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Allocation of tasks for reliability growth using multi-attribute utility

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Abstract
In reliability growth models in particular, and project risk management more generally, improving the reliability of a system or product is limited by constraints on cost and time. There are many possible tasks which can be carried out to identify and design out weaknesses in the system under development. This paper considers the allocation problem: which subset of tasks to undertake. While the method is applicable to project risk management generally, the work has been motivated by reliability growth programmes. We utilise a model for reliability growth, based on an efficacy matrix, developed with engineering experts in the aerospace industry. We develop a general multi-attribute utility function based on targets for cost, time on test and system reliability. The optimal subset is identified by maximising the prior expected utility. We derive conditions on the model parameters for risk aversion and loss aversion based on observed properties of preference. We give conditions for multivariate risk aversion under the general form of the utility function. The method is illustrated using an example informed by work with aerospace organisations.

Keywords: utility theory, reliability growth, Bayesian experimental design, multivariate risk aversion, expert judgement

1 Introduction
Selecting a programme of activities optimal against multiple criteria is cognitively challenging and time consuming for decision makers but can be aided with appropriate decision support tools if preferences can be represented mathematically. In the development of large, complex products or systems, the system is analysed at various stages for potential design weaknesses and, once weaknesses have been identified, they are designed out. This improves the system’s reliability. Examples of tasks which are used to identify weaknesses are fault tree analysis, failure modes and effects analysis, test, analyse and fix (TAAF), load strength analysis, vibration testing, simulation studies and accelerated life testing [24].

The outcomes of these tasks will not be mutually exclusive: tasks may expose multiple weaknesses and weaknesses may be exposed by various tasks. There will typically be neither the budget nor the time to carry out all of the potential reliability tasks. Therefore engineers choose and sequence a subset of tasks to improve the product’s reliability. This paper considers methods to select such a portfolio of reliability tasks.

While our motivation is concerned with managing reliability growth programmes, trading between performance targets, project duration and costs dynamically throughout a project is a concern for project risk management broadly. Previous approaches have used mathematical optimisation [13, 12, 16, 17] or fuzzy logic [23, 18, 27, 26] to solve the decision problem. We use a utility-based approach. If we have hard constraints, like in optimisation, we can miss some desirable solutions. As such, we need to develop methods that penalise as we move farther away from desirable targets. We have chosen to develop the decision support on utility theory, as we
seek to represent preference trade-offs rather than vagueness of decision makers. Multi-attribute utility has been used in a similar manner in the area of portfolio resource allocation [30, 14, 1] and the simplifying assumption of utility independence is identified as desirable to specify a utility function.

In the context of reliability growth [33, 28] developed a model which aimed to represent the process experienced by engineers. It explicitly considered all of the potential faults and tasks to identify them resulting in the use of an efficacy matrix. The efficacy of each task is assessed against each potential failure mode producing an efficacy matrix for each pairing to measure the conditional probability of exposing the failure mode given its presence in the design. Such a matrix could have uses across project risk management problems. Reliability improves as specific design weaknesses are identified and removed from the system. All of the parameters in the model can be elicited from observable quantities. We use this model as the basis to solve the decision problem of task allocation. [33] also considered task allocation and outlined an integer programming approach which minimised costs subject to constraints on expected reliability and time on test. The shortcoming of this approach is that it provides little sensitivity around the reliability and time targets: an allocation which just failed to meet the targets was unacceptable and an allocation which met the targets was equally desirable.

In this paper we propose a Bayesian solution to the task allocation problem; choosing the allocation which maximises the prior expectation of a utility function representing the engineers’ preferences over cost, reliability and time on test. A general utility function over these attributes, which utilises the idea of mutually utility independent hierarchies, will be developed. The form of this utility function will be adapted to satisfy observed properties of marginal preferences from decision makers in experiments. In particular, we develop conditional utility functions to represent risk averse preferences and loss averse preferences which satisfy the isolation effect. That is, preferences of individuals over lotteries generally discard elements that the lotteries have in common [19, 32].

We consider the impact of the form of the utility function on preferences over multiple attributes and give conditions for the individual risk averse and loss averse utilities to lead to multivariate risk aversion [29]. The resulting optimal allocation is more sensitive to small changes in expected reliability and time on test around the target values than the integer programming approach. This is the first time multi-attribute utility has been used for task allocation in reliability growth modelling.

The contribution of the paper takes two forms; a theoretical contribution on multi-attribute utility and a methodological contribution on reliability growth specifically and project risk management more generally. In the first case, we consider for the first time the implications for multivariate preference behaviour by assuming utility independence within a mutually utility independent hierarchy (MUIH). Proposition 4 shows that such structures are sufficiently flexible to represent multivariate risk aversion, risk neutrality and risk seeking behaviour. Proposition 3 shows that not all attributes within a MUIH are by necessity utility independent. The illustrative example quantifies the impact of assuming different preference behaviours of the decision maker within utility functions. The preferences of the decision maker over multiple attributes can result in different optimal allocations of reliability tasks. In the second case, we develop a methodology within a reliability growth framework which allows engineers to make decisions about which activities to undertake which explicitly considers trade-offs between the important attributes in their decision. The methodology captures varying preference behaviours and gives an analytically tractable solution to the decision problem. We indicate the generalisation of the methodology to similar decision problems in project risk management.

The rest of the paper is structured as follows. In Section 2 we outline the model for reliability growth developed by [33]. In Section 3 we outline our Bayesian expected utility approach to the allocation problem, giving the general form of the solution method and developing utility functions over reliability, cost and time on test. In Section 4 we present an illustrative example to compare the expected utility approach to the integer programming approach and to investigate the properties of the expected utility approach. We provide a simulation study to investigate the effects of assuming risk aversion and loss aversion of the decision maker. Finally, we summarise
2 An expert judgement informed reliability growth model

We adopt the approach developed in [33, 28]. In Section 2.1 we define the efficacy matrix, which is core to the reliability growth model. In Section 2.2 we derive the reliability assessment for a design prior to undertaking reliability tasks. In Section 2.3 we derive the updated reliability assessment following the outcome of a reliability task.

2.1 The efficacy matrix

Suppose that the current design of an engineering system has associated with it a number of identified potential faults, labelled \( i = 1, \ldots, I \). Then, for each fault \( i \), there is some probability, denoted \( \lambda_i \), that this fault will be realized as a failure at some point in the lifetime of the system. Define \( X_i \) to be an indicator variable,

\[
X_i = \begin{cases} 
1, & \text{if fault } i \text{ is ever realised}, \\
0, & \text{otherwise}.
\end{cases}
\]

The probabilities of \( X_i \) being in its two possible states are \( \lambda_i \) and \( 1 - \lambda_i \) respectively.

As part of the growth programme there are a number of possible tasks which could be performed on the system, labelled \( j = 1, \ldots, J \). Each task will have a certain efficacy at identifying each of the faults in the system. Denote by \( p_{i,j} \) the conditional probability that task \( j \) will realise fault \( i \) given that the fault exists within the system.

An illustration of the efficacy matrix is given in Figure 1. We see the \( J \) possible tasks to identify the \( I \) potential faults in the system. Each of the faults has an associated probability that it exists in the system. In the figure, task 1 will identify faults 1 and 3 with probabilities \( p_{3,1}, p_{1,1} \) respectively. Fault 1 could also be identified by tasks 2 and 3. Therefore there are multiple routes which could identify fault 1. By contrast, none of the tasks in the figure can identify fault 2. The probability that fault 2 exists, \( \lambda_2 \), will never change as a result of performing any task.

![Figure 1: A diagram illustrating the form of the efficacy matrix](image-url)

We can elicit both \( \lambda_i \) and \( p_{i,j} \), by asking questions about observable quantities, from engineering
experts inside the organisation. For more information see [15]. Similarly, [35] developed a Bayesian model based on observable quantities for reliability growth in the TAAF cycle.

2.2 Prior reliability

Assume that each time a fault is found and removed no new fault is added to the system. Then in the system there will be some fixed unknown number of faults, \( N \).

Assuming that the faults are independent then the reliability of the system at time \( t \) is \( R(t) = \prod_{i=1}^{I} R_i(t)^{X_i} \), where \( R_i(t) \) is the reliability associated with fault \( i \) at time \( t \). Prior to performing any tasks the expected reliability at time \( t \) \([33]\) is

\[
E_X[R(t)] = \prod_{i=1}^{I} \sum_{x_i \in \{0,1\}} \Pr(X_i = x_i) R_i(t)^{x_i},
\]

\[
= \prod_{i=1}^{I} [1 - (1 - R_i(t)) \lambda_i].
\]

That is, we can express the expected reliability of the system as a function of the reliability functions associated with each of the faults, which will typically be of a convenient parametric form, and the probabilities that each of the faults are present in the system.

2.3 Post-development reliability

Suppose we perform a number of the tasks. We either observe fault \( i \) in one of the tasks, \( d_i = 1 \), or not, \( d_i = 0 \). This will update, through Bayes Theorem, the probabilities of the faults truly existing to \( \Pr(X_i = 1 \mid d_i = 1) = 1, \Pr(X_i = 0 \mid d_i = 1) = 0 \), as when a fault is found it must exist and

\[
\Pr(X_i = x_i \mid d_i = 0) = \begin{cases} 
1 - \lambda_i & , x_i = 0, \\
\frac{1 - \lambda_i[1 - \prod_{j=1}^{J}(1 - p_{i,j})^{\theta_j}]}{\lambda_i \prod_{j=1}^{J}(1 - p_{i,j})^{\theta_j}} & , x_i = 1,
\end{cases}
\]

where \( \theta_j \) is an indicator variable which takes the value 1 if task \( j \) has been performed and 0 if not. The prior expectation of the reliability \([33]\) is then

\[
E_D\{E_X \mid D[R(t)]\} = \prod_{i=1}^{I} \left[ \sum_{d_i \in \{0,1\}} \Pr(D_i = d_i) \right. \\
\times \left. \sum_{x_i \in \{0,1\}} \Pr(X_i = x_i \mid D_i = d_i) R_i(t)^{I[x_i > d_i]} \right],
\]

where \( I[x_i > d_i] \) is an indicator variable which takes the value 1 when \( x_i > d_i \) and 0 otherwise. We see that we can evaluate the expected reliability of the system analytically once we know the reliability functions, \( R_i(t) \), associated with each of the faults.

3 The allocation of reliability tasks

In this section we extend the reliability growth model to include a multi-attribute utility function and explore the implications for decision makers with different attitudes towards risk. In Section
3.1 we discuss some general characteristics of our multi-attribute utility function. In Sections 3.2 to 3.6 we explore the implications of loss averse and risk averse preferences of the decision maker.

### 3.1 General Bayesian solution

Each task will have associated with it a certain cost, denoted $y_j$, and duration, denoted $\chi_j$. Before a product can be released it needs to attain a specific target reliability $R_0$. Any testing which is undertaken is also subject to time restrictions given by the maximum total time on test $\chi_0$ and cost restrictions given by the total budget for the testing $Y_0$. There may also be a target time on test $T_0 < \chi_0$.

The total cost and total time on test following a set of tasks are given by

$$Y = \sum_{j=1}^{J} y_j \theta_j, \quad \chi = \sum_{j=1}^{J} \chi_j \theta_j,$$

respectively.

The objective of the design problem is to identify a subset of tasks which lead to a system with high reliability, low costs and low time on test.

The general Bayesian solution to this allocation problem is

$$\max_{\theta_1, \ldots, \theta_J \in \{0, 1\}^J} \mathbb{E}_D \left\{ \mathbb{E}_{X|D} \left[ U(R, Y, \chi) \right] \right\},$$

where $U(R, Y, \chi)$ is the utility function. That is, we maximise the prior expectation, over all of the possible subsets of tasks, of a utility function which represents the engineer’s preferences over the attributes in the problem, namely, reliability, cost and time on test.

Suppose that a decision maker was asked to specify their preferences over lotteries which associate consequences (e.g. reliability, cost) with rewards $\rho$. We define a utility function as follows [31].

**Definition 1.** A utility function on rewards $\rho_1, \rho_2, \rho$ such that $\rho_1 < \rho < \rho_2$ satisfies

$$\rho \sim \alpha \rho_2 + (1 - \alpha) \rho_1,$$

$$U(\rho) = \alpha U(\rho_2) + (1 - \alpha) U(\rho_1),$$

for real number $\alpha \in (0, 1)$, where $U(\rho_1) < U(\rho_2)$ whenever $\rho_1 < \rho_2$.

Utility is as a measure of our attitude towards lotteries. The larger the utility, the stronger our preference is for the lottery.

Utility functions can, without loss of generality, be rescaled so that the utility of the best possible outcome is 1 and the utility of the worst outcome is 0. This is useful when defining utility functions over multiple attributes. However, defining a multi-attribute utility function such as $U(R, Y, \chi)$ is a difficult problem as we would need to ask engineers about their preferences in 3-dimensional space. Therefore, to make specification of the utility function a more manageable task, we can make use of the property of utility independence [21, 8].

**Definition 2.** Attributes $A_1 = (A_{1,1}, \ldots, A_{1,m})$ and $A_2 = (A_{2,1}, \ldots, A_{2,l})$ are utility independent if conditional preferences over lotteries on $A_1$ given $A_2 = a_2$ do not depend on the value of $a_2$.

In our case, for example, utility independence between cost and reliability would imply that preferences for reliability $R_1$ over $R_0$ would not change whether costs were $Y_1$ or $Y_0$. This may be a reasonable assumption in a situation where engineers are given stringent targets on the reliability the product must meet and the total budget for the programme. We can extend the idea to multiple sets of attributes [21].

**Definition 3.** Attributes $A = (A_1, \ldots, A_n)$ are mutually utility independent if every subset of $A$ is utility independent of its complement.
If all attributes \( A \) are mutually utility independent then [21] the utility function takes one of two forms:

\[
\text{Additive} \quad U(A) = \sum_{i=1}^{n} \alpha_i U_i(A_i), \\
\text{Multiplicative} \quad (1 + kU(A)) = \prod_{i=1}^{n} (1 + k\alpha_i U_i(A_i)),
\]

for constants \( \alpha_i, k \), where \( U_i(A_i) \) is the conditional utility for \( A_i \).

In order to construct complex multi-attribute utility functions it can be useful to consider utility hierarchies [20, 21]. We can represent such a hierarchy in graphical form. The overall utility is separated into the conditional utilities of its individual attributes, each of which is represented by a node. Arrows from each of the attributes into the overall utility node indicate that this is the ‘child’ node for each of the ‘parent’ attribute nodes. Each of the attributes can be separated into sub-attributes as necessary. The sub-attributes are the parent nodes of the child node for the corresponding attribute.

If, for each child node, the parent nodes are mutually utility independent, we call the resulting hierarchy a mutually utility independent hierarchy (MUIH) [8]. We can construct a utility function, given such a hierarchy, in the following way.

- For each parent set of sub-attributes at the lowest level of the hierarchy construct an additive or a multiplicative utility function for the child.
- Repeat this step for each node at the next level up in the hierarchy and continue this process until the overall utility is obtained.

In our case, if reliability is utility independent of costs and financial costs are utility independent of time costs then the utility function \( U(R, Y, \chi) \) can be written in terms of the following MUIH:

\[
U(R, Y, \chi) = q_1 U_R(R) + q_2 U_Y(Y, \chi) + q_3 U_R(R) U_Y(Y, \chi), \\
U_{Y,\chi}(Y, \chi) = r_1 U_Y(Y) + r_2 U_\chi(\chi) + r_3 U_Y(Y) U_\chi(\chi),
\]

where \( 0 < q_1, q_2, r_1, r_2 < 1 \), \( q_3 \leq 1 - q_i \), \( -r_i \leq r_3 \leq 1 - r_i \) for \( i = 1, 2 \), and \( q_1 + q_2 + q_3 = r_1 + r_2 + r_3 = 1 \). That is, we can represent the overall utility in terms of a binary utility function for cost and reliability and the utility for cost in terms of a binary utility function for financial and time cost. We reduce the specification of a 3-attribute utility into the specification of three univariate utilities and trade-off parameters between them. This would facilitate elicitation. The MUIH is given in Figure 2. We discuss the specification of the trade-off parameters \( (q_1, q_2, q_3, r_1, r_2, r_3) \) in a Section 4.1.3.

The following results provide insight into the relationship between the interaction parameter \( q_3 \) and how a decision maker trades off between aggregate cost and reliability while keeping utility constant. This is referred to as the marginal rate of substitution. The proofs for both results are given in the Supplementary Material.

**Proposition 1.** The marginal rate of substitution between aggregate cost and reliability has a monotonically decreasing relationship with the interaction parameter \( q_3 \).

This result tells us that decreasing \( q_3 \) will increase the value of reliability.

**Proposition 2.** Increasing the interaction parameter \( q_3 \) will decrease the utility level for aggregate costs.

These propositions will be used to interpret the results from the simulation study in section 4.2.

The structure of a MUIH is not as restrictive as it may at first seem. We give the following result. The proof is given in the Supplementary Material.

**Proposition 3.** Suppose we have attributes \( \alpha = (a_1, \ldots, a_n) \) such that \( a_i = (a_{i,1}, \ldots, a_{i,m_i}) \) represents the attributes in node \( i \) in a MUIH. Then \( a_{i,j} \) and \( a_{k,l} \) can be utility dependent for \( i \neq k \).
To solve the decision problem, the expectations will be taken over the utility function for the reliability, $U_R(R)$. 

**Remark 1.** If the utility function $U_R(R)$ is a polynomial function of the reliability $R$, and the reliabilities for each fault type $i$, $R_i(t)$, are analytically tractable, then, using the reliability growth model in Section 2, an analytic solution to the reliability task allocation problem will exist.

We can see this by considering the moments of the reliability. They are given by

$$E_D \{E_{X|D} \{R(t)^\beta\} \} = \prod_{i=1}^{J} \left[ 1 - (1 - R_i(t)^\beta) \lambda_i \prod_{j=1}^{J} (1 - p_{i,j})^{\theta_j} \right].$$

Thus, for any integer $\beta$, we can evaluate all of the moments of $R(t)$ analytically whenever $R_i(t)$ can be analytically evaluated. Hence there will be an analytic solution using any of the usual parametric forms of the reliability such as Exponential or Weibull, as well as for non-parametric forms. In the illustrative example in Section 4 we consider Exponential failure distributions. We do so without loss of generality, as with non-constant failure rates we can always warp the time axis so that failure rates are constant over the warped axis.

### 3.2 Risk aversion and loss aversion

In general, preferences of decision makers have been shown to be risk averse [7], with some notable exceptions which we discuss below. We define risk aversion of a decision maker in the following way [21].

**Definition 4.** Risk aversion can be measured, for consequences of a lottery $c$, by $g(c) = U''(c)$, where $U''(\cdot)$ is the second derivative of the utility function $U$. In this case $g(c) < 0$ for a risk averse individual, $g(c) = 0$ for a risk neutral individual and $g(c) > 0$ for a risk seeking individual.

In general, individuals’ preferences are risk averse [19, 32] and this implies convex utility functions for costs and concave utility functions for benefits. That is, we define $U_{1,Y}(Y), U_{1,\chi}(\chi), U_{1,R}(R)$ such that $\partial^2 U_{1,Y}(Y)/\partial Y^2 < 0, \forall Y$, $\partial^2 U_{1,\chi}(\chi)/\partial \chi^2 < 0, \forall \chi$, and $\partial^2 U_{1,R}(R)/\partial R^2 < 0, \forall R$.

[19, 32] and others have observed this risk averse property of preference in individuals in psychological experiments. However, they observed two further properties of preference which
do not satisfy such a solution: individuals generally discard components that are shared by all
lotteries under consideration and individuals generally underweight outcomes that are probable
in comparison to those obtained with certainty. They named these properties the isolation effect
and the certainty effect respectively. The isolation effect relates to reference points. Any resulting
wealth lower than the reference point is regarded as a loss and any resulting wealth higher than
the reference point is regarded as a gain. This implies utility functions should be concave for gains
and convex for losses from a reference point of anticipated wealth following the lottery.

The isolation effect implies that utility functions should represent loss averse rather than risk
averse decision makers. Loss aversion is a property of prospect theory rather than utility theory.
Consistency with the isolation effect in utility theory implies s-shaped utility functions around a
reference point. There are many cases of such utility functions being used. It will be useful for
our purposes to give a formal definition of loss aversion. Loss aversion is defined in the following
way (page 238 of [34]).

**Definition 5.** Consider a utility function on consequence \( c \), for which \( c > 0 \) is regarded as a gain
and \( c < 0 \) is regarded as a loss, of the form

\[
U(c) = u(c), \quad \text{for} \quad c \geq 0,
\]

\[
U(c) = \mu u(c), \quad \text{for} \quad c < 0.
\]

The utility function represents a loss averse individual if \( \mu > 1 \) and a gain seeking individual if
\( \mu < 1 \).

This suggests that a loss averse individual is focused on avoidance of losses with little attention
on gains and a gain seeking individual is focused on seeking gains with little attention for losses
[34].

Let us return to the idea of gains from lotteries. Suppose the references point as the anticipated
consequence (e.g. wealth) following the lottery is \( w \).

**Remark 2.** For a solution to satisfy preferences consistent with the isolation effect \( g(c) > 0 \) for
c < w and \( g(c) < 0 \) for c > w.

In terms of the reliability growth problem, the engineers would anticipate the product to be
released and so a reasonable reference point for the reliability would be \( R_0 \). Similarly, they might
anticipate to achieve their time on test target and so their reference point for time on test would
be \( T_0 \). In terms of cost, the budget for testing is \( Y_0 \) and any spend under this could be thought
of as a gain. Therefore we take this as the reference point in the utility function. Other reference
points are possible and utility functions could be adapted to these simply.

A utility function representing loss aversion \( U_{2,Y}(Y) \) for cost would be defined such that
\( \partial^2 U_{2,Y}(Y)/\partial Y^2 > 0 \), \( \forall Y \), a utility function representing loss aversion \( U_{2,\chi}(\chi) \) for time on test
would be defined such that

\[
\frac{\partial^2 U_{2,\chi}(\chi)}{\partial \chi^2} \begin{cases} > 0, & \text{for} \ \chi < T_0, \\ < 0, & \text{for} \ \chi > T_0, \end{cases}
\]

and a utility function representing loss aversion \( U_{2,R}(R) \) for reliability would be defined such that

\[
\frac{\partial^2 U_{2,R}(R)}{\partial R^2} \begin{cases} > 0, & \text{for} \ R > R_0, \\ < 0, & \text{for} \ R < R_0. \end{cases}
\]

We have given conditions for utility functions which represent risk aversion or loss aversion
in decision makers. However, since we have defined a utility function over three attributes, we
consider the multi-attribute preference behaviour implied by the resulting multi-attribute utility
function. [29] extended the idea of risk aversion to multi-attribute utility functions.

Consider a twice differentiable utility function with positive derivatives in both variables, for
two attributes \( a \in A, b \in B \), on a closed interval from the real line where \( a_0 < a_1, b_0 < b_1 \). Then
a bivariate risk averse (BRA) individual would prefer a lottery in which they receive \((a_0, b_1)\) or
(a_1, b_0) each with probability 0.5 to a lottery in which they receive (a_0, b_0) or (a_1, b_1) each with probability 0.5.

The idea was extended to utility functions in more than two attributes. Suppose we have attributes a_1, a_2, ..., a_n each defined on a closed interval on the real line. Then the twice differentiable utility function U(a) = U(a_1, ..., a_n) represents a multivariate risk averse (MRA) individual if and only if each pair (a_i, a_j), i ≠ j represents a BRA individual for all a_k \{a_i, a_j\}. The definition takes the same form for utility functions over multivariate risk neutral (MRN) and multivariate risk seeking (MRS) individuals.

We apply the definitions above to the general form of utility function we have developed for our problem. We obtain the following result, the proof of which is given in the Supplementary Material.

**Proposition 4.** A utility function U(R, Y, \chi) defined by the MUIH in (1) with twice differentiable increasing U(R) and decreasing U(Y), U(\chi) represents preferences which are

1. MRA if and only if r_3 > 0,
2. MRN if and only if q_3 = 0 and r_3 = 0, and
3. MRS if and only if q_3 > 0 and r_3 < 0.

Thus, using the general form of the utility function, for both risk and loss averse conditional preferences, we can incorporate multivariate risk averse, neutral or seeking decision makers.

### 3.3 Discussion

We propose a multi-attribute utility function where gains and losses are evaluated on an attribute specific basis. Foundations for such a multi-attribute utility function were developed by [5] which is supported by several empirical studies concerning decision making under risk (e.g. [2, 4, 32, 25, 9]). We require a reference point for each attribute about which we assess loss or gain.

Reference points from prospect theory [19] are typically defined as status quo. However, our interests are reliability growth where the purpose is change not status quo. Measuring performance for this context in relation to targets is more sensible, such as in [10], and these should be aligned with the targets negotiated at the start of the project.

We seek to develop prescriptive decision support for project management in reliability development where well established protocols for eliciting expert subjective probabilities exist (see for example [3, 36, 15, 22]). We do not make use of probability weighting functions which represent distortions of probabilities and as such our approach is consistent with classical utility theory.

### 3.4 Suitable utility functions

For a risk averse preferences approach, we wish to define convex utility functions over financial costs of the reliability tasks and times on test and a concave utility function over reliability. Suitable utility functions which satisfy this for financial cost and time on test are therefore

\[
U_{1,Y}(Y) = 1 - \left(\frac{Y}{Y_0}\right)^2 \quad U_{1,\chi}(\chi) = 1 - \left(\frac{\chi}{\chi_0}\right)^2.
\]

We see that, in both cases, the utility of the best possible outcome (Y = 0, \chi = 0) is 1 and the worst possible outcome (Y = Y_0, \chi = \chi_0) is 0. Also, g(Y) = -2/Y_0^2 < 0 and so the utility function represents risk aversion in cost. This is also true of the utility function for time on test.

A concave utility function for reliability can be defined as

\[
U_{1,R}(R) = -\gamma_{RA}R^2 + (\gamma_{RA} + 1)R.
\]

for parameter \(\gamma_{RA} > 0\). Again, in the worst case \(R = 0\) and so \(U_{1,R}(0) = 0\) and in the best case \(R = 1\) and so \(U_{1,R}(1) = 1\). The measure of risk aversion \(g(R) = -2\gamma_{RA} < 0\) since \(\gamma_{RA} > 0\) and
so this utility function represents risk aversion. The parameter $\gamma_{RA}$ represents the degree of risk aversion of the decision maker. We plot this utility function with different values of $\gamma_{RA} \in (0, 1)$ in Figure 3. We see that the utility gives a reasonable range of possible risk aversion. Larger values of $\gamma_{RA}$ imply larger risk aversion.

As the utility function for the reliability is a quadratic function in $R$, we have an analytic solution to the decision problem.

A suitable utility function representing loss aversion for reliability is

$$U_{2,R}(R) = \gamma_{LA} R^3 + (1 - \gamma_{LA}) R^2,$$

where $\gamma_{LA} = 1/(1 - 3R_0)$ to ensure the correct changepoint between convexity and concavity. We see that $U_{2,R}(0) = 0$ and $U_{2,R}(R) = 1$. Also, $g(R) = 2 - 2(1 - 3R)/(1 - 3R_0)$ and so $g(R_0) = 0$, $g(R) > 0$ for $R < R_0$ and $g(R) < 0$ for $R > R_0$ satisfying the condition in Remark 2. We give the following proposition.

**Proposition 5.** For $U_{LA}(R) = \gamma_{LA} R^3 + (1 - \gamma_{LA}) R^2$ to be monotonically increasing in $R$ and possess the loss averse concavity requirement at $R_0$ implies that $R_0 \geq \frac{1}{2}$ and as such $-\frac{1}{2} \leq \gamma_{LA} \leq -2$ or $R_0 = 0$ and $\gamma_{LA} = 1$.

A suitable utility function for loss aversion of time on test is

$$U_{2,X}(X) = \begin{cases} 
\phi_X \left( \frac{X_0 - X}{X_0} \right)^2, & X > T_0, \\
-\gamma_X \left( \frac{X_0 - X}{X_0} \right)^2 + (\gamma_X + 1) \left( \frac{X_0 - X}{X_0} \right), & X \leq T_0,
\end{cases}$$

where $\phi_X = -\gamma_X + (\gamma_X + 1)/T$ and $T = (X_0 - T_0)/X_0$ to ensure that the two functions are continuous at the changepoint. We have one free parameter $\gamma_X$. We see that $U_{2,X}(0) = 1$ and $U_{2,X}(X_0) = 0$ representing the best and worst cases respectively. Also in the second case $g(X) = -2\gamma_X/X_0^2 < 0$ whenever $X > T_0$ for $\gamma_X > 0$ and in the first case $g(X) = 2\phi_X/X_0^2 > 0$ whenever $X < T_0$ for $\gamma_X > 0, \phi_X > 0$. This gives a utility function which satisfies Remark 2.

The utility function is plotted in Figure 4 for different values of $\gamma_X \in (0, 1)$. We see there is a reasonable range of loss aversion possible using this utility function. Larger values of $\gamma_X$ lead to larger loss aversion.
The utility function representing loss aversion for cost simply needs to be concave as any spend under budget is a gain. A suitable form is

$$U_{2,Y}(Y) = -\gamma_Y \left( \frac{Y_0 - Y}{Y_0} \right)^2 + (\gamma_Y + 1) \left( \frac{Y_0 - Y}{Y_0} \right),$$

where $\gamma_Y$ is a parameter which represents the degree of loss aversion of the decision maker. We see that $U_{2,Y}(0) = 1$ and $U_{2,Y}(Y_0) = 0$ representing the best and worst case scenarios respectively. Also, $g(\chi) = -2\gamma_Y / Y_0^2 < 0$ for $\gamma_Y > 0$ and so the function is concave for all $Y \in (0,Y_0)$ and satisfies Remark 2.

The utility function is plotted in Figure 5 for different values of $\gamma_Y \in (0,1)$. We see there is a range of loss averse preferences possible using this utility function. Larger values of $\gamma_Y$ lead to larger loss aversion.

Thus we see that all of the utility functions satisfy the preference behaviour observed in the isolation effect.

The certainty effect implies that preferences are typically not linear in probability: an increase in the probability of an event from 0 to 0.01 does not affect preferences in the same way as an increase from 0.3 to 0.31. For the analyses in this paper we simply remark that preference changes are observed to be fairly linear except in such extremes of probability.

In practice, the preferences of many engineers would not take the convenient forms identified in this section. For information on the elicitation of multi-attribute utility functions see pages 99-101 of [11].

### 3.5 Properties

**Proposition 6.** When confronted with a choice between two alternatives, each with the same mean value, a risk averse decision maker whose utility function is described by $U_{1,R}(R_i) = -\gamma_{RA}R_i^2 + (\gamma_{RA} + 1)R_i$ will have the same ranked preference for the options as a loss averse decision maker whose utility who is described by $U_{2,R}(R_i) = \gamma_{LA}R_i^2 + (1 - \gamma_{LA})R_i$ if and only if the following condition is met (we denote the preferred option with subscript 1 and the other as 2).

$$E[R_2^2] - E[R_1^2] > \left( \frac{1}{\gamma_{LA}} - 1 \right) \left( Var[R_2] - Var[R_1] \right).$$

11
The implications of Proposition 6 concern how such a loss averse decision maker will value skewness compared with symmetry. Simply, when choosing between two risks where the first two moments are equal, then the less skewed distributed is preferred.

Moreover, the alternative with the smaller variance is only preferred if accompanied by a sufficiently smaller third moment, and so its distribution is more symmetric.

Corollary 1. A loss averse decision maker whose utility function can be expressed as 

$$U_2(R_i) = \gamma LA R_i^3 + (1-\gamma LA) R_i^2,$$

where $R_i$ represents the reliability of the system and $R_0$ is the target reliability of the programme, will prefer programme 1 over 2 under the following condition only.

$$E[R_1^3] < E[R_2^3] - 3R_0(\text{Var}[R_2] - \text{Var}[R_1]) \quad \text{if} \quad R_0 > \frac{1}{2}.$$

Framing the utility in terms of reliability provides an interesting insight into the trade-offs being made during a reliability development programme between the individual item reliability and a fleet, as we can interpret $E[R_k^3]$ as the expected proportion of a fleet of $k$ items surviving. As such, the implication is that specifying high reliability targets on an item basis can result in products will poorer fleet reliability.

### 3.6 Comparison of utility functions

In this section we consider the utility functions representing risk and loss aversion of decision makers defined in the previous two sections. We compare them to two other sets of utility functions, based on an integer programming approach.

[33] used an integer programming approach to solve the decision problem, minimising the expected cost of the tasks subject to meeting the target reliability and being below the maximum testing time. Their approach was consistent in flavour, though not giving identical results, with the Bayesian solution using the following utility functions.

The approach was risk neutral with respect to financial cost and so

$$U_Y(Y) = 1 - \frac{Y}{Y_0}.$$
In [33], two designs which met the target reliability were equally good and designs which did not were as poor as each other. Thus,

$$U_R(R) = \begin{cases} 
0, & E_D\{E_X|D[R(t)]\} < R_0, \\
1, & E_D\{E_X|D[R(t)]\} \geq R_0. 
\end{cases}$$

Similarly, two designs which used less than the target test time were equally good and those which did not were equally poor. Thus,

$$U_\chi(\chi) = \begin{cases} 
0, & \chi > T_0, \\
1, & \chi \leq T_0. 
\end{cases}$$

The linear programming approach assumes that two allocations which achieve the reliability target are equally good, though for two allocations equal in all else [33] would choose the one with higher expected reliability. We can build this preference for higher reliability even among designs which meet the target by using

$$U_R(R) = \begin{cases} 
E_D\{E_X|D[R(t)]\}, & E_D\{E_X|D[R(t)]\} < R_0, \\
1, & E_D\{E_X|D[R(t)]\} \geq R_0. 
\end{cases}$$

Similarly, it would seem reasonable that of two designs which are equal in all other aspects and meet the target test time threshold, we would prefer the one with the shortest test time. Thus we could use

$$U_\chi(\chi) = \begin{cases} 
0, & \chi > T_0, \\
1 - \frac{\chi}{\chi_0}, & \chi \leq T_0. 
\end{cases}$$

We will call these two sets of utility functions the integer programming approach and extended approach respectively.

In Figure 6 we have plotted the utility functions for cost, reliability and time on test using each of the four approaches detailed above. The target reliability is set to $R_0 = 0.8$, the target time on test $T_0 = 120$ and total budget $Y_0 = 500$. The utility functions for the linear programming approach are given in red, for the extended approach are given in green, for the risk averse approach in dark blue and the loss averse approach in light blue.

In the plot for cost we see that the utility functions for the integer programming approach and the extended approach are identical and linear. The utility functions for the risk averse approach and loss averse approach are also identical, given $\gamma_Y = 1$, and quadratic.

We see more differences in the utility functions for reliability. The integer programming approach results in a simple step function with little sensitivity and the extended approach represents a step function with a linear increase beyond the target reliability. There are differences between the risk averse and loss averse approaches in this case with the risk averse approach representing a decreasing gradient and the loss averse approach representing an increasing gradient below the target reliability.

Similarly, there are differences between all four utility functions for time on test. In particular, the utilities for the risk averse and loss averse approaches are very similar below the target time on test and very different above it.

For the loss averse approach, the utilities are defined in terms of the gain on the reference points rather than purely on cost, reliability and time on test. These are plotted in Figure 7.

In each case zero on the x-axis represents the reference point $(Y_0, R_0, T_0)$ respectively. From this we see the same pattern in each case, with risk seeking behaviour up to the target and then risk averse behaviour above the target value.

We now demonstrate each of the approaches developed in an illustrative example. The example uses simulated data but is consistent with the form of the problem faced by organisations.
4 Illustrative example and simulation study

4.1 Illustrative example

4.1.1 Background

During an elicitation exercise 15 design concerns and 14 reliability tasks are identified. This results in 16,384 possible combinations of tasks from which the programme manager must choose.

Each task has associated with it a cost of between 0 and 50 units and a duration of between 0 and 20 units. The target reliability is 0.8, the target time on test is 56 units, the maximum time on test is 84 units and the maximum total cost is 328 units.

In order to perform the analysis, the probabilities of each of the faults existing, $\lambda_i$, and the probabilities of finding the faults given that they do exist for each task, $p_{i,j}$, need to be elicited. We also require the reliability functions for the faults. We assume exponential reliability functions of the form

$$R_i(t) = \exp\left\{-\psi_i t\right\},$$

where $\psi_i$ is the rate of failures resulting from fault $i$. This can be elicited from an engineer by asking about the average number of failures of many similar items per unit time over a specified large period of time.

The final quantities which need to be elicited are the trade-off parameters for the binary utility functions and parameters for the conditional utility functions. We will investigate the sensitivity of the optimal allocation to the trade-off parameters in Section 4.1.3.

In this example, we simulate the $\lambda_i$ from a uniform distribution between 0 and 0.5, approximately 50% of the $p_{i,j}$ are equal to zero indicating that task $j$ will not find fault $i$ and the rest are simulated from Unif[0, 0.5] and each $\psi_i$ is chosen to be 0.02. The trade-off parameters are chosen to be $q_1 = 0.5, q_2 = 0.25, q_3 = 0.25$ and $r_1 = 0.5, r_2 = 0.5, r_3 = 0$. That is, we are bivariate risk seeking with respect to costs and bivariate risk neutral with respect to reliability and either financial or time costs.
4.1.2 Results

The expected utilities for the optimal design are 0.924, 0.758, 0.854 and 0.869 for the integer programming, extension, risk averse and loss averse approaches respectively. We see that the deterministic nature of the utility functions for the integer programming solution has resulted in a higher expected utility.

The optimal set of tasks for each approach is given in Table 1.

Table 1: The optimal set of tasks resulting from the four approaches.

<table>
<thead>
<tr>
<th>Task</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
<th>11</th>
<th>12</th>
<th>13</th>
<th>14</th>
</tr>
</thead>
<tbody>
<tr>
<td>Integer</td>
<td>×</td>
<td>×</td>
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<td>✓</td>
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<td>✓</td>
<td>×</td>
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<td>×</td>
<td>×</td>
<td>✓</td>
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<td>✓</td>
</tr>
<tr>
<td>Extended</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>×</td>
<td>×</td>
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<td>✓</td>
<td>✓</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Risk Averse</td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Loss Averse</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>×</td>
<td>✓</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
</tbody>
</table>

All four sets of utility functions offer similar optimal solutions, with the integer programming and risk averse approaches recommending performing 7 tasks and the extended and loss averse approaches 6. The integer programming approach offers an optimal allocation most different to the other three approaches. The extended and loss averse approaches give the same optimal set of tasks and only differ from the risk averse approach in whether to perform task 3.

We can also calculate the expected reliabilities, the costs and the times on test under each of the optimal solutions. The expected reliabilities are 0.837, 0.831, 0.865 and 0.831, the costs are 99.50, 118.98, 121.59 and 118.98 and the times on test are 33.48, 22.58, 31.43 and 22.58 for the integer programming, extended, risk averse and loss averse approaches respectively.

We see the integer programming approach has minimised costs subject to the other two constraints whereas the extended and loss averse approaches have increased the cost slightly in order to reduce the time on test. The risk and loss averse approaches have found a solution which has higher expected reliability than the other approaches, while sacrificing cost compared to the loss averse and extended approaches and time on test to the integer programming approach.

We can compare the expected utilities for each possible combination of tasks for all four approaches over the range of expected reliability. This is given in Figure 8.
We see the differences between the integer programming (and extended) and risk and loss averse approaches. As expected reliability increases then expected utility decreases for the integer programming and extended approaches as we have not yet reached the target reliability and costs are increasing. In the risk and loss averse approaches increasing expected reliability can increase the expected utility if the increases in costs and time on test are small.

We can also consider the trade-offs between the different attributes in order to help engineers in their decision making. Trade-offs between the attributes can be represented using isoquants [6] in which we hold utility and one of the attributes constant and plot the curve of values for the other two attributes which lead to that utility value. These are given for the loss averse approach in Figure 9. Those for the risk averse approach show a similar pattern.

In all three cases the expected utility is held constant at 0.7. We see that as costs and time on test increase, then we need to increase reliability to maintain the same utility. Interestingly, the higher the cost or time on test, the more we have to increase reliability to maintain the utility value. In contrast, as time on test increases, costs need to be decreased at a faster rate to hold the utility constant.

### 4.1.3 Sensitivity to trade-off parameters

We investigate the sensitivity of the optimal solution for the loss averse approach to the specification of the trade-off parameters in the utility function. To do so we vary $q_1, q_2, q_3$ and see how this affects the expected utility of the optimal solution, tasks (3, 4, 5, 6, 7, 8, 10, 13, 14). We also investigate how large a change in the trade-off parameters it would take for this solution to no longer be optimal. This indicates the robustness of the solution to specification of the trade-off parameters.

Figure 10 gives plots of the expected utility of the optimal solution when we vary the values of $q_1$ (left), $q_2$ (middle) and $q_3$ (right) and keep the other two parameters equal to each other. In each, subsequent points which are the same symbol indicate that the optimal solution has remained the same whereas a change in the symbols of points indicates that the optimal solution has changed.

We see from the plots that the optimal allocation of tasks is relatively sensitive to changes in $q_1$ and $q_2$ in comparison to $q_3$. If we consider the changes in $q_1$ the optimal solutions at each of the change-points are given in Table 2.
Figure 9: Isoquants (left to right) for cost against reliability, time on test against reliability and time on test against cost for the loss averse utility approach.

Figure 10: The expected utility of the optimal solution for varying values of trade-off parameters $q_1$ (left), $q_2$ (middle) and $q_3$ (right). A change in symbol indicates a change in the optimal allocation of tasks.

We see from the table that as the importance of the utility function for reliability is increased, it becomes more desirable to perform more tasks. The change in the optimal solution is fairly smooth: in all but a few cases once a task has been added to the optimal allocation it is not removed again but merely supplemented by further additional tasks at subsequent stages.
Table 2: The different optimal solutions as \( q_1 \) is increased and the other trade-off parameters are kept equal (\( q_2 = q_3 \)).

<table>
<thead>
<tr>
<th>Value of ( q_1 )</th>
<th>Task</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
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<th>9</th>
<th>10</th>
<th>11</th>
<th>12</th>
<th>13</th>
<th>14</th>
</tr>
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<tbody>
<tr>
<td>0.00</td>
<td></td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
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<td>×</td>
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<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
</tr>
<tr>
<td>0.05</td>
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<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
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<td>×</td>
<td>×</td>
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<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
<td>×</td>
</tr>
<tr>
<td>0.1, 0.15, 0.2</td>
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<td>×</td>
<td>×</td>
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<td>×</td>
<td>×</td>
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<td>×</td>
<td>✓</td>
<td>×</td>
<td>✓</td>
</tr>
<tr>
<td>0.25, 0.3</td>
<td></td>
<td>×</td>
<td>×</td>
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</tr>
<tr>
<td>0.5</td>
<td></td>
<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
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<td>×</td>
<td>×</td>
<td>✓</td>
<td>✓</td>
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</tr>
<tr>
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<td></td>
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<td>✓</td>
<td>×</td>
<td>×</td>
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</tr>
<tr>
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<td>✓</td>
<td>✓</td>
<td>×</td>
<td>×</td>
<td>×</td>
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<td>×</td>
<td>×</td>
<td>×</td>
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<td>0.8, 0.85</td>
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<tr>
<td>0.9, 0.95</td>
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<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
</tbody>
</table>

4.2 Simulation study

In this section we compare the impact of decision makers who are loss averse and risk averse with respect to reliability. Firstly we consider an illustrative example to assess the potential implications. Secondly we consider a simulation study to assess the propensity of such characteristics to result in disagreement.

4.2.1 Illustrative impact of loss versus risk aversion

Consider a design under development where ten concerns (A-J) have been identified, each with an associated probability of being a fault. In addition, ten reliability tasks (1-10) have been identified and, for each concern, the probability each task will expose the concern assuming it is a fault has been elicited. All elicited probabilities have been provided in Table 3. Table 4 provides the associated cost and duration of each activity. The programme manager is charged with identifying the optimal set of tasks with a target reliability of 0.7, target cost of 236.91 and target duration of 70.70. In this example, we compare the difference in optimal programmes between managers who are loss averse (LA) on reliability (where \( \gamma_{LA} = -0.9 \) in (3)) and risk averse (RA) on reliability (where \( \gamma_{RA} = 0.5 \) in (4)). Both are assumed to be multivariate risk neutral and their multi-attribute utility functions are expressed as in the following.

\[
U_{RA}(R, Y, \chi) = \frac{R}{4} (3 - R) + \frac{1}{4} \left[ 1 - \left( \frac{Y}{236.91} \right) \right]^2 + \frac{1}{4} \left[ 1 - \left( \frac{\chi}{70.70} \right) \right]^2,
\]

\[
U_{LA}(R, Y, \chi) = \frac{R^2}{20} (19 - 9R) + \frac{1}{4} \left[ 1 - \left( \frac{Y}{236.91} \right) \right]^2 + \frac{1}{4} \left[ 1 - \left( \frac{\chi}{70.70} \right) \right]^2.
\]

The RA manager chooses a more expensive programme, performing tasks (2, 3, 4, 9), that results in a higher expected reliability of 0.777, compared with the LA manager who performs tasks (3, 4, 9) which results in an expected reliability of 0.696, marginally below the 0.7 target. The additional activity chosen by the RA manager results in a 10% increase in project duration and a 50% increase in costs.

In Section 4.2.2 we consider a simulation exercise to obtain the likelihood of the RA manager and LA manager choosing the same programme more generally.
Table 3: Efficacy matrix showing the probability that each concern is a fault in the design and the probability that each task will reveal the concern assuming it is a fault.

<table>
<thead>
<tr>
<th>Concern</th>
<th>$\lambda_i$</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
</tr>
</thead>
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<td>0</td>
<td>0</td>
<td>0.52</td>
<td>0.09</td>
<td>0</td>
<td>0.55</td>
<td>0.46</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>B</td>
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<td>0.72</td>
<td>0</td>
<td>0.49</td>
<td>0.78</td>
<td>0</td>
<td>0.06</td>
<td>0.76</td>
<td>0</td>
<td>0.5</td>
<td>0.86</td>
</tr>
<tr>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0.65</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0.09</td>
<td>0.13</td>
<td>0</td>
</tr>
<tr>
<td>D</td>
<td>0.465</td>
<td>0.68</td>
<td>0.45</td>
<td>0</td>
<td>0.67</td>
<td>0.91</td>
<td>0.09</td>
<td>0.32</td>
<td>0.54</td>
<td>0.74</td>
<td>0.68</td>
</tr>
<tr>
<td>E</td>
<td>0.035</td>
<td>0.13</td>
<td>0.68</td>
<td>0.72</td>
<td>0.21</td>
<td>0.61</td>
<td>0</td>
<td>0.26</td>
<td>0.84</td>
<td>0.63</td>
<td>0</td>
</tr>
<tr>
<td>F</td>
<td>0.246</td>
<td>0</td>
<td>0.38</td>
<td>0.99</td>
<td>0</td>
<td>0.35</td>
<td>0.44</td>
<td>0.11</td>
<td>0</td>
<td>0.04</td>
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<td>0</td>
<td>0.3</td>
<td>0</td>
<td>0.56</td>
<td>0</td>
<td>0.19</td>
<td>0.98</td>
<td>0.08</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>H</td>
<td>0.011</td>
<td>0.61</td>
<td>0</td>
<td>0.44</td>
<td>0.4</td>
<td>0.95</td>
<td>0</td>
<td>0.48</td>
<td>0.9</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>I</td>
<td>0.037</td>
<td>0.87</td>
<td>0.28</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0.18</td>
<td>0.51</td>
<td>0.37</td>
<td>0.89</td>
<td>0.54</td>
</tr>
<tr>
<td>J</td>
<td>0.449</td>
<td>0</td>
<td>0.89</td>
<td>0.55</td>
<td>0.01</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0.98</td>
<td>0.53</td>
<td>0.01</td>
</tr>
</tbody>
</table>

Table 4: Task data on costs and duration.

<table>
<thead>
<tr>
<th>Task</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>5.49</td>
<td>41.67</td>
<td>26.93</td>
<td>49.32</td>
<td>22.95</td>
<td>26.92</td>
<td>46.00</td>
<td>48.63</td>
<td>5.92</td>
<td>42.05</td>
</tr>
<tr>
<td>Duration</td>
<td>5.75</td>
<td>1.57</td>
<td>10.23</td>
<td>2.21</td>
<td>1.99</td>
<td>15.19</td>
<td>18.60</td>
<td>19.04</td>
<td>3.47</td>
<td>16.22</td>
</tr>
</tbody>
</table>

4.2.2 Simulation results

We have theoretical results on when the optimal allocations of tasks will coincide for risk averse and loss averse decision makers based on their conditional utilities for reliability. In this section we consider the effect of MRA, MRN and MRS preferences of the decision maker on the optimal allocation and the relationship between this and the choice of risk or loss averse preferences marginally.

We consider 3 different decision makers, one of whom is MRA, one who is MRN and one who is MRS. Using Proposition 4, suitable representative trade-off parameters are chosen for these individuals. In practice, these would be elicited from the decision maker. We consider the effect of risk averse versus loss averse preferences of each of these decision makers over the conditional utilities. We also consider the effect of the decision which is in the power of the engineering manager: that of how high to specify the target reliability $R_0$ of the product. We vary the target reliability between a low, medium and high level. All of the parameter values used in the simulation are given in Table 5.

Table 5: Parameter values used for the simulation into the effects of different multi-attribute risk preferences.

<table>
<thead>
<tr>
<th>Risk Preference</th>
<th>$q_1$</th>
<th>$q_2$</th>
<th>$q_3$</th>
<th>$r_1$</th>
<th>$r_2$</th>
<th>$r_3$</th>
</tr>
</thead>
<tbody>
<tr>
<td>MRA</td>
<td>1/3</td>
<td>1/3</td>
<td>1/3</td>
<td>1/3</td>
<td>1/3</td>
<td>1/3</td>
</tr>
<tr>
<td>MRN</td>
<td>1/2</td>
<td>1/2</td>
<td>0</td>
<td>1/2</td>
<td>1/2</td>
<td>0</td>
</tr>
<tr>
<td>MRS</td>
<td>1/3</td>
<td>1/3</td>
<td>1/3</td>
<td>2/3</td>
<td>2/3</td>
<td>-1/3</td>
</tr>
<tr>
<td>$R_0$</td>
<td>0.5</td>
<td>0.7</td>
<td>0.9</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

In each case we consider a reliability growth programme with 10 potential faults in the product and 10 reliability tasks which could be undertaken. We find the optimal allocation for each type of decision maker and reliability target in 100 simulations and calculate the proportion of optimal allocations each decision maker and reliability target combination has in common with each of the other combinations. This is then repeated 10 times in order to ensure the robustness of the simulation results.

The results from a single set of 100 simulations are given in Figure 4.2.2. The scale on the right hand side of each sub-plot indicates the proportion of simulations in which two combinations of decision maker and reliability target share a common optimal allocation of reliability tasks.
The proportion of simulations which share the same optimal allocation for the different types of decision maker and reliability target. The sizes of the dots indicate the proportions, with larger dots indicating larger proportions.

We see that for MRA, MRN and MRS decision makers, whether they are risk averse or loss averse conditionally will have more of an effect on the final allocation of reliability growth tasks if the reliability target is lower. This is an important message, as it means for lower reliability products it will be necessary for engineers to be more careful about stating their preferences if they wish to obtain a suitable allocation of tasks. This has managerial implications, as for higher reliability products the reliability target can be set independently of the allocation of reliability tasks, whereas for lower reliability products the two decisions will need to be made in tandem. We also see a reasonable overlap in the optimal allocations of reliability tasks resulting from the MRA and MRN decision makers. Whether the decision maker is MRS or not (either MRA or MRN) does have a strong impact on the optimal allocation of reliability tasks.

The greater agreement between loss averse and risk averse decision makers for MRN where $q_3$ is 0 can be explained through Propositions 1 and 2. From Proposition 1, lower $q_3$ results in greater importance on reliability bringing the loss averse and risk averse decision makers closer together on how they rank programmes as trading between costs becomes less important. From Proposition 2, lower values of $q_3$ make programmes more attractive, increasing utilities and decreasing their differences.

It is important to check the robustness of the simulation results. In Table 6 we give the mean proportions of shared optimal allocations of reliability tasks for the combinations of type of decision maker and reliability target and their standard deviations over the multiple runs of the 100 simulations.

We see that the results of the different simulations are all fairly similar with means around the values give in Figure 4.2.2 and small standard deviations. This indicates that the results of the simulations are robust. The impact on the optimal allocation as we switch from risk aversion to loss aversion is not significantly different for MRA, MRN and MRS decision makers. The impact on the optimal allocation as we switch from risk aversion to loss aversion increases with increasing...
Table 6: Table showing the mean proportions of optimal task allocations that different combinations of decision maker and reliability target have in common over multiple simulation runs. Also given are the standard deviations in brackets.

<table>
<thead>
<tr>
<th></th>
<th>MRA RA</th>
<th>MRN RA</th>
<th>MRS RA</th>
<th>MRA LA</th>
<th>MRN LA</th>
<th>MRS LA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low Target Reliability</td>
<td>1.00(0.00)</td>
<td>0.82(0.05)</td>
<td>0.42(0.06)</td>
<td>0.98(0.01)</td>
<td>0.84(0.05)</td>
<td>0.44(0.06)</td>
</tr>
<tr>
<td>Medium Target Reliability</td>
<td>1.00(0.00)</td>
<td>0.81(0.03)</td>
<td>0.43(0.04)</td>
<td>0.79(0.01)</td>
<td>0.92(0.03)</td>
<td>0.57(0.06)</td>
</tr>
<tr>
<td>High Target Reliability</td>
<td>0.92(0.02)</td>
<td>0.78(0.04)</td>
<td>0.76(0.03)</td>
<td>0.79(0.02)</td>
<td>0.77(0.04)</td>
<td>0.78(0.02)</td>
</tr>
</tbody>
</table>

A summary of the simulation is provided in Table 7, where we see that switching between managers who are RA and LA with respect to reliability results in greater disagreement as we lower the target reliability. This is not surprising, as the higher a reliability target is, the less choice exists for programme managers.

Table 7: Proportion of simulations where a RA manager agreed with a LA manager, showing that agreement is higher for high reliability targets and MRN multiattribute preferences.

<table>
<thead>
<tr>
<th></th>
<th>MRA</th>
<th>MRN</th>
<th>MRS</th>
</tr>
</thead>
<tbody>
<tr>
<td>High reliability</td>
<td>0.98</td>
<td>0.97</td>
<td>0.97</td>
</tr>
<tr>
<td>Medium reliability</td>
<td>0.82</td>
<td>0.86</td>
<td>0.81</td>
</tr>
<tr>
<td>Low reliability</td>
<td>0.79</td>
<td>0.81</td>
<td>0.76</td>
</tr>
</tbody>
</table>

Moreover, we can observe that agreement is higher for MRN managers for medium reliability targets compared with MRA and MRS. As we lower reliability targets, there are more options from which to choose and a MRS manager will seek a portfolio that is strong in one attribute. As such, we see least agreement in this case. MRA managers are willing to sacrifice more for a balance between criteria and, as such, transforming the conditional utility of reliability from RA to LA provokes more disagreement.
4.3 Implications

There are important implications resulting from the analyses in Section 4. In particular, we have seen that

1. The use of smooth utility functions to represent a decision maker’s preferences can give additional sensitivity around targets compared to constraint based methods. By considering risk averse and loss averse utilities we do not discount potentially attractive solutions close to targets.

2. In a multi-attribute utility approach, the optimal solution to the decision problem can be sensitive to the preference behaviour of the decision maker over multiple attributes simultaneously. It is important for the analyst to elicit preferences over multiple attributes to come to a decision which is representative of the decision maker’s preferences.

3. The reliability target for high reliability products does not have an effect on whether there are different optimal allocations resulting from the different preference behaviours of the decision maker. From a managerial point of view, the reliability target can be set independently from the decision problem. For medium and low reliability products this is not the case.

5 Summary

We have investigated a Bayesian approach to the allocation of reliability tasks during product development. The optimal solution maximised the prior expectation of a utility function which represented the decision maker’s preferences over expected reliability, cost and time on test. To evaluate the expected reliability we utilised a reliability growth model which was developed with engineers in the aerospace industry. Suitable utility functions were identified using two approaches, a risk averse approach and a loss averse approach. The forms of these utility functions were consistent with observed preference of individuals in experiments.

The reliability growth model explicitly considers the process of reliability development undertaken by engineers. It is not seen as a black box approach and has advantages over other approaches in terms of buy-in. The Bayesian approach to the decision problem offers solutions which explicitly trade-off between the different attributes relevant to engineers and offers greater flexibility and sensitivity over integer programming, and other, approaches.

The utility functions developed display attractive properties but more work is needed in developing flexible utility functions. The elicitation of utility functions in general, and trade-off parameters in utility hierarchies in particular, require more investigation in the literature.

In practice, not only the optimal allocation but also the optimal sequencing of tasks is important and, while the methods in this paper can reduce a large space of possible reliability tasks down to a much smaller space, it would be interesting to consider the use of the approach to the sequencing of reliability tasks.

References


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Proof of Proposition 1

The utility function between reliability and costs is

\[ U(R, C') = q_1 U(R) + q_2 U(C') + q_3 U(R) U(C') \, . \]

If we differentiate it with respect to reliability,

\[
\frac{dU(R, C')}{dR} = (q_1 + q_4 U'(C')) U'(R) + (q_2 + q_3 U(R)) U'(C') \frac{dC'}{dR} = 0.
\]

The marginal rate of substitution is

\[ \text{MRS} = \frac{dC}{dR} = - \frac{U'(R)}{U'(C')} \frac{1 - q_2 - q_3 (1 - u(C'))}{q_2 + q_3 u(R)} . \]
Differentiating this with respect to \(q_3\),
\[
\frac{dMRS}{dq_3} = \frac{U'(R)}{U'(C)} \left( \frac{1 - U(C')}{q_2 + q_3 U(R)} + \frac{1 - q_2 - q_3(1 - U(C'))U(R)}{(q_2 + q_3 U(R))^2} \right)
\]
\[= \frac{U'(R)}{U'(C)(q_2 + q_3 U(R))} \left( (1 - q_2)U(R) + q_2(1 - U(C')) \right) < 0
\]
As the derivative of the marginal rate of substitution with respect to \(q_3\) is constant, the relationship is linear.

**Proof of Proposition 2**

To begin the proof,
\[U(C'(R)) = \frac{U_0 - q_1 U(R)}{1 - q_1 + q_3(U(R) - 1)}.\]
Differentiating this with respect to \(q_3\),
\[
\frac{dC'(R)}{dq_3} = \frac{U(R) - 1}{U'(C')} \left( U_0 - q_1 U(R) \right) \frac{1}{(1 - q_1 + q_3(U(R) - 1))^2} < 0
\]
As such, decreasing \(q_3\) increases the desirability of all programmes, improving the decision maker’s choice.

**Proof of Proposition 3**

*Proof.* We use proof by contradiction. Suppose a decision problem has three attributes with utility function \(U_a\), which can be further decomposed into \(U_{a,1}\), \(U_{a,2}\), and \(U_b\). Further suppose that the overall utility function is of the form of the MUIH
\[U = p_a U_a + p_b U_b,\]
\[U_a = q_1 u_{a,1} + q_2 u_{a,2} + q_3 u_{a,1} u_{a,2},\]
for constants \(p_a, p_b, q_1, q_2, q_3 \neq 0\). Then the utility function is given by
\[U = p_a q_1 u_{a,1} + p_a q_2 u_{a,2} + p_b q_3 u_{a,1} u_{a,2} + p_b U_b.\]
(5)
If the attributes in the MUIH are utility independent then this utility function must take either the additive or multiplicative forms. The additive form implies that all sub-combinations of utilities are additive and so is not suitable in this case. Consider the multiplicative form. This implies that, for constants \(c_{a,1}, c_{a,2}\) and \(c_b\),
\[1 + kU = (1 + kc_{a,1} U_{a,1})(1 + kc_{a,2} U_{a,2})(1 + kc_b U_b),\]
which can be expressed as
\[U = c_{a,1} + c_{a,2} U_{a,2} + c_{a,1} c_{a,2} U_{a,1} U_{a,2} + kc_{a,1} c_b U_{a,1} U_b + kc_{a,2} c_b U_{a,2} U_b + k^2 c_{a,1} c_{a,2} c_b U_{a,1} U_{a,2} U_b.\]
In order to be consistent with (5), we require \(c_{a,1} = p_a q_1\), \(c_{a,2} = p_a q_2\) and \(c_b = p_b\). Further, each of the cross terms involving \(U_b\) must have coefficient of zero. For example, we require
\[kc_{a,1} c_b = 0 \Rightarrow kp_a q_1 p_b = 0.\]
This implies that \(k = 0\). However this cannot be the case as we also require \(kc_{a,1} c_{a,2} \neq 0\). Thus the MUIH in (5) does not represent a multiplicative utility function. 
\[
\square
\]
Proof of Proposition 4

Proof. All conditional utility functions are twice differentiable and assumed to be on \([0,1]\) without loss of generality. We could define \(V(Y) = -U(Y), V(\chi) = -V(\chi)\) to ensure positive first derivatives and change signs in the binary utility functions but this does not affect the proof. Consider the cost utility \(U(C)\). Its cross derivative is

\[
\frac{\partial^2 U(C)}{\partial Y \partial \chi} = q_3 U'(Y)U'(\chi).
\]

Since \(U'(Y) > 0, U'(\chi) > 0\) for all \(Y, \chi > 0\), then using Theorem 1 in [29] this implies that we are BRS if \(q_3 > 0\), BRN if \(q_3 = 0\) and BRA if \(q_3 < 0\).

Let us now consider attributes \(R, Y\). The cross derivative is

\[
\frac{\partial^2 U(R, C)}{\partial R \partial Y} = r_3 U'(R)[q_1 U'(Y) + q_3 U'(Y)U'(\chi)].
\]

We know that \(U'(R) > 0, U'(Y) < 0, U(\chi) > 0, q_1 > 0\). We are therefore BRS for \(q_3 > 0\) if \(r_3 < 0\), if \(q_3 = 0\) we are BRA if either \(q_3 < -q_1/U(\chi), r_3 > 0\) or \(q_3 > -q_1/U(\chi), r_3 < 0\) and we are BRN for \(q_3 = 0\) if \(r_3 = 0\).

If we consider the final pair of attributes \(R, \chi\), the relevant cross derivative is

\[
\frac{\partial^2 U(R, C)}{\partial R \partial \chi} = r_3 U'(R)[q_2 U'(\chi) + q_3 U(\chi)U'(\chi)].
\]

We see that we obtain BRS and BRN preferences under the conditions outlined previously. This completes the proof for MRN and MRS solutions.

BRA solutions result for \(q_3 < -q_2/U(Y), r_3 < 0\) and \(q_3 > -q_2/U(Y), r_3 > 0\). Combining the conditions for MRA we have two candidates; \(r_3 < 0, q_3 < m\) and \(r_3 > 0, m < q_3 < 0\), where

\[
m = \min\{-q_1/U(\chi), -q_2/U(Y)\},
\]

\[
m = \max\{-q_1/U(\chi), -q_2/U(Y)\},
\]

for all \(\chi, Y\). In the first case there is no solution as when \(\chi \to \chi_0\) and \(Y \to Y_0\) then \(m \to -\infty\). In the second case as \(Y \to 0\) and \(\chi \to 0\) then \(U(Y) \to 1\) and \(U(\chi) \to 1\) giving the result.

Proof of Proposition 5

Proof. We want to know the restrictions on \(\gamma_{LA}\) such that \(\frac{dU_{LA}(R)}{dR} \geq 0\) for \(R \in [0,1]\). We have \(U_{LA}(R) = \gamma_{LA} R^3 + (1 - \gamma_{LA}) R^2\) and so

\[
\frac{dU_{LA}(R)}{dR} = 3\gamma_{LA} R^2 + 2(1 - \gamma_{LA}) R = R(3\gamma_{LA} R + 2(1 - \gamma_{LA})).
\]

For \(\frac{dU_{LA}(R)}{dR} \geq 0\) we require \(3\gamma_{LA} R + 2(1 - \gamma_{LA}) \geq 0\) for \(R \in [0,1]\). Assume \(\gamma_{LA} < 0\) and then \(2 - \gamma_{LA} \leq 3\gamma_{LA} R + 2(1 - \gamma_{LA}) \leq 2(1 - \gamma_{LA})\). We require \(3\gamma_{LA} R + 2(1 - \gamma_{LA}) \geq 0\). Therefore \(\gamma_{LA} \geq -2\). Assume \(\gamma_{LA} > 0\) and then \(2(1 - \gamma_{LA}) \leq 3\gamma_{LA} R + 2(1 - \gamma_{LA}) \leq 2 - \gamma_{LA}\). We require \(3\gamma_{LA} R + 2(1 - \gamma_{LA}) \geq 0\). Therefore \(\gamma_{LA} \leq 1\). From the monotonicity requirement we have the following, \(-2 \leq \gamma_{LA} \leq 1\), which implies \(-2 \leq \frac{1}{1 - 3R_0} \leq 1\). This solves for \(R_0 = 0\) or \(R_0 \geq \frac{1}{2}\). 

\]
Proof of Proposition 6

Proof. Assuming two alternatives with the same first moment implies \( E[R_1] = E[R_2] \). If alternative 1 is preferred to alternative 2 then the following is true for the risk averse decision maker,

\[
E[-\gamma_RA R_1^2 + (\gamma_RA + 1)R_1] > E[-\gamma_RA R_2^2 + (\gamma_RA + 1)R_2],
\]

which implies \( E[R_1^2] < E[R_2^2] \). As the means are the same we have \( \text{Var}[R_1] < \text{Var}[R_2] \). If alternative 1 is preferred to alternative 2 then the following is true for the loss averse decision maker,

\[
E[\gamma_LA R_1^3 + (1 + \gamma_LA)R_1^2] > E[\gamma_LA R_2^3 + (1 + \gamma_LA)R_2^2].
\]

This implies the following

\[
\gamma_LA(E[R_1^3] - E[R_2^3]) > (1 - \gamma_LA)(\text{Var}[R_2] - \text{Var}[R_1]).
\]

Setting \( \gamma_LA < 0 \) gives the result.

Proof of Corollary 1

Proof. For the utility function to be loss averse about the target \( R_0 \) we require \( \gamma_LA = \frac{1}{1 - 3R_0} \). Substituting this into Proposition 6 gives the result.