Determinants and Consequences of Poor Decisions in Health Insurance

Motivation

Health insurance market:
- Sub-optimal decision provision in the market: price not reflecting actual risk to assure equal access, one fit for all?
- Choice provisions increase surplus by better matching heterogeneous preference
- Ineffective decision making impair the policy motivation.

In this paper, we
- evaluate choice optimality;
- explore the decision patterns in the market: is there a certain pattern for decision quality?

Optimal Plan Choice

Expected Utility Model

Rank-Dependent Utility

Cumulative Prospect Theory

Implications:
- Risk appetite does not matter.
- Risk is crucial for choice optimality.

Policy Takeaway

1. Giving consumers choice in coverage has modest impacts on sorting high versus low-risk averse consumers.
2. Instead, its primary effect is redistribution
   - Sick consumers pay more, healthy consumers pay less, relative to a single plan choice.
   - Less sophisticated consumers make mistakes, which is an indirect subsidy to sophisticated/educated/ high-income consumers.

Conclusion

Finding 1: Dominated plans are selected by large population of consumers.

Finding 2: Inequality in choice quality: less sophisticated consumers make mistakes, which is an indirect subsidy to sophisticated/educated consumers.

Finding 3: Low-income individuals lose the most resulting from poor decision making.

Institutional Context

Swiss Health insurance market:
- Community rating;
- Individual mandate setting, no opt out option;
- Options: only differ in deductible level: coverage level, uniform covered service; premium difference for contracts fixed at 69 percent of the extra deductible level.

Data

National survey data
- Health care utilization
- Myriad socio-demographic data

Empirical Analysis

Overview of Deductible Choice

Consumers make mistakes if:
- High-cost consumers pick high deductible plan.
- They pick intermediate plan.
- Low-cost consumers pick low deductible plan.

Many People Pick Intermediate Plans

Findings:
- Consumers that makes subsidize those who don’t:
  - Less educated → more educated
  - Low-income → high income

Healthy People Select Low Deductible Plans

Findings:
- Low-income individual are over-insured compared to high-income individual.
- There is little difference in risk preference across two groups.

Most Related Literature
