes for Litigation, 13 J. Legal Stud. 1 (1984). However, the outcome of trial is rarely clearly a victory or a loss. A judgment for the plain-
of winning with and without high attorney effort, the client might offer to pay the attorney $x-e$ if he loses the case, and $x+d$ for winning the case. For example, suppose the attorney’s reservation wage is 90, high effort costs the attorney 25, and his probability of winning the case with high effort is .8. Also assume that his probability of winning with low effort is .2, and the cost of low effort is zero. The client can offer the attorney a contract under which the attorney receives 75 if he loses the case and 130 if he wins the case. Under this scenario, the attorney could exert low effort under the contract and receive

$$(.8)(75) + (.2)(130) - 0 = 86.$$  

Alternatively, he can work hard under the contract and receive

$$(.2)(75) + (.8)(130) - 25 = 94.$$  

A risk-neutral attorney accepts this contract and works hard because the contract gives him an expected return in excess of his reservation wage. Moreover, he does not shirk under the contract because to do so leaves him with nearly 4 less than his reservation wage. Assuming that the client’s return from winning the case exceeds 130, this incentive-based contract elicits behavior that maximizes the client’s gross return.

Characteristics of contingent fee arrangements make implementing an incentive-based contract for plaintiffs’ attorneys difficult. Plaintiff’s attorney compensation almost certainly is limited to a contingent fee in most civil cases due to the entrenchment of this fee arrangement in the United States. On the plus side, contingent fee arrangements are very similar to the incentive-inducing contracts outlined in the preceding paragraph. Under contingent fee arrangements attorneys are rewarded for improving their clients’ return. If an attorney performs poorly and the client loses, the attorney receives no return. However, the standard one-third contingency is hardly optimal. In order for the contract to provide a sufficient incentive to induce optimal effort, the return from the best outcome must be 1) large enough to provide the attorney with an expected return that exceeds his reservation wage, and 2) sufficiently greater than the downside outcome to make the gain from investing additional costly effort worthwhile. Under a contingent fee arrangement

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48 Professor Hay explicitly recognizes this issue by rejecting the question of what the optimal fee arrangement is, and instead asking what the optimal contingent percentage should be given the pervasiveness of this fee arrangement. See Hay, supra note 17, at 504-505.

49 In the principal-agent literature, the first condition is known as a participation constraint because it must be satisfied for the attorney to take the case, and the second is called the incentive constraint because it
the first condition is likely satisfied anytime an attorney accepts a case. An attorney who too often takes cases with negative attorney expected returns soon goes bankrupt.\textsuperscript{50} The second condition is difficult to satisfy with a contingent fee arrangement. Satisfaction of this condition provides the incentive to work hard. Unless the increased attorney benefit from exerting high rather than low effort exceeds the cost of working harder, the attorney shirks.

In low stakes cases, an attorney’s contingent fee return from hard work is unlikely to be sufficiently greater than his low-effort return to induce him to work hard. For example, suppose that a case has a payoff of $3000 and the hourly fee value of the attorney’s time is $100. If the attorney works hard and wins, his $1000 share under a standard contingent fee arrangement is likely to be too low to induce him to work hard if he can settle the case with little or no effort. Suppose he can settle the case for $1200 and receive a $400 attorney share with low effort. Then unless he can achieve the hard-effort result with less than six additional hours, he does not continue the case.\textsuperscript{51} Hence, it is highly unlikely that the contingent fee contract by itself can induce hard work in moderate-stakes cases.\textsuperscript{52} Monitoring also is unlikely to increase attorney effort in moderate-stakes cases. The expertise differential makes it difficult for the client in these cases to accurately evaluate his observations.\textsuperscript{53} Moreover, even if effective monitoring were feasible, it is unlikely to elicit the desired response without a greater attorney return. Without the larger return, the attorney could not exert the additional effort without losing money.\textsuperscript{54} Thus, the contingent fee arrangement is not conducive to eliciting hard work from attorneys in low to moderate stakes cases.\textsuperscript{55}

The contingent fee contract comes closer to eliciting welfare-maximizing effort in high stakes cases but is still inadequate. In high-stakes cases the high effort expected return is more likely to be sufficiently larger than the low-effort expected

\textsuperscript{50}See e.g., Cooper, supra note 35.

\textsuperscript{51}In an empirical study on attorney compensation, the average number of hours for contingent fee attorneys was 47.9 and exceeded 30 for low stakes cases. See Herbert M. Kritzer et al., The Impact of Fee Arrangement on Lawyer Effort, 19 LAW & SOC’Y REV. 251, 266-267 (1985).

\textsuperscript{52}This deviation may not be as stark as the example suggests. The contingent fee attorney may be able to take advantage of the high transaction costs that accompany litigation in order to obtain settlements that are as high or greater than the expected return from working hard. The defense may be willing to pay a substantial settlement in order to avoid extended litigation. See Avery Katz, The Effect of Frivolous Lawsuits on the Settlement of Litigation, 10 INT’L REV. L. & ECON. 3, 26 (1990). Thus, even if the hard-work expected return does not exceed the attorney’s cost difference between hard and low work, the plaintiff can still obtain a payoff close to the hard-work expected return.

\textsuperscript{53}See Birnholz, supra note 25, at 954 ("As a result, most clients generally will defer to the attorney’s expertise and agree with the attorney’s estimate of the risk and value of their case . . . “); Rhode, supra note 45.

\textsuperscript{54}See supra note 36 and accompanying text.

\textsuperscript{55}One study suggests that the limits of moderate stakes is about $6000. See Kritzer et al., supra note 51, at 267.
return to elicit hard work. For example, if you scale the preceding illustration by a factor of ten, then the attorney's shirk-work decision depends on whether he can win the case with 60 or less hours, an event that is more likely to occur at this effort level. What this means is, whereas the attorney may prefer to settle a $3000 case when a $12000 settlement is available, there is a much higher probability that the attorney continues to contest a $30,000 dispute rather than accept a $12,000 settlement offer. Scale the illustration by a larger factor, and the incentive to work hard is even greater. Hence, when stakes are greater the attorney likely works harder and obtains a greater proportion of the maximum possible expected return.  

However, the nearly continuous nature of both potential payoffs and effort levels may prevent a client from receiving welfare-maximizing effort from his attorney. In the agency examples the attorney is faced with a binary effort choice. In reality, the attorney's effort choice is essentially continuous and each effort choice has a distinct expected return associated with it. Faced with this multiplicity of choices, the attorney is likely to exert more than minimum effort in high stakes cases. However, he is unlikely to choose the effort level that is optimal for his client. Instead he chooses the effort level for which the marginal expected benefit from additional effort equals his reservation wage. If this description sounds familiar, it should. It is simply a description of the utility-maximization model using agency theoretic language.

The client's inability to limit the number of effort options and, more importantly, to control the difference between attorney returns for different outcomes provides the attorney with too much control over effort choices. Instead of facing the possibility of a substantially larger expected return for greater effort, the attorney can choose to work a little harder and receive a slightly greater expected return. Although the selected effort level is almost certainly greater than what he would choose in a low-stakes case, it is unlikely to approach the level that is optimal for the client. Thus, contingent fee contracting is incapable of aligning attorney-client interests due to the inability of clients to enter into optimal incentive contracts with their attorneys.

III. PSYCHOLOGICAL IMPLICATIONS OF SCRUTINY AND ESCALATION

A. Case Visibility and Incentives to Work Hard

Although the agency relationship alone cannot induce attorneys to work hard, the contract combined with public scrutiny or high case visibility may induce

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56 Professors Hay's analysis and simulations suggest that client return as a percentage of the maximum possible return increases with the attorney profit. See Hay, supra note 17, at 520. This result is consistent with a conclusion that attorneys work harder when the potential reward is greater which generally occurs in cases with larger stakes.

57 See supra text accompanying note 44.

58 See supra Part II.A.
attorneys to work hard. Direct monitoring as contemplated by agency theory is just as difficult in high-stakes cases as it is in low-stakes cases. However, with greater stakes, the quality of attorney representation is substantially more visible. For sufficiently high-stakes cases, the media may cover the trial on a regular or even daily basis. The quality of the case presented may be analyzed, and the trial outcome reported and dissected. Attorneys on both sides may be compared and contrasted, and have their representation evaluated. Even without intensive media coverage, the attorney’s actions are likely to receive greater scrutiny in high-stakes cases. Clients in such cases are likely to be more sophisticated or have access to advisers who can monitor attorney representation. Corporate clients have increasingly taken a more active role in monitoring attorney actions. Even in the absence of media attention and sophisticated clients, peer scrutiny from other attorneys may discourage attorneys from shirking in high-stakes cases. Thus, reputation building and embarrassment avoidance are likely to motivate attorneys where purely economic factors do not.

Public scrutiny or high case visibility is likely to induce hard work 1) by enhancing the reputation of attorneys who work hard and 2) embarrassing those who shirk or obtain poor results. Maintaining a reputation for working in clients’ interests motivates attorneys because failing to do so may make it difficult to obtain subsequent cases with high expected returns. To compete effectively for such cases, an attorney must establish a reputation for providing high quality representation. Shirking in his representation in even one high profile case may be sufficient to disqualify the attorney from competing for choice cases in the future.

59 In an earlier period, the trial of Bruno Hauptman for kidnapping the baby of aviator hero Charles Lindbergh received worldwide media attention, which some believe may have biased the outcome of trial. See Moses, supra note 13, at 1817-1818.

60 The following quote describes the fishbowl effect of media scrutiny focused on attorneys in high profile cases:

I suggest that we need to use common sense about how the media pressure tends logically to affect the different players and necessarily the outcome in high profile cases. The lawyers involved cannot help but in some fashion be affected by the attention. One does not get a call from network anchor people every day; it is a once in a lifetime experience. Many lawyers will naturally conclude his career could be made, depending upon how the press is handled and the outcome of the case.

Weaver, supra note 13, at 57.

61 Corporate clients are more likely to employ outside counsel on an hourly fee basis. Normally, in-house corporate counsel is expected to monitor the efforts of outside counsel. In cases of serious doubt, outside legal auditors may be called in to take apart billing records and evaluate the propriety of charges. Note, however, that these monitors pose their own sort of agency problems: the corporate counsel probably has a bias toward winning, as opposed to losing, even at great cost, and the outside legal auditor undoubtedly works by the hour. See Stephen Salop & Robert Litan, Reforming the Lawyer-Client Relationship Through Alternative Billing Methods, 77 JUDICATURE 191, 192-93 (1994) (monitoring problems).

62 See Miller, supra note 17, at 210; Weaver, supra note 13, at 57.

63 Like investing in education, reputation building is economically rational because it enhances the human capital of the reputation holder, which in turn can increase the holder’s income. See COOTER & ULEN,
fore, having a reputation as a provider of high quality legal representation provides a self-enforcing mechanism against shirking in high-stakes cases.

In order to maintain this reputation an attorney may overinvest in litigation by devoting more resources than is justified under short-run utility maximization.\textsuperscript{64} Whereas the apparent return from investing these resources may not exceed their costs, the willingness of an attorney to "burn" money signals potential clients that the attorney is willing to go all out on behalf of clients.\textsuperscript{65} Thus, an attorney in a high stakes case may be willing to invest an additional $1000 even though the increase in expected return is less than $1000 if the investment shows his devotion to the case. This behavior is especially likely to occur in a case in which the attorney's share is measured in the tens or hundreds of thousand dollars.

B. Escalating Commitment and Contingent Fee Attorney Behavior

In addition to promoting the economically rational behavior of reputation building, public scrutiny in high-stakes cases increases the likelihood that attorneys become entrapped by escalating commitment. Escalating commitment is the tendency for individuals to make increasing investments in a failing or risky course of action.\textsuperscript{66} While there are many factors that promote escalation, psychologists have discovered that individuals subject to scrutiny are prone to escalate their commitment in order to avoid appearing foolish, incompetent or wrong.\textsuperscript{67} Attorneys make many decisions that can be second-guessed. Rejecting a settlement offer, making a high demand, or choosing a high-risk strategy are examples. If the decision is not immediately validated, external scrutiny can pressure the attorney to take "face-saving" actions like refusing to settle or maintaining a high demand.\textsuperscript{68} If an attor-

\textsuperscript{64} See supra note 39.

\textsuperscript{65} In information economics, the expenditure of excess resources may be a signal to prospective clients that the attorney will provide high quality representation. The logic is that a shirking attorney would not invest so much in a case. Therefore, because this attorney in fact did invest an excessive amount in the case, he cannot be a shirking attorney. For a discussion of signaling models, see KREPS, supra note 44, at 629-638.


\textsuperscript{67} Bert R. Brown, The Effects of Need to Maintain Face on Interpersonal Bargaining, 4 J. EXP. SOC. PSYCHOL. 107 (1968) (noting that in laboratory experiments, observing audiences induce bargainers to willingly incur financial losses in order to retaliate against individuals who had previously made the bargainers appear foolish).

\textsuperscript{68} My primary interest is how being observed by others promotes escalating in contingent fee attorneys. Although attorneys for both plaintiff and defendants can escalate their commitment, the contingent fee attorney generally has a greater psychological investment in a case than the attorney for the defendant. Unlike the defendant's attorney, the contingent fee attorney accepts and files the lawsuit after evaluating the viability of the plaintiff's claim. Therefore, the attorney's judgment is in question if the case is unsuccessful or meritless. Hence, the plaintiff's attorney has the incentive to validate his prior decision by winning or obtaining a significant settlement. In addition, the contingent fee attorney has an ever-increasing financial invest-
ney succumbs to these pressures, escalation and entrapment often provide a better explanation for his decisions and choices than does his legal training or experience.

The need to validate decisions and investments has been repeatedly observed. In studies of escalation, subjects are often entrapped in games of escalating commitment and investment. Often the dynamic is so strong that subjects continue investing in the game long after one or both subjects have lost money and have no possibility of breaking even.69 Professor Shubik devised a fiendishly clever game called the dollar auction that illustrates this dynamic.70 The game administrator announces that he will auction a dollar bill to the highest bidder. All bidding is public, anyone can bid, and there is no limit to the number of bids that one person can make. Bidders can quit bidding at any time. The game deviates from a standard auction in that both the highest bidder and the second highest bidder pay their final bids, but only the highest bidder receives the dollar. Hence, if the final bids are $.55 and $.60, the highest bidder nets $.40 and the second highest bidder loses $.45.

Bidding, however, almost always exceeds the one dollar level. When bids reach the one dollar mark, students realize that if they quit, not only do they lose a dollar by finishing second, but they also feel extremely foolish because they were “sucker ed” into participating in this game. However, if they continue and the other side quits, they lose far less than one dollar and they save face by “winning” the game. Unfortunately, the other side has the same incentives. At every bid level, the pressure to continue in the game is intense. Increasing your bid almost always appears to result in a smaller loss than finishing second with your current bid. In addition, there is the validation of winning versus losing the game. Thus, a $1.90 bidder stands to lose nearly two dollars by finishing second, whereas increasing to a winning bid of $2.10 reduces the loss to $1.10. Although the bidder likely realizes that the other side has an incentive to increase her bid from $2.00 to $2.20, the bid increase allows the student to delay admitting defeat, and provides a possibility of victory. In my classes, subjects have spent over six dollars for the one-dollar prize.71

Escalating commitment fails to satisfy basic economic rationality requirements. Rationality requires individuals to exclude consideration of prior investments and expenses from their decisions because these (sunk) costs are irrelevant to

69 See ALLAN I. TEGER, TOO MUCH INVESTED TO QUIT 12-25 (1980); see generally WILLIAM POUNDSTONE, PRISONER’S DILEMMA (1992).


71 I have conducted this game several times in classes with final bids typically in the $2-$3 range. Bids typically start in the $.20-$3 range, and bidders do not realize that they have been trapped until bids exceed the one dollar mark. For a description of the game that ended with a six-dollar bid, see infra note 178.
current and future decisions. Therefore, if the most beneficial action from this moment forward is to terminate the previous course of action, a rational actor will do so whether he had spent zero, one, or one million dollars. The sunk costs would not be a consideration in selecting the proper course of action. Thus, a rational individual would never fall into the endless spiral of never-ending investments in a hopeless game of entrapment like the dollar auction. However, individuals do take prior expenditures into account in making prospective decisions. If those prior decisions can make the individual look foolish or incompetent, he is likely to take actions to rationalize such prior decisions.

The dollar auction is not the only circumstance in which prospective decisions depend on prior investments. Individuals consistently rely on sunk costs in making decisions. Some examples include waiting on hold for a caller when you have better things to do with your time, waiting for a bus to come when you could have walked the distance in a shorter time, and the U.S. military engagement in Southeast Asia. What drives us in these examples is a need to validate our investments. Recognizing that our costs are sunk, or lost, is an admission that previ-


73 See Brockner, supra note 8, at 40-41; Staw, supra note 8, at 28-29.


75 See supra note 8 and accompanying text.

76 See BROCKNER & RUBIN, supra note 8, at 1.

77 Professor Staw believes that the United States long involvement in Vietnam was due to escalation behavior. The investment in the war produced negative results for which two presidents felt a need to rationalize with additional investments of manpower and other resources. Professor Staw uses the following passage from a memo from Undersecretary of State George Ball to President Johnson early in the conflict to underscore his point:

Once large numbers of U.S. troops are committed to direct combat, they will begin to take heavy casualties in a war they are ill-equipped to fight in a non-cooperative if not downright hostile countryside. Once we suffer large casualties, we will have started a well-nigh irreversible process. Our involvement will be so great that we cannot -- without national humiliation -- stop short of achieving our complete objectives. Of the two possibilities, I think humiliation would be more likely than the achievement of our objectives -- even after we have paid terrible costs.

Staw, supra note 8, at 29.
ous investments were a waste, in essence, a poor choice. Therefore, the individual must admit that he made a bad decision. It is often easier to invest more in hope of validating the previous decision than to admit failure. Hence, when on hold or waiting for a bus, the individual may choose to wait a little longer rather than admit that he made an incorrect decision. Unfortunately, the longer he waits, the harder it is to admit that the time was wasted. We tend to feel even more foolish for investing even more time in the fruitless activity. Thus, we become even further entrapped with each additional investment of resources.

Researchers generally agree that an important contributor to escalating commitment is self-justification. When an individual (or group) has invested significant resources in an endeavor, it is difficult for that decision-maker to admit that the course of action was in vain and should not be continued. In order to justify or validate the correctness of the action, the decision-maker continues on the course, investing even more resources in the (often) futile enterprise. The insidious trap grows with each additional investment because the growing investment requires even greater justification. Often, even if the decision-maker achieves the desired outcome, the cost of achieving the goal exceeds the costs of alternative actions. Thus, a traveler will find that if he waits long enough for a bus to come, it will in fact arrive. However, walking instead of waiting would have gotten him to his destination in a shorter time.

Contingent fee attorneys are subject to escalating commitment. The attorney faces a multitude of decision nodes that provide him with an opportunity to stop investing in the case. Initially, he can refuse to take the case, or after taking the case he can pursue an early settlement. If these negotiations fail, the attorney can drop the case with his client’s consent or attempt to settle pre-trial. Each time the case progresses past a decision node, the attorney’s investment in time, labor and money mount. As expenditures mount, the litigator’s decision to terminate the case becomes increasingly difficult. Prior investments make it increasingly difficult for the attorney to accept a settlement that was available at a prior decision node when total investments were lower. Accepting the settlement becomes a tacit admission that the intervening investments were wasted. Thus, the attorney may find it cognitively easier to hold out for a better outcome rather than admit the stupidity of his prior decision to continue. The entrapped attorney becomes the addicted gambler.

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78 Other explanations include prospect theory, under which behavior depends on how a decision is framed, see Daniel Kahneman and Amos Tversky, Prospect Theory: An Analysis of Decisions Under Risk, 47 ECONOMETRICA 263 (1979), and decision dilemma theory, under which escalation occurs because decision-makers have not received truly negative feedback about their choices see M. G. Bowen, The Escalation Phenomenon Reconsidered: Decision Dilemmas or Decision Errors, 12 ACAD. MGMT. REV. 12 (1987). Professor Brockner considers these alternative theories and finds flaws in their arguments. See Brockner, supra note 8, at 50-53.

79 Settlement becomes hard but not impossible. Sometimes an approaching trial, a judge’s threat or the removal of an active combatant act as a catalyst to break a statement. Such actions allow parties to settle or end hostilities while saving face. See, e.g., Will McDonough, Finally, NFL makes a deal, BOSTON GLOBE, January 7, 1993, (Sports), at 37 (describing how judge’s threat facilitated settlement over free-agency based
who after blowing half of his life savings at the blackjack table, continues to play because winning a jackpot is the only way to prove that his prior actions were wise rather than a blunder. Similarly the litigator refuses to settle because winning or obtaining a substantially larger settlement is the only way to avoid admitting that his prior decisions were unwise. Hence, with the passage of time, the ability of an attorney to terminate litigation is countered by a growing pile of investments that he psychologically has to justify.

C. Escalation Explanations

Researchers have identified several factors that influence a decision-maker's susceptibility to escalating commitment. These factors include the use of models, the nature of the opponent, and face saving.\textsuperscript{80} A decision-maker is often uncertain about whether it is better to cut his losses immediately or persist with the hope of achieving his goal. When faced with this dilemma, for guidance, a decision-maker sometimes looks at how others have handled similar problems. For example, in deciding on whether to continue repairing an old car, a consumer may rely heavily on whether a friend or neighbor with a similar car continues to repair his vehicle.\textsuperscript{81} Or a company with a product line that loses money may continue to market the product line if it observes its competitor marketing a similar product line. The company may be unwilling to terminate the product line while a competitor continues marketing their line. If the competing company eventually turns its struggling product line into a profitable one, the company that terminated its line prematurely may be unable to justify its prior decision. Alternatively, if the competitor terminates its product line, the decision to terminate for the company facing the dilemma is easier. Hence, decision-makers may become more entrapped when their models are also entrapped.\textsuperscript{82}

Opponent characteristics also influence an individual's susceptibility to escalating commitment. A decision-maker is more inclined to compete against an opponent who escalates a conflict or an opponent who the decision-maker perceives to be dissimilar. In Professor Teger's studies conducted during the 1970s, a salient measure of difference was how a student ranked on the "freak-jock" dimen-

\textsuperscript{80} See Brockner & Rubin, supra note 8, at 101.

\textsuperscript{81} See id. at 75.

\textsuperscript{82} See id.
sion. Students with long-hair, and faded jeans were stereotypically associated with the drug culture of the time. By contrast, conservatively dressed students with short hair were stereotypically associated with the jock group because athletes of that era generally conformed to that style of dress. Teger found that freaks and jocks escalated their commitment to a greater extent when their opponents had appearances that conformed to the stereotype for the other end of the spectrum.

Face saving, in particular, can escalate a decision-maker's need to justify his actions. Many sociologists believe that most social behavior is motivated by the desire to look good in the eyes of those whose opinion we respect and hold in high regard. This drive to look good or maintain face is evident in escalation situations. A decision-maker's need to justify his actions is heightened when others are observing his behavior. Individuals are extremely concerned about being embarrassed or humiliated in public and will often go to great lengths to retaliate for a slight.

One of the most tragic examples of this face saving phenomenon was the U.S. involvement in Indochina. Commentators believe that during the Vietnam War era the need to avoid the humiliation and embarrassment of admitting that U.S. involvement in Vietnam was a mistake was so great that it drove U.S. foreign policy to continue in the war. At the time, U.S. leadership was concerned both with admitting a mistake to the rest of the world and to a U.S. populace that was sharply divided between supporting and opposing the war. Admitting that the war was a mistake would validate the beliefs of antiwar activists and would disenchant supporters of the war. The humiliation of giving in to the opposition and letting down supporters may have been such a distasteful alternative that none of the three presiding U.S. presidents were willing to end U.S. military operations in Indochina.

There are examples of face-saving-fed escalations that have dynamics closely related to the behavioral dynamics in high-stakes litigation. Brockner and Rubin provide an example of a labor dispute in which the respective leaders of the two sides felt pressured by their constituencies to press for yet greater concessions the longer the strike lasted. As losses mounted on both sides, leaders of each side increasingly believed that they had to produce a concrete gain in order to justify their constituencies' sacrifices. The Texaco and Pennzoil settlement negotiation provides an additional example. After losing the biggest court judgment ever in the

83 See Teger, supra note 69, at 79.
84 See id.
86 See Brown, supra note 67.
87 See supra note 77.
88 See Brockner & Rubin, supra note 8, at 102.
89 Id.
U.S., the Texaco board had tremendous difficulty settling the case. Settling the case at the time would have been a tacit admission to stockholders that the board had erred in failing to settle the case prior to trial. The board settled only after seeking Chapter 11 protection and being pressured by a shareholder committee. Both of these illustrations exemplify contentious adversarial disputes. In each case the stakes were high, and interactions occurred in the spotlight of public and constituency attention. These same characteristics are often present in high-stakes litigation as well.

D. Critical or Evaluative Scrutiny and Escalating Commitment

Laboratory research has shown that performance under scrutiny can exacerbate escalating commitment. By manipulating the number of observers, the accountability, and support for the decision-maker, researchers have gained a significant understanding of this dynamic. In general the number of observers has little effect. Instead a key variable is whether observers are in evaluative positions. In a study examining these issues, researchers manipulated the number of individuals observing subject behavior. Under one condition the experimenter was the sole observer. Under an alternative condition, the experimenter informed subjects that two graduate students with an interest in the research study would observe their actions. These graduate students would attend the sessions under this condition and would be visible but would have no other role in the study. The researchers found that subjects did not alter their decisions significantly when observers were present. Their result supports the proposition that mere observation without judgment power has limited effect on escalating commitment.

Other research has defined the connection more precisely. Fox and Staw employed a different methodology to investigate the role of scrutiny on escalating commitment. Instead of using actual observers, the researchers created a scenario under which the degree of scrutiny varied. Specifically, the experimenter informed

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91 One report suggested that the Texaco board believed that it would be liable whether or not it settled with Penzoil. Therefore, with nothing to lose, the board opted to pursue an appeal of the judgment, which would have absolved the board of liability and blame. See Matthew L. Wald, Clause in Texaco Pact Is Questioned, N.Y. TIMES, March 1, 1988, at D2.

92 Jim Kinneir is Pumping New Life Into Texaco, BUSINESS WEEK, April 17, 1989 at 50.

93 See BROCKNER & RUBIN, supra note 8, at 104-105.

94 A condition in a control experiment is a situation in which the experimenter holds the relevant variables constant. The experiment consists of multiple conditions. The experimenter allows one key variable to change between conditions. Thus, by comparing the results from multiple conditions in which a single variable changes, the experimenter can identify the effect of that variable.

95 See BROCKNER & RUBIN, supra note 8, at 104-105.

96 See Fox & Staw, supra note 74.
each subject that he was an administrator in a company who had just been appointed to the position of vice president of finance. The subject then made a decision about which of two company divisions to give $10 million in funding. The subjects justified their decision in writing and then received written feedback about the decision.

Behavior varied based on the degree of security and support the subject enjoyed. In what the researchers described as the high insecurity condition, instructions informed each subject that his appointment was temporary and that his continuation in the vice president slot depended on the success of his recommendation. Moreover, he enjoyed little support from envious peers who would enjoy seeing him fail. Alternatively, instructions in the low insecurity condition informed the subject that his appointment was permanent and independent of his current decision. The instructions informed the subject that he enjoyed strong support from his peers and that the support would remain strong even if his recommendation fared poorly. Hence, the subject had far more to lose under the high insecurity condition. The researchers found that there was a close connection between highly scrutinized performance and reward in this condition. The connection was far more attenuated in the low insecurity condition. As expected, subjects escalated their investments to a significantly greater extent in the high insecurity condition. The presence of evaluative and highly critical scrutiny contributed far more to escalating commitment than a less threatening, less critical environment.

Litigation, especially high-stakes litigation, shares many of the characteristics that researchers identify as contributing to escalating commitment. Litigation is highly competitive. However, competition alone is not always sufficient to induce face-saving behavior. In addition to being highly competitive, high-stakes cases levy a high degree of evaluative scrutiny on participating attorneys. Evaluative scrutiny is likely to come from sophisticated clients, media coverage, peers, or some combination of the three. The attorney’s role is likely to resemble Fox and

97 Fox and Staw also tested a resistance condition in which they manipulated the board of director’s support for the subject’s funding decision. Under the high resistance condition, the board is very critical of the subject’s decision and reluctantly defers to the subject’s choice. In the alternative, low resistance condition, the board views the decision very favorably and tends the subject high support. Hence, under the high resistance condition the subject is all alone in his decision. If the recommendation fails, it is all his fault and only he loses face. In the low resistance condition the board’s support ameliorates the sting of failure. Therefore, if the project fails the subject’s loss of face is not as great because he has the board’s support. Thus, theoretically, because the loss of face is greatest under the high resistance condition, subjects should exhibit greater escalation behavior under this condition than under the low resistance condition. Fox and Staw’s results support this hypothesis. See id. at 454.

98 See id. at 462-463.

99 If a large corporation is involved in a significantly litigated matter, it usually employs in-house counsel to monitor the efforts of its trial counsel. See supra note 61 (discussing the ability of in-house counsel to effectively monitor outside trial counsel). Media scrutiny and the use of attorney commentators has generated much concern over the impact of the media on litigation. See, e.g., Proposal to Ban Cameras and Pre-Trial Stage, S.F. CHRONICLE, February 24, 1996, at C1 (covering a California government response to the belief that televised media coverage influences the behavior of trial participants); James E. Lukaszewski, The
Staw's high insecurity condition. Whereas the client may be supportive, especially if there is a continuing relationship, it is unlikely that the attorney or his law firm will devote their entire practice to a single client. Therefore, the attorney in a high-visibility, high-stakes cases is in a constant high insecurity state because future business and employment depends on how well others evaluate his performance in each case. If evaluators rate the attorney's performance high, then the attorney is likely to be considered for future high-stakes cases. If, however, evaluators rate the attorney’s performance poor, then the attorney is unlikely to be considered for other high-stakes cases.\(^{100}\) Hence, the attorney’s continued livelihood, in terms of prestige and income level, is likely to depend on how others evaluate his performance.\(^{101}\)

Adding to the escalation pressure in high-stakes cases is the objectivity of evaluators. Fox and Staw call this measure resistance. The variable measures the degree of support that evaluators have for the attorney’s decision choices.\(^{102}\) If evaluators support the decision as proper and wise, the attorney feels less pressure to prove the correctness of his choice. If evaluators instead have misgivings or second-guess the attorney’s decision, then the attorney feels pressure to save face by proving his detractors wrong. The client in low-to-moderate stakes cases may not provide resistance to the attorney’s decision. If the attorney has a continuing and successful relationship with his client, the client may defer to the attorney’s judgment. Even in the absence of a relationship, the expertise imbalance may leave an unsophisticated client with little choice but to accept the attorney’s decisions with

\(^{100}\) An attorney’s poor reputation almost guarantees that he will have substantial trouble maintaining a viable practice. See, e.g., Frank B. Cross, The Role of Lawyers in Positive Theories of Doctrinal Evolution, 45 EMORY L.J. 523, 533 n.34 (1996) (noting that a lawyer with a good reputation is more successful than a lawyer without a good reputation); Eduardo J. Benitez et al., Telecommunication Reforms in the Americas: New Legislation and the Regulatory Framework, 13 AM. U. INT’L L. REV. 971, 984 (1998) (“[T]he reputation of being a deal killer, you will never work again”). In addition, it is important for the attorney to maintain an excellent reputation with the bench especially if he appears before a court on an ongoing basis. For example:

[If bankruptcy cases the reputation of an attorney, especially an attorney who regularly represents Debtors, is perhaps the most valuable asset that the lawyer owns. If a court believes that an attorney has failed to act properly in regard to his fiduciary duties as Estate Counsel, that belief will make the attorney's future bankruptcy practice that much more difficult.


\(^{101}\) See Miller, supra note 17, at 210.

\(^{102}\) See supra note 95.
little evaluative feedback.\textsuperscript{103}

The attorney's peers and the media are likely to be less accepting of suspect legal decisions. Peers with significant legal knowledge are likely to be far less forgiving in evaluating the attorney's choices. Viewed from the vantage of "what I would do" in the situation, peer attorneys are likely to be quite critical of any perceived miscues. This criticism is likely to be amplified in the press as legal reporters and consultants second guess attorney decisions. As the stakes and public interest in the case increase, the evaluative pressure is likely to increase as well.\textsuperscript{104} Hence, the level of escalation-induced work should be substantially greater in highly scrutinized high-stakes cases.

IV. EMPIRICAL SUPPORT

As a preliminary test of the theory, I designed and conducted a computer-based laboratory experiment using student subjects. The objective of the experiment was to find out whether the presence of scrutiny induces subjects to increase their investments in simulated lawsuits. I first discuss the use of experimental methods in law and economics research. It is particularly efficacious in situations such as this, where the investigated phenomena is independent of the subjects' legal knowledge.

A. Use of Experimental Methods in Law and Social Science Research

The use of experiments to illuminate litigant decision-making, although not yet commonplace, is not unprecedented. Coursey and Stanley used experimental methods to examine the impact of cost-shifting rules on settlement decisions.\textsuperscript{105} In a subsequent study Stanley and Coursey used a controlled experiment to examine certain characteristics of Priest and Klein's selection hypothesis.\textsuperscript{106} This hypothesis posits that trial cases are disproportionately chosen from cases in which the two sides have strongly divergent beliefs about the probable outcome of trial. One implication of this hypothesis is that when the two sides are extremely well prepared, the only cases that go to trial are ones in which the plaintiff has a .5 probability of winning (the 50 percent rule).\textsuperscript{107} I also contributed to the trial selection

\textsuperscript{103} See supra note 53 and accompanying text.

\textsuperscript{104} See supra notes 97-98.


\textsuperscript{107} See Priest & Klein, supra note 47. The selection hypothesis is often, incorrectly, considered to be synonymous with the 50% rule. I argued, however, that the selection hypothesis has significant explanatory power independent of the .5 implication. See Robert E. Thomas, The Trial Selection Hypothesis Without the
Microeconomists have recognized the value of experimental studies to augment traditional economic research. The experimental law and economics studies described above draw on the pioneering efforts of economists Charlie Plott, Vernon Smith and others. These researchers have found that carefully controlled experimental studies provide insights that are not available using traditional empirical techniques. The two areas where experimental work is especially efficacious are situations for which there are 1) lots of highly correlated information, or 2) missing or unobtainable variables. In litigation both situations are present. It is impossible to determine what an attorney would have done had his work been highly scrutinized, or if the stakes were different. Often settlement rates and amounts are essential variables required to understand the observed phenomenon. However, settlement information is rarely available. Moreover, the effects of such factors may be obscured by the nature of the case. An attorney may work harder if he believes the case has groundbreaking implications or if he has a positive relationship with his client. Thus, identifying the effects of scrutiny and case value (the stakes) is virtually impossible using data from actual cases. The use of controlled experiments allows researchers to isolate the effects of investigated variables from the effects of other variables.

In the physical sciences and medicine, researchers are often interested in how outcomes change when initial conditions are altered. These different conditions can include giving patients different dosages of a pharmaceutical product, or comparing the behaviors of sleep-deprived subjects with the behaviors of subjects with normal sleep patterns. Under such carefully controlled settings, differences in health or behavior across test groups can be reliably attributed to the effect of an investigated variable. In empirical studies that rely on non-experimental data sources, it is rarely possible to obtain data that cleanly isolates investigated variables. Sometimes desired conditions do not exist or it may be illegal to produce such conditions. Therefore, in order to obtain a valid understanding of different

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108 See Thomas, supra note 107.


110 See Stanley & Coursey, supra note 106, at 146.

111 Studies of cost-shifting rules are difficult to conduct because the English rule is rarely employed in the United States. Even when the English rule has been used, judges often tainted it by refusing to enforce it in its pure state. See Edward A. Snyder & James W. Hughes, The English Rule for Allocating Legal Costs: Evidence Confronts Theory, 6 J. L. ECON. & ORG. 345 (1990). The effect of attorney ownership of cases also cannot be observed through secondary sources due to prohibitions against, "(1) rules against alienation of choses in action, (2) rules against maintenance or champerty, or (3) state disciplinary provisions against acquisition by attorneys of a financial interest in litigation." Miller, supra note 17, at 197 (footnotes omitted).
conditions, or in our case, the behavioral effects of different fee arrangements, experimental methods provide the only real option. The research question considered here is particularly amenable to analysis using experimental methods. In order to measure the impact of critical scrutiny, it is necessary to compare attorney decisions under scrutiny with attorney decisions made in the absence of scrutiny. While such comparisons are virtually impossible in practice, researchers can easily make such comparisons in the laboratory.

B. Issues With Experimental Research

Experimental methods, however, are imperfect and subject to criticism. Two of the most common criticisms of experimental methods are artificiality and nongeneralizability.\textsuperscript{112} The artificiality criticism amounts to a complaint that the experiment lacks realism. To address this criticism, one must first understand that there are multiple types of realism. Aronson and Carlsmith suggest that experiments have both experimental and mundane realism.\textsuperscript{113} An experiment is realistic in the former sense if subjects “buy into” the design, take it seriously, and react to the provided stimuli. An experiment exhibits mundane realism if the experiment closely resembles the environment it models in the real world.\textsuperscript{114} Often the artificiality criticism amounts to a criticism that the experiment lacks mundane realism. Yet Aronson and his colleagues argue that an experiment that is low in mundane realism may still be valid provided it is high in experimental realism.\textsuperscript{115} By contrast an experiment that is high in mundane realism may be low in experimental realism if the experiment is boring, does not hold subjects’ interests, or does not provide an adequate stimulus.\textsuperscript{116} Hence, a low level or absence of mundane realism is not necessarily a fatal flaw.

The lack of generalizability criticism often focuses on the use of college students as subjects and low payoffs that subjects receive. There is a question about whether college students’ decisions correspond closely to decisions that an experienced litigator would make in corresponding situations. In support of using college students, the phenomena examined here do not depend on legal knowledge or ability. Most people are subject to escalating commitment. Moreover, the tendency to

\textsuperscript{112} See Elliot Aronson et. al., Methods of Research in Social Psychology 70-82 (2d ed. 1990).

\textsuperscript{113} See id. at 70.

\textsuperscript{114} See id.

\textsuperscript{115} See id. at 72.

\textsuperscript{116} Professor Aronson and his colleagues raise the example of an experiment that had college students read newspaper headlines about a candidate running for public office in a distant city and then provide their reaction to the candidate. Although this experiment rated high in mundane realism, it was low in experimental realism because few college students are profoundly affected by reading about political candidates in a distant city. Although this experiment rated high in the mundane realism dimension, it was extremely low in the experimental realism dimension. Not surprisingly, the data obtained were uninteresting. See id at 71.
be ensnarled by such psychological pitfalls appears to be independent of experience or the number of times the individual has previously fallen for the pitfall. 117

A recent study supports the conclusion that experience does not help lawyers avoid psychological factors that diminish their litigation effectiveness. In the study a group of students and a group of experienced litigators participated in a controlled experiment. 118 One of the study's objectives was to determine whether expected utility or prospect theory 119 from psychology is the better predictor of subject decision choices in a given case. Researchers randomly assigned subjects to the roles of either plaintiff's or defendant's attorney in a personal injury case. Each subject received an outline of case details and 100 jury decisions from similar cases. 120 Students in plaintiffs' attorneys roles as well as students and attorneys in defendants' attorneys roles gave unbiased estimates of the outcome. However, attorneys in plaintiff roles were overconfident in their appraisals suggesting that experience may make people more prone to the psychological bias of overconfidence. 121 But of greater interest to this study, the researchers found that subjects' decisions, whether by attorneys or students, were consistent with the predictions of prospect theory. Subjects in plaintiff roles exhibited risk aversion whereas subjects in defendant roles were risk-seeking. 122 Both legally astute and inexperienced subjects failed to realize that their decisions were biased by the positions in which they were arbitrarily placed. The experiment shows, provided that a well-designed study does not draw on subjects' legal knowledge, there is unlikely to be significant differences between students' and litigators' decisions.

Experience or training does not imply excellence even in matters that are highly related to one's field. In a test of learning effects, a researcher evaluated experienced psychologists' abilities to evaluate the Bender Gestalt test for brain damage in patients. 123 The Bender Gestalt test requires a patient to duplicate draw-

117 Learning from experience requires accurate and immediate feedback. See Max H. BAZERMAN & MARGARET A. NEALE, NEGOTIATING RATIONALLY 109 (1992). Professors Tversky and Kahneman suggest that 1) the separation between outcome and causative action is often too attenuated to make an accurate attribution, 2) environmental variation degrades the reliability of feedback, 3) it is usually impossible to project the outcomes of alternative actions, and 4) the uniqueness of most decisions provides little opportunity for learning. Unless all these problems are avoided, Tversky and Kahneman argue, there is little chance that an actor will avoid repeating the error. See Amos Tversky & Daniel Kahneman, Rational Choice and the Framing of Decisions, 59 J. Bus. 251, 274 (1986).


119 Prospect theory posits that a decision-makers risk attitude varies depending on whether he faces a gain or a loss. Actors facing gains are likely to be risk-averse, whereas actors facing losses are apt to be risk-seeking. See Kahneman & Tversky, supra note 78.

120 See Babcock et al., supra note 118, at 292.

121 See id. at 294-295.

122 See id. at 300.

123 Lewis R. Goldberg, The Effectiveness of Clinicians' Judgments: The Diagnostic of Organic Brain
ings of various overlapping shapes on a piece of paper. The absence of drawing segments, overlaps, and other imperfections in the drawing provide conclusive evidence of brain damage. However, interpreting the results can be quite difficult. The study measured the accuracy of experienced psychologists’ evaluations relative to a group of trainees, and the secretaries of the experienced psychologists. The accuracy rates ranged from 65 percent for the experienced psychologists to 70 percent for their secretaries. These results contrast with the accuracy of a purported expert in using the Bender Gestalt test who achieved an accuracy rating of 83 percent. The dilemma is that it is hard to avoid a problem that one does not know exists. Despite many years of experience, the psychologists’ failure to review consciously and objectively the results of their evaluations resulted in skills that were indistinguishable from neophytes in their field.

The low payoff criticism is related to experimental realism. If the payoff incentive is inadequate, then subjects do not take their assigned tasks seriously. Others reject this criticism on the assumption that the experiment will succeed provided subjects prefer more to less money. The amounts used in my experiment, $7-$64, were large enough to pay for lunch or sometimes dinner at a nice restaurant. Hence, the subjects actually had a significant incentive to perform well. In addition to this argument, the different conditions or fee arrangements provide a self-check for the effectiveness of the experimental payoff structure. If the potential rewards are insufficient, then subject behavior should not differ between conditions with different payoff structures. Thus, differences in decision making between conditions provide support for the adequacy of the payoff structure.

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Damage From the Bender Gestalt Test, 23 J. CONSULTING PSYCHOL. 25 (1959), discussed in J. EDWARD RUSSO & PAUL J. SCHOEBAKER, DECISION TRAPS 175 (1989).

124 The experienced psychologists had many years of experience with the test, the trainees averaged three years, and the secretaries had no training in interpreting test results. See supra note 123.

125 See id.

126 See id. at 176.

127 See Vernor L. Smith, Experimental Economics: Induced Value Theory, 66 AM. ECON. REV. 274, 275 (1976). As one researcher stated, “subjects prefer more money to less money in the same way that people prefer more to less in naturally occurring economic situations -- not always, but to an overwhelming degree and in certain regular, predictable ways. This is enough to make experimental data useful....” Elizabeth Hoffman & Matthew L. Spitzer, Experimental Law and Economics: An Introduction, 85 COLUM. L. REV. 991, 992 n.4 (1985).

128 In the experiment I conducted, the two highest paid subjects received $50.80 and $64.80. Average and median payments for the experiment were respectively $11.59 and $9.00. For a description of the payment methodology see infra discussion accompanying note 147.
C. Design of the Experiment

1. Overview

The experiment presented each subject with the sometimes conflicting twin objectives of representing a (fictional) client and maximizing the subject’s monetary compensation. Both male and female college students participated in a series of simulated computer-based lawsuits. In each session, subjects were involved in five simulated lawsuits. In each lawsuit, a certain amount of money, ranging from $7 to $90 was at stake. The “laboratory” was a computer room containing over twenty networked computers. Five to fifteen subjects participated during each session. A “master” computer, run by the experimenter, controlled each of the subject’s computers. As a result the experimenter had the ability to monitor every action that each subject took.

Each subject played the role of plaintiff’s attorney against a computer. All subjects received a $20 endowment to use for each simulated lawsuit. Subjects prepared for trial by purchasing units of evidence at $0.10 or $0.20 per unit. Each time a subject purchased evidence, the subject’s computer deducted the cost of that purchase from either the subject’s endowment or his client’s endowment. There were two types of evidence. P evidence favored plaintiffs and D evidence favored defendants. For each simulated case, there were 115 units of evidence. The experimenter determined the composition of the 115 units before the start of each simulation. For example, the experimenter might select seventy P units and forty-five D units for a case that favored the plaintiff, and fifty-seven P units and fifty-eight D units for a close case that favored the defendant.

The act of purchasing units was the proxy for case preparation. Subjects learned about the composition of evidence by purchasing evidence units. I equated purchasing units to the subject’s willingness to invest in the case. Subjects could purchase up to five units at a time by selecting the desired number on their computer screen.\(^\text{129}\) The computer then randomly chose the designated number of units from the unpurchased evidence and revealed the evidence to the subject. For example, suppose the subject purchased five evidence units by selecting the number five. The computer randomly selected five units from the set of unrevealed evidence units. The purchased units could contain from zero to five P units. Suppose the five units consisted of four P and one D units. The computer then revealed this information to the subject, the subject’s total collected evidence increased by four P and one D units, respectively, and the subject’s endowment decreased by one dollar. Hence, if prior to this selection the subject had purchased fourteen P and ten D

\(^{129}\) The cost of random purchases was $0.10 per unit. The subject could also purchase “biased” selections at a price of $0.20 per unit. These purchases purportedly were more likely than random purchases to select P units of evidence. The purpose of the $0.20 option was to give subjects the ability to exert greater effort as well as to continue purchasing evidence in cases that favored the defendant. In cases in which most of the 115 units were of type D, random purchases were highly likely to be overwhelmingly populated with D units as well. Therefore, the biased selection provided an incentive to continue working in losing cases.
units, after the selection the subject’s computer screen would indicate that he had collected a total of eighteen P and eleven D units. After this purchase, there would be 86 unrevealed units of evidence remaining. During each simulation, the subject could purchase at most 100 units at up to five units a time using this process. The experiment reserved the remaining fifteen units of evidence (“reserved evidence”) to help determine the case outcome.

The computer awarded cases that did not settle to the party with the most collected and reserved evidence favoring its side. For example, if the subject collected twenty-two P and eighteen D units, and there were seven P and eight D units of reserved evidence, the plaintiff won the case twenty-nine to twenty-six. If, however, there were ten or more D units of evidence reserved, then the subject lost the case because the twenty-eight or more D units exceeded the at most twenty-seven P units. The sixty unrevealed units of evidence did not factor in the case outcome. Hence, subjects could influence the outcome of the case. If the plaintiff purchased too little evidence, he would lose the case if the reserved evidence favored the defendant. However, if the subject purchased a large number of evidence units, and most of his purchased evidence were P units, reserved evidence had little effect on the outcome. Thus, subjects had an incentive to maximize the difference between P and D evidence they purchased.

In addition to purchasing evidence, subjects could make a settlement request or end the case by going to trial. Subjects indicated a desire to settle by pressing a screen button and entering a settlement demand. The computer accepted this amount if it did not exceed the original ratio of P units to total units of evidence times the amount at stake. Hence, if $60 was at stake and fifty-eight of the 115 units were of type P, the computer rejected settlements demands that exceeded $30. Therefore, a subject’s unwillingness to make a sufficiently low settlement demand to end the case could indicate high confidence or possibly escalated commitment. If the computer rejected a settlement demand, the subject could make a subsequent demand after purchasing at least one additional unit of evidence. The subject could make as many or as few settlement demands as he desired. This process continued until 1) the computer accepted the subject’s settlement demand, 2) the computer decided the case at trial (at the subject’s request), or 3) after the lapse of seven minutes. To encourage settlement, the simulation charged either the subject or client a five-dollar “trial tax” if the case ended at trial. This tax also served as a proxy for the additional costs of trial. Each session lasted approximately ninety minutes and time was not a constraint. Thus, spending more money purchasing more

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130 Subjects indicated a desire to end a simulation by pressing a screen button. To avoid mistakes, the computer requested two verifications of the trial request before ending a simulated case.

131 Time was only a factor during the first simulation in each session. Subjects quickly became familiar with the workings of the simulation. By the fifth dispute, the dispute used for data analysis, most subjects were completing the dispute in five minutes or less. Two subjects, all in the hourly fee group, used seven minutes in the fifth case of the simulation. I excluded data obtained for these two subjects. Including the data as either settled or trial cases would not alter the statistical inferences drawn from the study.
evidence than other subjects was a sign of escalated commitment.

Subject compensation depended on subject decisions and case characteristics. Each session consisted of five simulated lawsuits. The purpose of running five simulations per session was to allow each subject to become thoroughly familiar with the simulation software. The simulations varied from cases that strongly favored the plaintiff to cases that strongly favored the defendant. The final simulation in each session consisted of cases that were even, favoring neither side. I used data only from the fifth simulation in each session. I chose these disputes since even cases are thought to be the most contentious with the highest probability of ending in trial.\footnote{Attorneys in cases that clearly favor one side are less likely to become entrapped because the futility of continuing is hard to deny. When the case is even (.5 probability of winning), the attorney may be able to convince himself that fighting rather than settling is the best alternative. \textit{See} Priest \& Klein, supra note 47. \textit{But see} Wittman, supra note 47; Donald Wittman, \textit{Dispute Resolution, Bargaining and the Selection of Cases for Trial: A Study of the Generation of Biased and Unbiased Data,} 17 J. LEGAL STUD. 313 (1988).} The subject's return for each lawsuit equalled the remainder of his endowment plus the subject's share of the case award. Although each subject received a return for each lawsuit, they received pay for just one lawsuit chosen at random from the final four simulations in each session.

Dimensions that varied between sessions included the fee arrangement and the amount at stake. Each subject faced a single fee arrangement-stakes combination. Tested fee arrangements included hourly, contingent, and an interests-aligned fee arrangement. Under the hourly fee arrangement, each subject's return increased with the subject's purchases. Hence, if the subject purchased twenty units of evidence at $0.10 per unit, his endowment increased by two dollars. This return was independent of the case outcome. If the case went to trial, the subject's return increased by $5 due to the trial tax. The objective of this compensation scheme was to model the relationship between hourly fee attorney effort and compensation. Hence, hourly fee subjects' compensation increased with expenditures. The greater the effort put into a case the greater the compensation.

In the contingent fee and interests-aligned groups, subjects' endowments decreased with effort expenditures. The same twenty-unit purchase in these cases reduced the subject's return by two dollars. The return for subjects in contingent fee simulations equalled the remainder of the subject's endowment plus one-third of 1) the court award (the stakes if victorious and zero otherwise) or 2) the settlement amount. In either event, the subject was responsible for paying all costs out of his $20 endowment including, when applicable, the $5 trial tax. Therefore, if the subject spent $7 purchasing evidence and went to trial thereby incurring the $5 trial tax, the simulation subtracted $12 from his endowment. The interests-aligned group differed from the contingent fee groups in that the subject received 100 percent of the court award or settlement. In effect, the interests-aligned subject was both attorney and plaintiff simultaneous. This group provided the baseline comparison for the other groups.
2. Experimental Procedure

The subject pool consisted of 342 male and female undergraduate students from a major research university in the southeastern United States. Subjects were recruited from a large undergraduate, introductory business-management course. Subjects represented a variety of college majors, and were randomly assigned to each of the experimental conditions. The compensation method was critical to the objectives of the experiment. However, in order to elicit adequate participation, it was also necessary to offer subjects extra course credit equal to two points out of 150 available points. The experiment consisted of multiple sessions using five to fifteen subjects per session. Each subject was assigned an individual computer terminal. Subjects participated in one session only. At the beginning of each session, the experiment administrator gave subjects ample time to read the written instructions. The administrator then read the instructions out loud and responded to questions. Prior to beginning the simulations, the administrator ran a tutorial that covered simulation procedure. During this scripted tutorial, the administrator walked the subjects through a simulated lawsuit. A subject’s final pay was based on the subject’s return from one of the last four simulations in a session.

3. Differences Between Conditions and Implementation of Scrutiny

The experiment included two contingent fee conditions and an hourly fee condition. Furthermore, the experiment employed scrutiny with the hourly fee condition and one of the two contingent fee conditions (“CFS”), whereas no scrutiny was applied to the second contingent fee condition (“CF”). Under hourly fee and contingent fee conditions, the instructions informed subjects that they were attorneys representing a client. Hourly fee subjects received the amount they spent plus their endowments as compensation.

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133 In addition, I used forty-seven students in a pilot study to test aspects of the experimental design including the clarity of instructions, the cost functions, and the appropriate stakes. None of the forty-seven students participated in the final experiment.

134 See supra text accompanying notes 125-126.

135 In a previous study conducted by the author, volunteer rates were much lower without the extra credit inducement. Despite the ineffectiveness of money as a method for attracting student volunteers, the possibility of winning money did provide the desired incentives once students agreed to participate.

136 Written instructions and experiment software are on file with the author.

137 The subject’s pay equaled one-third of his or her return selected at random from one of the last four cases (the “counted return”). To enhance subject incentives, one to three randomly chosen subjects, referred to as lottery winners, per session received undiscounted payments for their counted return. For example, if a subject’s counted return was $28, he received a check for $9.33. However, if that subject was a lottery winner, he received a check for $28. The experiment guaranteed subjects a minimum payment of $7. Earnings before applying the minimum payment ranged from less than $3 to over $60. These earnings averaged $11.60.
The experiment used a multi-step process to implement scrutiny. The experiment employed deception in conditions without scrutiny to convince subjects that no one was observing their actions.\(^{138}\) Instructions informed subjects that decisions were entirely their own.\(^{139}\) The CF instructions directed subjects to act in their client's best interests and also falsely informed subjects that their decisions were invisible to the experiment administrator and could not be traced. In addition, the instructions continued that the simulation retained only enough information for the experiment administrator to calculate their pay. After starting each of the final four simulated lawsuits, the experiment administrator left the computer terminal used to administer the experiment and sat at an adjoining table that clearly did not have a sightline to either the control terminal or any of the subject terminals. During each simulation, the administrator pretended to read a book or write in a notebook, being careful not to look at any subjects. At the conclusion of the allotted time for each simulation, the administrator returned to the control terminal and began the next simulation. Thus, experiment procedures encouraged subjects in these conditions to believe that their actions were entirely free of scrutiny.

In conditions with evaluative scrutiny, experiment procedure encouraged subjects to believe that their actions were under scrutiny. In these two conditions, the instructions directed subjects to act in the best interest of their clients in accordance with their agency roles as attorneys. To reinforce this directive, a blinking message appeared periodically on each subject's computer screen reminding the subject to act in his client's best interests. The experiment administrator informed each subject that he controlled the experiment from his computer terminal. Although the administrator did not inform subjects that he could observe their actions from his terminal, the administrator's careful focus on his screen during each simulation suggested that he was in fact observing their choices. The administrator's behavior together with the blinking messages were intended to give subjects the impression that their actions were observed.\(^{140}\)

\(^{138}\) Based on the literature, implementing scrutiny is far easier than creating an unscrutinized treatment due to the existence of the administrator bias. See infra note 139. Therefore, it was necessary to take far more elaborate steps to create the perception of an observation-free environment in the unscrutinized treatments.

\(^{139}\) Studies have shown that subjects are concerned with and influenced by their perception of the experimenter's opinion of them. See, e.g., ARONSON ET AL., supra note 112, at 304-305 (rats as well as human performance varied with the experimenter's perception of the subject); BROCKNER & RUBIN, supra note 8, at 104 (pleasing the experiment administrator is a driving psychological force in subjects). Therefore, the experimental design focus on creating the appearance in the unscrutinized treatments that the experiment administrator was not concerned with or paying attention to subject decisions.

\(^{140}\) Other studies have used a variety of methods to implement evaluative scrutiny. One study had several graduate students present during sessions as observers. Subject decisions appeared to be independent of these observers. See BROCKNER & RUBIN, supra note 8, at 105-108. The absence of a reaction was most likely due to the non-evaluative nature of the observer's scrutiny and the continued presence of the experiment administrator. Id. If subjects were motivated to satisfy the experiment administrator's objectives, then the presence of outside observers would be irrelevant as long as the administrator did not change. Id. Another study used a fictional company to implement scrutiny. Subjects made investment decisions for a corpo-
4. Conditions

The experiment assigned subjects in the fee arrangement conditions to subgroups distinguished by the level of stakes they faced. No individual subject faced more than one fee arrangement or stakes level in their respective simulations. I tested $20, $30, and $60 stakes ("Stakes-20," "Stakes-30," and "Stakes-60," respectively) in interests-aligned, CFS, and hourly fee conditions. In addition, I also tested Stakes-90 for the CFS and Stakes-7 for the interests-aligned condition for additional hypothesis testing. For tests involving interests-aligned, CFS and hourly fee conditions, I used Stakes-20, Stakes-30 and Stakes-60. Furthermore, for the unscrutinized CF condition, I tested Stakes-20 (low) and Stakes-90 (high) only due to funding limitations. Even though this condition was limited to two stakes levels, the data obtained was sufficient to test the question of whether evaluative scrutiny impacts the behavior of contingent fee attorneys.

D. Results

The primary objective of the experimental analysis was to examine the impact of scrutiny on contingent fee-attorney litigation effort in a controlled environment. To achieve this objective, the analysis addresses two primary questions. First, whether the presence of scrutiny induces subjects to invest more heavily in the litigation effort than they would in the absence of such scrutiny, and if so, how this added effort compares with interests-aligned and hourly fee attorney effort. The comparison between the two contingent fee arrangements tells us whether scrutiny can elicit additional effort from attorneys in litigation. The remaining comparisons give us some idea of how the additional effort compares to effort under two baseline fee arrangements.

The statistical analysis tests five hypotheses. To keep the discussion as approachable as possible, I have relegated the statistical analysis to the Appendix.

ration and then were told whether or not the company's board approved the decision. See Fox & Straw, supra note 74 and accompanying text; see also supra notes 97-98 and accompanying text. Subsequent decisions varied depending on whether the subject had received board support. Other studies have noted that subject behavior can be influenced by an instructor or the experiment administrator. Apparently, subjects often feel an obligation, akin perhaps, to a fiduciary obligation to please the administrator. See discussion supra note 139. Hence, the continued presence of the experiment administrator and frequent reminders of the subject's duty provided the required scrutiny.

141 Economic theory predicts that contingent fee attorneys ignore their agency obligations and maximize their own returns. Mathematically, this selfish behavior is equivalent to a contingent fee subject behaving as though he was in an incentive-aligned group with one-third the stakes. Therefore, if this behavior occurred, then there would be no statistical difference between CFS-20, 60 and 90, and incentive-aligned-7, 20 and 30, respectively. However, the analysis of the variance test I ran showed that the two fee arrangements were statistically different from each other at the .01 level of significance. For a description of the analysis of the variance test see infra text accompanying notes 226-227.

142 Experiments frequently use high and low factors to test the effects of alternative treatments. See, e.g., Tosi supra note 43.
The discussion provided in the text identifies the tested hypotheses and presents the motivation for each tested hypothesis. After this discussion I provide the conclusions that I draw from the statistical analysis.

1. Hypotheses

Hypothesis One. Contingent fee attorneys subject to scrutiny exert greater litigation effort than unscrutinized contingent fee attorneys.

Economic theory contends that contingent fee attorneys exert less effort than their clients would select.\textsuperscript{143} This reticence should be particularly pervasive when there is little danger of losing face from a poor result. Hence, the standard economic model predicts that contingent fee subjects shirk. However, the presence of scrutiny should induce attorneys to exert effort in excess of the economic model's prediction.\textsuperscript{144} The rational behavior of maximizing one's payoff is countered by the psychological need to avoid looking bad in a competitive situation. The presence of a principal or other observer focusing critical attention on the performance of the attorney may induce effort that exceeds the attorney's profit maximizing level.

Hypothesis Two. Effort investments are greater in high-stakes cases than in low-stakes cases for contingent fee and interests-aligned attorneys.

Other than the expected difference between contingent fee arrangements due to scrutiny, decisions made in the experiment should be consistent with economic theory. Economic theory predicts that attorney effort investments increase with stakes for interests-aligned and contingent fee arrangements.\textsuperscript{145} For these fee arrangements, attorneys' expected returns are positively correlated with the stakes (i.e. the greater the stakes the greater the expected return holding all else constant). Hence, it follows that the incremental benefit of added effort is greater in a high-stakes case than in a low-stakes case.\textsuperscript{146} If the experiment is consistent with economic theory, then whether scrutiny is present or not, attorney effort should increase with the stakes.

Hypothesis Three. Contingent fee attorney litigation effort in the

\textsuperscript{143} See generally discussion supra Part II.A.

\textsuperscript{144} See generally discussion supra Part III.B.

\textsuperscript{145} If the marginal cost of effort is constant or independent of stakes, then greater stakes provide increased marginal returns to effort. These greater marginal returns provide an incentive to exert greater effort. See supra note 26 and accompanying text.

\textsuperscript{146} See supra note 26 and accompanying text.
presence of scrutiny is not significantly different from client-welfare-maximizing attorney effort.

Although it appears that contingent fee attorneys subject to scrutiny exceed the effort level that economic theory suggests, these attorneys may still exert less (or more) effort than their clients prefer. To maximize clients' welfare, attorney effort should be neither substantially greater nor substantially less than the effort that the hypothetical interests-aligned attorney would choose in the case. Therefore, to test this hypothesis, I compare the effort of the CFS groups with that of the interests-aligned groups.

Hypothesis Four. Hourly fee attorney effort investments are independent of stakes.

Economic theory predicts that hourly fee attorneys should be insensitive to the stakes because their returns are independent of case outcome. The return of hourly fee attorneys increases with their effort and not with the stakes available. Hence, there should be little correlation between stakes and attorney effort.

Hypothesis Five. Contingent-fee-attorney-litigation effort subject to scrutiny does not differ significantly from the litigation efforts of hourly fee attorneys.

The positive correlation between hourly-fee-attorney return and effort suggests that hourly fee attorneys have strong incentives to invest heavily in effort. The more effort the attorney exerts, the greater his return. Economically, the only limitation on the hourly fee attorney's effort investment is his client's willingness to pay and available time. Thus, given this incentive structure, one might expect hourly fee attorneys to outspend attorneys working under other fee arrangements. Therefore, under the assumption that there is a positive economic return to effort, hourly fee attorneys who outspend other attorneys should win the majority of close cases when facing contingent fee attorneys. It follows that overspending hourly

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147 See supra note 24 and accompanying text.
148 The disconnect between the hourly fee attorneys interests and case characteristics are so great that it may be difficult to limit hours or even settle the case under an hourly fee arrangement. See William G. Ross, The Ethics of Hourly fee Billing by Attorneys, 44 RUTGERS L. REV. 1 (1991) (reporting that over 50% of attorneys believe that other attorneys overbill their hours occasionally to frequently); Rhode, supra note 45, at 635; Miller, supra note 17, at 203 (observing that a purely self-interested hourly fee attorney never settles even when settling is in his client's best interest).
149 See Miller, supra note 17, at 203.
150 Id.
151 However, empirical research has not uncovered a connection between effort and outcome. See
fee attorneys should win more civil cases in which they are often paired against a supposedly underspending contingent fee attorney. The implication of this argument is that defendants should hold a decided edge in cases that go to trial.

However, there is little evidence to suggest that hourly fee attorneys have such an advantage. Priest and Klein argue that plaintiffs win approximately fifty percent of all cases.\footnote{152} Although this controversial claim has been rejected by many, research does not support the proposition that plaintiff win rates are less than 50\%.\footnote{153} The presence of scrutiny in high-profile cases may explain in part the absence of a clear defense bias in win rates. Scrutiny from principals, media and interested outsiders may induce contingent fee attorneys to increase their effort to levels comparable with those of defense attorneys. If so then this effort would equal or exceed that of interests-aligned attorneys whose effort is bounded by that of hourly fee attorney effort.

2. Conclusions

The data provides strong support for Hypotheses one and two and partial support for Hypothesis Three. The difference between contingent fee groups with and without scrutiny was significant at the .05 level with \( p = .04 \),\footnote{154} which supports the hypothesis that scrutiny elicits increased effort. In addition to the relationship between effort and scrutiny, the increase in effort over different stakes was also significant in both contingent fee cases, \( p = .03 \),\footnote{155} and in the interests-aligned groups, \( p < .01 \).\footnote{156} This latter result supports the hypothesis that effort increases with stakes. I found no significant difference between CFS and interests-aligned expen-

\footnote{Kritzer et al., \textit{supra} note 51, at 270 n.25. The lack of a correlation in empirical data may be due to escalation of commitment on both sides which would tend to neutralize the other side's hoped-for gains. See \textit{infra} note 245. If the two sides use the other side as a model for their effort decision, then the two sides counter each escalation with a counter-balancing increase resulting in no observed gained. See \textit{supra} notes 80-82 and accompanying text (discussing the role of models in promoting escalation behavior). Of course if this behavior does occur, then failing to match the other side's increases puts the non-escalating litigant at a disadvantage thereby feeding the entrapping effect of the encounter.}{\footnote{152} See Priest \& Klein \textit{supra} note 47.

\footnote{153} Empirical work in fact suggests that plaintiff win rates vary substantially depending on the nature of the case. In reported data, plaintiff win rates ranged from a low of twelve percent in land condemnation cases to over ninety percent in third-party suits against the IRS. See Theodore Eisenberg, \textit{Testing the Selection Effect: A New Theoretical Framework with Empirical Tests}, 19 J. LEGAL STUD. 337, 351-358 (1990).}{\footnote{154} See Table A1 in the Appendix. The parameter \( p \) is the probability that the magnitude of the relevant statistic occurred by chance. In essence, \( p \) represents the probability that the variation in the data attributable to the associated variable is zero. For \( p \) small, usually .05 or less, it is very unlikely that this variation is zero, so we can conclude that the treatment effect has a significant impact on the variable in question. See SAM K. KACHIGAN, \textit{STATISTICAL ANALYSIS} 276-279 (1986).}{\footnote{155} See Table A1 in the Appendix.}{\footnote{156} See Table A2 in the Appendix.}
This finding supports the hypothesis that scrutiny elicits welfare-maximizing attorney behavior. However, the coarseness of the data does not allow me to draw such a strong inference. The data can vary quite substantially before statistical tests identify any differences. Therefore, the lack of a detectable statistical difference between data from the two groups provides only tentative support for the hypothesis. Additional tests must be taken before unequivocally accepting the conclusion that scrutiny elicits optimal investments from attorneys.

Although the data also provides support for Hypothesis four, the data is inconclusive with respect to Hypothesis five. The data supports the hypothesis that hourly fee expenditures do not vary with the stakes. Unlike in the tests for other fee arrangements, the stakes variable in the hourly fee condition test was not statistically significant. The absence of significance suggests that there were no significant variations due to stakes in the hourly fee data. Hence, subjects' expenditure decisions did not vary with the stakes. This independence from stakes was also reflected in the settlement rates, which varied in the narrow range $.52 - .65. The statistical analysis I used to test hypothesis five was also insignificant. However, an examination of the data suggests the existence of a complex relationship between the two fee arrangements. In the experiment, hourly fee subjects outspent CFS subjects when stakes were low, but there was little difference in expenditures when stakes were high. Hence, whereas hourly fee expenditures substantially exceeded CFS expenditures when stake was $20 (7.56 versus 4.90), there was little difference when stakes were $60 (7.90 versus 7.78). Probably due to the differences between high-and-low-stakes cases, the test of this hypothesis was not statistically significant. Although the variable that measured the difference between fee arrangements was significant at the .05 level (p = .03), the lack of overall significance for this test precludes concluding that expenditures differed significantly between hourly fee and CFS subjects.

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157 See Table A4 in the Appendix.

158 In the ANOVA for the hourly fee data, the F statistic for Stakes was .94 with a p value of .40. The only statistically significant variable was Trial (F = 38.79 and p < .0001). This result suggests that subjects who went to trial spent more pre-trial than did their settling counterparts. This may be due to these trial subjects spending at the same rate as their settling counterparts but taking longer to resolve their disputes.

159 See Table A2 in the Appendix.

160 See Table A1 in the Appendix.

161 The difference between expenditures for the two fee arrangements at $20 was statistically significant at the .05 level (t = 2.6, p = .013). The corresponding difference for stakes = $60 was not statistically significant. (t = .11, p = .91).
E. Data Implications

The results provide strong support for the hypothesis that scrutiny induces contingent fee attorneys to exert effort in excess of predictions from economic theory. Investment decisions made under scrutiny exceeded corresponding unscrutinized effort in both low and high-stakes cases. Moreover, effort from the scrutinized contingent fee group equaled or surpassed effort of the interests-aligned group and the hourly fee group in high-stakes cases. Although one might be tempted to draw the conclusion that scrutiny induces client-welfare-maximizing effort, the data is too coarse to draw such specific inferences. Scrutiny may elicit more or less than client-welfare-maximizing effort, and the additional elicited effort may vary significantly from case to case. Nevertheless, I can conclude that in competitive litigated disputes, scrutiny fosters escalating commitment in individuals, which results in enhanced effort. Due to the psychological basis of this phenomenon, it is highly unlikely that attorneys fare any better in such situations. The result of such behavior is protracted and costly litigation for which opposing sides have difficulty resolving their disputes outside of trial or the threat of trial.\(^{162}\)

Other than the behavior attributed to scrutiny, the data is mostly consistent with economic predictions. Contingent fee subjects were sensitive to the size of stakes, investing less in low-stakes case and more in high-stakes cases. Interests-aligned subjects also showed an increasing expenditure trend with stakes. However, their expenditures plateaued at Stakes-30 and then declined slightly.\(^{163}\) Although the difference between Stakes-30 and Stakes-60 was not significantly different, the absence of an increasing trend between these two stakes levels is curious. The settlement rates enumerated in Table A2 may partially explain this observation.\(^{164}\) Settlement rates for the interests-aligned group started at .71 for Stakes-7 and rose fairly consistently to .81 at Stakes-60. Hence, roughly 14% more subjects settled at the highest stakes level than at the lowest stakes.

These differences in settlement rates suggest that interests-aligned subjects may have been more risk averse in high-stakes cases. The computer program accepted settlement offers based on the percentage of stakes the offer represented. Therefore, a greater settlement rate indicates that subjects made offers that were a lower percentage of stakes than offers made in cases with lower settlement rates. Hence, subjects in high-stakes cases made lower relative offers than did subjects in lower-stakes cases.\(^{165}\) The willingness to make these lower demands suggests that

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\(^{162}\) See supra note 79 (discussing how the threat of impending trial can break a deadlock in litigation and prompt a settlement).

\(^{163}\) See infra Table A1 in the Appendix.

\(^{164}\) See infra Table A2 in the Appendix.

\(^{165}\) For example, in a Stakes-7 case, the program would always accept a 50% demand of $3.50. Hence, the .71 settlement rate indicates that roughly 71% of the subjects made a $10 demand. In Stakes-60 cases, the 50% threshold was $30. In these cases, the .81 settlement rate indicates that about 81% of the
high-stakes subjects preferred receiving a lower proportion of the stakes for certain rather than gambling at receiving the entire amount. Thus, high-stakes subjects were more risk-averse. Although further research is needed to determine the genesis of this change in risk-preference, I suspect it is due to a wealth effect and prospect theory. The small gains obtainable by settling low-stakes cases were not sufficient to induce subjects to forgo a chance at receiving the entire amount at trial. However, in high-stakes cases, subjects found the reward for settling preferable to the trial risk. This is consistent with prospect theory, which suggests that decision-makers are risk-averse when choices are framed as gains rather than losses.

Whereas the unscrutinized contingent fee group appeared to be as risk-averse as the interests-aligned group, the scrutinized group did not show signs of risk aversion. The increasing settlement rates for the unscrutinized group compared with the decreasing settlement rates for the scrutinized group supports this conclusion. The CFS settlement rates declined from .78 at Stakes-20 to .52 at Stakes-90. Clearly the risk-aversion observed in data for the other groups was not present in CFS data. Rather, the data suggests that the effects of scrutiny may have been more pronounced in high-stakes cases. In low-stakes cases, a solvency constraint probably buffered the effects of scrutiny. Although the pressure of scrutiny may have influenced subjects in these cases, the certainty that excessive spending would result in a negative return tended to counter the effect. Facing a losing proposition gave subjects the excuse to quit before their losses mounted. Why spend more if the client is certain to lose money even if the attorney wins the case? In essence, the CFS subjects in low-stakes cases quit when they ran out of money. This limitation was not an issue in high-cases. The return from a victory in a high-stakes case more than covered the cost of excess effort. Whereas an extra ten dollars spent in a Stakes-20 case all but insured a loss, the same ten dollar expenditure in a Stakes-90 case could produce a positive return. Therefore, without the insolvency constraint, an attorney subject to scrutiny would have difficulty resisting the psychological desire to rationalize his case investments through additional expenditures.

Hourly fee subjects, by contrast, showed no significant sensitivity to the

subjects made settlement demands of $30 or less. Thus, over 14% more Stakes-60 subjects made 50% or less settlement demands than did Stakes-7 subjects.

166 See supra note 119 and accompanying text.

167 See supra note 119 and accompanying text.

168 See infra Table A2 in the Appendix.

169 This result is particularly striking in light of the prospect theory study discussed previously in which attorney decisions exhibited risk-aversion. See supra notes 118-122 and accompanying text. The major difference is that the previous study was static and noncompetitive. Attorney’s reviewed the case description, answered a questionnaire and then made their decision. In this, escalation behavior, which is inherently dynamic, was allowed to build as subjects repeatedly made purchase decisions and received feedback under evaluative scrutiny. Thus, it is likely the necessary elements for escalation were not present in the static study. Id.
stakes. Expenditure and settlement rates were very consistent showing little of the variability observed in the interests-aligned and contingent fees data. Expenditures were consistently higher than expenditures under other fee arrangements. These results were consistent with expectations. Research suggests that attorneys in hourly fee cases are relatively insensitive to economic factors, focusing instead on the quality of representation and winning the case.\(^\text{170}\) Interestingly, my concern that hourly fee subjects would ignore the case and spend excessively was not realized. Under the scenario, hourly fee subjects could maximize their payoffs by spending the maximum each round and refusing to settle.\(^\text{171}\) Although hourly fee subjects did outspend subjects working under other fee arrangements, the differences were not substantial. In fact, for high-stakes cases there was no significant difference between hourly fee and CFS expenditures.\(^\text{172}\) In an earlier study, researchers observed a crossover point at which contingent fee expenditures equaled and then exceeded hourly fee expenditures.\(^\text{173}\) The data is consistent with that earlier finding. Although I lacked a Stakes-90 data point for hourly fee subjects, the CFS Stakes-90 amount exceeded all hourly fee expenditure rates. Although this observation does not meet any measure of statistical significance, together with the earlier study it suggests that the observed behavior may not be unique.

V. IMPLICATIONS FOR ATTORNEY BEHAVIOR AND FEE REFORM

A. Applicability to Attorney Behavior

Although one could argue that practicing attorneys are not as vulnerable to escalation and face saving behavior, such arguments are not persuasive. Researchers have observed the role of scrutiny in escalation in many other settings.\(^\text{174}\) Therefore, the trap is likely to be quite prevalent and not due to an idiosyncratic experimental design. Given the high susceptibility that people have for succumbing to face-saving behavior, it is unlikely that even experienced attorneys resist it without consciously working to avoid the entrapping effects of escalating commitment. Such resistance requires learning from prior mistakes, a skill that few people mas-

\(^{170}\) See Robert H. Gertner & Geoffrey P. Miller, Settlement Escrows, 24 J. LEGAL STUD. 87, 98 (1995) (asserting that hourly-fee-attorney cost indifference and the requirement for concurrent or advanced payment puts the hourly fee arrangement out of the reach of many litigants); See also Kritzer et al., supra note 51 (presenting data that indicates that hourly fee attorneys work diligently in their clients' interests but may be less attuned to costs than are their clients).

\(^{171}\) See Miller, supra note 17, at 203 ("[A] purely rational and self-interested attorney would never settle an hourly fee case in which he or she is working for a profit.").

\(^{172}\) See supra note 161 and accompanying text.

\(^{173}\) See Kritzer et al., supra note 51, at 267.

\(^{174}\) See supra note 74 and accompanying text.
People, even trained professionals, have trouble learning from experience. The difficulty trained professionals have in learning from experience is well documented. As two decision theorists put it, "experience is inevitable; learning is not." Attorneys are almost certain to be susceptible to this same failing. In de-briefing a completed case, an attorney is likely to focus on the effectiveness of his research and investigative efforts. He might also evaluate the effectiveness of his settlement or trial techniques in hopes of enhancing these skills in future cases. However, it is unlikely that many attorneys consider whether their effort or willingness to resolve a dispute was negatively influenced by scrutiny, or the competitiveness of the situation. This failure to explicitly consider this potential pitfall almost guarantees that attorneys do not overcome the entrapping effects of escalating commitment.

The nature of litigation and psychological biases stand in the way of attorneys discovering their susceptibility to escalating commitment. Litigation is frequently compared to battle or war with the two sides characterized as antagonists or warriors engaged in hand-to-hand combat. This highly-charged competitive atmosphere contributes to escalating commitment. Hence, the psychological desire to keep up and not be bested by the other side makes it difficult for attorneys to realize that they are entrapped. People also have a need to believe they are in control of their environment. Admitting or even considering that one may have succumbed to the entrapping effects of escalation requires admitting that we do not have complete control. Instead, it requires considering that our behavior may have

175 See supra note 117 and accompanying text.
176 See supra notes 123-126 and accompanying text.
177 See Russo & Schoemaker, supra note 123, at 174.
178 For an outline of the requirements for effective learning, see supra note 117. Sometimes even recognizing a psychological trap is not enough to avoid it. In a dollar auction that I conducted in a class, one of the bidders had witnessed a previous running of the auction and believed he could beat the game by bidding $0.90. For a description of the dollar auction, see supra notes 70-71 and accompanying text. With a minimum bid increase of ten cents, the next bid had to be $1 or greater. The student was shocked to find that someone did indeed outbid him. When the game was completed, the overconfident initial bidder’s final bid was $6.10! Thus, even someone familiar with escalation behavior can become entrapped.
179 See, e.g., Ronald J. Gilson & Robert H. Mnookin, Disputing Through Lawyers in Litigation, 94 Colum. L. Rev. 509, 510-511 (1994) ("Today, the dominant popular view is that lawyers magnify the inherent divisiveness of dispute resolution."); in fact, Gilson and Mnookin identify a whole string of literature that evokes the metaphor of the attorney as Rambo, a fictional guerrilla warrior who takes no prisoners. Id. at 511 n. 9 (citing The Tenth Annual Judicial Conference of the United States Court of Appeals for the Federal Circuit, 146 F.R.D. 205, 216 (1992) (discussing "the Rambo Litigator"); Thomas M. Reavley, Rambo Litig-ators: Pitting Aggressive Tactics Against Legal Ethics, 17 Pepp. L. Rev. 637, 637 (1990); Leonard M. Ring, The Incivility Crisis, Trial, Aug. 1993, at 78-80; Helen W. Nies, Rambo Lawyering: The Need for Civility in Civil Litigation, 32 IDEA 1, 12 (1991)).
180 See supra notes 12-13 and accompanying text.
181 See Russo & Schoemaker, supra note 123, at 177.
resulted from external stimuli.\textsuperscript{182} In addition, we are all susceptible to rationalization. Distorted memory, shifting blame, and changing preferences are all elements of rationalization.\textsuperscript{183} Hence rather than recognizing escalating commitment, an attorney may rationalize that he wanted to exert the additional effort, or that the effort was no greater than he exerts in less competitive, less-public cases. Thus, it is highly unlikely that experienced attorneys recognize their susceptibility to escalating commitment, much less ward off its entrapping effects.

\textbf{B. Implications of the Experiment for Fee Reform}

The ability of scrutiny to escalate attorney commitment and effort has significant implications for regulating attorney fee arrangements. Escalation induces attorneys to invest more in litigation and reduces their willingness to settle. Instead of seeking to resolve a case in his client’s best interests, an entrapped attorney may try to prove he is right, avoid losing face and best the other side’s attorney.\textsuperscript{184} The entrapped attorney is likely to continue investing in the case until his client forces him to quit or settle, the other side capitulates to his demands, or the attorney has exhausted all means of financing the case. The implications of these responses have strong implications for fee reform efforts. For example, in a high-stakes case, a cap limit on attorney returns is unlikely to reduce the effort level of a well-financed contingent fee attorney, whereas a contingent fee attorney without substantial resources may reject the cap-limited case or seek a quick settlement. The remainder of this section discusses fee reform implications in detail.

\textbf{1. Graduated Payment Schemes}

The implications of escalating commitment are that measures designed to increase the client’s share of a court award may not work as designed nor have the effects predicted by economic theory. Reform measures generally provide for graduated payments, a cap on the contingent percentage, or are a hybrid under which payment depends on satisfaction of certain conditions.\textsuperscript{185} For example, one

\textsuperscript{182} \textit{Id.}

\textsuperscript{183} \textit{Id.} at 179.

\textsuperscript{184} \textit{See generally discussion supra} Part III.B.

\textsuperscript{185} Several states currently have contingent fee reforms ("limits") in place. \textit{See} \textit{CONN. GEN. STAT. \S\ 52-251c (1997)} (sliding scale for personal injury, wrongful death, and property damage actions); \textit{MICH. CT. R. 8.121 (1997)} (maximum one-third limit for personal injury or wrongful death actions in Michigan); \textit{N.J. R. GEN. APPLICATION 1:21-7 (1997)} (sliding scale for tort suits); \textit{N.Y. CLS Sup. CT. \S\S 603.7(e), 691.20(e) (1998)} (providing choice between sliding scale and capped contingent fee for personal injury or wrongful death suits). Other states have enacted limits on contingent fee payments associated with medical malpractice cases. These statutes take the form of a declining graduated payment scheme. \textit{See, e.g., 735 ILL. COMP. STAT. 5/2-1114 (West 1997); ME. REV. STAT. ANN tit. 24, \S 2961 (West 1996); MASS. GEN. LAWS ANN. ch. 231 \S 60I (West 1997); WIS. STAT. \S 655.013 (1995-1996).}
The proposal would increase the allowable contingent percentage based on how far the case goes thereby increasing the attorney's incentive to exert effort as litigation becomes more time consuming.186 Another proposal, typical of decreasing graduated payment schemes, would allow attorneys to take a maximum of 25% of the first $50,000, 15% of the next $50,000, and 10% of any amount above $100,000 recovered in litigation.187

The theoretical benefit of graduated payment schemes is that they reduce the share that an attorney receives without eliminating the attorney’s incentive to invest in the case.188 In increasing schemes, the attorney receives a small amount when little effort is required and a bigger percentage as the level of effort increases. Therefore, he should work harder.189 However, this scheme is problematic in that it contributes to escalating commitment by rewarding attorneys for prolonging cases. The attorney is unlikely to be in a hurry to settle because he gets a bigger share by waiting. However, once he gets serious, he may find that he cannot obtain a better settlement than one that was previously available. At this point face-saving and rationalization may kick in to prolong the lawsuit until the attorney finds a way to explain why the best available settlement now was unacceptable earlier.190 Thus, what might happen with increasing graduated payment schemes is that many cases settle immediately with most of the remaining cases going to trial. Hence, rather than increasing the client’s share, the proposal may instead dissipate greater proportions of large returns through excessive attorney effort.191

A decreasing graduated payment scheme based on the case return avoids this perverse incentive structure by decoupling the percentage from case length. Under a scheme linked to the case return, attorneys still have incentives to continue investing in cases because their returns increase, albeit at a lower rate, with clients’ returns. Hence, as with a standard contingent fee arrangement, attorneys’ expected returns increase only if they invest more in cases. However, this lower rate is also the source of criticism. The lower percentage that attorneys receive supplies re-

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187 This proposal entitled the Lawyer’s Fair Fee Act, or Proposition 106 was defeated as a 1988 California ballot measure. Proposed Cal. Bus. & Prof. Code § 6146.1, California Secretary of State, Ballot Pamphlet 110, 111 (General Election Nov. 8, 1988) (hereinafter “California Measure”) Contingent fee limits for medical malpractice cases typically employ a declining graduated formula similar to the California measure. See supra note 185.

188 This discussion implicitly includes percentage caps because such caps are merely graduated payments with a single allowable level.

189 See Rhode, supra note 186, at 854.

190 See supra notes 66-68 and accompanying text.

191 The judicial system is already subject to criticisms of prolonged litigation. Wayne D. Brazil, The Adversary Character of Civil Discovery: A Critique and Proposals for Change, 31 Vand. L. Rev. 1295 (1978) (discussing how the adversarial nature of civil litigation and hourly fees provides attorneys with incentives to protract and complicate discovery). This proposal may exacerbate the problem.
duced incentives to exert effort. The lower return leaves attorneys able to exert less effort while their marginal returns exceed marginal costs. Hence, attorneys are unlikely to exert as much effort resulting in a worst performance than the already suboptimal contingent fee.\textsuperscript{192}

This conjectured pitfall with graduated-payment schemes might not, considering the impact of scrutiny, be as problematic as theory suggests. First consider the scheme's impact on high-stakes cases for which escalation of attorney commitment is likely to be prevalent. Such entrapped attorneys are likely to be more concerned with winning than with profit-maximization. Therefore, unless the attorney is losing money on the case, his case investment may not differ substantially under the scheme from his investment under a standard contingent fee.\textsuperscript{193} This conclusion changes for low-stakes cases, cases that are not subject to scrutiny, or graduated payment schemes that so drastically curtail the attorney's fees that he stands to lose money by maintaining a high effort level.\textsuperscript{194} The low-stakes and unscrutinized attorney is less likely to be subject to escalating commitment,\textsuperscript{195} and the potential of losing money is likely to break the escalation spell.\textsuperscript{196} Hence, a graduated-payment scheme that reduces the attorney's return too quickly may induce attorneys in low-stakes cases to curtail effort.

It follows that a carefully crafted graduated-payment scheme can achieve the objective of increasing the client's share of settlements and court awards without substantially reducing the quality of attorney representation. Most high-stakes cases are likely to be high profile and subject to scrutiny. Hence, a graduated-payment scheme is likely to have little impact on attorney effort in these cases provided the restrictions are not excessive. In cases that are not high-stakes, attorneys are likely to be more sensitive to their personal return in the absence of scrutiny. However, since most of the unscrutinized, low profile cases have low-stakes, the awards obtained from such cases are likely to fall within the initial and highest percentage level. Therefore, the percentage on the initial level of recovery must be large enough to maintain adequate attorney incentives to work.\textsuperscript{197}

Reforms that may satisfy these requirements include a 1988 California ballot that allowed a one-third share of the first $50,000 award, and medical malpractice contingent fee limits with initial levels that range from $100,000 (Maine) to $1,000,000 (Wisconsin).\textsuperscript{198} Whether these levels are sufficient to maintain ade-

\textsuperscript{192} See RHODE, supra note 186, at 854.

\textsuperscript{193} PATRICIA DANZON, NEW EVIDENCE ON THE FREQUENCY AND SEVERITY OF MEDICAL MALPRACTICE CLAIMS: A SUMMARY OF RESEARCH RESULTS 5 (1986).

\textsuperscript{194} Id. at 5, 9.

\textsuperscript{195} See supra discussion accompanying notes 103-105.

\textsuperscript{196} See supra discussion accompanying note 169.

\textsuperscript{197} For a theoretical analysis of optimal contingent fee percentages see Hay, supra note 17.

\textsuperscript{198} See supra note 186, at 854.
quate attorney incentives in low-to-moderate-stakes cases is an empirical question.\(^{199}\) Nevertheless, there is evidence that suggests that these initial levels provide attorneys with adequate incentives. Researchers in the 1980s found that contingent fee effort equaled hourly fee effort in cases valued as low as $6,000.\(^{200}\) Therefore, even accounting for inflation, $50,000 to $100,000 for the initial level along with an appropriate percentage rate is likely to provide adequate attorney incentives.

2. The Manhattan Proposal

An alternative approach proposed by Manhattan Institute fellows ("the Manhattan proposal") provides one of the more unique and popular methods of shifting case returns to clients.\(^{201}\) The premise of the Manhattan proposal is to maximize the client's return by preventing contingent fee attorneys from obtaining unearned fees. Underlying the Manhattan proposal arguments is the premise that attorneys shirk and take cases for which they do not have to put forth much effort. These are cases for which liability is uncontroversial or the defendant for whatever reason does not want to contest the claim.\(^{202}\) The Manhattan proposal achieves its return-shifting objective by limiting the returns contingent fee attorneys receive. The proposal limits the attorney's recovery to at most ten percent of an initial defendant settlement offer made within sixty days of receiving the plaintiff's complaint.\(^{203}\) If the plaintiff rejects the settlement offer, the Manhattan proposal then restricts the attorney’s return to a percentage of the amount obtained in excess of the initial settlement offer plus at most ten percent of that initial offer amount. This rule forces a contingent fee attorney who receives a settlement offer to decide whether it is worth it to pursue a greater return. If an attorney rejects an initial offer and does not receive a greater reward or settlement later, he gets no return for his additional effort.

The Manhattan proposal provides a strong disincentive to continuing a case past an initial settlement offer. To understand this implication, consider the

\(^{199}\) The definition of adequacy must be determined as well. In this analysis the baseline has been the attorney effort that an omniscient plaintiff would have exerted in his behalf. However, this baseline does not account for such externalities as court costs and the costs of creating bad law. See supra note 28. A true determination of optimality would include these factors as well.

\(^{200}\) See Kritzer et al. supra note 51, at 269-270.

\(^{201}\) The Manhattan proposal was the basis of defeated 1996 reform measures introduced in the House of Representatives and California. See Angela Wennihan, Let's Put the Contingency Back in the Contingency Fee, 49 SMU L. REV. 1639, 1672-1673 (1996).

\(^{202}\) BRICKMAN ET AL., supra note 2, at 20-22. There are lots of reasons why a defendant settles cases. These reasons include finding it cheaper to settle than to incur litigation costs, not wanting to risk a huge adverse judgment or wanting to avoid poor publicity. See Katz, supra note 52.

\(^{203}\) Payment is based on an hourly fee basis and limited to a maximum of ten percent. BRICKMAN ET AL., supra note 2, at 27-28.
following example. Suppose a case has an expected return of $60,000. If the attorney wins an award for this amount, he receives $20,000 under a one-third contingent fee arrangement. Under the Manhattan proposal, the attorney’s return depends on whether the defendant makes a settlement offer and the amount of that offer. If the defendant offers $45,000, then the attorney receives at most $4500 of this amount. The utility-maximizing attorney must then decide whether to try to get more. He must decide whether to put forth the effort required to recover the additional gross $15,000 expected return. The additional investment yields a total attorney return of $9,500 (the pre-settlement-offer $4500 plus the attorney’s one-third share of $15,000), a $10,500 reduction from the amount he receives without the reform. This reduced potential return results in a reduced attorney incentive to continue the case. Hence, the Manhattan proposal strongly encourages early settlement.

The plaintiff may or may not be better off under the Manhattan proposal. In the example, the attorney receives at most $4500 if the case settles after the first offer and the plaintiff receives at least $40,500. This amount is in contrast to the $40,000 the plaintiff receives from winning instead of settling the case under a one-third contingent fee arrangement. Under the Manhattan proposal, the plaintiff’s share of a $60,000 judgment rises to $50,500, over $10,000 more than he receives under a one-third contingent fee arrangement. Hence, in this example even if the case settles the Manhattan proposal achieves its objective of limiting the attorney’s return while simultaneously maintaining plaintiff returns. However, the example is sensitive to parameter changes. The plaintiff benefit drops precipitously if the defendant’s offer is lower. For example, if the defendant offers $30,000 instead of $45,000, the plaintiff’s share of the settlement is now $27,000, $13,000 less than his pre-proposal return. The plaintiff may wish to reject the settlement offer in this case, but can do so only if his attorney cooperates. The attorney’s share for continuing and obtaining the additional $30,000 is $10,000. Although greater than the $5000 potential gain in the previous example, the additional return is still substantially less than the $20,000 the attorney would receive pre-proposal. Therefore, the attorney’s incentive to continue is substantially less than it is under a standard contingent fee arrangement. If $10,000 is less than his opportunity costs, the utility-

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204 The assumption is that the attorney is the decision-maker and can refuse to continue working on the case if the plaintiff rejects the offer. I do not discuss the validity of this assumption. However, others have argued that, for practical purposes, the attorney is indeed the decision-maker in litigation when he has a financial stake in the outcome. See Douglas E. Rosenthal, Lawyer and Client: Who’s In Charge? (1977). If the plaintiff wishes to continue but his attorney does not, there is a clear conflict of interest. See Miller, supra note 17.

205 I am assuming that the overall expected return to attorney effort is unchanged whether the Manhattan proposal applies or the attorney works under a traditional contingent fee arrangement.

206 See generally discussion supra Part II.A.

207 It is also substantially less than incentives under the California measure which does not reduce the attorney’s return until the client’s award exceeded $50,000. See supra note 187 and accompanying text.
maximizing attorney is unlikely to continue the case. Therefore, the Manhattan proposal may actually reduce rather than increase plaintiff returns.

This result has its strongest implication for low-to-moderate-stakes cases. In these cases scrutiny is limited or nonexistent so attorneys are likely to focus primarily on utility maximization. In such cases the Manhattan proposal is likely to encourage contingent fee attorneys to settle early due to the limited benefit of continuing the case. The defense in such cases is likely to take advantage of the limits on the contingent fee attorney’s return by making low-ball initial offers. With a strategically chosen settlement offer, the Manhattan proposal restrictions almost certainly makes the attorney-specific benefits from continuing a case past the initial settlement offer negative.\textsuperscript{208} If the attorney is unable to continue without losing money, the plaintiff’s recovery will be dramatically lower.\textsuperscript{209} Hence, whether the attorney settles the case early, or rejects it outright, the Manhattan proposal will not only limit the contingent fee attorney’s return in low-stakes cases, but it will slash the client’s return as well. The Manhattan proposal also may have a chilling effect on the ability of plaintiffs to obtain representation in low-to-moderate-stakes cases. The severe limits on the contingent fee attorney’s recovery may cause attorneys to reject such cases outright or find creative ways to receive advance payment.\textsuperscript{210} For plaintiffs unable to make such side payments, judicial access may be denied.

The impact of the Manhattan proposal in high-stakes cases is likely to be quite different due to increases in scale and the impact of scrutiny. When the stakes are high, the Manhattan proposal’s restrictions may not be as big of a disincentive because the returns from continuing are much greater. These returns may be sufficiently large that losing money on the case is not an issue. In such situations, the attorney is susceptible to escalating commitment due to the entrapping effects of scrutiny and the adversarial nature of the case.\textsuperscript{211} The defense has a lower probability of successfully using a low-ball strategy in high-stakes cases because it is possible for the contingent fee attorney to make money by continuing litigation. In effect, the likely impact of low-ball offers may be to insult the contingent fee attorney. If he interprets the low offer to signal a lack of respect then his anger might result in yet greater escalation of the conflict.

To illustrate the difference that high-stakes makes for Manhattan proposal implications, I recycle the example used previously to illustrate contingent fee in-

\begin{itemize}
  \item \textsuperscript{208} In light of the low expected return of such cases, attorneys may simply reject these cases because the return does not exceed the opportunity costs of taking them. See Bimholz, supra note 25, at 962 (summarizing the argument that fee limits make certain cases too unattractive for attorneys to accept).
  \item \textsuperscript{209} Drastic reductions in attorneys' returns are known to result in reduced settlements and fewer cases litigated to a verdict. See Danzon, supra note 193.
  \item \textsuperscript{210} Attorneys may exchange one abuse for another by requiring nonrefundable retainers. See Lester Brickman & Lawrence A. Cunningham, Nonrefundable Retainers Revisited, 72 N.C. L REV. 1 (1993).
  \item \textsuperscript{211} See generally discussion supra Part III.B.
\end{itemize}
centives.212 In that example, there are five possible actions that the attorney can take, each with a known numerical benefit. For simplicity, each action has an identical cost of 12. The benefit of each of the actions in a low-stakes case from most beneficial to least is 60, 45, 30, 15, and 6 using the same unit of measurement as costs. The interests-aligned attorney performs all but the last action, whereas his contingent fee attorney who receives a one-third contingent fee prefers to perform only the two most beneficial actions.213 The key point is that although his effort is suboptimal, the contingent fee attorney still invests in the case.

Now suppose the defendant makes a settlement offer under the Manhattan proposal for one-half the expected case return. The impact of this offer is to cut the value of continuing litigation in half. Hence, the feasible actions are now worth just 30, 22 1/2, 15, 7 1/2, and 3. The (risk-neutral) client prefers to continue because there are three actions that provide a positive expected benefit. Specifically, the client expects a net return of 31 1/2 from the attorney undertaking these three actions.214 However, the attorney entitled to receive only one-third of the additional gain prefers not to continue the case because he cannot receive a positive expected gain. His most beneficial action yields an expected return of -2 (30/3 - 12). Thus, under the Manhattan proposal the attorney prefers to settle in a case in which the client benefits by rejecting the initial offer.

Now suppose the stakes were higher. Specifically, consider the case in which the expected award is doubled, all else equal. Also suppose that the defense again makes an offer for one-half of the case expected return. The continuation values of feasible actions are now 60, 45, 30, 15, and 6, twice the values for the low-stakes example. Balanced against the unchanged costs per action of 12, the attorney continues litigating because he has a positive expected return of 11 from performing the two most beneficial actions. If the conflict escalates due to scrutiny, a perceived insult and/or the competitiveness of the case, the attorney may opt to undertake the third action as well. Although undertaking such an action does not maximize his return, it may pay psychic dividends by helping the attorney save face and rationalize his decisions.215

Thus, whereas the Manhattan proposal may have a chilling effect on judicial access and limit plaintiff returns in low-to-moderate-stakes cases, the proposal may achieve its stated purposes in high-stakes cases. If contingent fee attorneys escalate their commitment and become entrapped, the proportion of their returns relative to clients' returns will be much lower than under a unregulated contingent fee arrangement. The entrapped attorney's effort clearly exceeds that of a shirking attorney and perhaps the optimal level as well. Therefore, in high-stakes cases the

212 See supra text accompanying notes 27-28.


214 I obtained the net return figure by adding the three actions with a positive net benefit and subtracting their costs. Mathematically, this calculation is 30 + 22.5 + 15 - (3 x 12).

215 See supra notes 83-84 and accompanying text.
Manhattan proposal is likely to satisfy its objective of reducing the contingent fee attorney’s share.\textsuperscript{216} However, the costs of achieving this objective may be too high given the availability of less invasive alternatives. The Manhattan proposal may reduce access for plaintiffs in low-to-moderate-stakes cases. Moreover, in the cases that attorneys accept, the Manhattan proposal exacerbates the shirking problem by inducing attorneys to settle early in cases for which it is in their clients’ interests to continue.\textsuperscript{217} Hence, the price of increasing the client’s share of case returns in high-stakes cases is a drastic reduction in client returns in low-to-moderate-stakes cases. Graduated payment schemes provide similar gains in client shares in high-stakes cases without the losses in lower stakes cases. By allowing contingent fee attorneys a one-third or greater percentage of the initial $50,000 recovered, graduated payment schemes do not alter contingent fee-attorney incentives as drastically as does the Manhattan proposal in lower stakes cases. Yet, with a carefully selected schedule of applicable percentages for greater returns, graduated schemes reduce contingent fee attorney returns in the cases where many of the abuses are thought to occur.\textsuperscript{218}

VI. CONCLUSION

This research addresses the paradox of why many contingent fee attorneys do in fact shirk while others develop reputations for excellence.\textsuperscript{219} Attorneys who work in the relative obscurity of low-to-moderate-stakes cases do not suffer from glaring attention that elicits escalating commitment. Hence, such attorneys are likely to shirk as the economic model predicts. By contrast, attorneys who work on high-stakes and high profile cases face constant pressure to succeed due to their exposure to scrutiny. Such scrutiny can and does elicit effort far in excess of effort

\textsuperscript{216} However, it is unclear whether escalated effort is beneficial to the plaintiff. First, the plaintiff may be better off if the case settles. An entrapped attorney resists settling for any amount that does not rationalize his efforts. \textit{See supra} notes 70-71, 77-78 and accompanying text. Thus, the attorney may turn down a beneficial settlement opportunity. Second, the defense attorney is likely to suffer from escalation behavior as well since escalation tends to be exacerbated by the behavior of competitors. \textit{See supra} note 81 and accompanying text. Therefore, the increased effort that escalation induces may be countered and neutralized by a corresponding increases in defense attorney effort. This matching effect may explain why researchers have difficulty finding a connection between attorney effort and outcomes. \textit{See} Kritzer et al., \textit{supra} note 51, at 20 n.25.

\textsuperscript{217} \textit{See supra} notes 25-27 and accompanying text.

\textsuperscript{218} Many of the horror stories about contingent fee attorney abuse involve high-stakes cases in which attorneys obtain returns that may equate to hourly fee rates measured in the tens of thousands of dollars without investing substantial effort. \textit{See BRICKMAN ET AL., supra} note 34, at 76 n.186 (citing the 1979 DC-10 crash in Chicago in which at least one contingent fee attorney received $383,244 for twenty-five to thirty-five hours of work); \textit{BRICKMAN ET AL., supra} note 2, at 55 n.24 (citing a 1989 Texas school bus accident settlement for which contingent fee attorneys received more than $40 million for eight months of work).

\textsuperscript{219} Former Harvard Law School Dean Derek Bok suggests that such reputations have allowed some contingent fee attorneys to become millionaires \textit{See supra} note 39.
provided by economics’ self-interested rational attorney. Thus, explicit consideration of face-saving and escalation together with the economic model yields a world in which both shirking and hard-working attorneys coexist.

This augmented model has strong implications for litigation reform. The effects of scrutiny induce not just litigators but all of us to want to look good and do well. In litigation, doing well often translates into winning rather than settling a case, especially if the litigator has previously invested substantial resources in the case. Wanting to please and, more importantly, to not look bad elicits rationalizing behavior that makes settling very difficult. Hence, high profile cases that do not settle early become less likely to settle before trial or the onset of trial. Therefore, any litigation-reform attempts designed to elicit additional attorney effort may compound escalation in these cases. Yet, reforms that drastically limit contingent fee attorney payments may render many cases unattractive to attorneys leaving an unacceptably large proportion of citizens without access to the judicial system.

Nevertheless, it is possible to develop reforms that account for the divergent dynamics between high and low-stakes cases while meeting regulatory objectives. I suggest that decreasing-graduated-payment schemes go a long way towards balancing the competing goals of maintaining access in low-stakes cases and reducing excessive fees in high-stakes cases. However, there may be other perhaps more elegant means of achieving attorney fee reform without sacrificing beneficial characteristics of current compensation schemes. Certainly development of such proposals requires an understanding of the implications of escalating commitment. Only by explicitly recognizing litigator susceptibility to the psychological bias of escalation will policy makers be able to draft reforms that address real concerns while maintaining the legitimacy of the United States judicial system.

VII. STATISTICAL APPENDIX

Table A1 contains an overview of the means and standard deviations (in parentheses) for litigation expenditures. The CF means were consistently lower than their CFS counterparts. However, using a student to test for differences between CF and CFS means, only the difference between total litigation expenditures means at the $90 stakes level were statistically significant. The table also shows that CFS subjects spent amounts similar to interests-aligned subject expenditures at

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220 See generally discussion supra Part III.B.
221 See generally discussion supra Part III.B.
222 See supra note 79 (discussing how the threat of impending trial can break a deadlock in litigation and prompt a settlement).
223 See supra notes 208-211 and accompanying discussion.
224 See supra notes 218-219 and accompanying discussion.
225 For a description of this statistical test see KACHIGAN, supra note 154, at 175-181.
low-stakes levels and exceeded interests-aligned expenditures at high-stakes levels. However, none of these differences were statistically significant. Finally, the hourly fee condition shows relatively constant expenditures across the three stakes levels. These results are consistent with economic theory and the hypothesis that critical scrutiny affects contingent fee behavior.

Table A1
Means and (Standard Deviations) of Litigation Expenditures

<table>
<thead>
<tr>
<th>Stakes</th>
<th>Interests-Aligned</th>
<th>CF*</th>
<th>CFS*</th>
<th>Hourly Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>4.59</td>
<td>7.60</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(3.14)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>20</td>
<td>5.08</td>
<td>4.17</td>
<td>4.90</td>
<td>7.56</td>
</tr>
<tr>
<td></td>
<td>(3.65)</td>
<td>(2.30)</td>
<td>(3.21)</td>
<td>(3.73)</td>
</tr>
<tr>
<td>30</td>
<td>6.11</td>
<td>5.70</td>
<td></td>
<td>7.89</td>
</tr>
<tr>
<td></td>
<td>(4.25)</td>
<td>(3.42)</td>
<td></td>
<td>(4.71)</td>
</tr>
<tr>
<td>60</td>
<td>5.74</td>
<td>7.78</td>
<td></td>
<td>7.90</td>
</tr>
<tr>
<td></td>
<td>(3.98)</td>
<td>(3.70)</td>
<td></td>
<td>(3.92)</td>
</tr>
<tr>
<td>90</td>
<td>5.15</td>
<td>8.16**</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(2.60)</td>
<td>(5.03)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*CF = Contingent fee, and CFS = Contingent fee with scrutiny.
**Significantly different from same-stakes CF mean at the .05 level.

Table A2 provides additional support for the significance of scrutiny. The table contains means of settlement groups for the four fee arrangements. Although only the means of the CF and CFS groups at the Stakes-90 level were statistically significant at the .05 level, the table does reveal interesting patterns in the data. The interests-aligned groups’ settlement rates did not vary substantially. The interests-aligned subjects did appear to settle more as the stakes increased. By contrast, the CFS subjects became less willing to settle as the stakes increased. Hourly fee and CF settlement rates were relatively constant across stakes albeit at different levels. The means in these tables suggest that scrutiny induces additional effort and reduces the probability of settlement. In addition, the data suggests that hourly fee behavior, whether expenditures or settlement rates, is independent of the stakes.
Table A2
Means and (Standard Deviations) of Settlement Rates

<table>
<thead>
<tr>
<th>Stakes</th>
<th>Interests-Aligned CF(^a)</th>
<th>CFS(^a)</th>
<th>Hourly Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>7</td>
<td>.71 ( .46 )</td>
<td>.78 (.42)</td>
<td>.61 (.50)</td>
</tr>
<tr>
<td>20</td>
<td>.75 (.44)</td>
<td>.86 (.36)</td>
<td>.78 (.42)</td>
</tr>
<tr>
<td>30</td>
<td>.77 (.43)</td>
<td>.69 (.47)</td>
<td>.65 (.48)</td>
</tr>
<tr>
<td>60</td>
<td>.81 (.40)</td>
<td>.65 (.49)</td>
<td>.52 (.51)</td>
</tr>
<tr>
<td>90</td>
<td>.86 (.35)</td>
<td>.52** (.51)</td>
<td></td>
</tr>
</tbody>
</table>

\(^a\)CF = Contingent fee, and CFS' Contingent fee with scrutiny.

**Significantly different at the .05 level from the corresponding contingent fee treatment.

Although the means reported in Tables A1 and A2 are consistent with theory developed here and economic theory, the tests are inconclusive. Part of the reason for this inconclusiveness is that the tests are very weak. The test only considers two means at a time when our interest is how the whole group is affected by differences in condition. If our concern is how scrutiny affects behavior at different stakes levels, a better test is one that considers the means at all stakes levels simultaneously.

Analysis of variance ("ANOVA") is the appropriate statistical technique to test the comparison. ANOVA provides a means of understanding the source of variation in a collection of data. This technique can be used to determine whether different conditions produce significant levels of variation in a dependent variable.\(^\text{226}\) For my purposes, I use ANOVA to provide an indication of whether different fee arrangements, stakes, or scrutiny level provide significant variation in the experimental data. If I found significant variation due to differences in conditions or stakes, then I could accept the hypothesis that the relevant variable significantly influences subject behavior in the experiment.\(^\text{227}\) Table A1 contains the re-

\(^\text{226}\) For an elementary exposition of ANOVA see supra note 154, at 272.

\(^\text{227}\) Id.
sults of the expenditure analysis between the two contingent fee arrangements.  

Table A3
Result of Analysis of Variance on Contingent Fee
Expenditure Decisions

<table>
<thead>
<tr>
<th>Sources of Variance</th>
<th>Mean Square</th>
<th>df</th>
<th>F</th>
<th>p</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fee Arrangement (CF or CFS)</td>
<td>34.58</td>
<td>1</td>
<td>4.53</td>
<td>.04*</td>
</tr>
<tr>
<td>Stakes</td>
<td>24.30</td>
<td>3</td>
<td>3.18</td>
<td>.03*</td>
</tr>
<tr>
<td>Trial</td>
<td>16.36</td>
<td>1</td>
<td>2.14</td>
<td>.15</td>
</tr>
<tr>
<td>Fee Arrangement x Stakes</td>
<td>.82</td>
<td>1</td>
<td>.11</td>
<td>.74</td>
</tr>
<tr>
<td>Fee Arrangement x Trial</td>
<td>34.17</td>
<td>1</td>
<td>4.47</td>
<td>.04*</td>
</tr>
<tr>
<td>Stakes x Trial</td>
<td>2.93</td>
<td>3</td>
<td>.38</td>
<td>.77</td>
</tr>
<tr>
<td>Explained Variance</td>
<td>16.95</td>
<td>10</td>
<td>2.22</td>
<td>.02*</td>
</tr>
<tr>
<td>Residual Variance</td>
<td>7.64</td>
<td>132</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Variance</td>
<td>8.30</td>
<td>142</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*p ≤ .05.

*p ≤ .01.

The Fee Arrangement variable indicates whether the data is from the CF or CFS conditions. Stakes is self-explanatory. The trial variable is one if the case settled and zero otherwise. I included this variable due to the discontinuity in expenditures between cases that went to trial and cases that settled. Thus, regardless of the cost of going to trial, this variable and its interactions captured differences between subjects who settled and those who went to trial. The remaining terms are interaction terms that measure the covariation of two of the pure variables together. These terms measure variation that was present when the two factors were together or interacted. The significance of Fee Arrangement in Table A3 supports Hy-

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228 The F statistic is a measure of the statistical significance of the variable. The mean square for each variable (second column) is used in the ANOVA calculation and to compute the F statistic for the variable. The third column contains the degrees of freedom (df) for that variable. The p in the final column indicates the probability that an F statistic of that magnitude occurred by chance. See Kachigan, supra note 145, at 276-279.

229 For a description of the different stakes used, see supra text accompanying notes 141-142. The disparity (two versus four) in the number of stakes between the two fee arrangements was a source of concern. This unbalance (differing number of stakes between fee arrangements) could introduce bias or noise that would alter the data interpretation. To determine whether this was a problem, I reran this expenditures analysis using $20 and $90 stakes only for the two fee arrangements (a balanced design). The balanced design inferences did not change from the unbalanced design although the four factors that were significant at the .05 level were significant at the .01 level. Hence, it appears that using the unbalanced design does not significantly alter the analysis. Because the CF-CFS comparison presented the greatest disparity (all other tested fee arrangements contained at least three stakes levels in common), I opted to include all available data in the remaining tests.

230 See Kachigan supra note 154, at 292.
pothesis 1 regarding the importance of scrutiny. The significance of stakes supports Hypothesis 2, that expenditures are greater in high-stakes contingent fee cases.

Table A4
Results of Analysis of Contingent Fee and Hourly fee Arrangements
Pre-Trial Expenditures Decisions

<table>
<thead>
<tr>
<th>Sources of Variance</th>
<th>CFS v. Interests-Aligned</th>
<th>CFS v. Hourly</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>F</td>
<td>p</td>
</tr>
<tr>
<td>Fee Arrangement</td>
<td>1.09</td>
<td>.30</td>
</tr>
<tr>
<td>Stakes</td>
<td>2.04</td>
<td>.09</td>
</tr>
<tr>
<td>Trial</td>
<td>3.24</td>
<td>.07</td>
</tr>
<tr>
<td>Fee Arrangement x Stakes</td>
<td>2.22</td>
<td>.11</td>
</tr>
<tr>
<td>Fee Arrangement x Trial</td>
<td>2.09</td>
<td>.15</td>
</tr>
<tr>
<td>Stakes x Trial</td>
<td>.52</td>
<td>.72</td>
</tr>
<tr>
<td>Explained Variance</td>
<td>6.27</td>
<td>&lt;.01**</td>
</tr>
</tbody>
</table>

*p ≤ .05.

*p ≤ .01.

Table A4 reports the variance analysis of differences between the contingent fee and hourly fee arrangements. To include both comparisons in the same table, Table A4 only reports F and p parameters for each comparison. Whereas the explained variance for the CFS-interests-aligned comparison was highly significant, none of the other terms were significant at the .05 level. In particular, the p value for Fee Arrangement was a very large .30, there was no indication of investment decision differences between CFS subjects and interests-aligned subjects. This result supports Hypothesis 3 in that there was no statistically significant difference between data from the two fee arrangements.

The comparison between data from CFS and hourly fee groups showed a significant difference between the fee arrangements. However, the explained variance of the analysis with p = .07 did not satisfy either of the significance thresholds. So the difference observed for the fee arrangement variable cannot be accepted. The difference in spending patterns across stakes may explain this result. Hourly fee subjects' expenditures exceeded CFS subjects' expenditures substantially in low-stakes cases, whereas there was little difference between these expen-

231 See supra text accompanying notes 143-144.
232 See supra text accompanying notes 145-146.
233 See supra text accompanying notes 147.
ditures in high-stakes cases.\textsuperscript{234} The high variability in one fee arrangement combined with the low variability in the other was difficult for the ANOVA to capture. It did, however, distinguish between the two fee arrangements. The non-result of the comparison provides limited support for Hypothesis 5.\textsuperscript{235}

\textsuperscript{234} See supra Table A1. Earlier empirical researchers found a similar crossover in effort expended between hourly fee and contingent fee attorneys. See Kritzer et al., supra note 51, at 267. However, the difference observed in this study was not large enough to conclude that CFS subjects spent more than hourly fee subjects in high-stakes cases.

\textsuperscript{235} See supra text accompanying notes 149-151.