

**Insurer Management****Tax Management and Investment Strategies of Property-Liability Insurers,**

by J. David Cummins (University of Pennsylvania) and Elizabeth Grace (San Jose State University)

The Tax Reform Act (TRA) of 1986 reduced the incentives for institutional investors to participate in the tax exempt bond market. This paper develops a model of profit maximization incorporating the TRA provisions applicable to property-liability (PL) insurers. The theory predicts that PL insurers will use underwriting losses to shelter taxable investment income and invest the balance of their portfolios in tax favored securities. Our empirical evidence reveals that insurers continued to invest in tax exempts following the TRA, suggesting that implicit tax rates are low enough to attract insurers into the long-term tax exempt market. However, insurers reduced the proportions of income derived from tax exempt interest and dividends following the TRA. *Journal of Banking and Finance*, January 1994, 18(1): 43-72. (Reprinted with permission of the North-Holland Publishing Company.)

**Capacity Constraints and Cycles in Property-Casualty Insurance Markets,**

by Anne Gron (University of Chicago)

Underwriting cycles are unexpected in a structurally competitive industry where financial capital is the major determinant of output capacity. "Arbitrage" theories explain underwriting cycles as largely an artifact of institutional lags and reporting practices; "capacity-constraint" theories view insurance markets as characterized by real frictions that cause underwriting cycles by temporarily reducing the industry's capacity to insure risks. Arbitrage theories imply no systematic relationship between capacity and underwriting margins, while capacity-constraint hypotheses predict a negative relationship. This article provides a test of the two theories by examining the empirical relationship between capacity and underwriting margins. The results, using data on four insurance lines, generally support the capacity-constraint hypothesis; unanticipated decreases in capacity cause higher profitability and prices. *RAND Journal of Economics*, Spring 1994, 25(1): 110-127. (Reprinted with permission of the RAND Journal of Economics.)

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**Safety and Loss Control****The Impact of Airbag Adoption on Relative Personal Injury and Absolute Collision Insurance Claims,**

by Steven P. Peterson and George E. Hoffer (Virginia Commonwealth University)

This article examines the impact of airbag adoption on the relative injury and absolute collision loss data experiences of automotive vehicle lines. The data set consists of every automobile model for which overall injury data was