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BARGAINING THEORY

Priority Setting in Health Care: An Axiomatic Bargaining Approach, by Derek Clark

How axiomatic bargaining theory can be used to analyze different rules for dividing the health care budget between two patients is examined. This approach allows an explicit statement of the assumptions underlying the division rules and also provides a general characterization of the consequences of using these rules when the opportunity set changes. *Journal of Health Economics*, August 1995, 14(3): 345-360. (Reprinted with permission of ABI/Inform, copyright UMI.)

RISK PERCEPTION AND ECONOMIC BEHAVIOR

Forming Beliefs About Adjudicated Outcomes: Perceptions of Risk and Reservation Values, by Linda Babcock, Henry S. Farber, Cynthia Fobian, and Eldar Shafir

In negotiations where impasse is resolved via a dispute resolution mechanism (like the courts or arbitration), beliefs about a potential adjudicated outcome are central in determining the bargaining environment. Research investigates how negotiators involved in a hypothetical product liability case use the information encompassed in damage awards from previous, similar cases in forming beliefs about their own case. How the parameters of the distribution of previous outcomes affect the expected adjudicated outcome and the parties' reservation values are examined. It is found that the range of previous outcomes has no significant effect on subjects' reservation values, but that the variance does have a systematic effect, particularly on plaintiffs' behavior. It is found that, for the plaintiffs' attorneys, the reservation value is influenced negatively by the standard deviation of the distribution of previous adjudicated outcomes. However, for defendants' lawyers, there is no

significant relationship. *International Review of Law & Economics*, September 1995, 15(3): 289–303. (Reprinted with permission of ABI/Inform, copyright UMI.)

RISK THEORY

Individual Risk and Mutual Insurance, by David Cass, Graciela Chichilinsky, and Ho-Mou Wu

An examination is made of how, in the presence of individual risk, economic efficiency can be achieved without an unrealistically large number of contingent claims. Market uncertainty is specified in such a way that general types of individual risk and collective risk are properly accounted for and so that, specifically, market clearing is always satisfied ex post as well as ex ante. It is shown that consistency of beliefs and optimality of allocation can be guaranteed with an appropriate array of pure Arrow (1953) securities to spread collective risk and mutual policies to pool individual risk. When there is individual risk common to like groups of individuals, pooling risk by means of mutual insurance permits substantial economizing on market transactions, as compared to those required if dealing instead with the full compliment of pure Arrow securities. It is shown that if there are N households (consisting of H types), each facing the possibility of being in S individual states together with T collective states, then ensuring Pareto optimality requires only $H(S-1)$ independent mutual insurance policies plus pure Arrow securities. *Econometrica*, March 1996, 64(2): 333–341. (Reprinted with permission of ABI/Inform, copyright UMI.)

HEALTH CARE AND INSURANCE

Health Insurance and Precautionary Savings, by Martha Starr-McCluer (Federal Reserve Board of Governors, Washington, D.C.)

This paper examines whether health insurance is associated with lower wealth holdings, as the precautionary view of savings predicts. Using data from the 1989 Survey of Consumer Finances, I find that insured households maintain much *higher* levels of wealth than comparable households without coverage. Even when efforts are made to account for selectivity, there is only mixed evidence that households facing greater health risks save more as a result. This suggests that savings and health insurance are related for reasons that have little to do with uncertainty and precautionary motives. The findings may also be consistent with previous studies in which effects of risk on savings are found to be fairly weak. *The American Economic Review*, March 1996, 86(1): 285–295. (Reprinted with permission of *The American Economic Review*.)

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