FROM THE LIBRARY SHELF

Edited by Phyllis Schiller Myers
Virginia Commonwealth University

Theory of Contracts

Repeated Moral Hazard and One-Sided Commitment, by Christopher Phelan (Northwestern University)

This paper considers a repeated unobserved endowment economy with a restriction that agents can walk away from insurance contracts at the beginning of any period and contract with another insurer (one-sided commitment). An equilibrium is derived characterized by a unique, market-determined insurance contract with the property that agents never want to walk away from it. The paper shows that trade (or insurance) still occurs and that a non-degenerate long-run distribution of consumption still exists. A numerical example shows that this distribution is nearly log-normal. *Journal of Economic Theory*, August 1995, 66(2): 488-506. (Reprinted with permission of Academic Press, Inc.)

Game Theory

A Simple Forecasting Mechanism for Moral Hazard Settings, by Anil Arya (Ohio State University) and Jonathan Glover (Carnegie Mellon University)

This paper studies a multiagent moral hazard setting. We resolve the tacit collusion problem that arises in our setting while employing a solution concept that makes less demanding behavioral assumptions than Nash. A simple mechanism is constructed that approximately implements the second-best solution in two rounds of iteratively removing strictly dominated strategies. Under our mechanism, the agents' best-reply correspondences are well-defined, a small message space is employed, and the messages can be interpreted as divisional forecasts. *Journal of Economic Theory,* August 1995, 66(2): 507-521. (Reprinted with permission of Academic Press, Inc.)

Risk Perception and Economic Behavior

Insurance and Decision-Taking, by Yaffa Machnes (Bar-Ilan University, Ramat-Gan, Israel)

In this paper we show how the holding of an insurance contract influences the choice variable of a decision-taker. We analyze two decision problems: optimal saving by consumers and optimal production by firms. We find an unambiguous sign change in the decision variable under common assumptions about the utility of decision-takers. *Economics Letters,* May 1995, 48(2): 139-144. (Reprinted with permission of North-Holland Publishing Company.)

A Note on Risk Aversion and Learning Behavior, by D. Alepuz and A. Urbano (Universidad de Valencia, Spain)

This paper analyzes the learning behavior of a risk-averse agent. We find two conflicting effects in the experimental behavior: a stronger preference for the ex post reduction in uncertainty, but ex ante the returns to information are more uncertain. *Economics Letters,* July 1995, 49(1): 51-58. (Reprinted with permission of North-Holland Publishing Company.)

Weighing Risk and Uncertainty, by Amos Tversky and Craig R. Fox (Stanford University)

Decision theory distinguishes between risky prospects, where the probabilities associated with the possible outcomes are assumed to be known, and uncertain prospects, where these probabilities are not assumed to be known. Studies of choice between risky prospects have suggested a nonlinear transformation of the probability scale that overweights low probabilities and underweights moderate and high probabilities. The present article extends this notion from risk to uncertainty by invoking the principle of bounded subadditivity: An event has greater impact when it turns impossibility into possibility, or possibility into certainty, than when it merely makes a possibility more or less likely. A series of studies provides support for this principle in decision under both risk and uncertainty and shows that people are less sensitive to uncertainty than to risk. Finally, the article discusses the relationship between probability judgments and decision weights and distinguishes relative sensitivity from ambiguity aversion. *Psychological Review,* April 1995, 102(2): 269-283. (Reprinted with permission of the American Psychological Association, Inc.)

Health, Income, and Risk Aversion: Assessing Some Welfare Costs of Alcoholism and Poor Health, by John Mullahy (Trinity College and NBER) and Jody L. Sindelar (Yale University and NBER)

The economic costs of adverse health outcomes have typically been evaluated in a context of risk neutrality, an approach that ignores the potential welfare importance of individuals' risk preferences. This paper presents a framework

that unifies the research in health capital and earnings with that on risk preferences in the presence of stochastic outcomes. The model is implemented to obtain estimates of the economic damages due both to general health problems as well as to one specific health problem that is of considerable interest from society's perspective: alcoholism. *The Journal of Human Resources,* Summer 1995, 30(3): 439-459. (Reprinted with permission of *The Journal of Human Resources.*)

A Range-Frequency Explanation of Shifting Reference Points in Risky Decision Making, by Rodney G. Lim (Tulane University)

An integration of range-frequency theory, a theory of psychophysical judgement, and prospect theory, a theory of choice behavior under risk, is proposed. A critical assumption of prospect theory is that the reference point, which helps govern the riskiness of choice behavior, is modeled after Helson's (1964) adaptation level notion. It is proposed that range-frequency theory provides a better representation of the reference point and, thus, can be used to understand with greater precision the judgement of outcomes as gains or losses and the perceived riskiness of subsequent decisions. A computer-based decision task was performed using 199 graduate and undergraduate students. Hypotheses concerning range and frequency effects on the reference point were fully supported. The judgement hypotheses were generally supported under gains, but received inconsistent support under losses. Range and frequency effects on choice were consistent with predictions under both gains and losses with one exception. Implications of this work for previous and future research involving prospect theory are discussed. *Organizational Behavior and Human Decision Processes,* July 1995, 63(1): 6-20. (Reprinted with permission of Academic Press, Inc.)

Multiple Reference Points, Framing, and the Status Quo Bias in Health Care Financing Decisions, by Maurice Schweitzer (University of Miami)

Reference effects help account for several behavioral biases, including framing, status quo, and omission effects. Despite the importance of reference effects, little is understood about how decision makers adopt a referent. This study investigates the roles of status quo and framing conditions in the selection of reference alternatives. Full-time employees made health care financing decisions within a problem context containing multiple reference candidates. Results from this work demonstrate that the status quo bias does interact with framing. In addition, these results demonstrate that subjects manifest the status quo bias within the domain of health care financing decisions. *Organizational Behavior and Human Decision Processes,* July 1995, 63(1): 69-72. (Reprinted with permission of Academic Press, Inc.)

The Comparative Statics of Changes in Risk Revisited, by Christian Gollier (University of Toulouse, France)

In this paper, we consider the problem of determining the conditions under which a change in risk increases the optimal value of a decision variable for all risk-averse agents. For a large class of payoff functions, we obtain the least constraining (necessary and sufficient) condition on the change in risk for signing its effect without any additional restriction on the utility function than risk aversion. It entails all existing sufficient conditions as particular cases. Our results are applied to the linear model which describes the standard portfolio problem. The necessary and sufficient condition for unambiguous comparative statics in this class of problems is termed "greater central riskiness" (CR). It is shown that CR dominance is neither stronger nor weaker than second-degree stochastic dominance. *Journal of Economic Theory,* August 1995, 66(2): 522-535. (Reprinted with permission of Academic Press, Inc.)

Utility Theory

Increasing Risk, Decreasing Absolute Risk Aversion and Diversification, by Yoram Kroll, Moshe Leshno (The Hebrew University of Jerusalem), Haim Levy (The Hebrew University of Jerusalem and University of Florida), and Yishay Spector (The Hebrew University of Jerusalem)

This paper defines conditions for "increasing risk" when the utility functions of risk-averse investors are characterized by decreasing absolute risk aversion (DARA). Rothschild and Stiglitz (*Journal of Economic Theory,* 1970, 2: 225-243, and 1971, 3: 66-84) define cases when a random variable Y is "more risky" (or "more variable") than another variable X for the utility functions of risk-averse investors. They conclude that Y is riskier than X if G, the cumulative distribution of Y, can be formed from F, the cumulative distribution of X, by adding a series of mean preserving spread (MPS) steps to F. This paper suggests considering a sequence of steps which are denoted by "mean preserving spread and antispread" (MPSA). We define the condition under which a random variable Y is "more risky" (or "more variable") than another variable X for DARA utility functions. We prove that, for DARA utility functions, Y is riskier than X if and only if G, the cumulative distribution function of Y, can be formed from F, the cumulative distribution function of X by adding a series of MPSA steps to F, under the restrictions stated in the paper. The economic intuition and impact of MPS and MPSA steps on the optimum diversification strategy are demonstrated. *Journal of Mathematical Economics,* 1995, 24(6): 537-556. (Reprinted with permission of North-Holland Publishing Company.)

Mathematical and Statistical Models

On the Graduations Associated with a Multiple State Model for Permanent Health Insurance, by A. E. Renshaw and S. Haberman (City University, London)

The paper puts forward a comprehensive methodology for graduation the transition intensities in a multiple state model for permanent health insurance applications. The approach is based on generalized linear models (GLM) and utilises the data collected and analyzed by the U.K. Continuous Mortality Investigation Bureau (under the auspices of the Institute and Faculty of Actuaries) in respect of male standard experience of individual PHI policies for the period 1975-1978. The comprehensive and versatile nature of this approach is shown to be applicable to three sets of transition intensities for which data are available: for sickness recovery (as functions of age at sickness onset, x, and duration of sickness, z), for death and sickness (also a bivariate function of x and z), and for sickness inception (a function of x only). The full potential of the GLM methodology means that approximations to normality which would lead to complex, iterative methods of fitting can be avoided and that the presence to duplicate policies can be allowed for. A novel feature of the graduation proposed is the introduction of break-point predictors (similar to splines) into the graduation formula, and the method of location of the number and optimum positions of the underlying break-points (or knots). *Insurance: Mathematics and Economics,* August 1995, 17(1): 1-17. (Reprinted with permission of North-Holland Publishing Company.)

Health Care and Insurance

Health Insurance and Health Status: Implications for Financing Health Care Reform, by Pamela Farley Short and Tamra J. Lair

Self-reported health status measures from the 1987 National Medical Expenditure Survey indicate significant differences among each of five population groups defined by current health insurance coverage. These differences in health status imply that the groups are likely to exhibit different patterns of expenditures, even if enrolled in the same health insurance after health care reform. The healthiest group along most dimensions is the population covered by employer-sponsored insurance, followed in order by the population with nongroup private insurance, the uninsured population, the population that qualifies for public coverage based on income, and the population that qualifies for public coverage based on medical need. While the general health and mental health of the uninsured are slightly worse in comparison to the privately insured, the uninsured have fewer chronic health problems. The uninsured who recently lost private insurance or who live in working families are significantly healthier than the long-term or low-income and nonworking uninsured. *Inquiry,* Winter 1994/1995, 31(4): 425-437. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

HEALTH CARE ... INSURANCE

The Distributional Effects of Employer and Individual Health Insurance Mandates, by John Holahan and Colin Winterbottom

The impact of different kinds of employer and individual mandates on the cost to individuals, business, and government are assessed. The distribution of health care expenditures across individuals in different income groups are examined, assuming that individuals ultimately bear the cost of employer payments through lower wages and the cost of government payments through tax contributions. A major conclusion is that net benefits to lower income individuals improve under all alternatives to the current system with relatively small increases in payments by individuals in any income group. Additionally, while employer mandates reduce individuals' direct payments, individual mandates can have lower costs to the government and better distributional outcomes. A 50 percent employer mandate also has many desirable features. *Inquiry,* Winter 1994/1995, 31(4): 368-384. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

HEALTH CARE INSURANCE

Grading the Report Card: Lessons from Cognitive Psychology, Marketing, and the Law of Information Disclosure for Quality Assessment in Health Care Reform, by Jason Ross Penzer

The emergence of consumer-directed information disclosure proposals in the health care reform debate is examined. In his Health Security Act (HSA), President Clinton proposed to harness the opportunities of the information age and create report cards on health plans so consumers could compare competing plans and reward high quality providers by selecting their plans. The report card proposal has been more resilient than the HSA itself. By drawing on the literatures of cognitive psychology, marketing, and existing statutory information disclosure, the drawbacks of relying on health care report cards as a quality assurance system are explored. The report cards cannot currently assure quality, given limitations in the state of the art of quality measurement and an inadequate understanding of how consumers would process disclosed information. *Yale Journal on Regulation,* Winter 1995, 12(1): 207-256. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

Long-Term Care Issues

Estimating Family Long-Term Care Decisions in the Presence of Endogenous Child Characteristics, by Steven Stern (University of Virginia)

This paper estimates the effects of various parent and child characteristics on the choice of care arrangement of the parent taking into account the potential endogeneity of some of the child characteristics. This potential endogeneity is controlled for by using an instrumental variables approach with panel data. The procedure conditions on the parent receiving no significant care in the first year of the panel causing first year variables to be valid instruments for the

second year variables. The estimation procedure shows that, after controlling for endogeneity, potentially endogenous child variables have smaller effects. The estimates predict moderate effects of parent, sex, age, race, and health and child sex and marital status, and large effects of parent marital status and child distance. *The Journal of Human Resources,* Summer 1995, 30(3): 551-580. (Reprinted with permission of *The Journal of Human Resources.*)

Continuing Care Retirement Communities: Prospects for Reducing Institutional Long-Term Care, by Frank A. Sloan and May W. Shayne

Continuing care retirement communities (CCRC) combine housing and long-term care (LTC) services, including personal and nursing home care. CCRCs are potentially promising models for LTC delivery because they offer a full continuum of services and can substitute less expensive supportive care for institutional care. The effect of various contract types for LTC services offered by CCRCs and provision of support services on utilization of nursing home and personal care units are studied. Compared with other types of CCRCs, those offering completely prepaid LTC coverage reduced use of nursing home care by 13 percent and personal care by 5 percent. However, affordability is an important issue: CCRC residents with extensive contracts were wealthier than were other CCRC residents. *Journal of Health, Politics & Law,* Spring 1995, 20(1): 75-98. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

Government Insurance Programs

Stability in the Absence of Deposit Insurance: The Canadian Banking System 1890–1966, by Jack Carr, Frank Mathewson (University of Toronto), and Neil Quigley (University of Western Ontario and Victoria University, Wellington, New Zealand)

The Canadian banking system experienced a prolonged period of stability prior to the introduction of deposit insurance in 1967. Documenting the reasons for this stability provides important evidence in the debate over the impact of mandatory flat-rate deposit insurance. In this paper we use new archival data to refute recent claims that this stability resulted from an implicit deposit insurance scheme managed by Canada's largest banks and guaranteed by the federal government. We argue that the Canadian banking system was stable for two reasons. First, the absence of deposit insurance provided incentives for both prudence on the part of management, and monitoring by depositors and regulators. Second, the absence of unit banking and other regulatory barriers to competition facilitated efficient mergers which produced a relatively small number of well-managed banks. *Journal of Money, Credit, and Banking,* November 1995, 27(4), Part 1: 94-114. (Reprinted with permission of *Journal of Money, Credit and Banking.*)

Social Insurance

The Effects of Differential Mortality Rates on the Progressivity of Social Security, by Daniel M. Garrett (Stanford University)

Does the Old-Age and Survivors Insurance portion of Social Security become regressive once we allow for the shorter lifespan of poor people? This paper compares the net returns of poor households to the net returns of other households after taking into account differential longevity. Earnings and Social Security tax and benefit histories are simulated for families of various income levels in the 1925 birth cohort. These tax and benefit profiles are then weighted by the agents' probabilities of survival. For some plausible values of key mortality parameters, differences in mortality eliminate the progressive spread in returns across income categories. *Economic Inquiry,* July 1995, 33(3): 457-475. (Reprinted with permission of *Economic Inquiry.*)

SOCIAL INSURANCE

Equity in the Medicaid Program: Changes in the Latter 1980s, by E. Kathleen Adams

The possibility of health care reform has helped focus attention on equity in the receipt of health care. This is a particular issue for the Medicaid program, as state variations in eligibility and payment policies have historically created inequity. A study examines equity for Medicaid beneficiaries and state taxpayers during the latter 1980s. Findings indicate that federally mandated expansions significantly increased equity in the coverage of the poor, but inequality in real resources per enrollee remained significant. Although equity improved from 1984 through 1991, the increased use of provider-specific tax and voluntary donation programs by traditionally high-spending states played an important role in the 1992 figures. *Health Care Financing Review,* Spring 1995, 16(3): 55-73. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

SOCIAL INSURANCE

Unemployment Duration Stigma and Re-employment Earnings, by Christian Belzil (Concordia University and Aarhus University)

A non-stationary model of individual labour market histories where the distribution of wage offers depends on elapsed unemployment duration and where unemployment compensation is claimed for a limited period only, is estimated from sample information on completed unemployment duration, accepted earnings, and accepted job duration and can identify movements in the reservation wages induced by human capital loss from those caused by benefit exhaustion. The results indicate that individuals seem to be much more sensitive to benefit exhaustion than human capital loss. The estimated structural parameters provide an explanation for the existence of a statistical relationship between contiguous unemployment and accepted job durations. *Canadian Journal of Economics,* August 1995, 28(3): 568-585. (Reprinted with permission of *Canadian Journal of Economics.*)

Unemployment Insurance and Moral Hazard in Employment, by Louis N. Christofides and C. J. McKenna (University of Guelph, Canada)

Using the 1988–1990 LMAS, we examine whether the Variable Entrance Requirement (VER) that claimants must work for a minimum number of weeks conditions job durations. Estimated employment hazards contain a large, significant spike at the VER. *Economics Letters,* August, 1995 49(2): 205-210. (Reprinted with permission from North-Holland Publishing Company.)

The Impact of Unemployment Insurance Benefit Levels on Recipiency, by B. P. McCall

This paper studies the effect of unemployment insurance benefit levels on recipiency. Increasing benefit levels (as measured by the fraction of weekly earnings of the lost job that they replace) is found to significantly increase the probability of unemployment insurance recipiency among the eligible. There is some evidence, however, that the effect is smaller at high replacement rates. Cost increases resulting from take-up responses are found to be substantial for increases in the states' maximum benefit amount and for increases in the weekly benefit amount in low-replacement-rate states. *Journal of Business and Economic Statistics,* April 1995, 13(2): 189-198. (Reprinted with permission of the *Journal of Economic Literature.*)

Did Workers Pay for the Passage of Workers' Compensation Laws? by Price V. Fishback and Shawn Everett Kantor (University of Arizona and NBER)

Market responses to legislative reforms often mitigate the expected gains that reformers promise in legislation. Contemporaries hailed workers' compensation as a boon to workers because it raised the amount of postaccident compensation paid to injured workers. Despite the large gains to workers, employees often supported the legislation. Analysis of several wage samples from the early 1900s shows that employers were able to pass a significant part of the added costs of higher postaccident compensation on to some workers in the form of reductions in wages. The size of the wage offsets, however, was smaller for union workers. *The Quarterly Journal of Economics,* August 1995, 110(3): 713-742. (Reprinted with permission of *The Quarterly Journal of Economics.*)

Managing Work Disability: Why First Return to Work Is Not a Measure of Success, by Richard J. Butler and William G. Johnson

Studies of the effectiveness of medical and vocational rehabilitation and the disincentive effects of workers' compensation benefits frequently assume that a return to work signals the end of the limiting effects of injuries. A recent study is the first to test that assumption empirically. Using a rich data set on Ontario workers with permanent partial impairments resulting from injuries that occurred between 1974 and 1987, it is shown that the effects of injuries on employment are more enduring than previous studies indicated. The rate of

successful returns to employment, measured by first return to work, is 85 percent, but the rate of success evaluated over a longer time period is only 50 percent. *Industrial & Labor Relations Review*, April 1995, 48(3): 452-469. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

Employee Benefit Issues

Voice Asymmetries in ERISA Litigation, by Mitchell Langbert

ERISA's equitable remedies limit employees' access to the courts. The law fails to protect workers with short tenure and low wages, for example female workers, because trial costs often exceed damages. In single-employer plans, unions improve access, but in multiemployer plans they do not. The reason is that in single-employer plans unions bargain at arm's length with plan sponsors while in multiemployer plans they do not. Plaintiffs' win rates are approximately 50 percent in single-employer union ERISA cases but are significantly below 50 percent in nonunion and multiemployer cases. *Journal of Labor Research,* Fall 1995, 16(4): 455-465. (Reprinted with permission of ABI/INFORM, Copyright UMI.)

Pensions and Retirement

Constraints in Perfect-Foresight Models: The Case of Old-Age Savings and Public Pensions, by Lex Meijdam and Mariljn Verhoeven (Tilburg University, Netherlands)

The solution of discrete-time perfect-foresight models with constrained state variables differs considerably from the solution of models without constraints. In this paper this is worked out for a simple model of decision making on public pensions. *Economic Letters,* May 1995, 48(2): 129-137. (Reprinted with permission from North-Holland Publishing Company.)

Estate Planning and Distribution

Tax Saving Opportunities in Estate Freeze Transactions: An Application of the Black-Scholes Model, by James R. Hamill (University of New Mexico) and Joel S. Sternberg (University of Arizona)

Transfer tax valuation rules for interests in family businesses include a minimum value to reflect the option value of "junior" equity interests transferred to family members. We examine the option features of the junior interest and use the Black-Scholes model to identify situations in which an estate planner could structure a plan of ownership succession that results in undervaluation of the transferred interest. The Black-Scholes model may also be used

to identify situations in which a lifetime ownership transfer should be avoided because of the minimum value rule. *Financial Services Review,* 1995, 4(1): 9-22. (Reprinted with permission of JAI Press Inc.)

Insurer Management and Regulation

Insurance Cycles: Interest Rates and the Capacity Constraint Model, by Neil A. Doherty (University of Pennsylvania) and James R. Garven (University of Texas at Austin)

Insurance profits exhibit cyclical behavior that has been attributed to capital market constraints. We show that changes in interest rates simultaneously affect the insurer's capital structure and the equilibrium underwriting profit. Depending upon asset and liability maturity structure, capital market access, and reinsurance availability, insurers will be differently affected by changing interest rates. We find that average market response to changing interest rates roughly tracks market clearing prices. These "cyclical" effects are enhanced for firms with mismatched assets and liabilities and more costly access to new capital and reinsurance. This evidence supports the capacity constraint hypothesis. *Journal of Business,* July 1995, 68(3): 383-404. (Reprinted with permission of the *Journal of Business.*)

Restrictions of Competition on Insurance Markets and the Applicability of EC Antitrust Law, by M. Faure and R. Van den Bergh

This paper discusses the exemption of the insurance branch from the applicability of EC antitrust rules. It argues that the conditions for an exception are not met and that the exemption to remain in existence, which will seriously hinder the realization of a common insurance market. The exemption, which is the result of lobbying by the insurance industry, will reduce the importance of modest successes of liberalization of insurance markets. *Kyklos,* 1995, 48(1): 65-85. (Reprinted with permission of the *Journal of Economic Literature.*)

Insurance Pricing

Allocation of Solvency Cost in Group Annuities: Actuarial Principles and Cooperative Game Theory, by Antoni Alegre and M. Mercè Claramunt (University of Barcelona)

This article will compare two methods of allocating solvency cost: the first based on actuarial principles; the second based on cooperative game theory. The consistency of the actuarial principles will be analyzed by looking at the rationality of the allocation. Two numeric applications will also be made. *Insurance: Mathematics and Economics,* August 1995, 17(1): 19-34. (Reprinted with permission of North-Holland Publishing Company.)

Insurance Pricing and Increased Limits Ratemaking by Proportional Hazards Transforms, by Shaun Wang (University of Waterloo)

This paper proposes a new premium principal, where risk loadings are imposed by a proportional decrease in the hazard rates. This premium principle is scale invariant and additive for layers. It is shown that this principle will generate stop-loss contracts as optimal reinsurance arrangements in a competitive market when the reinsurer is less risk averse than the direct insurer. Finally, increased limits factors are calculated based on this principle. *Insurance: Mathematics and Economics,* August 1995, 17(1): 43-54. (Reprinted with permission of North-Holland Publishing Company.)

Safety and Loss Control

Injuries and Aging Workers, by Kathleen L. Ringenbach and Rick R. Jacobs (Pennsylvania State University)

The relationship between an aging workforce and injuries in the workplace was explored via attitudinal/background survey and accident/injury reports within a nuclear power plant. Hypotheses of the relationship between aging and safety orientations and the role of safety orientations in forecasting injuries were tested in a sample of 209 workers at the plant. Results indicated that age of worker is related to various reports of health status and safety orientations and that safety orientations are related to different measures of injuries. Implications of these results for dealing with aging workforces and accident prevention programs are presented along with perspectives on direction for future research. *Journal of Safety Research,* Fall 1995, 26(3): 169-176. Reprinted with permission of the *Journal of Safety Research.*)

Liability Rules

The General-Liability Reform Experiments and the Distribution of Insurance-Market Outcomes, by W. K. Viscusi and P. Born

Many states enacted tort liability reform laws in the late 1980s to limit liability costs and stabilize insurance markets. This paper uses firm-level data from two states that enacted reforms over the 1984–1991 period—New York and Colorado—to assess their effects. The liability insurance performance in Pennsylvania and Kentucky—two states that did not adopt reforms—provides a reference point for how insurance markets might have performed. The quantile regression models indicate that the improvement in insurer profitability was substantial. However, this improvement appears to be largely attributable to a secular trend rather than the effect of liability reforms. *Journal of Business and Economic Statistics,* April 1995, 13(2): 183-188. (Reprinted with permission of the *Journal of Economic Literature.*)

LIABILITY RISK

Modeling Potential Liability Costs in Large Class-Action Cases with Incomplete Information, by Robert D. Shriner and Philip B. Cook

Large class-action product liability cases pose special analytical problems for defendant firms. The firms need to assess realistically the likely costs of resolving claims presented by class participants plus suits and other claims filed separately by opt-outs, often at an early stage at which the number of claimants and the nature of their claims are still uncertain. A summary is presented of techniques used to develop simulation and forecasting models to estimate the probable extent of liabilities and the likely costs of settling claims arising from major product liability situations. In addition, some common problems are identified and means of handling them are suggested. *Business Economics,* April 1995, 30(2): 55-59. (Reprinted with permission of ABI/INFORM, copyright UMI.)

Risk Management

The Cost of Risk and the Concept of Risk Partnership, by John W. Reid (Glasgow Caledonian University, Scotland)

A recent survey in the United Kingdom has highlighted the large discrepancy between the insured and uninsured cost of losses, demonstrating that the true cost of risk is much higher than previous estimates. Risk is never totally transferred by insurance, and if insureds recognise that they retain a partial ownership of the risk there is a greater likelihood that there will be better loss control. The paper promotes the concept of "risk partnership" as a more correct representation of the contract between insurer and insured than the more generally used term of "risk transfer." *The Geneva Papers on Risk and Insurance,* July 1995, 20(76): 279-284. (Reprinted with permission of *The Geneva Papers on Risk and Insurance.*)