

THURSDAY, AUGUST 29, 2024

PERSPECTIVE

## Actuarial case valuation in mediation

By Evelio Grillo

People often overlook that mediation is (or should be) a collaborative process. Often, the difficulty involved in identifying a range within which both parties are willing to discuss settlement arises from one or both parties feeling that by agreeing to a range or “bracket” they are compromising their settlement position. The problem is compounded when each party has a defensible settlement position derived from a particular method of case valuation, and yet the parties have no common basis for discussing how or why either party’s number should move up or down during settlement discussions. This is due in no small part to the fact that many, if not most, case valuation methodologies are not interactive, and do not facilitate the type of back-and-forth exchange and collaboration that are the hallmarks of the mediation process, and ultimately of a successful mediation. Actuarial case valuation can supply the missing elements—interaction and collaboration—and lead to a successful mediated resolution.

Actuarial case valuation is an interactive settlement technique that borrows from probability theory and uses actuarial principles to estimate the settlement value of the case based on each party’s estimate of the value of a case, however derived. The technique’s effectiveness is owed to a major premise underlying this technique: that a party is more likely to accept a



Shutterstock

number generated by a case valuation technique that incorporates a party’s beliefs, estimates and analysis of case value than one based solely on a mediator’s or opposing party’s valuation of a case. Commonly used case valuation methodologies such as computer models, verdict analysis, jury verdicts and experience gained trying similar cases are neither interactive, nor are they collaborative. Any number obtained through these techniques typically represents no more than a party’s decision to rely on a number derived from a methodology chosen without consideration given to the opposing party’s evaluation

of the case. These methods are neither interactive nor collaborative and can be an impediment to settlement.

Actuarial case valuation facilitates settlement by affording equal dignity to each party’s perspective and conclusions regarding the value of a case and by promoting interaction and collaboration between the parties in arriving at the fair settlement value of a case. This is how actuarial case valuation works:

The mediator during separate sessions with each party asks the party to provide the mediator with the party’s estimate of the highest potential verdict value and the low-

**Hon. Evelio Grillo (Ret.)** is a neutral at ADR Services, Inc.



est potential verdict value. In most (but not all) cases, the low verdict value will be 0, an acknowledgment of the potential for a defense verdict in any case. The plaintiff and defendants invariably (but not always) diverge on the high verdict value, but that is of no consequence. After obtaining each party's estimate of the low and high verdict value the mediator then asks each party (separately again) to provide their estimate of the most likely size of the verdict. If one or both parties cannot or are unwilling to provide an estimated "likely" verdict, the mediator averages the low and high values provided by each party and uses the midpoint between the two (low and high) to complete the analysis. After obtaining estimates of the potential verdicts from each party, the mediator then asks each party to estimate the likelihood of achieving each of the estimated verdicts after trial, expressed in terms of a percentage. With this information in hand, the mediator takes the product of each of the verdict estimates against the percentage or probability each party attaches to each verdict estimate - a simple mathematical calculation. Except in the case of an estimated verdict value of 0 (a pure defense verdict) the product of the high and low verdict estimates taken against their estimated probability will be lower than the unadjusted verdict estimate. The summation of the products of the low, high and midrange estimated verdicts adjusted for the probability of realizing each estimated verdict is the actuarial value of the case.

Here is an example of how the technique can be applied. Assume the plaintiff's estimate of the low verdict value is 0; and of the high verdict value is \$500,000; and of the midpoint or estimated probable verdict is \$250,000. Assume the plaintiff estimates the likelihood (i.e., the probability) of each verdict as 25% to the low verdict; and 25% to the midpoint or probable verdict; and 50% to the high verdict estimate. The actuarial valuation in this example (based on the plaintiff's assumptions) will be \$312,500, or  $(0 \times .25) + (250,000 \times .25) + (\$500,000 \times .50) = \$312,500$ , or  $(0 + \$62,500 + \$250,000)$ . Now assume that the defense agrees with the high and low verdict amounts,

but disagrees with probabilities attached to each, and estimates that the probability of a defense verdict (0) is 50%; and the probability of the high verdict (\$500,000) is 25%; and the probability of the midrange verdict (\$250,000) is 25%. In this example, the actuarial evaluation (based on the defense's assumptions) is \$187,500, or  $(0 \times .50) + (250,000 \times .25) + (\$500,000 \times .25) = \$187,500$ , or  $(0 + \$62,500 + \$125,000)$ . The range established by this exercise is \$187,500 to \$312,500, and the mediator has effectively bracketed the case, using each party's own numbers to establish a foundation for further settlement discussions. Both sides will rarely agree on the high and low verdict values, or on the size of a "likely" verdict. It doesn't matter. The mediator works with whatever estimated values and probabilities the parties provide to the mediator. The actuarial valuation obtained through the mathematical calculation above is unadjusted, i.e., it does not account for attorneys' fees, expert witness and discovery costs, or other litigation expenses. These types of hard litigation expenses can be incorporated into the settlement discussions with the parties and will usually have the effect of raising the low (defense) estimated case value and lowering the high (plaintiff's) estimated case value.

Actuarial case valuation adds value to the mediation process because it allows the mediator to estimate how far apart the parties actually are without having to make a subjective guess based on each party's initial demand. Settlement demands often represent a party's estimation of how high or low the starting point for settlement negotiations should be in order to leave room to move up or down during the mediation. Unrealistic demands or counteroffers—say two or three times or more times more than, or a small fraction of, the actuarial value of the verdict—are unproductive and may often stall settlement discussions. Worse yet, they can stalemate the mediation session or lead to a complete cessation of settlement discussions. Untethered demands and counter offers that do not reflect a realistic estimate of case value are often associated with or result from a party's adoption of posi-

tional bargaining as a negotiation strategy and are poison. In these types of situations, actuarial case valuation can be used by the mediator to more accurately determine each party's true valuation of the case, rather than having to rely on a number or numbers asserted by the parties solely to protect bargaining positions. The technique can also be used as a tool to break stalemate. Here is another example of this technique's usefulness.

When confronted with a party or parties who are threatening to terminate settlement discussions in the face of the opposing party's "unreasonable" demand or counter offer, the mediator requests the parties to participate in an exercise—actuarial case valuation—as a last ditch effort to help the mediator evaluate the parties' respective positions, or to determine whether mediation or settlement discussions should continue. In almost 100% of the cases both parties will give their consent, the "yes" to the mediator's request costing neither party either position nor loss of face. Working with the parties separately, the mediator completes the actuarial valuation and then discusses the results of the valuation separately with both parties. In most cases the valuation will yield one of three results.

Either the parties are truly so far apart, based on the underlying assumptions of each party about the case (sometimes likely, particularly where the parties are both engaging in extreme positional bargaining); or the parties are much closer to each other in position than either party would admit in absence of engaging in the valuation exercise (somewhat likely, and more likely than a walkaway number); or the exercise suggests a bracket that can be used as the basis for further discussions (always a possibility, and somewhat likely). Depending on the result, the mediator may continue settlement discussions using the results of the valuation to shape further settlement discussions, or in a truly deadlocked case, conclude discussions. Or, the mediator may ask the parties to vary their probability and verdict estimates to come up with alternate values as a means of keeping settlement discussions going. This effectively allows parties to lower or raise their settle-

ment demands without losing face or conceding weakness of position, or committing to a specific number too early in the settlement discussions.

Finally, when an actuarial case valuation is undertaken, there is always the possibility that the plaintiff's and the defendant's valuations overlap. When this occurs, a settlement is almost surely to result, as both parties generally will accept a number proposed by the mediator that is within the overlapping ranges of the plaintiff and the defendant.

When actuarial case valuation is used to bracket a case, typically the mediator should elicit verdict and probability estimates from the parties somewhat informally, and conduct the valuation analysis without initially disclosing to the parties how the case information will be used by the mediator. After the mediator has determined a range or bracket based on the information provided by the parties and the mediator's calculations, the mediator may then decide whether and when to disclose the bracket and how the mediator arrived at the range. Conversely, if the mediator is using actuarial case evaluation to break a deadlock or to keep parties negotiating, typically the parties should be told upfront that the valuation exercise is being conducted to help the mediator guide further settlement discussions or determine whether further settlement discussions are warranted at the time. In the latter case the parties are told that the valuation will be conducted to establish a bracket within which the parties should be willing to discuss settlement.

Irrespective of why the actuarial value is conducted, there are a few simple practices that must be followed in all cases in which actuarial case valuation is used. The first is to honor the parties' confidences. A party's disclosure of the probability the party attaches to a particular estimate of the size of a verdict, or the probability of a verdict is work product and should not be disclosed to the opposing party unless the party providing this information to the mediator clearly consents to the mediator doing so. The second practice suggests, but does not require in all cases, that the mediator initially share the re-

sults of the valuation with the parties separately. This allows a party to react to the mediator's conclusions privately and to share or disclose any information that may be relevant to the upcoming discussions, but which the party is unwilling to disclose to the opposing party at a particular stage of the mediation. The third practice requires the mediator disclose only the mediator's conclusions as to probable verdict value, and not the opposing party's conclusions and estimates as to case value.

#### So, Why Does Actuarial Case Valuation Work?

The actuarial case valuation process continues to provide value to the mediation and settlement process even in the face of software and AI programs that purport to evaluate the claims of litigants based on hundreds of variables and big data. While not to denigrate big

data analysis, modeling through the use of computers or similar methods of case analysis is just that -data analysis. Actuarial case evaluation on the other hand is an analytical process that is dynamic and promotes trust building and collaboration. This allows for intangibles such as judgment to be incorporated into the settlement process, and at some level psychologically vests the parties in the process and result -none of which occurs when case valuation is based solely on computer modeling or data analysis alone. Actuarial evaluation also requires a party to question the assumptions underlying the party's estimates of case value as, for example, when the probable verdict value as established by an actuarial case valuation is significantly lower or higher than one based solely on "experience," or the guess work of the at-

torney or client. Finally, an added benefit of actuarial case evaluation is that by utilizing the variables of probability and estimated value, the mediator (or the parties) can adjust the estimate of case value up or down as information developed during the mediation suggests that one or the other's estimate of the probability of verdicts of certain sizes requires adjustment. This could occur where the results of published jury verdicts are at extreme odds with one or the other party's estimates of the amount or number of verdicts for particular types of cases in the jurisdiction where the case will be tried.

One final note and an observation. Actuarial case valuation is not a panacea, nor is it a method that lends itself to utilization in every case, nor should it be attempted in every case. In this writer's experience, as a settlement judge

for over seven years, in the vast majority of cases the attorneys mostly come to settlement with a basically realistic but occasionally somewhat skewed view of their case. In these types of cases, the mediator's role is much simplified, often amounting only to helping the parties tease out the strengths and weaknesses of their cases in an attempt to move the parties closer to resolution. However, in those difficult cases in which the parties are either unwilling or unable to engage in productive settlement discussions, whether due to a particular bargaining strategy, client control issues, or an unreasonable and unwavering estimate of the value of their case, actuarial case valuation can and does offer a method for moving the parties closer together, avoiding stalemate, and sometimes settling an otherwise unseizable case.