

Litigation: Actors and Outcomes

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Litigation: Why?

Question

- Why do people litigate?
 - Why don't/can't people settle their dispute through private negotiations?
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- At times, disputants are not guided by monetary consideration.
 - Irrationality: One or both of the parties is/are not willing to settle
 - Emotions: For example, matrimonial and domestic disputes
 - Even if disputants are guided by monetary consideration, private negotiations may not success.
 - Informational asymmetry about the judicial outcome
 - Different beliefs about judicial outcome; optimum biases

Rules, Politics and Litigation

Under two conditions, there can be litigation:

- 1 Low initial offer is low. This can happen if
 - G has to make initial offer based on a signal of market value of property. However, the signal is noisy.
 - During negotiations the initial offer cannot be changed substantially
 - most states in the US have rules that the official offer cannot be more than 125 percent of the assessed market value
 - officials may fear being accused of corruption.
- 2 There are judicial delays and incumbent G can pass the burden on its successor
- 3 Safe play by government officials - use of manuals

Social Benefits of Litigation

If litigation happens the payoffs will be litigation payoffs.

Question

Are there social benefits of litigation?

- Litigation is desirable if it makes the law clearer
- A clear law is a public good
- The law can reduce second category of disputes, by providing clarity of judicial outcomes

Readings: Miceli (2003-04) Ch 8 Sections 1 and 2.

Eminent Domain Law

- Empowers the state to acquire private property for public purpose.
- Entitles the owner to compensation equal to the 'market value' of the property
- The market value is determined by using 'similar' properties that have been transacted through voluntary exchanges.
- Acquiring department assesses market value and offers to the owner.
- The owner can accept or reject the offer.
- The owner has right to litigate the compensation amount, if not satisfied with the compensation offered by the condemnor.

De-jure Entitlements Vs De-facto Payoffs I

- Compensation is required to be based on (equal to) the 'Market' value.
- Instances of litigation over compensation are frequent.
- The differences between the compensation received, on one hand, and the market value, on the other hand, is significantly large, especially for very low and very high value properties, Munch (1976) and Chang (2008);
- Compensation for high-value properties is much greater than their market value;
- Compensation for the low-value properties is significantly less than the market value.

De-jure Entitlements Vs De-facto Payoffs II

- The regressive nature of compensation persists, regardless of whether the compensation is received by accepting the official offer or through the litigation process.
- A study of 798 properties in Chicago by Munch (1976) concludes:
“low-valued properties receive less than market value and high-valued properties receive more than market value,” and “[a]s a rough approximation, a 7,000 parcel receive about 5,000, a 13,000 property breaks even and a 40,000 property may get two or three times its market value.”
- For New York City, Chang (2010) shows similar results.

Evidence from India:???

Issues/Questions

- What is the basis used by the government and courts, for determination of compensation/market price
- Why there is rampant litigation over compensation amount?
- Why are the gains from litigation different for the high and the low value properties?
- What are the incentives for the actors and agencies involved: Owners, Government officials, Lawyers and Judges?
- Why is the compensation structure under eminent domain laws regressive?

Existing Literature: Limitations

Theoretical literature on the subject

- Attributes above-mentioned outcomes to
 - ignorance of low-valued properties (Chang (2008)),
 - poor quality of government lawyers (Munch (1976), and Bell and Parchomovsky (2007)), and
 - different precedent values of court awards (Posner (2003)).
- Takes 'black-box' view of litigation:
 - assumes litigation costs to be fixed and exogenously given. (see Nalebuff (1987), Bebchuk (1984), Shavell (1989) Spier (2005), Chone and Linnemer (2010), Friedman and Wittman (2007), Howard et al. (2000), Daughety and Reinganum (2005)).
 - court can correctly ascertain the quantum of obligations of the defendant.
- Informational asymmetry among litigants not sufficiently analyzed.
- Information acquisition by uninformed party not sufficiently analyzed.

- model the incentive structure for owners and officials
- consider symmetric as well as asymmetric information structure
- show that the following factors account for the above-mentioned findings:
 - The incentive structures for official
 - the award makers - commonly known as the Land Acquisition Collectors
 - the government lawyers during litigation
 - The incentive structure for the owners
 - Informational Asymmetry among the parties involved
- Courts are assumed to be neutral

Model: Features

We

- allow litigation efforts to be endogenous choices.
- allow for informational asymmetry between litigant.

Our results apply to any bargaining situation where:

The disagreement payoffs are

- stochastic.
- interdependent - the higher are payoffs for one party, the lower will be the payoffs of the other.
- endogenously determined by each party's effort.
- asymmetric information.

Model: Basics I

- Two parties: Owner, O and Government, G .
- O has property of value r .
- At $t = 0$, O learns about r .
- The law entitles O to claim compensation from G .
- At $t = 1$, G makes a Take-it-or-Leave-it offer, denoted by r^o to O .
- If offer is rejected, litigation takes place at $t = 2$.

Model: Basics II

- During litigation the two parties choose litigation efforts to play Nash equilibrium.

Let,

- x denote the litigation effort put in by O ;
- y denote the litigation effort put in by G ; and
- r^c denote the court awards.
- Fixed cost of litigation efforts is x_0 and y_0 .
- The cost of effort function is given by $\psi(\cdot)$. Assume $\psi'(\cdot) > 0$ and $\psi''(\cdot) > 0$.
- At $t = 1$, uncertainty about the court awards.

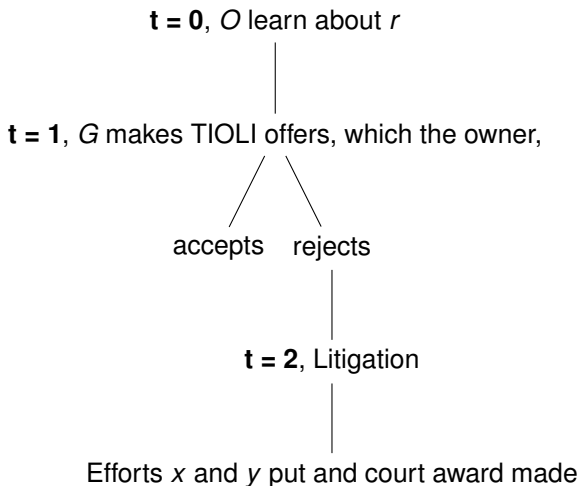
Model: Basics III

- r^c is a random variable with support $[\underline{r}^c(r), \bar{r}^c(r)]$, and
- $F(r^c|r, x, y)$ and $f(r^c|r, x, y)$ as the conditional distribution and density function, respectively.
- The expected court award is given by:

$$E(r^c|r, x, y) = \int_{\underline{r}^c(r)}^{\bar{r}^c(r)} r^c f(r^c|r, x, y) dr^c$$

- Plausibly, $\frac{\partial E(r^c|r, x, y)}{\partial r} > 0$, $\frac{\partial E(r^c|r, x, y)}{\partial x} > 0$ and $\frac{\partial E(r^c|r, x, y)}{\partial y} < 0$.
- Marginal gains from litigation effort decrease with effort levels, i.e., $\frac{\partial^2 E(r^c|r, x, y)}{\partial^2 x} < 0$ and $\frac{\partial^2 E(r^c|r, x, y)}{\partial^2 y} > 0$.

The Game Tree



Equilibrium

Given y and r , the O solves:

$$\max_x \{E(r^c | r, x, y) - \psi(x) - x_0\}, i.e., \quad (2.1)$$

$$E_x(r^c | r, x, y) - \psi'(x) = 0. \quad (2.2)$$

For given x , G solves:

$$\min_y \{\lambda [SE(r^c | r, x, y) + y_0] + \psi(y)\}, i.e., \quad (2.3)$$

$$-\lambda S \frac{\partial E(r^c | r, x, y)}{\partial y} - \psi'(y) = 0; \quad (2.4)$$

where

λ is the weight put by G on the costs of litigation to the exchequer.

Let the solution be:

$$(x^*(r), y^*(r, \lambda))$$

$\lambda < 1? |$

- Smt. Poonam v. State of Haryana and another (R.F.A. No. 3008 of 2008), the HC of P and H observed

"This court is constrained to comment upon the conduct of the State as well as HUDA ...

even though they had notice of the fact that the land owners had produced on record various sale deeds showing the consideration paid therein ranging from Rs. 12,00,000/- to Rs. 80,00,000/- per acre, no documentary evidence was led by the State or HUDA to rebut this evidence. ...

What is generally seen is that practically no evidence is led by HUDA in any of the cases before the Reference Court and similar is the position with regard to addressing arguments before the higher courts..."

$\lambda < 1? \text{ II}$

- State of Haryana and another Vs. Gram Panchayat of village Jharsa and another (R.F.A. No. 2125 of 2010), the HC of P and H observed

“ What has been experienced in number of cases, which came before this court is that in none of the case(s), wherever HUDA was represented by a counsel, anything was done by him except getting his presence marked.

The position is not different even in the proceedings before the court below.”

Expected Court Awards

For symmetry and simplicity, let

$$\frac{\partial^2 E(r^c | x, y)}{\partial y \partial x} = 0.$$

$$E(r^c | r, x, y) = \phi(r)(ax^{\frac{1}{k}} - by^{\frac{1}{j}}),$$

where $j, k > 1$. Note:

- $k = j$ and $a = b$: lawyers of O and G are equally capable.
- $k = j$ and $a > b$: lawyer of O is more capable than that of G.
- $k = j$ and $a < b$: lawyer of G is more capable than that of O.
- $a = b$ and $j > k$: lawyer of O is more capable than that of G.
- $a = b$ and $j < k$: lawyer of G is more capable than that of O.