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## THE EFFECTS OF EXAGGERATION IN LABOR LAWSUITS IN MEXICO\*



**Alexander Gotthard**

**David S. Kaplan**

**Joyce Sadka**

**[Estados Unidos / México]**

Licenciado en Economía, Instituto Tecnológico Autónomo de México. Programa de Maestría en Teoría Económica, Instituto Tecnológico Autónomo de México.

Doctor en Economía por la Universidad de Cornell. Especialista en Desarrollo del Sector Privado. Unidad de Análisis Empresarial del Banco Mundial.

Doctor en Economía por la Universidad de Rice. Licenciada en Derecho por la Universidad George Mason. Profesora de Economía del Centro de Investigación Económica del ITAM.

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\* We thank Cesar Acosta, Juan Luis Enciso, Fernando Espino, Argelio Gazca, Gerardo Marquez, and Adrian Muñiz and for data collection and research assistance. Financial support from the Interamerican Development Bank and the Asociación Mexicana de Cultura is gratefully acknowledged.

## **Resumen**

Este artículo utiliza datos obtenidos por los autores del archivo de una junta laboral local en el Estado de México. El derecho laboral en México obliga a las juntas laborales a registrar en el expediente de una demanda la cantidad intercambiada como parte de un convenio antes de llegar a un laudo. Este registro permite que examinemos el efecto de diversas estrategias de las partes sobre los resultados de las demandas, incluyendo los convenios. En particular, este trabajo se enfoca en la decisión del trabajador de demandar horas extra como parte de su demanda total contra la empresa. Las horas extra no son generalmente sujetas a verificación, especialmente en juntas laborales locales donde la mayoría de las empresas, siendo medianas y pequeñas, no tienen procesos formales para registrar horarios de trabajo. Además, la jurisprudencia en materia laboral sugiere que los presidentes de juntas laborales deben evaluar de manera conservadora los reclamos no verificables de horas extra. Esto quiere decir que no deben reconocer un número exagerado de horas extra. Encontramos que estos reclamos, aunque con frecuencia parecen exagerados, afectan positivamente la cantidad de compensación obtenida por el trabajador cuando el proceso acaba en un laudo. Cuando el proceso acaba en un convenio, encontramos que si el abogado es privado, el demandante obtiene más compensación si pide más en horas extra. Con abogados públicos el resultado es el opuesto: el demandante tiende a obtener menos compensación si pide más horas extra. Este último resultado podría reflejar estrategias muy diferentes, relativo a las horas extra, entre abogados públicos y privados. Alternativamente podría reflejar un efecto de selección, es decir que los casos que utilizan un abogado público son diferentes, tanto en características observables como no observables, a los casos que utilizan un abogado privado.

## **Abstract**

This paper uses data gathered by the authors from the archives of a local labor court in the State of Mexico to study the effects of overtime claims on lawsuit outcomes. Labor law in Mexico dictates that labor courts must record the amounts of compensation in all pre-trial settlements. This allows us to measure the impact of strategies chosen by the parties on all lawsuit outcomes, including settlement. In particular, this paper focuses on the plaintiff (employee)'s choice of overtime claim as part of her total claim. Overtime claims are generally unverifiable, particularly because firms that are sued in this court tend to be small or medium-sized firms that do not have formal time-keeping procedures. In addition, labor jurisprudence indicates that judges in labor courts should evaluate unverified overtime claims conservatively, that is they should not recognize unreasonable amounts of overtime. We find that these overtime claims, although often large enough to be considered unreasonable, do affect court rulings, making them more favorable to workers. In addition, in cases that settle, workers whose cases are handled by private lawyers tend to receive higher payments as their claims contain relatively more overtime, while workers whose cases are handled by public lawyers tend to receive lower payments as their claims contain relatively more overtime. This may indicate that private and public lawyers choose very different strategies in relation to the amount of overtime claimed, but may also reflect the selection effect of lawyer type, that is the fact that cases going to public lawyers tend to be different, in both observable and unobservable ways, from cases going to private lawyers.

## Introduction

Labor law in Mexico is highly protective of workers. However, using data from individual lawsuits filed by workers after being fired by their employers, we find that workers in fact receive a much smaller amount than what they ask for. An important consideration is that what workers claim in a firing lawsuit may exaggerate the amount of compensation they are owed under the law based on the true facts of the case.

To study possible exaggeration and its effects on the outcomes and success in lawsuits, we select an element of the labor claim that is most easily given to exaggeration, namely unpaid overtime. Overtime hours claimed may be useful as a measure of exaggeration for two reasons. First, they are generally unverifiable from the perspective of the worker. Even if the firm uses time-cards to record workers' daily hours, and even if the firm keeps such records over long periods of time, the worker will very rarely have access to this type of proof. Second, labor jurisprudence from appeals courts in Mexico indicates that when a worker claims uncompensated overtime for the entire period of time she worked at the firm, the labor court may choose to accept only a "reasonable" proportion of the overtime as valid.

From the policy perspective, it is important to figure out how much workers exaggerate in their unfair dismissal claims, and what the effects of such exaggeration are. In previous work on similar data we find that workers generally receive a much smaller (less than 30% of their claim). Amount of compensation than what they initially demand. This may lead policy makers to believe that the actual protections afforded by the labor law in Mexico are far lower than the letter of the law would indicate. On the other hand, if workers receive much less than they claim because a large part of their claim is exaggerated, then perhaps the protections provided to workers by Mexican law are not so ineffective.

Using overtime hours and the worker's overall claim, we propose several measures of possible exaggeration by plaintiffs in firing lawsuits. We provide descriptive statistics of these measures and econometric analysis of their effects on lawsuit outcomes, in particular on worker success, controlling for other case characteristics that we observe.

This chapter is divided as follows. Section 2 provides a brief review of relevant literature in the areas of litigation and communication games. Section 3 discusses Mexican labor law and enforcement institutions. Section 4 provides and discusses statistical results. Section 5 concludes and offers suggestions for further work.

## 1. RELATED LITERATURE

Here we review related literature on bargaining, litigation, and more specifically on bargaining games in which costless communication between the players is allowed. In the standard litigation model, parties bargain to decide whether to settle a case or take it to court. Since going to court is always (and rightly) assumed to be costly, parties would never go to court unless they had divergent expectations about their chances of winning in court.

One well-known model of divergent expectations that results in trials is Priest and Klein (1984).<sup>1</sup> These authors propose a non-strategic model of pretrial bargaining. Each party draws an independent signal from the same distribution of probabilities of plaintiff prevailing in court, and using this signal as well as her costs of going to court, sets a minimum (or maximum) amount of feasible settlement. If the plaintiff's minimum is lower than the defendant's maximum, then settlement occurs, otherwise they go to court.

Priest and Klein assume that plaintiffs and defendants have access to signals of equal accuracy. Hence as these signals become more accurate, plaintiffs' win rate at trial should tend to 50%, regardless of the position of the legal standard with respect to parties' behavior. While many studies have failed to verify that the 50% win rate hypothesis is correct, this is mostly likely due to the highly restrictive nature of the model's assumptions. As shown below, we find that controlling for case characteristics and claims made by the worker, the latter receives much lower compensation on average when her case goes to trial. This indicates a negative selection effect of going to court, i.e. cases that go to court are weak cases for the plaintiff. This suggests a framework in which there is asymmetric information, so that the worker is either initially or eventually less informed about the value of the lawsuit than is the firm.

P'ng (1983) one-sided asymmetric information in pretrial bargaining.<sup>2</sup> With an exogenously fixed settlement amount, he shows that in the Nash

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<sup>1</sup> Priest, George L. and Benjamin Klein (1984). The Selection of Dispute for Litigation, *The Journal of Legal Studies* 13(1): 1-55.

<sup>2</sup> P'ng, I.P.L. (1983). Strategic Behavior in Suits Settlements and Trial, *The Bell Journal of Economics* 14(2): 539-550.

equilibrium no information will be revealed by the informed party. Therefore, in this setup the average quality of cases that settle and go to court may be the same. Bebchuk (1984) allows the uninformed party to choose an amount that is offered as a settlement to the informed party.<sup>3</sup> He shows that in equilibrium the cases more likely to settle are those in which the informed party has a lower likelihood of winning at trial, so that on average cases that go to trial will be relatively favorable to the informed party. Our evidence is consistent with this result.

Since our main goal is to examine the possibility that plaintiffs exaggerate their claims using their overtime claim, our paper is related to theory on games with costless communication between players, commonly called “cheap-talk” games. These games are to be distinguished from signaling games because signals imply some cost to the player that sends the signal, and are more costly for some player types, which can give rise to a signaling equilibrium. In cheap talk games, a player with some private information can make a statement without paying any cost. Given that there is no explicit cost to making an overtime claim, and these claims are not generally verifiable, we can consider the overtime claim made by the worker as costless communication.

The seminal paper on cheap talk is Crawford and Sobel (1982).<sup>4</sup> They develop a model in which a better informed sender gives a noisy signal to a receiver. With that information, the receiver takes an action which determines the payoffs of both in equilibrium. They find that in a Bayesian-Nash Equilibrium, the sender partitions the support of the probability distribution of the variable that represents his private information and only informs the receiver about the element of the partition in which the information lies. The number of elements in the partition depends on how aligned the preferences of the players are. When the goals of the two agents coincide, the sender tells the receiver his actual value.

In our context, the plaintiff is sending the “message” by making an overtime claim. While we see the employer as having better information about the likelihood of the worker prevailing in court, clearly the worker has some relevant private information, such as his opportunity cost of time, discount rate, or simple willingness to go to court. On the receiving end of this message, there are two relevant agents, the firm and the judge. In our results below we find that the final payment ordered by the judge in cases that go to court does depend on the overtime claim made, and

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<sup>3</sup> Bebchuk, Lucian Ayre (1984). Litigation and Settlement under Imperfect Information, *The Rand Journal of Economics* 15(3): 404-415.

<sup>4</sup> Crawford, Vincent P. and Joel Sobel (1982). Strategic Information Transmission, *Econometrica* 50(6): 1431-1451.

also find evidence that the final payment received by the worker is related positively to relative measures of exaggeration.

Kim (1996) develops a model in which a plaintiff knows the exact value of his case and a defendant only knows its probability distribution, and the two parties engage in pre-trial settlement negotiations.<sup>5</sup> In this context, infinitely repeated interaction between a defendant and plaintiff can make cheap talk more credible and makes more outcomes feasible. This is because players are concerned about their reputation. If they use “costless” communication in an opportunistic way to achieve current gains, they will lose future payoffs because of damaged reputation. Cheap talk can thus be effective at making the informed party reveal its true value. Aumann and Hart (2003) sustain that “long” cheap talk (the better informed party is allowed to send more than one message) expands the set of outcomes of a game in contrast to an environment where only a single message is allowed, and allowing long cheap talk may thus lead to outcomes preferred by all players.<sup>6</sup>

As far as we know, there is no empirical work verifying cheap-talk models’ predictions in the context of litigation. This is due mostly to the fact that in many data sets on litigation, there is no information about the initial claim made by the plaintiff, and also no information about the specific components of this claim. Empirical work in this area has focused mostly on experimental data. Pecorino and Van Boening (2004) design a bargaining experiment between a plaintiff and a defendant under asymmetric information. There are two possible types of plaintiff, with different distributions of damages for each type.<sup>7</sup> They set up several treatments, allowing cheap talk in one of them. They find that with cheap talk, there is no increase in the settlement rate for plaintiffs with strong cases, but they observe that when a player says she is a high type, she gets a higher settlement offer. These results are somewhat consistent with ours. We find that our constructed variables for exaggeration have no significant effect on the mode of termination of a lawsuit, but are positively correlated to the final payment received by the worker.

## 2. LEGAL BACKGROUND

Mexican labor law is highly structured and regulates most aspects of the employment relationship. Since we deal with firing lawsuits and with

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<sup>5</sup> Kim, Jeong-Yoo (1992). Does Cheap Talk Matter in Pre-trial Negotiation? *Seoul Journal of Economics*, 5(4): 301-315.

<sup>6</sup> Aumann, Robert J. and Sergiu Hart (2003). Long Cheap Talk, *Econometrica* 71(6): 1619-1660.

<sup>7</sup> Pecorino, Paul and Mark Van Boening (2004). An Empirical Analysis of Bargaining with Voluntary Transmission of Information, *Journal of Legal Studies* 33(1): 131-156.

elements of the worker's claim which include fringe benefits and overtime, we will focus on related sections of the law. To begin with, note that although we study the application of this law in a local labor court in the State of Mexico, labor law is federal in Mexico, as is the jurisprudence (the equivalent of precedents under US law) which the court we study is obliged to follow.

All regulations discussed here apply to both formal and informal sector workers. The usual definition of an informal worker is one who is not registered by the employer at the Social Security Administration (*Instituto Mexicano del Seguro Social*, or IMSS). However, under labor law being an informal employee is not considered to be the fault of the worker, but rather of the employer. In fact, informal workers may choose to sue under the labor law in order to force their firm to register them at IMSS as well as to pay other taxes related to pensions. While we do not observe any lawsuits filed solely for this purpose, in 35% of the cases we observe, in addition to claiming unfair dismissal, the plaintiff demands that the firm pay back taxes for social security and pensions. In court rulings, judges stipulate that firms must pay these back taxes in 89 cases, roughly 10% of the cases in which these benefits are claimed.<sup>8</sup>

In what follows we discuss the rules on fringe benefits, length of workday and workweek, compensation for overtime, and the procedures and costs of firing. Fringe benefits are mainly composed of vacation pay and an end-of-year bonus. Vacation days per year are determined by worker tenure, and for each of those days the worker is entitled to 125% of her daily salary.<sup>9</sup> Also, every employee is entitled to an end-of-year bonus of at least 15 days' wages.<sup>10</sup>

A normal workweek is defined as having up to 48 hours. If an employee works more than 48 hours, she is entitled to overtime pay. The law mandates double pay for up to 9 hours of overtime, and triple pay for any hours above 57 per week. However, working more than 57 hours per week is considered illegal except in case of an emergency.<sup>11</sup>

Firing is viewed as justified or unjustified under the law. Firing for just cause requires clear obvious wrongdoing on the part of the workers, such as repeated and unexplained absences, repeatedly showing up drunk to work, deliberately destroying the firm's physical capital, and

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<sup>8</sup> Interestingly, claiming social security benefits drives a wedge between the amount of money the firm may have to pay if it loses, and the amount of money the worker will receive. This is equivalent to raising the stakes for the firm but not for the worker, and could possibly have a different impact on settlement rates and amounts.

<sup>9</sup> Articles 76 and 80, *Ley Federal del Trabajo* (LFT).

<sup>10</sup> Article 87, LFT.

<sup>11</sup> Articles 65-68, LFT.

attacking a supervisor.<sup>12</sup> Firing for other reasons, such as low worker productivity, or layoffs during a recession, is considered unjustified and implies a much higher firing cost.<sup>13</sup>

Whether a dismissal has just cause or not, the firm must cover all payments owed to the worker up to the firing date, including overtime, unpaid end-of-year bonuses, as well as the percentage of the worker's fringe benefits that corresponds to the proportion of the last year in which the worker was employed. Additionally, the worker is entitled to severance pay equivalent to 12 days' wage for each year worked, with wage/day capped at twice the minimum wage.<sup>14</sup>

At the time of firing the firm must notify the worker of the exact cause of firing as defined under the law, at which time the worker may decide to sue, claiming that the firm in fact has no legally acceptable cause for firing, and demanding reinstatement.<sup>15</sup> In all lawsuits related to firing, the firm carries the burden of proving that it fired the worker for just cause.<sup>16</sup>

Clearly in relation to firing the letter of the law favors workers highly. Hence unjustified firings constitute the vast majority of worker-job separations, and in these cases the firm incurs much greater costs. To begin with, a worker who proves that she was fired without justification can ask to be reinstated in her job.<sup>17</sup> For the majority of workers, the letter of the law indicates that unless the firm can prove justification for firing, it cannot defeat the work's plea for reinstatement.<sup>18</sup>

One category of workers cannot demand reinstatement. Called *trabajadores de confianza*, these are essentially managerial employees as well as those with direct contact with the firm owner or top executives (such as executive secretaries or assistants).<sup>19</sup> While some studies translate this term as "at-will employees", they are only at-will in

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<sup>12</sup> Not that "unexplained absence" is not defined in the LFT, and anecdotal evidence suggests that it is quite difficult for employers to fire their workers on this basis alone.

<sup>13</sup> Article 47, LFT.

<sup>14</sup> Article 162, LFT.

<sup>15</sup> The worker is to be informed in writing of the cause of firing. Failure to notify in writing and in a timely fashion implies that the firing is considered unjustified under Mexican labor law, regardless of the underlying cause. Article 47, LFT.

<sup>16</sup> Article 48, LFT.

<sup>17</sup> In case the worker is reinstated, she receives only back-pay plus fringe benefits for the period of time from firing to reinstatement. Article 48, LFT.

<sup>18</sup> Considering that low worker productivity is not a valid cause to for firing, the right to demand reinstatement probably constitutes a large firing cost for employers, regardless monetary firing costs. In our data we find 17 instances in which the judge orders reinstatement, but no cases in which reinstatement appears to have effectively taken place. Clearly, however, the right to reinstatement could affect workers' bargaining power and lawsuit outcomes.

<sup>19</sup> Articles 9 and 49, LFT.

the sense that the firm cannot be forced to reinstate them, and not in the sense that the firm may fire them without severance pay, which would be the case for employees classified as “at-will” under US labor laws. Other than these managerial workers and personal staff, the firm need not reinstate temporary workers and those with less than one year of tenure at the firm.

When a worker is fired without just cause and is not reinstated, besides the payments discussed above for all firings, the worker receives full pay including benefits for the period between the date of firing and the date of payment by the firm, following either a settlement or court ruling. In addition, the worker receives severance pay of 90 days with benefits, and if the worker is classified as managerial or personal staff, she received an additional 20 days of wage per year worked at the firm, with benefits and with no cap on the wage.<sup>20</sup>

Besides the payments owed to all workers separated from their jobs, all workers fired unjustifiably are owed two types of payments. First, they receive back pay including benefits covering the period between the date they were fired and the date at which the court’s decision in the lawsuit is executed. Second, they receive three months’ salary with benefits. In addition, those workers for whom the firm can refuse reinstatement are entitled to 20 days’ wage plus benefits for each year worked, without any cap on the wage rate. Finally, workers found to have been fired without just cause receive back pay including benefits covering the period between the date they were fired and the date at which the court’s decision in the lawsuit is executed.

A firm may also avoid having to reinstate workers it fires without just cause in the case of layoffs that are warranted given the economic situation of the firm. However, this is a cumbersome and costly process involving hearings and expert testimony, in which workers and their representatives such as unions participate along with the firm, and after which the firm is still considered to be firing workers without just cause under the law.<sup>21</sup> In our sample we do not find any layoff cases, although we do see instances of mass firings that appear to be layoffs; however, the firm chooses to treat these as individual firing situations that all happened to occur simultaneously. Our interpretation of these data is that the formal layoff procedure is highly inefficient, so that firms basically never use it.

Labor courts in Mexico, called *Juntas de Conciliación y Arbitraje*, are in fact administrative courts that belong to the Federal Department of Labor, in the case of federal labor courts, or to the State Department of Labor, for state-level courts such as the one we examine in this paper.

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<sup>20</sup> Articles 48 and 50, LFT.

<sup>21</sup> See Articles 434-II and 900-919, LFT.

Since labor law is federal, state and federal courts apply the same statutes. Federal jurisdiction is reserved for a list of industries which at the time the labor law was written were considered large or strategic. Residual jurisdiction belongs to state-level courts, and is determined by the geographical location of the firm. All states have at least one *Junta Local de Conciliación y Arbitraje*, although many of the larger states will have several districts with a court in each.

As their title suggests, these courts serve both mediation and adjudication functions.<sup>22</sup> When a lawsuit is filed, the first hearing held is a conciliation hearing in which a court clerk supposedly will promote possible settlement agreements between the parties. If settlement occurs at this or any other point before the final court ruling, the court approves and records the details of the settlement, and the procedure ends.<sup>23</sup> Should settlement fail to occur, a subsequent hearing similar to a trial is held. After this hearing the judge makes a ruling on matters of law and of fact, and submits this ruling to the labor “board” consisting of himself, a lay representative of labor, and a lay representative of industry. The ruling becomes final when at least one of the lay representatives votes along with the judge in favor of the decision.

Finally, since we study the effects of overtime claims, it is important to note that labor jurisprudence, while not conclusive, frowns on using these claims to exaggerate the worker’s total claim. In early 2000, as part of its response to an appeal from a labor lawsuit, the administrative and labor division of the Appeals Court for the 4th Circuit published jurisprudence relating to how courts should treat a firing lawsuit in which the worker claims unpaid overtime over her entire tenure at the firm.<sup>24</sup> The statement made by the court explicitly prohibits judges from discarding such a large overtime claim solely on the grounds that the worker does not have full proof. However, the court proceeds to state that labor judges must “ponder” the fact that the worker had never claimed overtime during her entire tenure at the firm, and must require some concrete proof from the worker, otherwise the judge should “limit” the compensation due to the worker under this part of the claim.

Labor lawyers with whom we consulted consider that this jurisprudence is tantamount to shifting the burden of proof from the firm to the

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<sup>22</sup> Title 14, LFT, establishes these courts and describes their functions.

<sup>23</sup> In fact, out-of-court settlements only become valid under labor law in Mexico when they are ratified by the relevant labor court, which leads us to believe that dropped cases mostly indicate the worker actually received no compensation.

<sup>24</sup> Jornada Extraordinaria, Demanda Contestada en Sentido Afirmativo. Para determinar su pago, la Junta DEBE PONDERAR EL HECHO DE QUE DURANTE EL TIEMPO DEL SERVICIO NUNCA SE HUBIERE RECLAMADO. Segundo Tribunal Colegiado en Materias Administrativa y de Trabajo, Cuarto Circuito.

worker, when it comes to large, but not necessarily all, overtime claims in the context of a firing lawsuit. Hence, one might expect to find that large overtime claims are either irrelevant in explaining the amount of compensation awarded by the court or received in a settlement, or that these large claims are even counterproductive because judges discard the overtime claim itself and also suspect exaggeration in other elements of the claim. As we discuss in section 5, we find that overtime claims, including large ones, positively impact the amount of money received by the worker at the end of the lawsuit.

### 3. DATA

Our data set consists of all labor lawsuits filed at the *Junta Local de Conciliación y Arbitraje del Estado de México, Valle de Cuautitlán-Texcoco*, during 2000 and 2001. The data were obtained by the authors in conjunction with a confidentiality agreement under the Mexican Freedom of Information Act.<sup>25</sup> We collect data from the 718 cases initiated in 2000 and the 1,850 cases initiated in 2001.

For each lawsuit, we code the motive for filing (generally unjust dismissal) and the date of filing. We extract detailed information about the claim from the initial statement filed by the worker and her lawyer. Here we register the job description, date the worker began at the firm, alleged firing date, salary, fringe benefits, hours, the specific demands made by the worker, including overtime, as well as some worker characteristics such as age and gender. In this paper we analyze only firing lawsuits; in these procedures the worker generally claims reinstatement, back pay, severance pay, benefits, and overtime pay.

We observe how each lawsuit ended, whether by being dropped, by settling, or by going to court and obtaining a court ruling. As explained above in section 3, labor courts in Mexico are atypical because they have a mandate to ratify and record all settlements that terminate a filed lawsuit. Hence, we observe detailed information about payments received by workers in both settled and tried cases.

We observe the date the procedure ended as well as any payment received by the worker. For trial decisions, we observe whether the judge characterizes the ruling as being in favor of the firm, in favor of the worker, or mixed. Also, we record the votes in favor of or against the judge's ruling, by the lay magistrates that represent general labor or industry interests. Finally, for court rulings we observe the facts that are conceded by the judge and the corresponding elements of the award, including the overtime claim. When a court ruling results in a constitutional appeal (or

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<sup>25</sup> Ley Federal de Transparencia y Acceso a la Información Pública Gubernamental, 2002.

more), we observe the number of these appeals, and if there is a subsequent court decision after appeal, we keep data from the first and last court rulings.

#### 4. STATISTICAL ANALYSIS

We begin our analysis of the data by describing the overtime claims made by plaintiffs, and comparing these claims to two benchmarks. Under Mexican labor law, the normal work week consists of a maximum of 48 hours, and the maximum number of overtime hours per week is 9. We calculate given the worker's per hour wage the peso amount of her overtime claim for one year, or for the number of weeks she worked if her tenure is below one year. We chose one year as a benchmark because we were told by the officials at the public labor prosecutor's office that a rule of thumb used by many public lawyers was to only demand one year's worth of overtime hours, due to the fact that judges generally applied labor jurisprudence discussed above by not awarding more than one year of overtime. Another benchmark we calculate is the same 9 hours per week, for the entire tenure of the worker. Since this is the maximum amount of legal overtime the worker could have accepted, it can be seen as an upper bound on overtime claims.

Table 1 reports these two benchmarks, the overtime claim, and the ratio of claimed hours to imputable hours over one year and over the entire tenure. We report statistics for all lawyers and then for private and public lawyers separately. Clearly public lawyers tend to request much smaller amounts of overtime, although they do demand almost three times what the rule of thumb cited to us would indicate. Private lawyers on the other hand claim very high amounts of overtime, on average more than six times the imputable overtime for one year. This may reflect a difference in strategies used by private and public lawyers, including instructions received by public lawyers to claim low amounts of overtime. However, it may also reflect differences in the underlying characteristics of cases that go to public lawyers vs. private lawyers. Specifically, since overtime actually worked is unverifiable, it is possible that fired workers who have a larger true overtime claim are more likely to opt for private lawyers. As discussed above, we examine overtime as a good candidate for exaggeration because of its unverifiable nature, however we cannot assert that overtime claims consist wholly of exaggeration.

Since we will examine the effects of overtime claims on court awards, we report statistics on the proportion of overtime claims awarded by each judge. Table 2 shows that there is considerable variation in the proportions of overtime claims awarded by the 17 judges we observe in our dataset, including judges with relatively large number of court awards.

While lawyers' claims may be entirely driven by the selection effects of case assignments to public or private lawyers, this is not likely to be the case for judges because case assignments to judges are not controlled by parties. During 2000, cases were assigned to a *Junta* based on the geographical location of the defendant firm. As of the beginning of 2001, all four Juntas were moved to the same location and cases were assigned in a round robin-fashion: the first case filed on a given day goes to Junta 1, the second case to Junta 2, and so on. The number of judges is larger than the number of Juntas because judges are changed or rotated during the time period. Since these judges are civil servants in the Department of Labor of Mexico State, they may be moved in and out of judicial posts many times during their careers.

To further investigate the effects of overtime claims on court awards, we construct the following variables:

*Exaggeration:* We subtract the cash value of one year's worth of overtime hours (9 hours per week as explained above) from the overtime claim made by the plaintiff. If the worker has tenure below one year, we subtract the value of 9 hours per week worked from the claim. When our calculation yields a negative number, we set exaggeration to zero.

*Imputed claim:* This is what the worker would be entitled to under Mexican law given her firing is found to be unjustified, and based on parts of the claim which are easily verifiable such as salary and tenure. The variable is the sum (conditional on claiming each element) of the following: unpaid wages during the month the worker is fired (for example if he is fired on the 21st and gets paid at the end of each month, he is owed 21 days of wages), 3 months of wage (constitutional indemnity awarded to workers fired unjustly), 12 days of wage per year worked (tenure benefit for all fired workers; the calculation caps wage at twice the minimum wage), and 20 days of wage for each year worked in case the worker is classified as "at will" (the law does not cap wages for this calculation).

Table 3 shows results from regressing the judge's award in cases that go to court against the imputed claim as well as a dummy for worker gender. We find weak evidence that a larger overtime claim is correlated with a higher court ruling, and also that women, especially those with private lawyers, do relatively worse in court rulings. In all our regression analysis we report both OLS and Tobit specifications. The latter is necessary because our left hand side variable is censored at zero, and indeed the court award and the amount of money received at the end of the process by the worker are often zero. It is important to note that using the Tobit specification, once the imputed claim is accounted for, the overtime claim is not statistically significantly correlated to the award.

Table 4 attempts to measure the effect of a measure of relative exaggeration, by using the exaggeration variable as a proportion of the im-

puted claim. Interestingly, we now find no significant results when all lawyers are grouped together, but find statistically significant results with opposite signs for private and public lawyers. For private lawyers, as overtime claim grows as a proportion of the imputed claim, the judge's award increases; for public lawyers, increasing relative exaggeration is correlated to lower judge awards. There are two possible explanations of this difference between private and public lawyers. First, the selection of cases to private vs. public lawyers is non-random: individuals who opt for a public lawyer may on average have less income, lower claims, and perhaps have lower quality claims, including the overtime hours claimed. Second, discussions with public lawyers indicate that they are instructed to be conservative in overtime claims, in deference to jurisprudence that limits judges' awards in this area. Hence, public lawyers who make large overtime claims may be inexperienced or simply inept, so that along with the exaggerated overtime claim they generally handle the case badly, resulting in a low court award.

Next, we attempt a slightly different measure of relative exaggeration. We calculate exaggeration as a proportion not of the imputed claim, but as a proportion of the sum of the imputed claim and the overtime claim. Table 5 shows that for all lawyers, this measure of relative exaggeration is correlated to higher court awards and is statistically significant at the 95% confidence level in both the OLS and Tobit specifications. For private lawyers stronger results in the same direction obtain, while for public lawyers, we again find negative coefficients, but they are not statistically significant.

Tables 3-5 in general show that exaggerating one's claim of overtime hours does seem to be correlated to higher judge awards for private lawyers, and sometimes is correlated to lower judge awards for public lawyers. We now turn to a broader measure of success in the lawsuit, which includes all outcomes, namely dropped cases, settlements, and court awards. This allows us to exploit one extremely rare feature of our data, which is that we observe the amount of compensation received by the worker at the end of the process for all lawsuits, including settlements. Moreover, considering that the amount of money claimed in overtime could act as a signal or a message in a bargaining game, clearly the plaintiff would have to consider the effects of this message on the defendant's behavior as well as the judge's decision. Hence we would like to find out how claiming larger amounts of overtime affects the final payment received by the worker as well as the likelihood of reaching a settlement.

Table 6 shows the results of regressing the final payment on our imputed claim and measure of exaggeration, as well as a gender dummy and a dummy for whether the lawsuit ended up in court. In regressions of the final payment received by the worker, we report results including and ex-

cluding dropped cases. This is mainly because we do not observe directly why cases are dropped. Given the fact that Mexican labor law only considers settlements registered at the court to be legally binding, we do not believe that a large proportion of dropped cases represent settlements. Nevertheless, in case some of these cases are in fact plaintiff victories, we estimate each specification excluding dropped cases. When dropped cases are excluded, we find that women tend to do significantly worse than men in terms of the final payment received. However, when all cases are included there is some evidence that women do better on average. This result appears to be driven by the fact that women are much less likely to drop cases, which we will show in Table 9 below.

Our imputed claim turns out to be a good predictor of final payment, which indicates that this may be a good measure of the amount the worker is entitled to under the law. Our measure of exaggeration is not significantly related to the final payment for all lawyers. However, there is evidence that for public lawyers, exaggeration is again negatively and significantly related to final payment obtained, while for private lawyers the opposite relationship obtains, although the relationship is only statistically significant when dropped cases are included.

Finally, Table 6 shows a strong result which is consistent with other work on similar data, that controlling for other information about the lawsuit, the dummy indicating that a case went to court has a very strong and significant negative impact on the final payment obtained by the worker. This seems to indicate that the selection of cases that go to court is driven by a failure of bargaining between the worker and the firm, and that in this bargaining game the firm is more informed than the worker about the true value of the claim.

Table 7 reports results on a similar regression, that uses the proportion of exaggeration to the imputed claim rather than each variable separately. This proportion is not significantly related to the final payment received by the worker, except for the case of public lawyers when dropped cases are excluded, in which case it is negatively correlated with the final compensation. Table 8 reports results using our measure of exaggeration as a proportion of the imputed claim plus the overtime claim. As in Table 5, this measure of relative exaggeration appears to be significantly correlated to the amount of money received by the plaintiff. Both for all cases grouped together and for private lawyers, this measure of relative exaggeration results in higher amounts of final compensation for workers. For cases handled by public lawyers, it appears that more relative exaggeration leads to lower final compensation, although this result is only mildly significant when dropped cases are excluded.

Apart from the effects of exaggeration and relative exaggeration on court rulings and final payments received by plaintiffs, we would like to

investigate the possible effects of exaggeration on how the lawsuit ends. We test these possible effects in Table 9, which shows the results of a logit regression in which the dependent variable is each of the three case outcomes (drop, settle, or trial) when dropped cases are included, whereas when dropped cases are excluded, the dependent variable is the dummy indicating whether the case settled. Here results are mostly negative. The exaggeration variable does not appear to affect the mode of termination of the lawsuit, except for the cases of private lawyers, in which there is weak evidence that suit with higher levels of exaggeration tend to settle more often.

## 5. CONCLUSIONS

This paper exploits the fact that in data from individual firing lawsuits in the State of Mexico, we observe the claim made by the worker initially, as well as the components of this claim. Among the elements of the claim, overtime is almost always non-verifiable. Therefore we believe overtime claims are a good candidate to study possible exaggeration in the worker's claim. Clearly, without direct observation of the number of overtime hours worked during the worker's tenure at the firm, we cannot prove that these claims are habitually exaggerated. However, they are clearly susceptible of exaggeration, and therefore we focus on measuring the effects of overtime claims on the outcomes of lawsuits and the payments received by workers.

We find evidence that some information is conveyed to the judge through the worker's overtime claim. Controlling for other observable case characteristics, these claims do have a positive effect on final court awards to workers. In negotiations leading to settlements, exaggeration in overtime claims also appears to result in higher payments to workers, except for cases handled by public lawyers in which the opposite is true. However, in negotiations that lead to settlements, these claims do not seem to have a statistically significant effect on the probability of reaching a settlement.

Hence we conclude that our data may be consistent with a cheap talk situation in which workers send a "message" to firms and to the judge about their willingness to fight all the way to court, and this affects lawsuit outcomes, including settlement amounts. More work is needed, specifically we can exploit the fact once the claim is filed, cases are assigned randomly to judges, and there is significant variation across judges in the percentage of overtime claims that are granted.

**Table 1:** Overtime Claims (2002 pesos)

<b>All lawyers</b>					
	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
Imputed Overtime (1 year)	2487	24532.37	63023.27	45.3749	1422021
Imputed Overtime (tenure)	2487	150644.4	1168548	45.3749	49900000
Overtime Claim	2487	120400.5	573948.5	0	12100000
Claim Hours/Imputed Hours (1 year)	2487	3.972372	16.38514	0	591.4476
Claim Hours/Imputed Hours (tenure)	2487	1.252022	3.540819	0	116.2599
<b>Private lawyers</b>					
	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
Imputed Overtime (1 year)	1826	27664.06	67394.84	78.202	1422021
Imputed Overtime (tenure)	1826	179030.4	1350624	78.202	49900000
Overtime Claim	1826	152933.8	651905.3	0	12100000
Claim Hours/Imputed Hours (1 year)	1826	4.789938	18.50662	0	591.4476
Claim Hours/Imputed Hours (tenure)	1826	1.429538	3.890375	0	116.2599
<b>Public Lawyers</b>					
	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
Imputed Overtime (1 year)	661	15881.12	47951.63	45.3749	994454.1
Imputed Overtime (tenure)	661	72228.51	301438.1	45.3749	5591042
Overtime Claim	661	30527.77	233774.2	0	5546625
Claim Hours/Imputed Hours (1 year)	661	1.713861	7.565677	0	154.9714
Claim Hours/Imputed Hours (tenure)	661	0.761635	2.246234	0	34.0553

**Table 2:** Hours awarded/hours claimed  
(Judges' rulings only)

<b>Judge</b>	<b>Obs</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min</b>	<b>Max</b>
1	22	0.0403428	0.1311436	0	0.4832229
2	7	0.0759699	0.1814948	0	0.4857153
3	8	0.0933224	0.2639557	0	0.7465795
4	2	0.734142	0	0.734142	0.734142
5	62	0.3083267	0.6190027	0	2.682972
6	3	0.4994139	0.4922216	0	0.9841132
7	20	0.1536058	0.3510048	0	0.9729089
8	0				

Judge	Obs	Mean	Std. Dev.	Min	Max
9	9	0.0690815	0.1161092	0	0.3248049
10	32	0.3901083	0.9317888	0	4.933112
11	19	0.0566663	0.2201621	0	0.9589821
12	6	0.3008494	0.4715499	0	1.015844
13	46	0.1253637	0.4425081	0	2.698033
14	0				
15	0				
16	1	0	0	0	0
17	1	0	0	0	0

**Table 3:** Effects of imputed claim, exaggeration, and gender on judge's award (Dependent Variable: judge's award)

	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
In (imputed claim)	-0.019 (0.947)	0.053 (0.784)	-0.139 (0.666)	-0.028 (0.891)	0.520 (0.377)	0.47 (0.288)
In (exaggeration)	0.089 (0.271)	0.075 (0.185)	0.156 (0.104)	0.117 (0.072) *	-0.252 (0.182)	-0.159 (0.232)
female	-1.318 (0.144)	-1.053 (0.064) *	-1.791 (0.111)	-1.374 (0.04) **	0.159 (0.892)	0.115 (0.897)
R <sup>2</sup>		0.024		0.044		0.041
Number of obs	510	510	425	425	85	85
Censored obs	167		145		22	

General note on tables 3-9: P-values are reported in parentheses after each coefficient. Standard errors are calculated allowing for heteroscedasticity and for the possibility that the outcomes in cases that have been grouped into the same proceeding may be correlated. We use the notation of \*\*\* to denote significance at the 0.01 level. Similarly \*\* denotes significance at the 0.05 level and \* denotes significance at the 0.10 level.

**Table 4:** Effects of (exaggeration/imputed claim) and gender on judge's award

	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/imputed	0.052 (0.111)	0.038 (0.112)	0.082 (0.043) **	0.059 (0.048) **	-0.513 (0.060) *	-0.116 (0.000) ***
female	-1.389 (0.135)	-1.156 (0.046)	-1.863 (0.104)	-1.480 (0.028) **	0.237 (0.836)	0.168 (0.850)
R <sup>2</sup>		0.022		0.041		0.050
Number of obs	510	510	425	425	85	85
Censored obs	167		145		22	

**Table 5:** Effects of exaggeration/(imputed claim + overtime) and gender on judge's award

	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/imp.claim+ overtime	2.609 (0.037) **	2.050 (0.020) **	3.833 (0.007) ***	2.844 (0.003) ***	-5.54 (0.104)	-3.397 (0.120)
female	-1.246 (0.179)	-1.032 (0.075)*	1.710 (0.140)	-1.348 (0.047) **	-0.052 (0.964)	-0.044 (0.961)
R <sup>2</sup>		0.036		0.064		0.040
Number of obs	510	510	425	425	85	85
Censored obs	167		145		22	

**Table 6:** Effects of exaggeration, imputed claim, mode of termination and gender on final payment

	Dropped Cases Included					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
In (imp. claim)	0.316 (0.025) **	0.238 (0.002) ***	0.299 (0.096) *	0.225 (0.016) **	0.267 (0.177)	0.217 (0.094) *
In (exaggeration)	0.045 (0.221)	0.032 (0.146)	0.108 (0.020) **	0.062 (0.019) **	-0.125 (0.065) *	-0.075 (0.089) *
Court ruling	-8.053 (0.000) ***	-3.961 (0.000) ***	-8.450 (0.000) ***	-3.953 (0.000) ***	-6.619 (0.000)	-3.761 (0.000) ***
female	0.666 (0.064) *	0.407 (0.051) *	0.451 (0.323)	0.286 (0.252)	1.025 (0.051)	0.671 (0.054) *
R <sup>2</sup>		0.127		0.138		0.099
Number of obs	2,494	2,494	1,833	1,833	661	661
Censored obs	1,041		819		222	

	Dropped Cases Excluded					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
In (imp. claim)	0.291 (0.000) <sup>***</sup>	0.266 (0.000) <sup>***</sup>	0.253 (0.009) <sup>***</sup>	0.235 (0.001) <sup>***</sup>	0.298 (0.003) <sup>***</sup>	0.281 (0.002) <sup>***</sup>
In (exaggeration)	0.028 (0.106)	0.024 (0.075) <sup>*</sup>	0.036 (0.102)	0.026 (0.111)	-0.053 (0.042) <sup>**</sup>	-0.043 (0.058) <sup>*</sup>
Court ruling	-8.628 (0.000) <sup>***</sup>	-6.727 (0.000) <sup>***</sup>	-9.163 (0.000) <sup>***</sup>	-6.970 (0.000) <sup>***</sup>	-7.061 (0.000) <sup>***</sup>	-5.962 (0.000) <sup>***</sup>
female	-0.586 (0.001) <sup>***</sup>	-0.456 (0.001) <sup>***</sup>	-0.772 (0.001) <sup>***</sup>	-0.569 (0.001) <sup>***</sup>	-0.270 (0.125)	-0.247 (0.199)
R <sup>2</sup>						
Number of obs	1,850	0.592	1,348	0.621	502	0.511
Censored obs	406	1,850	343	1,348	63	502

**Table 7:** Effects of (exaggeration/imputed claim), mode of termination and gender on final payment

	Dropped Cases Included					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/imp. claim	-0.005 (0.685)	-0.002 (0.787)	-0.003 (0.800)	-0.001 (0.868)	-0.080 (0.118)	0.036 (0.114)
Court ruling	-8.075 (0.000) <sup>***</sup>	-3.967 (0.000) <sup>***</sup>	-8.547 (0.000) <sup>***</sup>	-4.006 (0.000) <sup>***</sup>	-6.513 (0.000) <sup>***</sup>	-3.705 (0.000) <sup>***</sup>
female	0.510 (0.155)	0.295 (0.158)	0.210 (0.648)	0.126 (0.621)	1.112 (0.031) <sup>**</sup>	0.727 (0.033) <sup>**</sup>
R <sup>2</sup>		0.119		0.127		0.089
Number of obs	2,494	2,494	1,833	1,833	661	661
Censored obs	1,041		819		222	

	Dropped Cases Excluded					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/imp. claim	-0.002 (0.781)	-0.001 (0.840)	-0.004 (0.666)	-0.003 (0.696)	-0.045 (0.046)**	-0.029 (0.027)**
Court ruling	-8.672 (0.000)***	-6.743 (0.000)***	-9.254 (0.000)***	-7.030 (0.000)***	-7.013 (0.000)***	-5.910 (0.000)***
female	-0.731 (0.000)***	-0.585 (0.000)***	-0.946 (0.000)***	-0.717 (0.000)***	-2.260 (0.239)	-0.238 (0.221)
R <sup>2</sup>		0.581		0.604		0.494
Number of obs	1,850	1,850	1,348	1,348	502	502
Censored obs	406		343		63	

**Table 8:** Effects of exaggeration/(imputed claim + overtime claim), mode of termination and gender on final payment

	Dropped Cases Included					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/(imp.claim+ overtime)	1.195 (0.058)*	0.845 (0.025)**	2.127 (0.005)***	1.297 (0.003)***	-1.843 (0.124)	-1.080 (0.159)
Court ruling	-8.078 (0.000)***	-3.975 (0.000)***	-8.503 (0.000)***	-3.986 (0.000)***	-6.564 (0.000)***	-3.726 (0.000)***
female	0.588 (0.101)	0.351 (0.093)*	0.327 (0.471)	0.202 (0.419)	1.036 (0.048)**	0.677 (0.052)*
R <sup>2</sup>		0.123		0.135		0.091
Number of obs	2,494	2,494	1,833	1,833	661	661
Censored obs	1,041		819		222	

	Dropped Cases Excluded					
	All lawyers		Private lawyers		Public lawyers	
	Tobit	OLS	Tobit	OLS	Tobit	OLS
exag/(imp.claim+ overtime)	0.568 (0.049) **	0.519 (0.025) **	0.657 (0.064) *	0.539 (0.049) **	-0.890 (0.092) *	-0.719 (0.119)
Court ruling	-8.669 (0.000) ***	-6.744 (0.000) ***	-9.225 (0.000) ***	-7.008 (0.000) ***	-7.037 (0.000) ***	-5.927 (0.000) ***
female	-0.684 (0.000) ***	-0.540 (0.000) ***	-0.884 (0.000) ***	-0.664 (0.000) ***	-0.292 (0.196)	-0.267 (0.181)
R <sup>2</sup>		0.583		0.606		0.496
Number of obs	1,850	1,850	1,348	1,348	502	502
Censored obs	406		343		63	

**Table 9:** The effects of exaggeration, imputed claim and gender on mode of termination

	All lawyers			
	Dropped cases included		Dropped cases excluded	
	settlement	dropped cases	trial	trial
In (exaggeration)	0.00095 (0.926)	-0.00708 (0.571)	0.00715 (0.617)	0.00521 (0.751)
In (imp. claim)	0.03220 (0.355)	-0.01887 (0.666)	-0.02656 (0.535)	-0.03851 (0.394)
female	0.34456 (0.003) ***	-0.46258 (0.000) ***	0.00304 (0.986)	-0.14946 (0.393)
Pseudo R <sup>2</sup>	0.0048	0.0074	0.0004	0.0013
Number of obs	2494	2494	2494	1850

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	Private lawyers			
	Dropped cases included		Dropped cases excluded	
	settlement	dropped cases	trial	trial
In (exaggeration)	0.02079 (0.083)*	-0.01860 (0.204)	-0.00930 (0.566)	-0.01748 (0.280)
In (imp. claim)	0.05069 (0.212)	-0.01295 (0.808)	-0.05445 (0.249)	-0.07246 (0.146)
female	0.33566 (0.014)**	-0.39444 (0.007)***	-0.05037 (0.799)	-0.20900 (0.293)
Pseudo R <sup>2</sup>	0.0071	0.0067	0.0017	0.0049
Number of obs	1833	1833	1833	1348

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	Public lawyers			
	Dropped cases included		Dropped cases excluded	
	settlement	dropped cases	trial	settlement
In (exaggeration)	-0.02354 (0.289)	0.02768 (0.282)	0.00118 (0.971)	0.00930 (0.769)
In (imp. claim)	-0.01041 (0.870)	-0.02063 (0.760)	0.07807 (0.518)	0.07454 (0.540)0
female	0.42682 (0.030)**	-0.65589 (0.004)***	0.17090 (0.521)	0.01287 (0.962)
Pseudo R <sup>2</sup>	0.0096	0.0184	0.0021	0.0014
Number of obs	661	661	661	500

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