**Judgement Contingent Settlements**

***Shay Lavie***

***Joint with*** *Avraham Tabbach*

**Abstract:**

Asymmetric information is widely considered a major obstacle to settlements.

In this paper, we argue that litigants facing asymmetric information can use a simple add-on to the settlement offer to alleviate the information barriers to settlements.

In particular, we show that informed parties can promise to pay an additional sum should they lose at trial (if the settlement proposal is rejected and a trial takes place) in exchange for a (possible) payment from the other party.

We refer to the general class of these provisions as “Judgment-Contingent Clauses” (JCC).

We show that JCC’s enable informed parties to signal their type to the uninformed party costlessly, and accordingly decrease litigation rate and at the limit eliminate it altogether.

JCC’s manage to reduce litigation because they are costly to a party who misrepresents herself, but they could be costless to a party who presents herself truthfully through the settlement offer.

We further discuss possible limitations to such settlement clauses including wealth-constraints and endogenous litigation costs.

We also provide the conditions under which our asymmetric information model predicts inverse-JCC’s, i.e., agreements to decrease rather than inflate the stakes of the trial, which resemble the more familiar high-low agreements.