

Setting a Course to Mediation Success: Understanding Information Asymmetry

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Our previous articles discussed how Navigator uses rigorous financial analysis, and evaluates risk aversion and excessive optimism, to achieve mediation success.ⁱ This article reviews the issue of information asymmetry in negotiating settlements.

The Problem of Asymmetric Information In Mediation

To settle a case, lawyers and their clients (“Parties”) on both sides must identify a compromise perceived to be more attractive than pursuing litigation outcomes. Divergent expectations of litigation outcomes will cause Parties not to settle.ⁱⁱ

Such divergent expectations are frequently the result of information gaps among the Parties: if one side has different or more information than the other side about liability, damage, or other variables, that creates a gap between the plaintiff’s net expected gain and the defendant’s net expected liability at trial.ⁱⁱⁱ Only full sharing of information will close that gap on the expected litigation outcome.^{iv}

Asymmetrical information can also permit a Party with “weak” claims or defenses to pass themselves off as having “stronger” positions and thereby reduce the middle ground for settlement.^v These problems occur even in complex bargaining environments where “signaling” occurs that reveals information disparities.^{vi}

Finally, there are two more well-known consequences of asymmetric information that reduce the chances of mediation success:

- Settlement positions of one Party are more likely to be discounted by the other side if based on undisclosed information; and
- Expectations of a likely litigation outcome by one Party are more likely to be inflated if unrebutted by the other side because of undisclosed information.

Why Do Parties Fail To Share Information In Mediation?

Parties should have strong incentives to share the information necessary to persuade the other side about the strength of their case and the value of their settlement position. Since all cases ultimately settle,^{vii} mediation can be the decisive event. Fully utilizing key information can enable Parties to achieve the best return on their investment in litigation.^{viii}

Nevertheless, there are numerous instances where Parties may be unwilling to disclose before trial some key facts or opinions still being developed or not yet uncovered by the other side, or work product that is the result of superior strategy or preparation.^{ix} As a result, it may be unrealistic to always expect information symmetry among the Parties in mediation given these strategic considerations.

Addressing Asymmetric Information In Settlement Negotiations

Even if the Parties will not fully share information initially with each other, some of the consequences discussed above can be mitigated if both sides share information first with the mediator on a confidential basis to support their respective settlement positions and agree to close the gaps as the Parties grow closer to compromise.

Moreover, some information can be productively utilized by each side in mediation even if it is not shared. That information includes each Party's net present value of its expected costs for litigating the case to trial, how that affects their expected outcome in the litigation, and what they are gaining/giving up in a settlement.^x

Conclusion

Navigator can help you set a course to mediation success by identifying the reasons for and the results of asymmetric information among the Parties, and how that imbalance can be addressed in ways consistent with the Parties' litigation positions.

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- i [Setting-a-Course-for-Mediation-Success.pdf \(navmas.com\)](#); <https://www.navmas.com/wp-content/uploads/2024/05/Navigator-Accounting-for-Risk-Aversion.pdf>; <https://www.navmas.com/wp-content/uploads/2024/05/Excessive-Optimism-In-Litigation-Outcomes.pdf>.
- ii Bruce Hay and Kathryn Spier, *Litigation and Settlement*, Harvard Law School John M. Olin Center for Law, Economics and Business Discussion Paper Series, p. 5 (1998), <https://citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=b7fe7c460503e395f43afea95cc924cac53dc9c0>. (“*Hay and Spier Article*”).
- iii Oren Bar-Gill, *The Success and Survival of Cautious Optimism: Legal Rules and Endogenous Perceptions in Pre-Trial Settlement Negotiations*, Discussion Paper No. 375 07/2002, p. 1-5 (The Harvard John M. Olin Discussion Paper Series: http://www.law.harvard.edu/programs/olin_center)(“*Bar-Gill Article*”); *Hay and Spier Article, supra*, at 6.
- iv *Hay and Spier Article, supra*, at 4; see also Brian Grenadier and Steven R. Grenadier, *The Valuation of a Dynamic Litigation Process: The Lawsuit as a (real) Option on an Option*, p. 18 (March 2024) (“*Grenadier Article*”), available at: <https://ssrn.com/abstract=4566390>.
- v *Hay and Spier Article, supra*, at 8; see also Keith N. Hylton, *Mutual Optimism and Risk Preferences in Litigation*, 75 INTERNATIONAL REVIEW OF LAW AND ECONOMICS PP. 2, 10 (2023).
- vi *Hay and Spier Article, supra*, at 7-8.
- vii *Grenadier Article, supra*, at 18.
- viii *Hay and Spier Article, supra*, at 8.

ix *Hay and Spier Article, supra*, at 8-9.

x [Setting-a-Course-for-Mediation-Success.pdf \(navmas.com\)](#).