I. Introduction
- decisions facing potential plaintiffs and defendants, suit, settlement or trial
  - bring suit?
  - go to trial?
  - appeal?
  - the decision tree

- Costs of litigation in the U.S.
- If costs are high, why so much litigation?
  - the social justice theory
  - the ambulance theory
  - economic theory

II. Shavell, "Suit, Settlement and Trial..." - an economic theory of why people file suits and go to trial.
- Assumptions of the model (what are they?)
- 4 systems of allocating legal costs (how does each system work?)
  - American system
  - British system
  - plaintiff system
  - defendant system

- definitions of key variables in the model
- when do plaintiffs sue (i.e., file a case)?
  - only sue if the expected benefits from suit exceed the expected costs
  - what is the condition for suit under each of the 4 systems?

- the frequency of suits
  - defendant system has the lowest frequency of suits (why?)
  - plaintiff system has the highest frequency of suits (why?)
  - Under what conditions will frequency under the American system exceed frequency under the British system?
  - what impact does risk aversion have on the frequency of suits?

- the frequency of trials
  - assumptions
    - risk neutrality
    - the parties always settle if a cooperative surplus (what's that) exists
  - always settle if the parties have the same expectations about the outcome at trial
  - only go to trial if one, or both, parties are over-optimistic about their chances at trial (does over-optimism always lead to a trial?)
  - American system has the lowest frequency of trials
  - British system has the highest frequency of trials
  - what impact does risk aversion have on the frequency of trials?

- problems with Shavell's paper
  - sole focus is on the plaintiff's decision but defendants can affect the decision to sue (how?)
    - avoid causing harm in the first place (as the expected award increases, how does the defendant respond?)
    - take action to decrease the probability that the plaintiff will win at trial (how?)
    - what, then, is the relationship between the expected award and the frequency of suits? Under shavell? in actuality?
  - Over-optimism about their chances at winning at trial is not the only reason why individuals go to trial (we will subsequently discuss two additional reasons, make sure you know each.)
III. Game Theory - (this is the first additional reason which explains why disputes happen. However, our discussion here also allows us to use game theory to explain other important issues.)

- example of a dispute

- assumptions about the dispute
  o strategies (bargain hard or soft)
  o trial costs
  o when do we go to trial?
  o how do the parties split the disputed amount if they don't go to trial?

- suppose the parties can only play a pure strategy? When do they go to trial?
  o what is a pure strategy?
  o what is a cooperative solution?
  o what is a non-cooperative solution?
  o what are threat values?
  o what is the equilibrium?
    ▪ of this specific game
    ▪ of games in general (a nash equilibrium is when ...?)
  o what is the efficient outcome?
  o under what conditions will they go to trial? If either:
    ▪ the amount under dispute is high enough or
    ▪ trial costs are low enough
  o then trials can happen. why? (hint: they are making strategic moves in an attempt to increase their own private profits.)

- suppose the parties play a mixed strategy? When do they go to trial?
  o what is a mixed strategy?
  o what is the equilibrium when the parties play a mixed strategy?
  o each party must equate their expected values given what the other party does.
    ▪ when do trials occur?
  o both parties must play hard (note: under mixed strategies, a probability exists that a trial will occur, whereas under pure strategy, the equilibrium is to either go or not to go to trial.)
    ▪ what increases the frequency of trials (i.e., the probability that a trial will occur)?
    ▪ as the amount under dispute increases, then so does the probability of trial
    ▪ as court costs increases, the probability of a trial decreases.

- main point of this discussion - trials occur even when the parties are not overoptimistic - they may occur because of strategic reasons (i.e., the parties trying to make sure that they get more of the cooperative surplus.)

IV. The Efficiency of the Common Law

- what do we mean by efficiency?
  o technological efficiency? (what's that?)
    ▪ not relevant in this context – why not?
  o strong pareto optimality? (what's that?)
    ▪ requires no externalities (no harm to 3rd parties)
    ▪ a strong assumption that is almost never met
  o weak pareto optimality? (what's that?)
    ▪ externalities can occur but the benefit of the exchange must outweigh the harm imposed on 3rd parties
    ▪ assuming risk neutrality this equals societal wealth maximization.
    ▪ wealth maximization is what we mean by efficiency in this context.
- criticisms of the premise that the common law is efficient
  o the idea that the law promotes efficiency over justice is repulsive and, hence, inconceivable
    ▪ often times justice and efficiency are the same things.
    ▪ the two are not mutually exclusive goals

- why is the common law efficient?  What forces cause the common law to move toward efficiency?  Two possible answers.
  o Judges have a preference for efficient laws
  o inefficient laws are more likely to be litigated => over time they are more likely to be overturned in the common law system.  This is the point that Rubin makes.

V.  Rubin - "Why is the common law efficient?"

- The model
  o assumptions
  o variable definitions

- suppose both parties are interested in precedent (i.e., both parties know they will likely face a similar case in the future)
  o under what conditions will the parties go to trial?
    ▪ only go to trial if a cooperative surplus does not exist
    ▪ never go to trial if the law is efficient
    ▪ sometimes go to trial if the law is inefficient.  More likely to go to trial as:
      • the cost of the inefficiency increases,
      • the inefficient law is less well entrenched, or
      • court costs are lower.
  o what happens if they do go to trial?
    ▪ the inefficient law is probably confirmed but eventually, as trials continue, the inefficient law will be overturned.

- suppose only one party is interested in precedent?
  o assumptions
  o under what conditions will the parties go to trial?
    ▪ will never go to trial if the precedent favors the party interested in the future
    ▪ may go to trial if the precedent does not favor the party interested int he future.  More likely to go to trial as:
      • court costs fall or
      • the precedent (which does not favor the party interested in the future) weakens
  o again, eventually the law will be overturned regardless of its efficiency

- suppose no parties are interested in precedent?
  o always settle and never litigate (why?)

- although not the main point of Rubin's paper (what was his main point?), he does point out a third reason why trials occur - because the parties are interested in the future and the law affects them in the future.