Prospect Theory

I recently had the opportunity to hear Richard W. Painter speak at an American Bar Association Conference on Professional Responsibility. Mr. Painter was an associate White House counsel for ethics under President George W. Bush. He appeared on a panel with John Dean (President Nixon's White House Counsel) and discussed Watergate's effect on lawyering and legal ethics. It seems remarkable that forty years later the subject of Watergate remains compelling, especially for those who recognize its importance as a spur to the professionalization of lawyer discipline and the emphasis on professional responsibility in law schools.

Mr. Painter has studied "the psychology of cover-up." He determined that there is a psychological bias that fosters actions consistent with choosing the risk of a greater loss as against the certainty of a small loss. With respect to the Watergate cover-up, he said, "Many more people put themselves in jeopardy by engaging in a cover-up out of hope of not losing anything." Mr. Painter's research into the psychological basis for this observation is fleshed out in a 2000 Minnesota Law Review article (84 Minn. L. Rev. 1399), in which he sets forth findings of psychological research that identifies cognitive biases that cause decision makers to make choices that are not always "rational." He explained "prospect theory," which posits that decision makers are risk averse when deciding between two decisions that result in a gain, but risk preferring when deciding between two decisions that result in a loss. His simple example: A person confronted with a choice between (a) receiving $10 and (b) a one in two chance of receiving $20 is more likely to take the $10, but someone choosing between (a) a sure $10 loss and (b) a one in two chance of a $20 loss is more likely to take his chances. 84 Minn L Rev., at 1414.

In a litigation setting, Professor Jeffrey Rachlinski, cited by Painter, concluded: "People facing potential losses from litigation make riskier choices than people facing potential gains." Plaintiffs are risk averse when weighing settlement offers against taking their chances in litigation for even larger potential gains, whereas defendants are risk preferring when weighing the certain costs of a settlement offer against taking their chances in litigation that could result in even larger potential losses. *Id*.

Prospect theory would help explain a phenomenon of which my colleagues and I are all too familiar: The highly risky cover-up of misconduct ordinarily warranting a warning or minor sanction. In order to avoid a sanction for failing to communicate with clients, an absence of diligence or improper recordkeeping, attorneys have been known to forward to our office bogus or fraudulently altered documents. The risk of the much more substantial sanction, probably disbarment, is readily apparent. One might perceive such conduct as irrational, but certainly most lawyers in practice for any length of time are familiar with such conduct. While I cannot say that prospect theory explains, even to a great extent, the phenomenon of the cover-up or even the choices made in litigation settlements, it certainly is thought-provoking and can guide attorneys when they seek to manage client expectations.

Perhaps framing a settlement in terms of a “win” for the client may be more persuasive than framing a settlement as a mitigation of loss. Of course, the risks of exacerbating a difficult situation should be recognized and addressed in the course of any representation in which these issues are present. The lawyer's understanding of the possible bias against "rational" behavior could be invaluable in not only effectively representing clients but in assessing the lawyer's own conduct when faced with daunting choices.

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