Book Reviews

Deregulating Property-Liability Insurance: Restoring Competition and Increasing Market Efficiency, by J. David Cummins, editor, 2002, Washington D.C.: AEI-Brookings Joint Center for Regulatory Studies

Reviewer: Lorilee A. Schneider, Georgia State University

Given the purpose of the book—to provide an observational framework for considering the wisdom of property-liability insurance price regulation in general—the choice to focus on automobile insurance pricing makes sense. The size and importance of the auto insurance line to the property-liability insurance industry is staggering, such that the question of whether to deregulate it is of significant interest to a mass group. And it is one of only a few property-liability insurance lines that remain regulated, thus providing ease of observation. Finally, private-passenger auto insurance is dominated by the personal lines, therefore making the findings of these researchers relevant to public policy concerns.

Based largely on case studies conducted by several current leaders in risk management and insurance research, the compilation of their findings makes a compelling overall argument for deregulation of auto insurance pricing. Cummins, in the introductory chapter, provides an excellent synopsis of the research findings, and concludes overall that the auto insurance marketplace is more than competitive enough to allow competitive market equilibrium to do its work without the intervention of regulators. Indeed, he makes clear that none of the case studies found evidence of excessive rates or collusion in states where competitive market pricing is heavily used, but rather that rates are lower and less volatile within deregulated as opposed to regulated markets.

The findings are largely based on five case studies presented at a conference on the topic of auto insurance price regulation (or deregulation) in five states: California (Jaffee and Russell), Massachusetts (Tennyson, Weiss, and Regan), and New Jersey (Worrall) where prices are heavily regulated, as well as Illinois (D'Arcy) and South Carolina (Grace, Klein, and Phillips) where prices have been largely deregulated in recent years. Observations on the effects of prior-approval-based rating of auto insurance across states (Harrington) and form regulation of commercial insurance (Butler) add support to the findings. The book also provides an informative summary of the effects of regulation in other industrial countries (Dionne).

The book is a valuable read for anyone interested in regulatory and public policy issues pertaining to insurance and financial services. A relevant, engaging, and objective analysis of regulatory issues, the book does, however, leave one critical issue largely untouched. An addendum that examines how to avoid potential pitfalls of

deregulation would be most welcome to accompany this text. Even if deregulation of property-liability insurance pricing makes sense, any adjustments necessary to ensure a smooth transition need to be addressed.

Risk and Medical Decision Making, by Louis Eeckhoudt, 2002, Norwell, MA: Kluwer Academic Publishers

Reviewer: Patricia Born, California State University, Northridge

Risk and Medical Decision Making is a new addition to the "Studies in Risk and Uncertainty" series published by Kluwer Academic Publishing. Books in this series cover a variety of topics relevant to insurance research including risk, valuation, and decision making under uncertainty. This latest addition reviews and expands on the existing theories of decision making in the medical care context. This focus is motivated by the fact that, "unlike many financial risks that can be either divided or transferred to others (e.g., through diversification, insurance or social security) the personal aspects of medical risks are by essence indivisible and nontransferable."

While the models are developed in the context of diagnostic and therapeutic risks, they may be generalized for decision making in a variety of contexts.

The book contains an Introduction, followed by eight chapters divided into two parts. In the first part, the author focuses on medical decisions within the expected utility (EU) model. Part 2 addresses new non-EU models of choice including the "dual theory" of choice under risk. The reader should be familiar with the basic concepts of decision sciences, the use and notation of decision trees and the notion of risk aversion in the EU model. At the end of each chapter the author provides a summary of the key findings and several review questions (some solutions are provided).

In the Introduction (Chapter 1), Eeckhoudt provides a literature review to place his work in context. He notes that much of the book follows the seminal work in medical decision making by S. Pauker and J. Kassirer (PK) in the 1970s. These works included (1) optimal therapeutic decisions in the presence of diagnostic risks, and (2) the valuation of diagnostic tests, and relied on the EU model to evaluate risky situations. Eeckhoudt recognizes and classifies the developments that followed PK's work, and structures this book along two categories of research. First, he notes that models of medical decision making have been expanded to include background risks, or comorbidities. These models develop a concept of "prudence" to complement "risk aversion." Eeckhoudt provides several examples in the following chapters to illustrate this new concept. The second category of research involves new models of choice under uncertainty. Eeckhoudt notes that these new models deserve more attention because they give new intuitions about optimal behaviors. The last two chapters of the book provide a basic introduction to these areas of research.

Chapter 2 is devoted to a review of the 1975 PK paper, in which the decision is to treat or not to treat, when the patient may or may not have a disease. Thus, the decision tree involves four outcomes, which are stated in terms of "quality adjusted life years" or QALYs. The choice of whether or not to treat depends on the benefit of treatment (known), the loss of QALYs because a healthy patient is treated, and the utility function of the decision maker. Eeckhoudt evaluates the decision tree in the case of a risk neutral decision maker to obtain a threshold for treatment. He shows