Bargaining with a Residual Claimant: An Experimental Study

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Abstract: Many negotiations involve risks that are only resolved ex-post, and often these risks are not incurred equally by the parties involved. We experimentally investigate bargaining situations where a residual claimant faces ex-post risk, whereas a player does not. In line with the predictions of a benchmark model, we find that residual claimants extract a risk premium, which increases in risk exposure, and that this premium can be high enough to make it beneficial to bargain over a risky rather than a risk-less pie. In contrast to the model's predictions, we find that the comparatively less risk averse residual claimants benefit the most from risk exposure and this is driven by players' adoption of weak bargaining strategies when the pie is risky. We find evidence for a behavioural mechanism where asymmetric exposure to risk between the two parties creates a wedge between their fairness ideas, which shifts agreements in favour of residual claimants but also increases bargaining friction.