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# Opening offers – Who's on first?

## The opening offer sets the stage for the rest of the negotiation. Get it right.

In Abbott and Costello's classic baseball comedy sketch, "Who's On First," Costello was befuddled with keeping track of "Who" was on first base, and other players' names.

In negotiations, some say that it is best to wait for your opponent to make the first offer. One school of thought is that the recipient of the opening offer has the advantage of learning about his opponent's bargaining position and negotiating strategy.

Plaintiffs' attorneys are accustomed to making opening demands. At mediation, defense attorneys almost always want to hear the plaintiff's demand first. Some plaintiffs' counsel present a demand in advance of the mediation, to enable defense counsel to appear at mediation with an appropriate range of authority, pre-approved by the insurance carrier.

I would like you to consider that aside from what appears to be an industry custom of "plaintiff goes first," first offers – whether proffered by plaintiff or defense – have a profound psychological effect on how people react to the negotiation process. Recognizing this phenomenon is useful for crafting a demand that will lead to fruitful negotiations.

### Frame of reference

How a problem is perceived is the decision-maker's frame of reference. In a negotiation, several reference points might be available to a party, such as the status quo, a party's opening demand, the other side's initial offer, a statutory cap on damages, a settlement or a jury verdict reached in a similar case. Depending upon which reference point a party brings to the table, a negotiation outcome might be viewed (or framed) as a gain or loss. Whether a problem is seen in terms of a gain or loss may result from the language used to describe the problem.

If a solution is framed negatively (as one between losses), then people tend to be more risk-prone than if it is framed positively (as one between gains). Thus, if a solution to a problem is described as "saving lives" (gains), a decision maker is more likely to avoid risky behavior to "save lives." If the same problem is described as an effort to "avoid deaths" (losses), the decision maker will most likely determine a riskier plan of action to "avoid deaths," even though the potential outcome appears to be the same. The result is that people tend to be loss-averse. We would rather take more risk, such as go to trial, to avoid receiving what is perceived as a loss in a negotiation. In contrast, if a negotiation provides the hope of gains, we will take less risk to try to acquire larger gains.

### Anchoring

Counsel for plaintiffs and defendants (and their clients), each have their own reference points for the "value" of the case. Creating or altering an opponent's frame of reference is called "anchoring," because it creates a point to which the opponent is tied. Anchors are values that influence our thinking about possible outcomes, similar to reference points. However, reference points establish the neutral point between gains and losses, while anchors can be anywhere along the scale and are usually at the extreme ends of the scale. A relevant opening offer acts as an anchor, as it can pull our judgment of the offer's value towards that number. Any concession during negotiations should be characterized as a gain for the opponent, which the opponent should not risk losing.

Negotiators are often influenced by an anchor that they know (or should know) to be irrelevant, such as an outrageously high or low offer. Even experts are not immune to the anchoring effect.

Law professors, Chris Guthrie and Jeffrey Rachlinski, and U.S. Magistrate Judge Andrew J. Wistrich, tested for the effect of anchoring on federal magistrates, by providing them with a description of a serious personal injury suit in which liability was clear but the amount of damages was in dispute (Guthrie, Rachlinski and Wistrich, Inside the Judicial Mind, 86 Cornell Law Review 777 (2001)). Half of the judges were asked to indicate what they thought an appropriate damage award would be in light of the plaintiff's extensive injuries. The other half of the judges were asked the same question, but not until after they ruled on a motion to dismiss the case on the ground that the plaintiff failed to meet the $75,000 jurisdictional minimum for a diversity case. The motion had no merit, but the study found that the motion had a large effect on the judges' damage awards.

The judges who did not rule on the motion awarded, on average, $1,249,000. The judges who did rule on the motion awarded, on average, only $882,000. The frivolous motion to dismiss, which forced the judges to consider whether the case was worth more than $75,000, lowered damage awards by 29 percent. These results indicate that judges are affected by anchors, even those that seem unrelated to the likely value of the case.

### Constructing the first offer

In constructing your first offer, Professor Adam D. Galinsky suggests that

*See Diliberto, Next Page*

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there are generally two values on which you should focus:

First, consider your alternatives to agreement and create a reservation price (the number at which you'd prefer to walk away rather than reach a deal). Now you're prepared to accept a number that exceeds your reservation price and reject a number that falls below it.

Second, determine your ideal outcome, or target price (the number or values that fulfill your negotiation goals). Knowledge of your reservation price is crucial, but it is your target price that you should pay attention to when constructing a first offer.

Your first offer should keep your opponent engaged, so consider your opponent's alternatives to agreement and try to determine her probable reservation price (while being cognizant of trends in your field of law). Your first offer should be beyond your opponent's reservation price, but not so far outside as to disengage the recipient.

Be prepared to allow your opponent to extract concessions from you, a necessary part of the negotiation dance.

By making concessions, you avoid having your opponent experience "Winner's Curse," in which an offer is accepted too quickly. Victims of "Winner's Curse" are left with the unsatisfactory result of questioning their negotiation strategy, or wondering whether they misjudged the value of the case. People feel more satisfied with their negotiation outcome if they extract concessions (gains), and they are more likely to honor the final agreement and not seek additional concessions.

You can protect yourself against the anchoring effects of someone else's first offer by basing your counteroffer upon the same information you would use to construct a first offer: Your ideal outcome and your opponent's alternatives to settlement and likely reservation price.

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