THE BUSINESS OF LAWSUITS

BY HENRY KRASNOW

Lawsuits are often initiated or fully defended in court because the participants have strong feelings about justice. Unfortunately, finding someone "guilty" or "not guilty" does not prove someone "right" or "wrong." Forget the romantic notions you learned from the movies about how the legal system works.

Let's Make a Deal

The most cost-effective result you can get from the litigation process has nothing to do with "justice" in any absolute sense, just as a good deal on a new truck doesn't require buying the "best" truck. You pass up the Mercedes-Benz and buy a Chevy or Ford because it's more efficient and there are other things you can do with the money you save. In a lawsuit, your money "buys" the resolution of a dispute and the best result is still the one that's most cost-effective. Spending $10,000 in legal fees for a negotiated settlement of $50,000 is better than spending $40,000 in fees to win a $75,000 judgment in court.

Forget revenge. Considering the bad feelings created by the exchange of threats and insults, it's not surprising that many otherwise rational business owners treat a lawsuit as a means for revenge. But as with any business transaction, when the goal is revenge, the result is a bad deal. A lawsuit sets the price of a resolution to a dispute according to the odds of winning or losing. To refuse to pay the market price or to insist on more than the market price in order to get revenge makes no sense.

Know Your Costs

The most important thing your lawyer can do for you is provide the information you need to decide which alternative is more cost-effective: going to trial or settling out of court.

EVEN IF YOU WIN, YOU CAN LOSE, UNLESS YOU CAREFULLY EVALUATE A LAWSUIT AS A BUSINESS PROPOSITION

Written predictions. A lawyer should be able to give you periodic written estimates of both the cost and the likelihood of success of going to trial. Far from a sign of distrust, putting this information in writing protects you and your lawyer from later confusion about who said what and when.

Strategy. An experienced lawyer should be able to break down the litigation process into phases and to articulate in advance a strategy for each phase. Again, you should ask for a written estimate of the approximate cost for each phase and each strategy.

Poker Anyone?

Many business owners believe that settlements are always defeats, but nothing could be further from the truth. Settlements are business deals that should be evaluated in terms of the available alternatives and their relative costs and risks.

A trial is a gamble. In the construction business, nothing is a sure thing. Regardless of your market share, the skill and loyalty of your employees, and the reliability of your suppliers, things can and do go wrong. The same is true of a trial. No matter how talented or self-confident your lawyer is or how many of your friends believe you are "in the right," going to trial is always a gamble. Key witnesses may die, move away, or forget what happened. Even if you tell

ILLUSTRATION BY ROBERT HUNTOON

CASE STUDY: AN UNSETTLING MATTER

Years of experience in construction litigation have proved to me that builders misunderstand and misuse lawsuits. This composite case study, based upon several actual cases, illustrates the cost of a misguided quest for "justice."

Two weeks after submitting a final bill for $17,500, representing 5% retainage on a new $350,000 house he has just completed, a builder gets a call from the owner. He is told that nail pops and cracks in the wallboard have begun to appear in two first-floor rooms.

At the house, the builder explains to the owners that new houses experience normal settling in the first year. He tells them that his warranty covers these repairs, but that it's best to wait and then make all repairs at once. If he fixes the problems now, he doesn't want to be called back in five months to redo them when they recur. The owners explain that it's "very important" to make the repairs now because they have a number of dinner parties planned and it will embarrass them if their friends see these cosmetic problems. "Whatever you want," the builder replies. He comes the next week and makes the cosmetic repairs.

A few weeks later the problems recur, as predicted, and the owners want the builder to come back again. The builder reminds the owners of his policy and the outstanding retainage. The owners maintain that they thought the original repairs were done as a "favor." They never insisted he come back at all; they remember saying only that it was "very important."

Over the next few weeks, the discussions deteriorate rapidly. The builder feels that he is being punished for being right about the recurring problems and doesn't think he should be expected to do more free work. Feeling frustrated, he puts a lien on the house. The owner, angry now, and feeling that the builder is refusing to stand behind his work, files a lawsuit. When the builder gets the summons, he sends it to his lawyer, telling him to "take these people to court" to get the $17,500 retainage. The lawyer files a counterclaim.

Things quiet down for six months while lawyers for both sides photograph the house and take depositions from both parties. The owners get an estimate from another contractor of $18,000 to repair the damage. He says that he thinks the house is settling more than usual because one corner of the foundation is built on inadequate fill. The builder thinks this price is high and that he could do the repairs for $12,000.

June – September Expenses	
Repair costs:	$400
Legal fees:	$650

In March, the court sets an August trial date. In May, the builder hires a soils expert to testify that settling in the first six months is normal. He doesn't determine the quality of the fill because the builder doesn't want to pay for the heavy equipment and testing procedures. In July, the builder's lawyer orders copies of all of the depositions, prepares the builder and the soils expert for direct testimony, and prepares his cross-examination of the owners and their new contractor.

October – March Expenses	
Legal fees, incl. depositions	$6,150
Photographs:	$350

As the trial date approaches, the builder asks his lawyer what the outcome is likely to be. The lawyer says he has a 50-50 chance. The conversation between the builder and owner is not disputed, but it's ambiguous as to what each side meant by what they said. The testimony from the two experts could be a wash, and in the absence of clear-cut guidelines, the judge may rule in favor of the side who evokes the most sympathy.

April – July Expenses	
Legal fees:	$3,000
Soils expert:	$1,550

Settlement discussions continue until the eleventh hour. Not trusting the builder to do the work, the owners hire the second contractor to begin the repairs.

Finally, fourteen months after the original problems arose, the builder agrees to settle for $9,000 — 50% of the repair cost. His total investment is $22,100: out-of-pocket expenses of $11,700, including the settlement, and legal fees of $10,400.

August Expenses	
Settlement:	$9,000
Legal fees:	$1,000

Had he made the repairs himself a year earlier and split the costs with the owner, his total costs would have been $7,050. And he may even have gotten a referral.

Total Expenses	
Total Out-of-pocket:	$11,300
Total Legal Fees:	$10,800
Total Cost:	**$22,100**

— H. K.

the truth and your opponent lies, the jury may not believe you because of the way you look, dress, or talk. Remember also that judges, like other people, make mistakes, and that the law is often unclear. If it were simple, thousands of lawyers wouldn't be arguing about it.

Delays are expensive. A wait of several years until trial is common in many locations. This means you will pay or be paid in inflated dollars, which, if you had them now, could be invested in your business. There's also a chance you won't be paid at all. I remember a case where the plaintiff rejected a settlement offer of $75,000 in favor of going to trial to recover the full claim of $100,000. The delay was only six months, but it was long enough for the defendant to go out of business, leaving the plaintiff with nothing.

Hidden costs. Finally, litigation diverts time and energy from other aspects of your business. You need to supply information and make decisions throughout the process, and the confrontational aspects often drain your emotional energy. This is as much a "cost" as legal fees or a settlement payment.

Settling Out of Court

It's a cinch to determine which cases should be settled: They should *all* be settled, *provided the price is right*. What you and your lawyer need to determine is whether a settlement is a rational business alternative to the cost, risks, and rewards of going to trial, and what negotiating tactics you can use to persuade the other party to make a more favorable settlement offer. This analysis is one of the main functions your lawyer should perform and should take place during discovery (the period of time leading up to trial when information is exchanged between parties).

Lawsuits are usually initiated after talks break down. But far from signaling the end of negotiations, a lawsuit actually propels negotiations forward, for several reasons.

Pay to play. Talk is cheap until a lawsuit is filed. After that, the process gets more expensive the longer the parties disagree. This has the effect of putting a penalty on refusing to take the negotiation seriously.

No exit. When you negotiate in the face of a lawsuit, there is no way out except to settle or go to court. Without the lawsuit, the parties can ignore each other indefinitely.

Actions speak louder than words. Once a lawsuit is initiated, the parties no longer talk directly to each other. Instead, they speak through their lawyers, who are paid to appear self-confident and to say "no." It quickly becomes apparent that a lawyer cannot simply talk the other side into a good deal. Consequently, what the parties *do*

is more important than what they *say*. For example, if you offer to settle for 80% of a claim shortly after a case is filed against you, nothing your lawyer says will ever persuade your opponent that you seriously believe you have a good chance of winning. The timing and amount of the offer will overpower whatever is said when conveying it.

Changing the odds. All of the tools used in negotiating a lawsuit are actions, not words. For instance, you can find new witnesses, or make a motion to exclude critical evidence or for "summary judgment" (which asks the judge to resolve disputed questions of law prior to trial). The overall strategy is to alter one or more of the elements that determine your opponent's settlement position. When the odds of winning change, negotiating positions almost always change, too.

Each of these actions, however, costs money to pursue. As with any business decision, the cost of a particular action must be weighed against the likelihood that it will significantly change the other side's perception of its chances of winning or losing.

Strategies For Negotiation

No one wants to leave anything on the table. Effective negotiating strategies help you to "shake the tree" to make sure that everything that's there has fallen out. There are several important rules you can follow.

Don't get mad, except on purpose. Some lawyers coach their clients in deliberately staged displays of anger with the idea of convincing the other side that they're dealing with an irrational person. But even if you can pull it off, there's no guarantee it will have the desired effect. Anger is almost always a liability because it impairs good judgment and prevents you and your opponent from making rational decisions. If you must display your anger, make it brief and then walk away. A prolonged display may deteriorate into an exchange of insults that will hurt your case.

Don't make an offer that is too low or demand a settlement that is too high. For example, if you and your lawyer determine that, as a defendant, there is a 30% to 40% chance of winning the case, your final settlement offer should be in the range of 60% to 70% of the claim. You may offer slightly less to test the other side's resolve or information, but if you offer only 5% or 10%, you run the risk of your offer being viewed as "not in the ball park."

Don't negotiate against yourself. When you reach a stalemate — because of an unrealistic offer, for example — it's important not to "sweeten" the offer until the other side has countered with a meaningful compromise. By increasing the amount of your offer (or decreasing the amount of your demand) without any movement from the other side, you are making a gesture that will always be viewed as a form of weakness.

Don't make your best offer first. Some people think that offering their real "bottom line" and threatening not to budge will shorten the costly negotiating process. But this works only if the other side believes the threat and does not test it by "shaking the tree." If they don't believe you (and they usually don't), the process goes on and both sides still incur the costs they wanted to avoid. More importantly, the party who gave its best offer first will almost always change that offer if the other side comes close. Giving your best price too early also prevents you from shaking the tree.

Don't sell your case. Many business owners want their lawyers to trumpet the strengths of their case and catalog their opponent's weaknesses. This is probably because the technique is so similar to how most businesses sell products and services. But in litigation, you often don't want to educate the other side.

Force your opponent to spend money. Like you, your opponent is spending money for attorney's fees that they would rather spend on something else. Increasing the investment reduces the return, which diminishes the desire to go forward.

Litigation almost always disrupts a person's business and personal life. A deposition, for example, can really inconvenience someone, and it's worth considering its disruptive effect on your opponent when planning your strategy.

Divide and conquer. Nothing makes a client more willing to give up than losing confidence in their lawyer. If you can frustrate the other lawyer's strategy through motions or delay, your opponent will begin to doubt the reliability of his lawyer's judgment and predictions.

Similarly, your lawyer can work behind the scenes to make the other side's lawyer think that his or her client has not told the whole story. This lowers the lawyer's motivation to give optimistic predictions, which may in turn encourage your opponent to settle.

Doing nothing is sometimes the best strategy. Not responding to a settlement proposal is a dramatic way of stating that it is not acceptable. ■

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