A Decision Procedure for Making and Evaluating CCP 998 Offers

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A DECISION PROCEDURE FOR MAKING AND EVALUATING CCP §998 OFFERS TO COMPROMISE

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I. Introduction

As California litigators are well aware, pursuant to California Code of Civil Procedure section 998, any party to an action may serve a written offer to compromise upon any other party to the action, such that if the offeree fails to accept the offer and then fails to obtain a judgment greater than the offer, the offeree must pay the offeror’s various costs and/or fees from the time of the offer to the time of judgment. 998 offers become quickly significant when a case involves substantial costs, expert witness fees, or when there are independent grounds for recovery of attorney’s fees or prejudgment interest. Despite this, in practice counsel often advise clients to accept or reject 998 offers based on a mere hunch, or rough estimation at best.

What follows is a formal decision procedure that attempts to codify and refine the attorney’s natural decision-making process when making and evaluating the CCP § 998 offer. By adopting the following method, the attorney can make and evaluate 998 offers with greater precision, and avoid exposing clients to unwarranted and unnecessary risks.¹

II. Interpreting the Statute

Specifically, pursuant to CCP § 998:

If an offer made by a defendant is not accepted and the plaintiff fails to obtain a more favorable judgment or award, the plaintiff shall not recover his or her postoffer costs and shall pay the defendant’s costs from the time of the offer. In addition . . . the court or arbitrator, in its discretion, may require the plaintiff to pay

¹ Other jurisdictions will have similar statutory offers to compromise. The method can be adapted to the applicable statute. See, e.g., NY CPLR 3221 for New York’s statutory offer to compromise.
a reasonable sum to cover costs of the services of expert witnesses ...
. . . actually incurred and reasonably necessary in either, or both, preparation for trial or arbitration, or during trial or arbitration, of the case by the defendant.²

Recall that pursuant to CCP § 1032:

Except as otherwise provided by statute, a prevailing party is entitled as a matter of right to recover costs in any action or proceeding, where ‘prevailing party’ includes the party with a net monetary recovery, a defendant in whose favor a dismissal is entered, a defendant where neither plaintiff nor defendant obtains any relief, and a defendant as against those plaintiffs who do not recover any relief against that defendant.

In evaluating 998 offers, it is thus critical to distinguish the “prevailing party” to the suit from the “prevailing party” to the 998 offer. A plaintiff may be the prevailing party to the suit but not the 998. A defendant may be the prevailing party to the 998 but not the suit.

Pursuant to CCP § 998(a) “costs” affected by the statute are those recoverable by the prevailing party to the suit under CCP § 1032, as enumerated in CCP § 1033.5.³

² Similarly, “[i]f an offer made by a plaintiff is not accepted and the defendant fails to obtain a more favorable judgment or award . . . the court or arbitrator, in its discretion, may require the defendant to pay a reasonable sum to cover postoffer costs of the services of expert witnesses . . . actually incurred and reasonably necessary in either, or both, preparation for trial or arbitration, or during trial or arbitration, of the case by the plaintiff, in addition to plaintiff’s costs.” Cal. Code Civ. Proc. § 998(d) (West 2010).

³ Costs at issue in a 998 offer include: (1) Filing, motion, and jury fees; (2) juror food and lodging; (3) various deposition costs; (4) service of process costs; (5) expenses of attachment, including keeper’s fees; (6) premiums on necessary surety bonds; (7) ordinary witness fees pursuant to Section 68093 of the Government Code; (8) fees of expert witnesses ordered by the court; (9) transcripts of court proceedings ordered by the court; (10) attorney’s fees, when authorized by contract, statute or case law; (11) court reporters fees as established by statute; (12) exhibit costs at trial; and (13) any other item that is required to be awarded to the prevailing party pursuant to statute as an incident to prevailing in the action. See Cal. Code Civ. Proc. § 1033.5 (West 2010).
prevailing party only, a party prevailing on the claim, but not the 998 offer, recovers its pre-offer—but not post-offer—attorney’s fees. Where a plaintiff prevails in the suit but not the 998, and is otherwise entitled to attorney’s fees, the plaintiff thus recovers pre-offer costs and fees, while the defendant recovers post-offer costs and fees. See Murillo v. Fleetwood Enterprises, Inc., 51 Cal. App. 4th 1033 (1998); See also Scott v. Blount, 20 Cal. App. 4th 1103 (1999).

III. The Decision Procedure (EERCC)

The decision procedure for making and evaluating 998 offers consists of five steps, summarized as “EERCC”: (1) Evaluate, (2) Estimate, (3) Research, (4) Calculate, and (5) Compare. Since defendants make most 998 offers, the method is presented from the perspective of a plaintiff assessing a defendant’s offer, although the analysis will be similar for any offeror and offeree.

Evaluate. Scrutinize the language of the 998 and determine what the language entails given the facts of the case and applicable statutes and case law. Is there any independent basis for recovery of attorney’s fees that the 998 will affect? Is prejudgment interest at issue? And so on.

Estimate. Estimate defendant’s and plaintiff’s expected post-offer fees and costs in order to determine what is at stake. For example, is it a case where defendant will hire many experts, whom plaintiff may have to pay for if defendant prevails on the 998? How

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4 I thank actuary and mathematician, David Dobor, for his enthusiastic help in working out the details of this method.
5 For example, Engle v. Copenbarger & Copenbarger, 157 Cal. App. 4th 165 (2007), held that an offeree that accepts a 998 offer is entitled to recover as prevailing party pre-offer costs and attorney’s fees (if applicable by contract or statute) in addition to the offer, if the offer is silent as to fees and costs and does not explicitly exclude them from the offer; and CCP § 3291 explicitly provides plaintiffs in personal injury actions who make and prevail on 998 offers ten percent per annum prejudgment interest calculated from the date of the offer to satisfaction of judgment—case law and statutes important to accurately interpreting the implications of a 998 offer.
many post-offer depositions will the parties likely take? Assign an estimated number to both defendant’s projected post-offer costs through trial—as the amount plaintiff may have to pay—and to plaintiff’s post-offer costs—as the amount plaintiff will fail to recover—should defendant prevail on the 998.

**Research.** Estimate case value by researching verdict amounts of past similar cases and calculating an average. A jury verdict research company, such as Verdict Search or Trials Digest, can be used for this purpose. The greater number of previous similar cases one researches and reviews, the more accurate the estimated verdict will be.

Some cases will be more on point than others. With multiple similar cases and verdicts, legal judgment is required to determine which cases more resemble, and therefore have more predictive value for, the case at hand. Factors will include salient facts and applicable law pertaining to liability, jurisdiction/venue, judge and jury, and defendant and opposing counsel. With multiple prior cases with different degrees of relevance, counsel may elect to calculate a statistically weighted average, which will complicate the method but make it more accurate.

**Calculate.** Calculate plaintiff’s *definite versus expected gain*. Definite gain in this context is the amount plaintiff would receive by accepting defendant’s 998—i.e., the amount apparent on the face of the offer, plus any implications due to contract, statute or case law.

Expected gain is the amount plaintiff would expect to gain by rejecting defendant’s 998 offer and proceeding to verdict. To calculate total expected gain, the basic idea is to: (1) calculate the average verdict above the 998, (2) calculate the average verdict below the 998, (3) multiply the average verdict amount above the 998 by its
likelihood of occurrence (= result A (for ‘above’ 998)), (4) multiply the average verdict amount below the 998 by its likelihood of occurrence (= result B (for ‘below’ 998)), and (5) add results A and B for total expected gain. This is more thoroughly illustrated below.

**Compare.** Having calculated plaintiff’s actual versus expected gain, and assigned numbers to each, plaintiff should accept or reject the 998 offer based on which number is greater. If actual gain is greater, plaintiff should accept the 998. If expected gain is greater, plaintiff should reject the 998 and proceed to trial.\(^6\)

**Summary:**

- **Evaluate:** Amount of 998 offer and what its phrasing entails given facts of case (e.g., whether attorney’s fees or prejudgment interest are issues and will be affected);
- **Estimate:** Defendant’s post-offer costs paid, and plaintiff’s post-offer costs not recovered, if defendant prevails on the 998;
- **Research:** Similar past cases to obtain range of verdict amounts and relevant statistical percentages;
- **Calculate:** Definite versus expected gain;
- **Compare:** Definite versus expected gain values and act according to larger number.

**IV. Example of the EERCC Method**

In a personal injury action, defendant serves a 998 offer for 1 million. There are statutory grounds for attorney’s fees to the prevailing party. Trial is 6 months away. Should plaintiff accept the offer?

**Evaluate:** Post-offer costs and fees include, e.g.: jury fees, service costs, depositions, transcripts, exhibits at trial, expert witness fees if so ordered, as well post-offer attorney’s fees.

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\(^6\) This assumes risk neutrality, but one could incorporate risk aversion—when applicable—into the method by assigning it a numerical, money value (plaintiff’s “risk premium”) and subtracting it from total expected gain before comparing expected gain and actual gain. This is discussed in more detail below.
Estimate: $60,000 for defendant’s post-offer costs; $180,000 for defendant’s post-offer attorney’s fees; and equally $60,000 for plaintiff’s post-offer costs, and $180,000 for plaintiff’s post-offer attorney’s fees. Total: $480,000.

Add plaintiff’s pre-offer costs and fees to plaintiff’s estimated post-offer costs and fees for plaintiff’s total estimate of costs and fees. Assuming plaintiff’s pre-offer costs and fees are $160,000: ($160,000 + $240,000 (post-offer)) = $400,000.

Research: Reveals that 30% of previous similar cases resulted in verdicts between 1 and 6 million, whereas 70% resulted in verdicts between .2 and .9 million.

Calculate: (i) The average verdict above the 998: \((1 + 6)/2 = 3.5\) million.\(^7\)

(ii) Add plaintiff’s attorney’s fees and costs for entire action to the average verdict above the 998: \((400,000 + 3.5\) million\) = 3.9 million.\(^8\)

(iii) The average verdict below the 998: \((.2 + .9)/2 = .55\) million.

(iv) Add defendant’s post-offer costs and fees ($240,000) and plaintiff’s post-offer costs ($60,000) and subtract that sum ($300,000) from the average verdict below the 998: (.55 million - .3 million) = .25 million. Add plaintiff’s pre-offer fees and costs to that total: (.16 + .25) = .41 or $410,000.\(^9\)

(v) Multiply the average verdict amount above the 998 (plus plaintiff’s costs and fees) by its likelihood of occurrence: \((3.9 \times .3) = 1.17\) million). Call that Result A (for ‘above’ 998).

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\(^7\) We assume that there are only 2 sample verdicts, or that the multiple sample verdicts are evenly distributed between 1 and 6 million. In practice, more sample verdicts would be used and averaged, resulting in a more accurate estimated verdict. Also, if one had multiple sample verdicts with some closer to one’s present case—whether because of jurisdiction/venue, defendant and/or counsel, or salient facts—one could calculate a statistically weighted average to properly account for that greater similarity. Legal judgment and experience would be critical to determine which cases warranted which weighting.

\(^8\) We assume that the sample past verdicts from which the averages were derived did not include amounts from post-judgment motions for costs and fees. Since plaintiff beats the 998 in these cases at hand, plaintiff is entitled to all recoverable costs and attorney’s fees. Although, strictly speaking, plaintiff’s costs are not “gained” so much as reimbursed if/when plaintiff prevails, costs are included in the calculation for expected gain, since they have already been put at risk and are lost if/when plaintiff loses.

\(^9\) We assume that there are no defense verdicts in this example (where verdicts below the 998 range from .2 to .9 million), and hence where plaintiff is always prevailing party to suit and entitled to post-offer fees and costs. We did not subtract plaintiff’s post-offer attorney’s fees from the average judgment below the 998 in this example, assuming that plaintiff has a contingency fee agreement and is not expending money on attorney’s fees. Plaintiff’s post-offer attorney’s fees would represent a loss to the attorney, not the client, should the client fail to beat the 998 but still prevail in the action. The method thus, as presented, assesses risk for the client only—the attorney must assess his/her own risk as appropriate based on those results. The plaintiff’s post-offer attorney’s fees should be so subtracted if the plaintiff is paying hourly.
(vi) Multiply the average verdict amount below the 998 (subtracting defendant’s post-offer fees and costs and plaintiff’s post-offer costs, while adding plaintiff’s pre-offer fees and costs) by its likelihood of occurrence: (.41 x .7) = .287 million. Call that Result B (for ‘below’ 998).

(vii) Add Result A and Result B for total expected gain: (1.17 + .287) = 1.457 million.

Compare: Definite gain of 1 million versus expected gain of 1.457 million. Since expected gain is larger than definite gain, the plaintiff should reject the 998 and proceed to trial.

V. Risk Premiums and Analysis of the EERCC Method

Note how an attorney judging from preliminary research alone may recommend settling for one million, since 70% of prior similar cases resulted in verdicts less than that. As the method shows, this would be a mistake. Even for a plaintiff that is particularly risk averse, the EERCC method allows the attorney to put a price on risk avoidance. In this case, the price of risk avoidance (plaintiff’s “risk premium”) is a tangible $457,000 that the plaintiff can carefully consider. The question will be whether the plaintiff wants to pay a $457,000 premium for risk avoidance.

The EERCC method also provides, more generally, a framework within which to make and assess 998 offers. Plaintiffs should only make and accept 998 offers in which actual gain is greater than expected gain; whereas defendants should only make and accept 998 offers in which actual loss is less than expected loss.\(^\text{10}\)

The language of actual versus expected gain and loss in the context of 998 offers also reveals that there is no such thing as a 998 offer that is reasonable for both offeror and offeree. That is, any offer that a defendant should rationally make, a plaintiff should rationally reject, and vice versa.

\(^{10}\) The example and method presented here can be easily altered thus for defendant’s making and evaluating offers to and from plaintiffs.
Rationally compelling offers to plaintiffs are essentially mistakes in which a defendant miscalculated or otherwise erred and served an offer in which a plaintiff’s actual gain exceeds expected gain. Plaintiffs should in all cases take these offers, unless there is an overwhelming desire for precedent for which plaintiff is prepared to pay. Various factors explain why defendants on occasion make these unreasonable offers: they may be extremely averse to risk or the publicity and precedent accompanying a jury trial, or there may be an asymmetry of information between the parties or differing views of law, creating differing views of case value and/or probability of recovery.

In other cases, defendant’s offer will be strictly speaking unreasonable—in that plaintiff’s actual gain is less than expected gain—yet still compelling in that defendant has accurately assessed plaintiff’s risk tolerance and overall circumstances and served an offer in which plaintiff accepts less than expected gain as a reasonable risk premium.\textsuperscript{11}

VI. Conclusion

As Aristotle noted long ago, you can’t make a science more exact than its subject matter. Calculating expected gain or loss by the EERCC method will depend on the quality and volume of data available and will involve making legal and factual determinations about past relevant cases, parties, venues, judges, juries and attorneys—determinations that require good judgment and experience, but with respect to which reasonable minds may differ.

The EERCC method nevertheless offers much more guidance than a rough estimation or hunch and can be crucial to determining the fundamental questions of

\textsuperscript{11} The concept of a plaintiff’s (reasonable) risk premium is a topic in itself and may or may not include the plaintiff’s time, attorney’s time and risk tolerance, as well as prudential (personal or business) factors favoring timely resolution—all factors that plaintiff may be (reasonably) willing to pay for, but that should be acknowledged and assessed on a case by case basis.
whether a 998 offer is reasonable, and if not, the exact risk premium a party will be paying in accepting it.

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