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## When Strategies Go Awry: Part 3 In A Series On Cognitive Biases And Their Impact

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# Commentary

## When Strategies Go Awry: Part 3 In A Series On Cognitive Biases And Their Impact

**By**
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*[Editor's Note: This is part 3 of a series of articles on Cognitive Biases and their impact on Litigation and Negotiation. Laura A. Frase, Of Counsel with Cantey Hanger L.L.P. in Dallas, has over 30 years' experience in Insurance Defense Litigation. She also serves as Negotiation/Settlement Counsel for a number of her clients, having resolved thousands of matters generating significant cost savings. Ms. Frase earned her law degree from St. Mary's School of Law. In 2013, she earned a Master's Degree in Dispute Resolution from Southern Methodist University, concentrating on Negotiation. Ms. Frase is also a trained Mediator and an Adjunct Professor at UNT Dallas College of Law. She is recognized as a Top Woman Lawyer in Texas and AV Peer Preeminent rated. Any commentary or opinions do not reflect the opinions of Cantey Hanger LLP or LexisNexis® Mealey Publications™. Copyright © 2018 by Laura A. Frase. Responses are welcome.]*

### *Loss Aversion and its Collaborators or "I hate losing. I hate losing more than I even wanna win."[1]*

Losing. It is one of the more distasteful consequences of participating in life, society and the economy. Losing something can have deep psychological pain, even when we are not using the service or item we have lost.[2] It is about more than challenging our feelings of entitlement, self-worth, or self-preservation. Sales people will tell you that losing can even be motivational. Yet, ingrained within our very psyche is this innate, automatic repugnance to losing.[3] We are thus laser-focused on averting and avoiding the potential of suffering losses.

Multiple psychological studies have proven that when deciding a course of action, we make different decisions when faced with a chance to achieve a gain or a chance we will sustain a loss.[4] Basically, "we react more strongly to perceived losses then we do to perceived gains of equivalent size."[5] *And most illogically, we will take more risk to avoid losses then we will to attain gains.*

Historic economic theories hold that rational actors choose options by assessing the utility and probability of each outcome.[6] Decision-makers are assumed to "have stable, well-defined preferences and make rational choices consistent with those preferences."[7] Probabilities are approached as calculations, with no regard to the emotional context of the decision. Therefore, in theory, we should be willing to engage in equal amounts of risk whether we are choosing to prevent a loss or working to accomplish a gain.

In 1979, Amos Tversky and Daniel Kahneman turned these historic economic theories on their heads[8] by proposing the ground-breaking *Prospect Theory.*[9] They hypothesized that we base decisions not upon the probabilities and efficacy of the final outcome, but on the psychological/economic value of changing our current position and the potential/prospect of a loss or a gain occurring because of that change.[10] Utility is not the driving force. Instead, risk tolerance influences choice.

Led by **Loss Aversion**, an amalgamation of cognitive biases "pile on" to affect risk tolerance choices in decision-making. These various biases intermingle, are viewed as causes and consequences of each other and, one is sometimes used to define another. These reactions are emotionally grounded and psychologically complex. In this third part of this Series, I endeavor to explain a few of the stimuluses, why they interlace and how they impact our legal practices.

### *Why is Losing Hard? Loss Aversion and the Negativity Bias*

Seeking out heightened risk to overcome a loss makes little sense. So why do we react this way? Loss Aversion is stimulated by the **Negativity Bias.** Generally, we are more likely to process and remember negative information rather than positive information. Negative happenings are more powerfully retained in our memories.[11] As one neuropsychologist put it, our brains are "like Velcro for negative experiences and Teflon for positive ones."[12] Uncertainty intensifies our focus on potential negative outcomes. As we are prompted to avoid bad results, when we attempt change, we concentrate more on the possible negative consequences rather than the positive probabilities. The more meaningful the imagined loss, the more risk we are willing to take. We don't want to give up even when it may be more emotionally and economically beneficial to do so.[13]

Psychologists believe that, in the abstract, the emotional impact of conceptually losing what is ours hurts more than potentially receiving something in the future.[14] In that light, Daniel Kahneman asked subjects "what is the smallest gain that I need to balance an equal chance to lose $100?" He found that most people would answer about $200, or twice as much to overcome the potential loss.[15] Indeed, experiments have shown that the loss-averse ratio is about 1.5 to 2.5.[16] "[P]eople tend to find it more difficult to give up money that they are used to receiving than to choose not to receive money that they do not already have."[17]

When strong emotions are involved, Loss Aversion is exacerbated. "Losses compounded by outrage are much less acceptable than losses that are caused by misfortune or by legitimate actions of others."[18] In an amendment to his Prospect Theory, Kahneman also suggests that regret influences Loss Aversion. We fear making a bad deal, particularly if we are unsure as to the value of what we are losing. Our emotional "mental accounting" keeps score of our wins and losses.[19] Fear and uncertainty pushes us to risk more.

### *I Like Where I Am: Status Quo Bias*

Because negative consequences are palpable with change, we can sometimes become human sloths. The status quo dominates decision-making. Consider the old adage - "When in doubt, do nothing." We prefer to keep what we have and where we are rather than choose an uncertain path and risk losing through that change. For example, studies show that when people are required to opt-out of 401K plans[20] or organ donation involvement,[21] participation in those plans increases significantly. Think about the replay option now favored in baseball and football. The decision made on the field is only overturned with "clear and convincing evidence." Thus, the on-field or default choice is given greater predilection, even in "close calls."[22] Consider also the purpose of an injunction, an excellent example of the primacy of the status quo. An injunction is issued to either preserve the parties' positions[23] or "require a party who has recently disturbed the status quo to reverse its actions."[24] We regularly elect incumbents,[25] purchase the same food brand and stay in our jobs.[26] Other examples of "default" preferences are mortgage escrow accounts, electronic billing, and targeted digital adverting by businesses we have purchased from previously. In these instances, we generally have to opt-out to pay our property taxes separately from the mortgage, to get paper bills, or to keep unwanted coupons from filling up our email in-box. Default is powerful.

The **Status Quo Bias** explains that we often prefer our current state of affairs over risking improving our position.[27] Recall that, evolutionarily, survival demanded we pay attention to potential bad outcomes.[28] Studies show in this Bias, we substantially prefer stasis and resist change.[29] The default position serves as our reference point (or Anchor) and we compare staying where we are to the uncertain consequences of changing. The default choice "sets the choice for a person who does not choose."[30] We prefer to maintain the status quo sometimes because of "convenience, habit or inertia, policy or custom, or fear"[31] but nevertheless, the status quo is viewed as less risky than change. Sometimes the Status Quo Bias is so prominent that we do not even recognize that there is a choice to be made.[32]

The Bias is magnified in difficult decisions or when multiple or conflicting choices are presented, particularly if the person deciding holds weak preferences.[33] Choosing the status quo option also gives us the illusion that we are more in control of our circumstances.[34] The disadvantages of changing our state of affairs looms larger than the advantages gained by changing.[35]

The Bias regularly plays out in negotiations, particularly if the negotiations surround changing relationships or statuses (think labor union contracts, arms treaties and trade deals).[36] The "existing terms define reference points [Anchors] and a proposed change . . . is inevitably viewed as a concession."[37] Since concessions may be viewed as losing, negotiations may intensify. Participants may express preferences for risk-seeking options (such as a strike or trade war) and the value of making those concessions increases.

Loss Aversion discourages changing. The status quo is known and comfortable. The Status Quo Bias coerces us to "choose" to stay put. Yet, doing nothing eventually becomes the least optimal choice. Think about a company that is stagnating. Do the officers take affirmative (and potentially risky) steps to overcome the stagnation or do they do nothing? Inertia is formidable. Overcoming the Status Quo Bias is challenging because change is perceived as exceedingly risky. Change mean potentially losing.

### *Mine is Worth More Because it is Mine: Endowment Effect*

As a repercussion of Loss Aversion and the Status Quo Bias, in the **Endowment Effect**[38] we believe the property we own is more valuable than others do.[39] We may also demand much more to sell something we own than we would pay to buy that same item from others. For example, a study found that hunters demanded an average of $1,044 to give up the option of hunting on a specific wetland development but would only pay an average of $247 to continue hunting on the same land.[40]

Ideally, the value of an item should not change whether we own it or not. But because of our unwillingness to sustain losses (and our love of inertia), our behavior suggests otherwise. Sometimes called the "Offer-Asking Gap,"[41] mere ownership causes divergent valuations and expands the negotiation zone. We often become emotionally attached to what is ours so we assign a higher value.[42] This Effect impacts decision-making even if the ownership of the item is hypothetical.[43] If the property is acquired because of the demonstration of a skill or talent (i.e., awarded vs. received by chance), the Effect becomes even stronger.[44] Ownership is simply viewed as less risky than giving up our stuff.[45] The Effect, at its essence, is tied psychologically to our "normatively defensible entanglement of personal property with selfhood"[46] or, as described by Oliver Wendell Holmes Jr., reminiscent of "the deepest instincts of man."[47]

In a famous example of the Endowment Effect, Daniel Kahneman and his colleagues divided subjects into two groups. Each member of one group was given a coffee mug, and each member of the other group was given $6. The first group was asked the amount of money each would accept to sell a mug and the other group was to state the amount each would pay to buy a mug. After averaging the numbers, the sellers valued the mugs at around twice the amount that buyers were willing to pay.[48] The results were the same, even when the experiment was repeated to allow the subjects to learn from the experiment.[49] This result harkens back to Kahneman's other findings that the typical loss-averse ratio is 1.5 to 2.5.

I replicated this experiment at UNT Dallas College of Law. I passed out pens with my firm's name (something I hoped law students believed had a modicum of value) to half of my class. The other half of the students were given the opportunity to handle the pens and assess the quality. The first group was then asked to write down the amount for which each would sell a pen while the second group was asked to write down the amount each would pay for a pen. The results showed the average seller price was 1.4 times higher than the average buyer price,[50] despite the fact that the students were studying the very bias that drove their choices.

If the entitlement or property owned has few substitutes on the market[51] or is of such consequence that there is resistance in the market in establishing a dollar value,[52] the Endowment Effect may play a role in assigning a price. In an interesting study, violinists attending an international competition were asked in a double-blind study to determine which of a variety of violins provided the best sound. Multiple violins were tested, including three new violins and two rare Stradivarius violins.[53] Musicians were blind-folded, asked to play the instruments, and then asked to pick the violin they preferred. A surprising number of the musicians chose the newer violins over the old masters.[54] After an outcry from professional musicians, the experiment was repeated with more talented players and in a better venue. The results were the same.[55] In an effort to justify the disquieting results, one commentator suggested that "the joy of owning and playing a Stradivarius comes not from any objective advantage in its sound, but simply from the knowledge that it is a Stradivarius. . . . [It] carries status in its name, gravitas in its price tag and the weight of centuries in its wood."[56] Owners endowed these rare, coveted instruments with value which others believe they may not rightfully possess.[57]

Our legal system is infused with the Endowment Effect. For example, the concept of adverse possession satisfies those who believe they acquired property rights over time.[58] We separate past damages (like lost wages) from future loss of earning capacity to adjust for the power of the Effect. Other types of out-of-pocket damages are treated differently from opportunity costs.[59] "Good will" that is often built into a business transaction sales price may be regarded as an effort to assuage the Effect, or to quantify the intangible value "of a well-known and well conducted business."[60] Finally, we employ evaluation experts and appraisers to help determine "fair market value" in an effort to overcome the sway of the Endowment Effect.

Whether a cause of or a consequence of Loss Aversion, the Endowment Effect significantly impacts the choices we make. Ownership, whether real or perceived, boosts value. During negotiations, if the Offer-Asking Gap seems large or unsubstantiated by independent evaluations, the Endowment Effect may be in play. And, if we are not careful, it may play out in our own presumptions of worth.

### *Losing More to Recuperate Losses: Sunk Cost Fallacy*

Most understand that future investments must be justified on the probability of future returns and not as a means of recuperating past expenditures.[61] But the **Sunk Cost Fallacy** clouds our reasoning. This Fallacy causes us to incorporate the project's spent resources into future goals of recovery. The continued involvement in the Vietnam War is a classic example of Sunk Cost Fallacy.[62] And think of the stock market: is it reasonable to panic when a stock you own, which has now doubled in value since you bought it, was worth even more two days ago? Think of the gambler who risks more because she wants to "win back" money, even though she is still ahead of her initial bet. Past outlays (or the split milk we should not cry over) are erroneously calculated as part of expected future returns.

Richard Thaler conducted a simple experiment demonstrating the Sunk Cost Bias. He advertised a $3 all-you-can-eat-lunch at a local pizza shop. Once the shop was full, he randomly refunded the $3 to half of the customers. Rational economic theory suggests that the refund of a sunk cost would not affect pizza consumption. Yet the diners who received the refund ate less, even though they were previously committed to invest the full amount in all-you-can-eat.[63]

We continue to invest in losing propositions for a variety of reasons. Perhaps we are trying to delay cognitive realization of the loss. Perhaps we want to prove that we are consistent and that our original plan was appropriate.[64] Perhaps we want to avoid appearing stupid, foolish[65] or wasting resources.[66] Perhaps we are willing to pay for vindication rather than compromise.[67] Economically, none of these reasons justify throwing good money after bad or doubling-down our commitment to an inferior plan.

Like the others mentioned, the Sunk Cost Fallacy also impacts litigation and negotiation. In all-day mediations, for example, parties may feel that their investment of time, emotional energy, or other resources necessitates a deal, even a poor one. Parties may engage in expensive and unnecessary discovery to counter uncontested bad facts, just to "be sure" or "in case something changes."

We have seen too often how attorney fees outpace the value of a case. In one study, a hypothetical breach of contract case was presented to a group of attorneys. Given identical facts, each group evaluated an attractive $480,000 settlement offer. They were told the maximum recovery was $1,000,000 and the contract did not permit recovery of attorneys' fees. They had to assume that it would take $70,000 in fees through trial. One group was told that they already spent $90,000 in fees while the other group was told they already spent $420,000. Of those who learned they had already spent $90,000, 76% suggested settlement. Of those told of the greater amount of fees spent, only 45% recommended settlement.[68] Over-commitment misaligned the attorneys' original objectives and created a new incentive to recapture already spent fees.[69] High past investment of fees provoked the attorneys to select the more risky and uncertain gamble, that of trial.

### *Words Matter: Loss Aversion and Framing Effect*

So what triggers our risk tolerance preferences and Loss Aversion? Traditional/rationalist economic theory suggests that an individual's choice should be made independently from the wording used to describe options. It should not matter how the alternatives are phrased. For example, is something 90% fat free or does it contain 10% fat?[70] It is the same reality, described differently.[71] Yet we know the former phrase has greater impact on sales. One study suggests that a golfer putts better when she is trying to avoid a bogey rather than going for a birdie.[72] Why?

Numerous experiments prove that ***how we phrase or "frame" options drives decision-making***.[73] In Loss Aversion, if an option is framed as a gain, we take less risk. If an option is phrased as a loss, we take more risk.[74]

> "When decision options are perceived as 'gains' relative to the reference point, individuals are risk-averse; that is, they prefer more certain options to gambles with the same expected value. But when decision options are perceived as 'losses' relative to the reference point, the same individual will be risk-seeking; that is, they will prefer to gamble to the certain option when both have the same expected value."[75]

Additionally, studies show when the status quo is explicitly included as an option, such framing greatly increases its selection over other options.[76] We are driven toward choices by the way the alternatives are framed.[77] This **Framing Effect** has been demonstrated in everything from gambling, purchasing decisions, medical/life-threatening choices, and what one declares on one's taxes.[78] For example, people are more likely to have surgery if they know that 90 of 100 people survived rather than 10 out of 100 died.[79] We are driven toward choices by the words used to describe the alternatives.[80]

How risk is framed impacts the preferences of parties in litigation.[81] Plaintiffs generally choose between a sure option (settlement) and an uncertain but potentially lucrative gain (verdict). Because Plaintiffs are choosing between two perceived gains, studies demonstrate that they make more risk-averse choices. Defendants, on the other hand, choose between a sure loss (settlement) and a potentially more substantial loss (verdict). Consequently, as Defendants are essentially choosing between two losses, they prefer more risk-seeking options, like trial.[82] A "defendant protecting his assets preferred riskier options than . . . the plaintiff trying to add to her own wealth."[83] Even if the payoff is the same under both options, offers made using loss language are more often rejected than identical offers phrased as a gain.[84] Finally, expectations matter. If the Plaintiff believes a settlement is a loss, risk-seeking options are more often chosen.[85]

Loss and gain "frames" are not the only way language influences decisions. How we frame the problem we are attempting to solve also greatly impacts the decisions made. In one famous example, personnel with Morton Thiokol, the manufacturers of the booster rockets for the space shuttle *Challenger*, recommended launching when the supervisors asked them to decide "like managers" rather than framing the decision as a safety issue.[86] When daycare centers started charging parents for being late picking up their children, tardiness went up. The frame was changed from an ethically-tinged choice (not wanting to burden staff) to an economic decision (I can pay to be late).[87] When a life insurance company improperly induced customers to cash-in their equity on existing policies to fund purchasing larger policies, the company told its employees that they were helping underinsured customers. The framing reassured their employees and justified potentially unethical behavior.[88] And of course, there are those attorneys who rationalize violating ethical rules by framing the choices as "zealous advocacy."[89] Phrasing matters.

Similarly, we may accidentally infuse Loss Aversion into our litigation plans if we phrase our problem using loss-language. For example, "how do I keep my client from going out of business" may increase the likelihood that risk-seeking options are emphasized. "Setting out to solve the wrong problem because you have created a [negative] mental framework for your decisions [can] cause you to overlook the best options."[90] In "goal framing," emphasizing the negative consequences of a plan of action (i.e., preventing business dissolution) can accentuate the attractiveness of the risk-seeking options.[91]

For lawyers and other professionals, Loss Aversion and Framing also have ethical implications. Studies have shown that people choose differently when a question is posed through an ethical rather than a business lens. When asked whether it was ethical to sell a drug that caused just under a dozen unnecessary deaths (and when there was a safer alternative), 97% of the study subjects said it was unethical to continue selling the drug. When subjects were asked the same question while in the role of the company's directors, overwhelmingly the participants made the business decision to leave the drug on the market.[92] Other studies have shown that "people trying to avoid a loss are more likely to draw upon lower-road ethical choices than are people trying to attain a gain."[93] And finally, how we phrase options to our clients can help them overcome or exacerbate their own cognitive biases. Using positively phrased language may help them chose the option that maximizes their recovery.[94]

Choice-framing is a complex mode of communication. It can focus attention on different aspects of the message (a glass is half empty vs. half full) and on the motivations of the speaker (a choice means security or potential).[95] Choices can convey negative potential outcomes (if you refuse, I will bury you in paper), disclose choice-relevant information, or hint at the perspective of the speaker. Imagine, for example, these phrases describing a plane crash: "a few people were saved, which is a good thing," which implies that not all died and compare it to "a few people died, which is a good thing," now implying some were saved.[96] The frames tell us from which perspective the speaker approaches the problem.[97] In Framing, whether positive, negative or neutral, one reality is presented as most palatable. And if that reality is expressed in negative terms or consequences, the decision-maker may be tempted to select the higher risk option, to her detriment.

### *Battling Status Quo/Loss Aversion/Endowment Effect*

We subconsciously resist giving up our position and our stuff. We will risk more to keep from doing so. We risk less to achieve betterment. So how can we combat these tendencies?

- Reframe the choices using "gain language" rather than "loss language."[98] Discuss how, for example, a settlement for a client is a benefit rather than focusing on money outlaid. Point out the losses the company will incur from continued litigation.[99] How we phrase the deal may also determine whether our opponent will accept our proposal.[100] "When positive frames exist, risk-aversion dominates."[101] Given our predisposition to recall the negative, phrasing options in terms in promoting good results may also make our litigation plans more effective.[102]
- Confirm that non-recoverable sunk costs are not creeping into your valuations and goals. Ask yourself, is it worthwhile at this point to spend money in the future to achieve a desired gain? Ignore past expenditures. Let bygones be bygones.
- Minimize the number of choices presented so the person making the decision is less likely to choose the status quo. For example, if you recommend hiring a new expert in mass tort litigation, give the client no more than the three best options rather than offering up multiple choices that may increase the risk that the client chooses to stick with the current expert. If the choices conflict with each other, a client is also apt to select the status quo. Phrase your alternatives to minimize conflicts.
- Delaying the decision is also an effective way to diminish the Status Quo Bias. If we are prompted to make a quick decision, human nature nudges us toward the default option. Procrastinate a bit. Delaying also lets us consider the options when we are well rested and in a positive mood. Finally a delay allows us to collect any additional, necessary information. Be careful not to trigger the Sunk Cost Bias. Set a deadline so the decision is not put off indefinitely.[103]
- To further counter Loss Aversion, Richard Thaler and Cass Sunstein, suggest "nudging" a decision-maker to better choices by changing the default choice to one that maximizes benefits.[104] For example, instead of telling a patient with knee pain that she must choose between intensive and painful physical therapy or have risky surgery, set physical therapy as the default option and then discuss alternative therapies beyond the default. Frame participation in mediation as the default portion of the litigation plan ("*when* we go to mediation"), remembering to frame settlement as a gain. Be thoughtful and transparent about

framing the new default choice so that the decision-maker does not feel manipulated and ultimately benefits.

### *Conclusion*

As attorneys, we are naturally reluctant to concede or be perceived as "giving up" – to concede is to lose. It seems logical that aggressive litigation or negotiation tactics (such as reminding our opponent of the consequences of their refusing) will push the other side toward agreement or recalcitrance. Yet study after study has shown that the possibility of looming losses is perceived as much more painful than gains.[105] Thus, aggressive postures may increase the other side's desire to choose more risky alternatives (such as finding another vendor or pushing toward trial) rather than generating submission.

Reframing is key. Positive framing is more than just sweetening the deal or adding provisions that enhance the agreement (although those can be helpful). It is about presenting the proposal in a light that demonstrates to the other side all she will certainly gain with agreement. Know the risk tolerance level of your opponent and client. Emphasize certainty and the advantages. "People tend to simplify their thinking about probability into categories of sure thing (certain), possible or impossible."[106] Gain language may turn "possible" into "yes."

### Endnotes

1. MONEYBALL. Screenplay by Steven Zaillian and Aaron Sorkin (Columbia Pictures 2011).

2. Recall the customers' reaction to Netflix© announcing that certain movies would be removed from their service. Bryce Orlin, *Why Does Netflix Remove Shows and Movies*, NETFLIXLIFE.COM. https://netflixlife.com/2017/10/08/why-does-netflix-remove-shows-movies/ (retrieved Dec. 29, 2017).

3. One author suggests that the pain of losing can be explained through mathematical calculations using a pre-loss/gain yardstick and a post-loss/gain yardstick. For example, if a 4-year old child has to wait a year to get a pony, that is equivalent to 25% of that child's life. For adults that one year is a marginal amount of time. Thus the consequence of waiting, or losing, has greater impact because of the life circumstances or our "placement" in the environment. Michael Moffa, *The Simple Math Underlying Why We Hate to Lose*, RECRUITOR.COM https://www.recruiter.com/i/the-simple-math-underlying-why-we-hate-to-lose/ (Feb. 4, 2011) (retrieved Dec. 27, 2017).

4. Robert Prentice, *Behavioral Ethics: Can it Help Lawyers (And Others) Be Their Best Selves,* 29 NOTRE DAME J.L. ETHICS AND PUB. POL'Y 35, 49 (2015).

5. JENNIFER K. ROBBENNOLT and VALERIE P. HANS, THE PSYCHOLOGY OF TORT LAW 214 (2016).

6. Russell B. Korobkin and Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics,* 88 CAL. L. REV. 1051, 1055 (July 2000). The Rational Choice Theory assumes people decide rationally and logically to maximize utility or self-interest, with no emotional context. It was challenged as a viable theory because there was too much evidence that people acted in ways inconsistent with maximizing utility or self-interest. Bounded Rationality Theory was born. Rather than people deciding incorrectly, mistakes were then viewed as exceptions or limitations. *See* Herbert A. Simon, *Rational Choice and the Structure of the Environment*, in MODELS OF MAN: SOCIAL AND RATIONAL 261, 270-71 (1957).

7. Daniel Kahneman, Jack L Knetsch, Richard H. Thaler, *Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias*, 5 J. ECON PERSP. 193, 193 (Winter 1991).

8. Economists have attempted to incorporate a fundamental understanding of Loss Aversion in the concept of Marginal Utility Theory – that losses and satisfaction, when plotted from a specific reference point, are measured by the utility of the consumption of goods.

9. *See generally* Amos Tversky and Daniel Kahneman, *Advances in Prospect Theory: Cumulative Representation of Uncertainty*, 5 J. RISK AND UNCERTAINTY 397 (1992); DANIEL KAHNEMAN, THINKING FAST AND SLOW 278-288 (2011).

10. DANIEL KAHNEMAN, THINKING FAST AND SLOW 278-288 (2011).

11. Roy F. Baumeister, Ellen Bratslavsky, and Catrin Finkenauer, *Bad is Stronger than Good,* 5 REV. GEN. PSYCHOl. 323, 355 (2001).

12. Kenneth Chestek, Of Reptiles and Velcro: The Brain's Negativity Bias and Persuasion, 15 NEV. L. J. 605, 624 (Spring 2015).

13. See generally, ORI BRAFMAN AND RON BRAFMAN, SWAY: THE IRRESISTIBLE PULL OF IRRATIONAL BEHAVIOR (2008).

14. Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1250 (Spring 2003).

15. DANIEL KAHNEMAN, THINKING FAST AND SLOW 284 (2011). "The typical person losing from his pocket a thousand dollars of past earnings feels more aggrieved than a person losing from a settlement of a thousand dollars meant to compensate lost future earnings. A person palpably possesses the former and palpably feel the loss; a person only abstractly possesses the latter and more abstractly feels the loss." *Schwade v. Total Plastics, Inc*. 837 F. Supp. 2d. 1255, 1279 (U.S.D.Ct. Florida, 2011).

16. DANIEL KAHNEMAN, THINKING FAST AND SLOW 284 (2011).

17. *Abrahamson v. Board of Education of the Wappingers Central School Dist.,* 2002 W.L. 1354711 (U.S.D.C. New York June 21, 2002) (changes in teacher union retirement options impact those who chose lesser retirement options under previous plan). *See also* Russell Korobkin and Thomas Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics,* 88 CAL. L. REV. 1051, 1107-13 (2000).

18. Robert H. Mnookin, *Why Negotiations Fail: An Exploration of Barriers to the Resolution of Conflict,* 8 OHIO ST. J. ON DISP. RESOL. 231, 235 (1993) *in* NEGOTIATION: THEORY AND PRACTICE (2nd ed., Edited by Melissa Nelken 2007).

19. DANIEL KAHNEMAN, THINKING FAST AND SLOW 342-352 (2011). *See also*, Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1254-55 (Spring 2003). Kahneman initially referred to the phenomena as "responsibility costs" which may result by voluntarily assuming additional risk. Daniel Kahneman, Jack L. Knetsch, and Richard H. Thaler, *Anomalies: The Endowment Effect, Loss Aversion and Status Quo Bias*, 5 J. ECON PERSP. 193, 202 (1991).

20. Brigitte C. Madrian and Dennis F. Shea, *The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*, 116 Q.J. ECON. 1149, 1149 (2001). The authors' studies also confirmed that when the contribution rate and investment allocation was a default choice, it positively influenced savings behavior of the participants. *Id.* at 1184.

21. Eric J. Johnson and Daniel Goldstein, *Do Defaults Save Lives?* 302 SCI. 1338, 1339 (2003).

22. Shane Frederick, *Automated Choice Heuristics*, in HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 548-558, 555 (Thomas Gilovich, Dale Griffin, and Daniel Kahneman eds., 2002).

23. *O Centro Espirita Beneficiente Uniao Do Vegetal v. Ashcroft*, 389 F. 3d 973, 1012 (10th Cir. 2004) and cited cases. The court went on to opine that "[f]undamentally, the reluctance to disturb the status quo prior to trial on the merits is an expression of judicial humility." *Id* at 1015.

24. *Id.* at 1013.

25. One study demonstrated that incumbents have a margin of victory of 59% to 41%. When more than two candidates run, the chances the incumbent wins increases. William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. RISK AND UNCERTAINTY 7, 9 (1988).

26. William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. RISK AND UNCERTAINTY 7, 8 (1988).

27. Andrea Caputo, *A Literature Review Of Cognitive Biases in Negotiation Processes*, INTERN. J. OF CONFLICT MANAGEMENT, *24 (4)*, 374-398.

28. Roy F. Baumeister, Ellen Bratslavsky, and Catrin Finkenauer, *Bad is Stronger than Good,* 5 Rev. Gen. Psychol. 323, 325 (2001).

29. Wendy Netter Epstein, *Nudging Patient Decision-Making,* 92 Wash. L. Rev. 1255, 1294 (October 2017).

30. *Id* at 1293.

31. William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. Risk and Uncertainty 7, 10 (1988).

32. *Id.*

33. Wendy Netter Epstein, *Nudging Patient Decision-Making,* 92 WASH. L. REV. 1255, 1294 (October 2017). *See also* William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. Risk and Uncertainty 7, 39 (1988).

34. William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. Risk and Uncertainty 7, 39 (1988).

35. Daniel Kahneman, Jack L Knetsch, and Richard H. Thaler, *Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias*, 5 J. Econ Persp. 193, 197-198 (Winter 1991).

36. DANIEL KAHNEMAN THINKING, FAST AND SLOW 304 (2011).

37. *Id.*

38. I like to call it the Garage-Sale-Gone-Wrong Effect. Why won't anyone buy my perfectly good, used toaster for $20?

39. One possible exception to the Endowment Effect occurs when homeowners are notified of their property taxes.

40. Judd Hammack and Gardner M. Brown, Jr. *Waterfowl and Wetlands: Toward Bioeconomic Analysis* 26, (1974) *as cited in O Centro Espirita Beneficiente Uniao Do Vegetal v. Ashcroft*, 389 F. 3d 973, 1016 (10th Cir. 2004).

41. Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 Nw. U. L. Rev. 1227, 1229 (Spring 2003). Some argue the Endowment Effect is a consequence of Loss Aversion while others believe is it a cause. *See* Owen D. Jones and Sarah F. Brosnan, *Law, Biology, and Property: The New Theory of the Endowment Effect,* 49 Wm. and Mary. L. Rev. 1935, 1950-1953 (2008).

42. Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1251 (Spring 2003).

43. *Id.* at 1235-36.

44. *Id.* at 1236.

45. Owen D. Jones and Sarah F. Brosnan, *Law, Biology, and Property: The New Theory of the Endowment Effect*. 49 Wm. and Mary. L. Rev. 1935, 1950-1953 (2008).

46. Govind Persad, *When, and How, Should Cognitive Bias Matter to Law*, 32 Law and Inequality 101, 123 (2014).

47. "A thing which you have enjoyed and used as your own for a long time, whether property or an opinion, takes root in your being and cannot be torn away without your resenting the act and trying to defend yourself, however you came by it. The law can ask no better justification than the deepest instincts of man." Oliver Wendell Holmes, Jr. *The Path of the Law*, 10 Harv. L. Rev. 457, 477 (1897) as cited in *O Centro Espirita Beneficiente Uniao Do Vegetal v. Ashcroft*, 389 F. 3d 973, 1016 (10th Cir. 2004).

48. Daniel Kahneman, Jack L Knetsch and Richard H Thaler, *Experimental Tests of the Endowment Effect and the Coase Theorem*, 98 J. Pol. Econ. 1325, 1330-31 (1990).

49. *Id.* at 1332.

50. At the end of the experiment, all students were given a pen – fairness is also highly valued.

51. Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1236 (Spring 2003).

52. Russell Korobkin, Psychological Impediments to Mediation Success: Theory and Practice, 21 OHIO ST. J. ON DISP. RESOL. 281 (2006).

53. Many believe Stradivarius violins have an almost mythical reputation for quality of sound.

54. Claudia Fritz, Joseph Curtin, Jacques Poitevineau, Palmer Morrell-Samuels and Fan-Chia Tao, *Player Preferences among New and Old Violins,* 109 PNAS NO. 3. (P. 760-763) (2011) http://www.pnas.org/content/109/3/760.full

55. Ed Young, *Violinists Can't Tell the Difference between Stradivarius Violins and New Ones*, DISCOVER MAGAZINE (Jan. 2, 2012. http://blogs.discovermagazine.com/notrocketscience/2012/01/02/violinists-cant-tell-the-difference-betw een-stradivarius-violins-and-new-ones/#.V6ojE8JTGM).

56. *Id.*

57. In an NPR interview about this study, internationally renowned violinist Joshua Bell suggested that those participating were simply wrong because they did not know what to listen for in deciding the quality of the instruments. He simply knew that the Stradivarius had better quality sound. He thus engaged in a classic example of Egocentric Bias, to be introduced later in this series. *See Id.*

58. Some scholars argue that the Endowment Effect is an attractive explanation of adverse possession only when we assume that the adverse possessor feels entitled to the property AND the real owner does not. Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1260 (Spring 2003).

59. Daniel Kahneman, Jack L Knetsch, and Richard H. Thaler*, Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias*, 5 J. ECON PERSP. 193, 203 (Winter 1991).

60. Lynda J. Oswald, *Goodwill and Going-Concern Value: Emerging Factors in the Just Compensation Equation*, 32 B.C.L. REV. 283, 287 (1991).

61. Andrew J. Wistrich and Jeffery Rachlinski, *How Lawyers' Intuitions Prolong Litigation*, 86 S. CAL. L. REV. 571, 615 (March 2013).

62. JONATHAN BARON, THINKING AND DECIDING 305 (2008). In a speech to veterans in the early years of the Iraq war, then President George W. Bush justified continued involvement by referring to soldiers already lost "arguing that '[w]e owe them something' and asserting that '[w] will finish the task that they gave their lives for.'" Andrew J. Wistrich and Jeffery Rachlinski, *How Lawyers' Intuitions Prolong Litigation*, 86 S. CAL. L. REV. 571, 614 (March, 2013).

63. Russell B. Korobkin and Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics,* 88 CAL. L. REV. 1051, 1124-1125 (July 2000).

64. Andrew J. Wistrich and Jeffery Rachlinski, *How Lawyers' Intuitions Prolong Litigation*, 86 S. CAL. L. REV. 571, 615 (March 2013). At times, honoring sunk costs may be important – reputation for commitment or ability may justify continuing when faced with mounting litigation costs. *Id.*

65. Robert Adler, *Flawed Thinking: Addressing Decision Biases in Negotiation,* 20 OHIO ST. J. ON DISP. RESOL. 683, 739 (2005). The Hindsight Bias will be discussed in the next installment of this series.

66. Andrew J. Wistrich and Jeffery Rachlinski, *How Lawyers' Intuitions Prolong Litigation*, 86 S. CAL. L. REV. 571, 615 (March 2013).

67. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 SO. CAL. L. REV. 113, 123 (Nov. 1996).

68. Andrew J. Wistrich and Jeffery Rachlinski, *How Lawyers' Intuitions Prolong Litigation*, 86 S. CAL. L. REV. 571, 616-617 (March, 2013).

69. DANIEL KAHNEMAN, THINKING FAST AND SLOW 345-346 (2011).

70. Think about the phrase "you are not losing a daughter, you are gaining a son-in-law."

71. Anton Kühberger, *Framing* in COGNITIVE ILLUSIONS: A HANDBOOK ON FALLACIES AND BIASES IN THINKING, JUDGEMENT AND MEMORY 79 (2nd ed. Edited by Rüdiger F. Pohl, 2017).

72. DANIEL KAHNEMAN THINKING, FAST AND SLOW 177 (2011).

73. Ian K. Belton, Mary Thomson, and Mandeep Dhami, *Lawyer and Nonlawyer Susceptibility to Framing Effects in Out-Of-Court Civil Litigation Settlement,* 11 J. of Empirical Legal Studies 3, 578-600 (Sept. 2014).

74. Ian Weinstein, *Don't Believe Everything You Think: Cognitive Biases In Legal Decision Making*, 9 Clinical L. Rev. 783, 797 (2002).

75. Russell B. Korobkin and Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics,* 88 Cal. L. Rev. 1051, 1104-1105 (July 2000).

76. William Samuelson and Richard Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. Risk and Uncertainty 7, 8 (1988).

77. Joseph W. Rand, *Understanding Why Good Lawyers Go Bad: Using Case Studies in Teaching Cognitive Bias in Legal Decision-Making*, 9 Clinical L. Rev. 731, 739 (2003).

78. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 So. Cal. L. Rev. 113, 124-125 (Nov. 1996).

79. CASS R. SUNSTEIN, WHY NUDGE? THE POLITICS OF LIBERTARIAN PATERNALISM 29 (2014).

80. Joseph W. Rand, *Understanding Why Good Lawyers Go Bad: Using Case Studies in Teaching Cognitive Bias in Legal Decision-Making*, 9 Clinical L. Rev. 731, 739 (2003).

81. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 So. Cal. L. Rev. 113, 144 (Nov. 1996).

82. *Id.* at 118-119.

83. *Id.* at 145.

84. Melissa Nelken, NEGOTIATION: THEORY AND PRACTICE (2nd ed., Edited by Melissa Nelken 2007).

85. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 So. Cal. L. Rev. 113, 145 (Nov. 1996).

86. ALLAN J. MCDONALD AND JAMES R. HANSEN, TRUTH, LIES, AND O-RINGS: INSIDE THE SPACE SHUTTLE CHALLENGER DISASTER 228 (2009). *See also*, Chris Bergin, *Remembering the Mistakes of Challenger* (January 28, 2007) NASA Space Flight https://www.nasaspaceflight.com/2007/01/remembering-the-mistakes-of-challenger/ (retrieved on Dec. 15, 2017).

87. Uri Gneezy and Aldo Rustichini, *A Fine as a Price*, 29 J. Legal Stud. 1, 14 (2000). As the fine was not increased based on the number of minutes a parent was late, they started arriving later and later, testing the daycare's reaction. When the "fine" was cancelled, the parents still arrived later on average, perhaps because they did not anticipate a worse penalty than the fine, or perhaps believing that tardiness was now an entitlement. *Id* at 11.

88. Tammy L. MacLean, *Framing and Organizational Misconduct: A Symbolic Interactionalist Study*, 78 J. Bus. Ethics 3, 9-10 (2008).

89. Robert Prentice referred to this slippery slope for attorneys as "ethical fading." He suggests that decisions framed solely with business goals in mind may cause the ethical dimensions of a decision to fade away. *Behavioral Ethics: Can it Help Lawyers (And Others) Be Their Best Selves*, 29 Notre Dame J.L. Ethics And Pub. Pol'y 35, 48 (2015).

90. *See generally* J. EDWARD RUSSO AND PAUL J. H. SCHOEMAKER, DECISION TRAPS: THE TEN BARRIERS TO DECISION-MAKING AND HOW TO OVERCOME THEM (1989).

91. Anton Kühberger, *Framing* in COGNITIVE ILLUSIONS: A HANDBOOK ON FALLACIES AND BIASES IN THINKING, JUDGEMENT AND MEMORY 83-84 (2nd ed. Edited by Rüdiger F. Pohl, 2017).

92. Robert Prentice, *Behavioral Ethics: Can it Help Lawyers (And Others) Be Their Best Selves*, 29 Notre Dame J.L. Ethics and Pub. Pol'y 35, 50 (2015).

93. Mary C. Kern and Dolly Chugh, *Bounded Ethicality: The Perils of Loss Framing*, 20 PSYCHOL. SCI. 378, 381 (2009).

94. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 SO. CAL. L. REV. 113, 120 (Nov. 1996).

95. Anton Kühberger, *Framing* in COGNITIVE ILLUSIONS: A HANDBOOK ON FALLACIES AND BIASES IN THINKING, JUDGEMENT AND MEMORY *79,* 94 (2nd ed. Edited by Rüdiger F. Pohl, 2017).

96. *Id.* at 93.

97. One need only listen to news commentators for a short time to appreciate how framing clearly conveys perspective.

98. Jeffery J. Rachlinski, *Gains Losses, and the Psychology of Litigation*, 70 SO. CAL. L. REV. 113, 147 (Nov. 1996).

99. *Id* at 120. Of course, as easily as an attorney can frame settlement as improvement of the client's position, she also has the power to encourage "costly irrationality" by phrasing a settlement as a significant loss. *Id*. at 172.

100. Robert Adler, *Flawed Thinking: Addressing Decision Biases in Negotiation,* 20 OHIO ST. J. ON DISP. RESOL. 683, 742 (2005)

101. Andrea Caputo, *A Literature Review Of Cognitive Biases in Negotiation Processes*, INTERN. J. OF CONFLICT MANAGEMENT, *24 (4).* (p. 374-398).

102. Kenneth Chestek, *Of Reptiles and Velcro: The Brain's Negativity Bias and Persuasion*, 15 NEV. L. J. 605, 606 (Spring 2015).

103. Harry L. Munsinger and Donald R. Philbin, Jr. *Why Can't They Settle? The Psychology of Relational Disputes*, 18 CARDOZO J. CONFLICT RESOL. 311, 359 (Winter 2017).

104. *See generally*, RICHARD H. THALER AND CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT WEALTH, HEALTH AND HAPPINESS (2008).

105. Daniel Kahneman, Jack L Knetsch, and Richard H. Thaler, *Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias,* 5 J. ECON PERSP. 193, 203 (Winter 1991).

106. JONATHAN BARON, THINKING AND DECIDING 270 (2008). ■

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