NOTES
RISK-PREFERENCE ASYMMETRIES IN CLASS ACTION LITIGATION

The world is full of risks. One of the ways society seeks to reduce those risks is through the tort system.\(^1\) Anyone who has had the misfortune to be party to a lawsuit knows, however, that litigation itself is not without risks.\(^2\) Class action litigation is even riskier for litigants than the paradigmatic two-party case: the stakes are higher, the issues are more complex, and more people stand to lose. Class actions also pose risks to society. A well-calibrated class action system can deter costly accidents. But an erratic or skewed system can be dangerous: Imposing too much liability can destroy jobs and deprive consumers of desirable products. Imposing too little liability may leave corporations free to inflict tremendous harm on the public. This Note argues that improving the tort system’s ability to reduce societal risk requires managing individual risk preferences within the tort system itself.

Any comprehensive account of the class action tort system must be informed by an understanding of how people make decisions when confronted with risk. Traditional economic models often oversimplify reality by ignoring the role of lawyers in suit and settlement decisions\(^3\) and by attributing a stable risk preference — either risk neutrality or risk aversion — to litigants.\(^4\) Empirical research shows that human risk preferences are far more complicated. An accurate account of risk preferences is necessary because the natural frame of litigation creates risk-preference asymmetries that can yield inefficient outcomes. Furthermore, the attorney’s role in suit and settlement is central because many lawyers — particularly plaintiffs’ attorneys in class actions —

\(^1\) Professor Mark Geistfeld describes the compensation and deterrence functions of tort as tools of risk management: “The tort system reduces the risk of uncompensated injury in . . . giving victims monetary compensation for injuries that would otherwise be uncompensated . . . [and] inducing potential injurers to take safety precautions.” Mark Geistfeld, Should Enterprise Liability Replace the Rule of Strict Liability for Abnormally Dangerous Activities?, 45 UCLA L. REV. 611, 619 (1998) (emphasis added).

\(^2\) “It is a fact of life that litigation is risky and that a plaintiff with a claim to compensation for his losses must consider the possibility that the claim might be lost at trial, either wrongly, because of litigation error, or rightly, because the defendant was innocent.” Ford Motor Co. v. EEOC, 458 U.S. 219, 238 (1982).

\(^3\) See Ronald J. Gilson & Robert H. Mnookin, Disputing Through Agents: Cooperation and Conflict Between Lawyers in Litigation, 94 COLUM. L. REV. 509, 510 (1994) (“The economic literature, with rare exceptions, shares a troublesome feature. Almost by convention, litigation is modeled as a two-person game between principals, thereby abstracting away the legal system’s central institutional characteristic — litigation is carried out by agents.”) (footnote omitted).

have different risk preferences than their clients do. This Note applies
the vast body of empirical research on risk preferences to class actions
in order to provide insights and suggest reforms.

Part I applies prospect theory’s four-fold pattern of risk preferences
to class action litigants and concludes that plaintiffs and defendants
are likely to have asymmetrical risk preferences dependent on the
strength of the legal claims presented. Part I further argues that both
firms and plaintiffs’ attorneys are likely to have muted risk preferences
or to behave as if risk neutral.

Part II asserts that risk-preference asymmetries are of particular
concern in class action litigation because they may lead to settlements
that either overdeter or underdeter tortious behavior. Part III applies
the framework of risk-preference asymmetries to two commonly criti-
cized phenomena in class action litigation — blackmail and sweetheart
settlements — and finds that both scenarios emerge from low-merit
lawsuits. Finally, Part IV applies these insights to recommend reforms
likely to minimize the inefficiencies created by risk-preference
asymmetries.

I. RISK-PREFERENCE ASYMMETRIES

Litigation is risky by any definition. In economic terms, “risk”
simply “refers to a situation where the outcome is not certain, but
where the probability of each possible outcome is known or can be es-
timated.”5 Litigation presents risk because parties can estimate the
probability that a trial will result in one of at least two outcomes: a
finding of liability or no liability.

Because risk is an inherent feature of litigation, the parties’ atti-
dutes toward risk will inevitably affect their litigation decisions.
Commentators developing economic suit-and-settlement models often
rely on an expected utility theory that attributes risk neutrality or risk
aversion to both plaintiffs and defendants.6 These models fail to cap-
ture what empirics have long demonstrated: that plaintiffs and defen-
dants likely have asymmetric risk preferences.7 One basis for risk-

5 EDWIN MANSFIELD, MICROECONOMICS 521 (7th ed. 1991). For decision researchers,
“risk” is different from “uncertainty,” which exists when the outcome is not certain and the prob-
ability of each possible outcome is unknown.

6 See id. For purposes of this Note, “[a] risk averter is defined as one who, starting from a
position of certainty, is unwilling to take a bet which is actuarially fair.” KENNETH J. ARROW,
ESSAYS IN THE THEORY OF RISK-BEARING 90 (1971). A risk-neutral person is indifferent be-
tween the certain payment and the actuarially identical bet. A risk seeker prefers the gamble to
the sure payoff.

7 For a justification for using an empirical account rather than the simplified and normatively
attractive models traditionally used, see Amos Tversky & Daniel Kahneman, Rational Choice and
the Framing of Decisions, 59 J. BUS. 251 (1986), which argues that “the deviations of actual be-
havior from the normative model are too widespread to be ignored, too systematic to be dismissed.
preference asymmetries between plaintiffs and defendants emerges from prospect theory, an empirically demonstrated account of how people make decisions in uncertain situations. Prospect theory posits that human decisions vary based upon certainty, probability of outcome, magnitude of outcome, and framing of the potential outcomes as gains or losses. Among the most robust empirical findings in the field is the four-fold pattern (FFP) of risk preferences. According to this theory, an individual’s risk preferences emerge from two assessments: whether the individual views the potential outcomes as gains or losses, and the probability that the individual attributes to each potential outcome. As set out in Table 1, empirical data suggests that people are generally (1) risk averse about high-probability gains, (2) risk averse about low-probability losses, (3) risk seeking about high-probability losses, and (4) risk seeking about low-probability gains. Of course, the theory does admit some variation in preferences between individuals, but in the aggregate, the FFP of preferences is stark.

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<th>Low Probability</th>
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<th>Loss</th>
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The exact reason that people consistently exhibit these preferences is unclear. Professors Amos Tversky and Daniel Kahneman explain as random error, and too fundamental to be accommodated by relaxing the normative system.” Id. at S252.

8 See generally Daniel Kahneman & Amos Tversky, Prospect Theory: An Analysis of Decision Under Risk, 47 ECONOMETRICA 263 (1979) (providing the first account of prospect theory); Amos Tversky & Daniel Kahneman, Advances in Prospect Theory: Cumulative Representation of Uncertainty, in CHOICES, VALUES, AND FRAMES 44–65 (Daniel Kahneman & Amos Tversky eds., 2000) [hereinafter Advances in Prospect Theory].

9 These findings refine traditional expected value analysis, which attributes stable preferences to actors. For general descriptions and evaluations of theories designed to compensate for the lack of “empirical accuracy of expected utility (EU) theory,” see David W. Harless & Colin F. Camerer, The Predictive Utility of Generalized Expected Utility Theories, 62 ECONOMETRICA 1251 (1994). See also Advances in Prospect Theory, supra note 8, at 45–46 (identifying empirical observations that contradict expected utility theory’s assumptions).

10 See Advances in Prospect Theory, supra note 8, at 54.

11 For example, if a person is given a choice between a 70% shot at $100 or a certain award of $70, he will normally choose the certain $70. On the other hand, if forced to choose between paying a $70 fee or taking a 70% chance of having to pay a $100 fee, he will normally choose to gamble and face the 70% chance of paying the $100 fee. When people face low-probability outcomes, however, their risk preferences flip. If given a choice between a 5% chance of winning $100 or a certain $5 award, a person will normally choose to gamble on winning the $100. If forced to choose between paying $5 or facing a 5% chance of paying $100, a person will normally prefer to pay the certain $5 fee.

12 See Advances in Prospect Theory, supra note 8, at 55.
that their findings are intended to provide “a descriptive, not a normative, theory.”13 One possible explanation is “the principle of diminishing sensitivity,” in which “the impact of a change diminishes with the distance from the reference point.”14 According to this principle, individuals are more sensitive to probabilities close to the reference points of 100% and 0% than to probabilities far from a reference point. For example, a person might be willing to pay more to reduce his chances of suffering some risky event from two percent to one percent than from 52% to 51%.

Perhaps the best explanation for the FFP is that people overweight low probabilities and underweight high probabilities. People get very worried about low-probability losses and very excited about low-probability gains. Real-world markets have developed in response to these common human desires: people can buy insurance against the risk of their houses burning down — a highly improbable event — and can buy tickets for lotteries they, sadly, have a similarly small chance of winning. Although the “rational” explanation for the FFP of risk preferences is elusive, its presence is difficult to deny.

A. Litigant Risk Preferences

The FFP suggests that a litigant’s risk preferences turn on his estimated probability of success in litigation and his characterization of the potential outcome as a gain or a loss. Litigation provides a natural frame for gains and losses. Intuitively, a plaintiff sees the outcome of a suit as a potential gain, while a defendant sees the outcome as a potential loss. If the plaintiff wins, he gets paid; if he loses, he does not have to pay. If the defendant loses, he has to pay; if he wins, he stays even.15

Because a plaintiff views the outcome as a potential gain, prospect theory suggests he will be risk averse about suits in which he has a high probability of success (high-merit suits) and risk seeking about

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13 Id. at 65.
14 Id. at 50.
15 Some might argue that a plaintiff should not view a tort suit as a gain but should instead assess the situation based on his entire experience with the defendant. If he loses the suit, he has in fact lost because of the loss imposed by the tort itself. Studies show, however, that people quickly internalize previous gains and losses. Cf. Amos Tversky & Daniel Kahneman, Loss Aversion in Riskless Choice: A Reference-Dependent Model, in CHOICES, VALUES, AND FRAMES, supra note 8, at 143, 145 (describing “an endowment effect which is produced, apparently instanteously, by giving an individual property rights over a consumption good”). By the time a suit arises — often years after a tort occurred — a plaintiff has already internalized the previous loss. Thus, the plaintiff views the suit in isolation as a potential gain. Similarly, a defendant, having internalized any gains from the tort itself, is more likely to view the suit as a potential loss than as a gain derived from externalizing the loss on the plaintiff.
suits with a low probability of success (low-merit suits). Conversely, because a defendant views a suit as a potential loss, he will be risk seeking about suits in which he has a high probability of defeat (high-merit suits) and risk averse about suits with a low probability of defeat (low-merit suits). Thus, the FFP of risk preferences translates into the litigation setting as set out in Table 2.

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Empirical research supports this application of prospect theory to the suit-and-settlement model. Professor Jeffrey Rachlinski, in presenting his “framing theory of litigation,” demonstrates that plaintiffs are risk averse and defendants are risk seeking in high-merit suits. Professor Chris Guthrie completes the application of prospect theory with a “frivolous framing theory” demonstrating that risk preferences were reversed in low-merit suits. Experimental research thus confirms what prospect theory predicts: litigants’ risk preferences diverge depending on whether they are the plaintiff or the defendant and on the probability that a suit will succeed at trial.

This risk-preference asymmetry likely makes a difference in settlement negotiations. As Professors Robert Mnookin and Lewis Kornhauser explain: “In any negotiated outcome, a risk preferer will have an advantage over the party who is risk-averse.” Litigation risk preferences thus create perverse results: plaintiffs with shoddy claims have a negotiation advantage, and plaintiffs with strong claims face a

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16 For simplicity, this Note assumes that a suit’s merit determines whether it will succeed and that parties are reasonably adept at judging the strength of legal claims.
18 See id. at 135–38 (finding that plaintiffs showed risk aversion and defendants showed risk seeking in an experimental property dispute with a moderate-to-high probability of plaintiff success); id. at 150–60 (finding consistent results in an analysis of actual jury verdicts and settlements).
20 See id. at 188–90. In this experiment, plaintiffs who were offered a certain $50 settlement from the defendant or a 1% chance of winning $5000 at trial chose the risk-seeking option of going to trial 62% of the time. Conversely, defendants who were offered a certain $50 settlement to the plaintiff or a 1% chance of losing $5000 at trial chose the risk-averse option of paying the settlement 84% of the time. Id. at 189. Another more complicated experimental design yielded consistent results. See id. at 190.
negotiation disadvantage. Consider the low-merit suit with the risk-seeking plaintiff and the risk-averse defendant. Suppose both parties understand that the plaintiff has a five percent chance of winning $100 million at trial. Whereas some theories suggest that symmetric information will enable parties to reach an actuarially fair settlement of $5 million, prospect theory suggests asymmetric risk preferences may cause things to go awry. A risk-seeking plaintiff has psychological leverage over the risk-averse defendant. His greater willingness to go to trial means that the defendant must pay him a risk premium above the expected value of $5 million to induce him to settle. The defendant’s deep aversion to going to trial makes him willing to pay that premium. Empirical work could quantify the necessary premium, but the key point is that in low-merit class action litigation, settlements are likely to be systematically higher than the expected value of proceeding to trial.

B. Firm Risk Preferences

The assumption thus far has been that firms’ risk preferences resemble those of individuals. Because defendants in class actions have allegedly harmed a large group of people, they are almost by definition firms. But the diffuse decisionmaking procedures in firms make questionable the applicability of typical risk-preference profiles.

As a technical matter, “[c]orporations may act ‘as if’ they are risk averse, but as legal fictions, they cannot be risk averse.” Risk preferences inher in human decisionmaking, and our understanding of those preferences emerges from studies of individuals. Shareholders drive firms to maximize profits, so the market would punish any corporation that consistently succumbed to managerial risk preferences at

22 The merits of the suit also affect relative advantage, but risk preferences act as a drag on strong suits and wind at the back of weak suits. The plaintiff with a weak claim may still be at an overall disadvantage, but his risk-seeking behavior increases his relative level of negotiating power.

23 “[O]ne of the most potent sources of power a litigant can possess is a greater tolerance for risk than his adversary.” Guthrie, supra note 19, at 192.

24 Even if the defendant was risk neutral, he would be willing to pay some premium over the actuarially fair settlement to avoid trial costs.

25 See Guthrie, supra note 19, at 192 (“Assuming that defendant’s inflated offer exceeds the plaintiff’s inflated demand, the parties to a frivolous suit are likely to settle for an amount greater than the expected value of the claim, thereby benefiting the plaintiff.”).

26 See Fed. R. Civ. P. 23(a) (permitting class certification only if “the class is so numerous that joinder of all members is impracticable”).

27 Charles Silver, “We’re Scared to Death”: Class Certification and Blackmail, 78 N.Y.U. L. Rev. 1357, 1411 (2003). Similarly, a corporation cannot be risk seeking but may act as if it is risk seeking. Professor Silver thus cautions against assuming that corporations are risk averse in litigation. He suggests that while there is “a credible basis for thinking that corporations sometimes make economically rational decisions that seem to be driven by risk aversion,” there is little strong evidence that class action defendants are in fact risk averse. Id. at 1408–16.
the cost of profit-maximizing behavior. Moreover, liability insurance offsets firms’ potential risk-averse behavior because damages will be paid by an insurer rather than the company. It is thus reasonable to assume that “most [firms] are organized and operated to respond in a relatively risk-neutral fashion to all sorts of major business uncertainties, including those posed by civil litigation.”

Despite the incentives for risk neutrality, corporations are ultimately managed by flesh-and-blood individuals, so the FFP of risk preferences could bleed into corporate decisionmaking. But even if a corporate defendant neutralizes the risk preferences of its managers, plaintiff risk preferences will endure. In low-merit suits, plaintiffs will derive an advantage from greater risk tolerance, and in high-merit suits, defendants will reap the benefits of greater risk tolerance.

| Table 3 |
|------------------|------------------|------------------|------------------|
| Plaintiff Firm   | Defendant Advantage |
| Low-Merit Suit   | Risk Seeking      | Risk Neutral     | Plaintiff        |
| High-Merit Suit  | Risk Averse       | Risk Neutral     | Defendant        |

25 Cf. Michael Abramowicz, On the Alienability of Legal Claims, 114 YALE L.J. 697, 749 (2005) (“Large corporations, for example, may be relatively risk-neutral, especially because they are generally held by shareholders in diverse portfolios.”); David Charny & G. Mitu Gulati, Efficiency-Wages, Tournaments, and Discrimination: A Theory of Employment Discrimination Law for “High-Level” Jobs, 33 HARV. C.R.-C.L. L. REV. 57, 84 n.25 (1998) (noting that “the assumption of risk-averse firms is not very believable in a world of nearly perfect capital markets with investors who hold diversified portfolios”). Risk aversion might make economic sense when the firm’s ultimate survival is at stake, but “many class actions pose no practical risk of catastrophic loss.” Silver, supra note 27, at 1412.

29 See Bruce Hay & David Rosenberg, “Sweetheart” and “Blackmail” Settlements in Class Actions: Reality and Remedy, 75 NOTRE DAME L. REV. 1377, 1403 n.51 (2000); Silver, supra note 27, at 1414–15. On the other hand, one might question why a risk-neutral firm would purchase liability insurance — a tool used to shift risk — in the first place. Perhaps “[t]he idealized firm in law and economics is risk neutral, [but] because shareholders can manage risk by diversification in financial markets[,] . . . firms purchase insurance either because risk averse managers suffer agency problems, or because insurance provides some benefit other than shifting risk.” Michael J. Meurer, Law, Economics, and the Theory of the Firm, 52 BUFF. L. REV. 727, 736 n.37 (2004) (citing Stephen D. Sugarman, Doing Away with Tort Law, 73 CAL. L. REV. 555, 574 (1985)). It makes sense that managerial risk aversion might create firm risk aversion because unlike shareholders who can diversify their capital investments, managers cannot diversify their human capital. See Abramowicz, supra note 28, at 749 & n.217.

30 Hay & Rosenberg, supra note 29, at 1403 n.51.

31 Some studies indicate that corporate actors do in fact make decisions consistent with the individual decisionmaking preferences predicted by prospect theory. See, e.g., William J. Qualls & Christopher P. Puto, Organizational Climate and Decision Framing: An Integrated Approach to Analyzing Industrial Buying Decisions, 26 J. MARKETING RES. 179, 191 (1989) (analyzing managerial purchasing decisions).
C. Attorney Risk Preferences

To complete a realistic picture of the risk preferences at work in the class action, one must consider the role of attorneys. Class counsel’s risk preferences likely diverge from the class because, unlike his clients, the counsel faces a potential loss from litigation costs if the claim fails. Nevertheless, the risk preferences of class counsel may not have a significant effect for two reasons: lawyers’ analytical approach may diminish the influence of risk preferences, and diversifying through a portfolio of suits can approximate risk neutrality.

Attorneys are generally barred from financially aiding their clients, but ethical rules permit lawyers to advance litigation costs. Because of this dynamic, the plaintiffs’ lawyer — unlike either of the parties — operates in a mixed decision frame. For the lawyer, a suit represents neither just a potential gain nor just a potential loss, but the potential for either. Win big at trial, and the lawyer walks away with a handsome gain. Lose, and the lawyer has emptied his pockets and feels a tangible loss. According to prospect theory, in which the utility an actor attributes to an option depends upon his framing of an outcome as a potential gain or loss, the presence of a mixed decision frame distinguishes the lawyer from the client.

The consequences of this divergence are unclear, as mixed decision frames are not well understood. Prospect theory assumes that individuals facing mixed decision frames will assess a mixed decision as the sum of the independent valuations of the gain and loss portions of the decision. If this assumption is true, then class counsel’s risk preferences are aligned with those of class members.

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33 See MODEL RULES OF PROF'L CONDUCT R. 1.8(e) (2004).

34 In a mixed decision frame, rather than all of the potential outcomes being positive or all of the potential outcomes being negative, there is at least one positive and at least one negative outcome.

35 See George Wu et al., Decision Under Risk, in BLACKWELL HANDBOOK OF JUDGMENT AND DECISION MAKING 399, 416 (Derek J. Koehler & Nigel Harvey eds., 2004) (“The little research on mixed gambles is particularly surprising since most real-world gambles involve some possibility of gain and some possibility of loss, at least relative from the status quo.”).

Recent research, however, has cast doubt on the value of prospect theory in the domain of mixed decisions. Some research suggests that mixed decision frames will always lead to increased risk aversion. If that finding is true, class counsel’s involvement should diminish risk-preference asymmetries in low-merit suits but should exacerbate risk-preference asymmetries in high-merit suits. Whether the influence of plaintiffs’ lawyers on the risk-preference problem is positive or negative thus depends on assumptions about the general merit of class action lawsuits. If most class actions have a small chance of success, the role of the plaintiffs’ lawyer is beneficial, pushing the plaintiff toward risk aversion and closing the risk-asymmetry gap. If most class actions have a high probability of success, then the plaintiffs’ lawyer unfortunately widens the risk-asymmetry gap.

Because the evidence about mixed gambles is, well, mixed, one might worry about the complex interaction of lawyer risk preferences with client risk preferences. Fortunately, theory and experimentation suggest that lawyers may, in their professional capacity, be able to eschew risk preferences and make nearly risk-neutral judgments. Giving attorneys greater decisionmaking power could, therefore, effectively diminish risk-preference asymmetries in all cases, which would encourage class action settlements closer to social optimality.

There are two ways in which lawyers are better able than their clients to approximate risk neutrality. First, attorneys can diversify against risks. For a class member, each trial is an all-or-nothing bet, so he must bear all the risk. Class counsel, by contrast, can diversify against risk much like an insurer can. Just as “a purchaser of tort claims [in a market for claims] may be able to diversify — for exam-

37 See id. at 3–4 (finding that subjects preferred sets of gains and losses differently when valued independently than when valued together in a mixed gamble).

38 See John C. Hershey & Paul J.H. Schoemaker, Probability Versus Certainty Equivalence Methods in Utility Measurement: Are They Equivalent?, 31 MGMT. SCI. 1213, 1226 (1985). Loss aversion, a prospect-theory finding that individuals weight potential losses more heavily than potential gains, may contribute to the mixed decision frame result. The increase in risk aversion may be enhanced for plaintiffs’ counsel in the class action context by the fact that the baseline is a risk-seeking potential-gains frame.

39 “[A]n insurer diversifies risks by accumulating insurance contracts for uncorrelated risks, and then by investing premiums in common stock or other assets whose investment risks are uncorrelated, or by reinsuring (hiring other insurers to perform the diversification function).” George L. Priest, The Current Insurance Crisis and Modern Tort Law, 96 YALE L.J. 1521, 1542 (1987). Similarly, a plaintiffs’ attorney can diversify risks by taking on contingent-fee interests in tort claims with uncorrelated risks. See Janet Cooper Alexander, Contingent Fees and Class Actions, 47 DEPAUL L. REV. 347, 350 n.14 (1998) (“[C]ontingent fees allow the lawyer to spread risk by diversifying . . . .”); Alon Harel & Alex Stein, Auctioning for Loyalty: Selection and Monitoring of Class Counsel, 22 YALE L. & POL’Y REV. 69, 113 (2004) (describing how “attorneys who run portfolios of cases (including class actions)” hope to “diversify the risk” of new information causing bad outcomes in cases by assuming it will cause good outcomes in other cases in their portfolios).
ple, by purchasing a variety of different tort claims, some of which will be more successful than others — a plaintiffs’ lawyer, who in effect owns a piece of each claim through contingent fee arrangements, can diversify by holding a portfolio of claims of differing strength. The increasingly sophisticated plaintiffs’ bar has grown adept at assuring a constant stream of income by diversifying its set of claims and the risk that any particular claim represents. When the attorney is effectively diversified, there is less risk presented by any single case, and the lawyer, facing less overall risk, can make decisions less influenced by risk preferences.

Some research also suggests that lawyers — even in individual cases — are less influenced by risk preferences than their clients are. Though experts often prove susceptible to cognitive heuristics that cause them to depart from expected value analysis, a series of studies that presented litigation decisions to potential litigants and practicing lawyers found that “certain cognitive and social-psychological phenomena that can distract from expected value analysis are more likely to influence litigants” than their lawyers.

In particular, one experiment tested the influence of these risk preferences on litigant and lawyer test subjects, hypothesizing that litigants “would be more likely to favor the certainty of a settlement over the risk of the trial if the settlement is coded as a gain, rather than a loss.” Presented with the choice of settlement or trial, the litigants (as prospect theory predicts in the sort of high-merit suit used in the experimental case) were risk averse when they viewed the outcomes as potential gains and risk seeking when they viewed the outcomes as potential losses. Despite the statistically significant effect on litigants, the “experimental manipulation had virtually no effect on the lawyer subjects.” The studies’ authors suggest several reasons why lawyers might be less vulnerable to risk preferences: selection through law school admissions processes that reward analytical skills, training through law school techniques that emphasize analytical rigor, and

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40 Abramowicz, supra note 28, at 736.
43 Korobkin & Guthrie, supra note 41, at 96.
44 See id. at 96–99.
45 Id. at 100.
practice through repeated employment of actual expected value analysis.\footnote{Indeed, self reports from the study showed some of the lawyers actually made their decisions using expected value analysis. See id. at 101. Whether such techniques transfer into actual practice is unknown.} Even without any definitive explanation for attorneys’ behavior, this finding assuages some of the concern about risk-preference asymmetries by providing a figure closer to the risk-neutral ideal.

II. WHY RISK-PREFERENCE ASYMMETRIES ARE PROBLEMATIC IN MASS TORT CLASS ACTIONS

The disparity between parties’ risk preferences is troublesome because it subverts one of the central goals of the mass tort class action: minimizing the sum of the cost of accidents.\footnote{By internalizing the sum of the cost of accidents and the cost of avoiding accidents on the potential tortfeasor, the party is deterred ex ante from taking any risks that are not outweighed by benefits. See David Rosenberg, Decoupling Deterrence and Compensation Functions in Mass Tort Class Actions for Future Loss, 88 VA. L. REV. 1871, 1880 (2002). For a general account of this public-regarding purpose of tort law, see GUIDO CALABRESI, THE COSTS OF ACCIDENTS: A LEGAL AND ECONOMIC ANALYSIS 26 (1970).} When a party’s idiosyncratic risk preferences — activated by the particular frame that our litigation system creates — increase or decrease the size of a settlement, it either overdeters or underdeters the defendant’s tortious behavior. This suboptimal deterrence will almost inevitably lead to some additional harm.

Using prospect theory, first consider the high-merit suit, in which a plaintiff, facing a high-probability gain, will be risk averse and the defendant, facing a high-probability loss, will be risk seeking. Suppose the parties have symmetric information about the likely outcome of a trial, agreeing that the class has an 80% chance of winning $100 million dollars at trial. Therefore, the class’s expected value at trial is $80 million. Despite this expected value, the class’s risk aversion will drive it to give up some of its settlement to lock in a gain. Conversely, a risk-seeking defendant must get extra concessions from the class to give up the chance of avoiding liability at trial. The likely settlement is therefore some amount below $80 million, meaning that the defendant will not internalize the full cost of the damages it caused. This scenario leads to suboptimal deterrence, with future potential defendants causing more harm because they do not expect to bear the full costs of the damage they inflict.\footnote{This analysis assumes that the expected value at trial is the optimal deterrent. This assumption may be unlikely, but this Note presumes that expected trial value is the best available metric for measuring optimal deterrence.}

Risk-preference asymmetries in a low-merit suit produce similar inefficiencies. Assume both the class and the defendant recognize that the class has a 10% chance of winning $100 million at trial, an ex-
pected value of $10 million. If the defendant offers the class $10 million, a risk-averse or risk-neutral plaintiff will snap up the offer. But in a low-merit suit, the plaintiff is risk seeking and will opt to go to trial. To induce the plaintiff class to forgo trial, the risk-averse defendant must offer a premium above the socially optimal settlement value of $10 million. Firms will build this excessive liability into their production decisions, which will lead to higher prices or less availability of socially valuable goods.

When risk preferences drive settlements, the class and the defendant benefit because integrating those preferences into settlements increases the utility the parties derive from the litigation. The cost of satisfying those preferences, however, is to increase the cost of accidents to society. Even with rigorous empirics, it is difficult to determine how much difference risk asymmetries actually make. Nevertheless, when dealing with class actions — in which enormous sums are at stake — even slight deviations from the optimal settlement figure can bring about substantial spikes in the societal costs of accidents.  

III. APPLICATION OF PROSPECT THEORY TO TWO CLASS ACTION CRITICISMS

The application of prospect theory to class actions demonstrates that, theoretically, risk-preference asymmetries can create social cost. This finding is not surprising. It is surprising, however, that several common critiques of class actions can be explained by reference to differing risk preferences.

A. Blackmail Settlements

An oft-repeated criticism of the class action system is that it allows plaintiffs with meritless suits to “blackmail” defendants into settling for more than their claims are actually worth.  The most common blackmail scenario, famously articulated by Judge Posner in *In re Rhone-Poulenc Rorer Inc.*, goes like this: If each plaintiff files a separate, worthless claim, defendants will never compromise, defeating these suits at trial. Implicit in this theory of blackmail is the assumption that the underlying suits have little chance of success without aggregation of claims.  

49 See George L. Priest, *Procedural Versus Substantive Controls of Mass Tort Class Actions*, 26 J. LEGAL STUD. 521, 542 (1997) (arguing that the “importance of precision in damages valuation cannot be overstated,” for otherwise “defendants will be encouraged to engage in socially excessive accident-causing behavior” or “reduce the value created for society from the activity implicated in the lawsuit”).

50 For a thorough description of various theories of class action blackmail, see Silver, *supra* note 27, at 1360–85.

51 51 F.3d 1293 (7th Cir. 1995).

52 Implicit in this theory of blackmail is the assumption that the underlying suits have little chance of success without aggregation of claims. See *id.* at 1298 (noting that “the defendants have
action, however, the potential damages become enormous. Rather than confronting each claim individually, class certification forces defendants into an all-or-nothing gamble. There is an infinitesimal chance that the defendants will lose, but the threat of crushing liability and probable bankruptcy is too risky. In the face of such risk, defendants pay to settle claims that are worth nothing.

Prospect theory suggests that Judge Posner’s intuitions may be correct — for a limited class of claims. Posner describes a world in which defendants are outrageously risk averse and willing to part with their money despite an infinitesimal chance of defeat. Plaintiffs, faced with the same all-or-nothing gamble, show not risk aversion but complete willingness to proceed to a trial they are practically certain to lose. The risk profile that Posner describes only occurs when those potential gains and losses are low probability. In other words, Posner’s blackmail scenario probably exists only for those class actions that have exceedingly little merit.

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<thead>
<tr>
<th>TABLE 4: BLACKMAIL SUITS</th>
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<tr>
<td>Low-Merit Suit</td>
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<tr>
<td>Plaintiff: Seeking</td>
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<tr>
<td>Defendant: Averse</td>
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<tr>
<td>High-Merit Suit</td>
</tr>
<tr>
<td>Plaintiff: Averse</td>
</tr>
<tr>
<td>Defendant: Seeking</td>
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Notably, the risk-preference asymmetry Posner describes exists in any instance of frivolous litigation, not just in class actions. In all low-merit suits, defendants will be risk averse and plaintiffs will be risk seeking. Simple aggregation of claims should not change the expected value for either party; the probability of success and failure should remain the same. Nevertheless, the class action device does exacerbate the effects of risk-preference asymmetries by increasing the variance of the defendant’s potential outcomes.

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53 See id. (suggesting that defendants could “easily be facing $25 billion in potential liability”).
54 See id. at 1299 (explaining the court’s "concern with forcing these defendants to stake their companies on the outcome of a single jury trial"). Of course, individual plaintiffs in the separate claims process and plaintiff classes face the same all-or-nothing gamble. It is only mass tort defendants that have the advantage of spreading their potential risks over a series of trials.
55 Professor Silver marshals the evidence demonstrating that "risk aversion provides a crucial predicate for overpayment" in Posner’s scenario. See Silver, supra note 27, at 1373–75 ("Posner’s point appears to be that substituting a single class action trial for a series of individual trials increases variance and magnifies defendants’ aversion to risk, causing them to overpay."). This description is surprising — and unlikely, according to many — because one would expect markets to reward risk-neutral firms and punish risk-averse ones. See supra section I.B, pp. 592–93.
56 See Guthrie, supra note 19, at 187–88.
For instance, imagine a mass tort in which 100 plaintiffs each claim damages of $1 million. Suppose that in each case the plaintiff has a fifty-fifty chance of prevailing. If each plaintiff files a separate action, the expected value of going to trial is $100 million ($1 million x 0.5), or $50 million. In a class action trial, the expected value is the same: $100 million x 0.5, or $50 million. However, the number of potential outcomes is reduced to two: complete absolution from liability or total loss. In the separate action context, it is extremely unlikely that the plaintiffs will win every case or lose every case. Instead, the actual outcome will likely fall somewhere close to the expected outcome. In the class action, the actual outcome will be far from the expected outcome, win or lose.

In this way, the variance engendered by the class action magnifies the risk of the enterprise. In a low-merit suit, this increased variance will heighten the defendant’s risk aversion and the plaintiffs’ risk seeking. A risk-averse defendant would likely pay a high premium to avoid the variance of a class action trial. According to Judge Posner, that high premium is a “blackmail settlement[].” Of course, in a high-merit suit, the plaintiffs are likely to be the risk-averse party, giving the defendant an advantage in the settlement negotiations. In class actions in which the claims are well-founded, there is a different form of blackmail at work; defendants use the threat of trial to extort concessions from the risk-averse plaintiff class, leading to underdeterrence of tortious behavior.

To address concerns about blackmail settlements, Professors Hay and Rosenberg have suggested one reform to reduce the variance in—
volved in class action trials. Their proposal involves conducting a series of trials and averaging the verdicts to determine the aggregate recovery.\textsuperscript{62} Variance drops with this proposal as “the odds drop substantially that the class will recover nothing or that the defendant will lose everything.”\textsuperscript{63} The authors rightly note that their proposed regime comports with many norms of our legal system — and could be implemented rather painlessly\textsuperscript{64} — but their proposal is nonetheless a significant departure from current practice and is certain to face resistance. In addition, their proposal, while successful at reducing the role of risk preferences to that of the separate action process, fails to eliminate the distorting effect of risk preferences altogether,\textsuperscript{65} allowing blackmail settlements to continue to some degree.

Fortunately, the problem of blackmail settlements can be confronted through existing legal processes. The central point that prospect theory highlights is that the Posnerian notion of blackmail is not inherent in the class action; the threat of unfairly high settlements only emerges when the underlying action has little merit.\textsuperscript{66} Eliminating low-merit claims will eliminate any chance of blackmail. Weeding out low-merit claims through aggressive use of traditional tools like dismissals for failure to state a claim, summary judgment, and Rule 11 sanctions will significantly discourage the prospect of blackmail.\textsuperscript{67}

\textbf{B. Sweetheart Settlements}

Another critique of the class action system focuses on the notion of “sweetheart settlements” in which class counsel betrays the class by settling for an amount beneath the actual value of the plaintiffs’ claims.\textsuperscript{68} In exchange, the defendant rewards class counsel with more efficient contract. This is because variance measures risk, and risk neutral parties are indifferent to risk.

\textsuperscript{62} See Hay & Rosenberg, supra note 29, at 1404.

\textsuperscript{63} Id.

\textsuperscript{64} See id. at 1404–06.

\textsuperscript{65} The best solution would be to foster risk neutrality in both parties, allowing them to reach a socially optimal settlement that maximizes their utility and efficiently deters accident costs. Risk-neutral parties would not care about the variance of the class action. \textit{See} Alan Schwartz & Robert E. Scott, \textit{Contract Theory and the Limits of Contract Law}, 113 YALE L.J. 541, 576 (2003) (“A risk-neutral party cares about the mean of the interpretation distribution but not the variance. This is because the variance term measures risk while risk-neutral parties are indifferent to risk.”).

\textsuperscript{66} Professor Silver has suggested this “combination of conditions” necessary to engender blackmail settlements may not have even been present in \textit{Rhone-Poulenc} itself. \textit{See} Silver, supra note 27, at 1376.

\textsuperscript{67} Courts have already adopted such strategies due to general antipathy toward the class action. \textit{See} id. at 1399–1400 (noting that “[m]any [class actions] end in dismissals, not settlements” and listing statistics on class actions dismissed on motions or defeated on summary judgment).

\textsuperscript{68} For a summary of this critique, see Hay & Rosenberg, supra note 29, at 1399–91. \textit{See also} Bruce L. Hay, \textit{Asymmetric Rewards: Why Class Actions (May) Settle for Too Little}, 48 HASTINGS L.J. 479, 487–89 (1997) (proposing regulation of attorney’s fees to avoid the sweetheart
fees than he would have expected had the parties proceeded to trial.\textsuperscript{69}

Prospect theory suggests that sweetheart settlements may not be as prevalent as class-action critics suggest — or that many apparent sweetheart settlements better approximate social optimality than settlements plaintiffs would insist on absent counsel’s influence. Class action critics cite many instances in which class members object to a deal their counsel has struck, saying the settlement figure is too low.\textsuperscript{70} There are a number of benign explanations for such situations. For example, class counsel could simply be better at assessing the expected value of going to trial.

Prospect theory offers another benign account for an apparent sell-out by class counsel. By diversifying risk and approaching risky litigation analytically, class counsel may act as if they are risk neutral. In some cases, the lawyer’s risk neutrality conflicts with the client’s risk aversion or risk seeking, creating divergent opinions on the desirability of a proffered settlement.

This theory of risk-preference asymmetries predicts cases in which — if class counsel acts somewhat risk neutrally — the class wrongly objects that its lawyer has settled for too little. This problem would emerge in low-merit suits with risk-seeking plaintiffs. A risk-neutral class counsel is willing to settle for the expected value of trial and will not demand a risk premium to compensate the loss of utility from forgoing a risky trial. Risk-seeking clients, however, will perceive as inadequate any settlement offer that does not include a premium above the expected value of trial.

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<thead>
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<th>Table 5: Sweetheart Settlements</th>
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<tr>
<td>Low-Merit Suit</td>
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<tr>
<td>High-Merit Suit</td>
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\textsuperscript{69} This account assumes that courts are incapable of ferreting out these sweetheart deals because they cannot accurately assess the value of the claims. See Hay & Rosenberg, supra note 29, at 1391.

Such a scenario presents the fundamental conflict between the utility of the parties and the social utility we hope the tort system provides. In situations in which class and class counsel risk preferences diverge, it is true that the counsel's choice differs from what the class would choose if perfectly situated — with time, information, and expertise — to make the settlement decision. At the same time, however, the risk-prefering class would have opted for a socially suboptimal settlement. Its desire for risk would have driven the settlement above the true value of the lawsuit, overdeterring socially desirable conduct. By depriving the class of a settlement that maximizes its utility, class counsel may increase social utility.

As with blackmail settlements, sweetheart settlements should only occur in the realm of low-merit suits. When a suit has more merit, class counsel will have greater tolerance for risk and thus be more willing to avoid settlement and go to trial. That both of these phenomena emerge from low-merit suits is encouraging: it means that reforms can be targeted at this class of cases, reducing the likelihood that unintended consequences disrupt other features of the tort system.

In some cases, prospect theory flips the notion of sweetheart settlements on its head. When class members and counsel disagree over a proposed settlement, the client-attorney conflict may have nothing to do with collusion. Instead, the dispute may arise from the actors' differing attitudes toward risk. It might not be the class counsel that has the selfish incentives, seeking to profit at the expense of his clients, but rather the class members themselves who are selfish, seeking to satisfy their own risk preferences by externalizing increased accident costs on the larger society. Sometimes, sweetheart settlements might not be agency problems, but principal problems.

Undeniably, there may be situations in which greedy plaintiffs' lawyers and opportunistic defendants collude to deprive class members and enrich themselves. What this analysis questions is how prevalent that phenomenon really is. More specifically, it suggests that every class objection that a proposed settlement is too low should not be immediately accepted as evidence of a sweetheart deal. It could in fact indicate a situation in which plaintiffs, not their lawyers, have incentives contrary to the public interests of the tort system.

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71 It may seem troubling to label litigants “selfish” for trying to maximize their utility, because the proper functioning of our system depends on self-interested parties vigorously pursuing their claims. This term is used here because it is frequently applied to plaintiffs’ attorneys who are pursuing the same goal — maximizing their own utility — and because it accurately characterizes the fundamental dynamic at work when risk-preference asymmetries create the appearance of sweetheart settlements: plaintiffs seek a bigger payday despite the fact that a bigger settlement will inflict harm on society as a whole.
IV. CORRECTING FOR RISK-PREFERENCE ASYMMETRIES IN CLASS ACTION LITIGATION

At present, risk-preference asymmetries skew class action litigation outcomes, preventing the tort system from minimizing the cost of accidents. There are a number of reforms that could narrow or eliminate these asymmetries, leading to more efficient outcomes.

A. Increasing Class Counsel Control

As explained in section I.C, counsel are often the only risk-neutral players in a class action. Risk-neutral actors will systematically settle or go to trial based on their actual understanding of the probability of success. This prevents litigants from externalizing the costs of satisfying their risk preferences onto society. Any reforms that place greater decisionmaking power in the hands of plaintiffs’ attorneys are therefore likely to increase the efficiency of class settlements.

Two impediments to class counsel control allow settlements to veer off course. First, ethical rules place key litigation decisions — those most likely to be influenced by skewed risk preferences — in the hands of plaintiffs. For instance, plaintiffs control choices to accept or reject settlement offers, regardless of whether their investment in the litigation or the decision frame allows them to make a risk-neutral decision. Plaintiffs’ lawyers may feel constrained in their ability to settle for what their risk-neutral assessments dictate due to concerns that risk-biased class members will pursue bar discipline. Second, when courts are asked to approve settlements, courts may give class members undue deference because they do not recognize that plaintiffs’ risk preferences might skew their decisions away from the social optimum.

It is unclear how relevant these concerns are in practice. Many commentators have noted how quickly class members fade into the background in class actions. The named plaintiff has a small relative stake in the litigation and was probably selected by the plaintiffs’ attorney, so there is little chance that he will challenge the counsel’s settlement decision.

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72 See MODEL RULES OF PROF’L CONDUCT R. 1.2(a) (2004) (“A lawyer shall abide by a client’s decision whether to settle a matter”); see also Macey & Miller, supra note 32, at 42 (“Read literally, the ethics codes require class action and derivative lawyers to defer to the named plaintiff’s wishes.”).

73 See, e.g., Priest, supra note 49, at 560 (noting that “[f]ew plaintiffs in contingency-fee litigation . . . exert serious substantive litigation control” and that “[l]ack of plaintiff control, of course, is exacerbated in the context of a class action”); see also Macey & Miller, supra note 32, at 7–8 (“Because [class action plaintiffs’] attorneys are not subject to monitoring by their putative clients, they operate largely according to their own self-interest, subject only to whatever constraints might be imposed by bar discipline, judicial oversight, and their own sense of ethics and fiduciary responsibilities.”).

74 See Macey & Miller, supra note 32, at 41–42.
gation decisions, the risk-preference problem suggests that this arrangement should not make us uncomfortable.

Giving class counsel greater control could be socially beneficial regardless of the direction in which class members’ preferences are skewed. If plaintiffs are risk averse, their risk-neutral lawyer will push for a higher settlement that is closer to social optimality. If plaintiffs are risk seeking, the lawyer could overrule an aggressive push for trial that would drive the settlement away from social optimality. Professional rules should make explicit exceptions recognizing the unique role of class lawyers in serving both the interests of the named plaintiff and those of the public. Such an exception would not be so radical: such rules already provide similar exceptions for government lawyers, recognizing that conceptions of ethical representation must change based on the identity of the client. Perhaps more importantly, judges reviewing proposed class action settlements should be mindful of how these risk preferences affect class members’ choices.

B. Changing Class Members’ Decision Frames

If empowering attorneys is undesirable, other reforms could push plaintiffs themselves toward risk neutrality by changing their decision frames. Reforming plaintiff frames, however, is more complicated than empowering class counsel and may prove less successful.

Shifting class members’ frames to elicit risk neutrality is difficult because the reframing required may differ depending on the litigation’s merits. Blackmail and sweetheart settlements may be driven by low-merit litigation characterized by plaintiff risk seeking. Encouraging risk neutrality in those situations requires greater aversion, which can be achieved by making potential losses salient for plaintiffs. One method for achieving this goal would require plaintiffs to bear at least some portion of litigation costs themselves. Facing the prospect of trial, a plaintiff confronting the possibility of a loss from increased litigation costs will make far different choices in a mixed-decision frame than if he sees nothing but upside in the choice between settlement and trial.\(^75\) Rather than holding out for a risk premium, a class member bearing some of the costs will accept an actuarially fair settlement. Class counsel have already intuitively implemented this approach to some extent. Faced with recalcitrant clients who desire to push on to trial despite a generous settlement offer, plaintiffs’ attorneys have sometimes required clients to contribute to the costs of litigation before agreeing to go to trial.\(^76\)

\(^75\) Guthrie, supra note 19, at 212–14 (describing how requiring plaintiffs to bear their own litigation costs would make them more risk averse).

\(^76\) See id. at 214 & n.232 (citing Herbert M. Kritzer, Contingent-Fee Lawyers and Their Clients: Settlement Expectations, Settlement Realities, and Issues of Control in the Lawyer-Client
Forcing plaintiffs to bear some of the expenses of litigation obviously entails costs. First, this approach could make it more difficult for plaintiffs of limited means to pursue valid claims. Second, to the extent that the class’s litigation investment is limited by the plaintiffs’ ability to pay, plaintiffs will be unable to make the investment necessary to achieve optimal deterrence. This proposal, however, is unlikely to implicate seriously those concerns because it may only require plaintiffs to bear a small portion of the actual costs. All that is required for this strategy to succeed is for plaintiffs to conceive of their decision not solely in terms of potential gains. Prospect theory posits loss aversion — that individuals tend to weight losses more heavily than equally large gains. Therefore, even small potential losses might be salient enough to cause significant shifts in plaintiffs’ decision frames. Imposing nominal costs on plaintiffs could eliminate inefficient risk preferences while preserving access to justice.

Even a fairly dramatic reform like the cost-imposing method of frame shifting, however, will not eliminate all risk-preference asymmetry concerns. Although such an approach might effectively address inefficiencies caused by class risk seeking, it could exacerbate risk-preference asymmetries in high-merit litigation in which the class is unduly risk averse. But even in those situations, there are efficiency gains to be earned by directly affecting plaintiffs’ risk preferences through debiasing.

Once again, the risk-neutral plaintiffs’ lawyer can play a central role. To encourage clients to make decisions unaffected by risk preferences, class counsel can pursue several alternatives. A lawyer can simply share general information about decisionmaking that might be relevant to the situation without imposing his own value judgments. Similarly, the lawyer could encourage the client to view the settlement

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78 “Loss aversion refers to the fact that people tend to be more sensitive to decreases in their wealth than to increases . . . . Empirical estimates find that losses are weighted about twice as strongly as gains.” Richard H. Thaler et al., The Effect of Myopia and Loss Aversion on Risk Taking: An Experimental Test, 112 Q. J. Econ. 647, 648 (1997) (citing Amos Tversky & Daniel Kahneman, Advances in Prospect Theory: Cumulative Representation of Uncertainty, 5 J. Risk & Uncertainty 297 (1992)).


80 See Korobkin & Guthrie, supra note 41, at 115–16 (describing an experimental setup employing this strategy).
decision through a variety of frames by asking him to consider competing perspectives.81 More aggressively, the lawyer could recommend that the class accept a settlement, suggesting that the clients rely upon the lawyer’s judgment and experience.82 Class counsel could even provide an expected-value analysis that explains the reasoning behind his recommendation.83 Experimental use of these lawyer-influence techniques suggests that they can effectively bring client decisionmaking closer to the efficient outcome.84 In fact, attorneys already likely use some of these techniques to persuade their clients to agree with their judgments.85 Plaintiffs’ attorneys can use their role as intermediaries to communicate with class members in a way that dampens the inefficiencies engendered by divergent risk preferences.86

C. Increasing the Use of Class Actions

The inefficiencies created by risk-preference asymmetries exist in all litigation, not just class action litigation. In many ways, however, the increased use of class actions themselves can combat the pathologies of risk-preference asymmetries. Encouraging more class actions could promote optimal deterrence in two ways.

First, the requirements of a class action naturally shift control to a risk-neutral plaintiffs’ attorney.87 This truth is often cited with contempt because it may increase agency costs or decrease plaintiff autonomy. In focusing on the risk-preference asymmetry problem, however, one sees that risk-biased plaintiffs can create inefficiency after inefficiency if allowed to satisfy their risk preferences in the separate action

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81 See id. at 116–17; see also Linda Babcock et al., Creating Convergence: Debiasing Biased Litigants, 22 LAW & SOC. INQUIRY 913, 916 (1997) (“In the literature on debiasing, one type of intervention stands out as effective against a wide range of biases. This involves having subjects question their own judgment by explicitly considering counterarguments to their own thinking.”).

82 See Korobkin & Guthrie, supra note 41, at 118.

83 See id.

84 See id. at 120 (“At least in some circumstances, lawyers taking an active role in their client’s litigation decisionmaking processes probably can affect the extent to which psychological factors, as opposed to the comparison of the expected financial values of alternative litigation options, motivate litigants’ ultimate decisions.”).


86 Though class attorneys are likely best positioned to debias their clients because superior information allows them to determine the extent to which risk preferences are skewing client judgments, courts could also use debiasing techniques. In settlement conferences, judges could educate the parties about decisionmaking biases and encourage the parties to view decisions through various frames. See Babcock et al., supra note 81, at 922 (suggesting how a “relatively simple and inexpensive debiasing technique . . . could be incorporated into the routine efforts of courts to encourage pretrial settlement”).

87 See supra section IV.A, pp. 604–05; see also sources cited supra note 32.
process. The risk-neutral class counsel can negotiate an efficient settlement based on expected trial outcome rather than risk preference and apply those efficiencies across the class.

Second, in dealing with the specific problem of low-merit litigation, class actions can successfully shift the decision frame by increasing plaintiffs’ chances of success. Allowing plaintiffs access to litigation economies of scale through class actions encourages the class to make the optimal investment to maximize its recovery.\(^{88}\) In this way, a suit that might appear to have little merit if pursued through the separate action process can become a high-merit class action when cost-spreading allows investment in experts, aggressive discovery, and the like. As the suit’s likelihood of success increases, the decision frame also shifts, with plaintiffs becoming more risk averse and defendants becoming less so. Of course, it may be cold comfort to the defendant to avoid a blackmail settlement by paying an enhanced settlement because the class has improved its chances of success through increased investment. For society, however, accident costs can be reduced as deterrence is optimized through a settlement based on expected trial outcomes rather than risk preferences.

**CONCLUSION**

Class action critics have long been concerned that plaintiffs’ attorneys with selfish motives and skewed incentives craft settlements that disserve the public interest in deterrence. It now seems likely, however, that parties themselves will craft defective settlements because of risk-preference asymmetries. Resisting the ill effects of those asymmetries requires reforms like empowering class counsel or changing the decision frame in which class members operate. Without such changes, attitudes toward risk in litigation may undermine the deterrence of risks outside litigation.

\(^{88}\) See Rosenberg, *supra* note 77, at 415.