

# Health Economics Forum

Canberra, 14 December 2011

## Comments on the four papers presented

Peter Zweifel

Economics Dept., University of Zurich (Switzerland)

[peter.zweifel@econ.uzh.ch](mailto:peter.zweifel@econ.uzh.ch)

# 1. Preventive Health No Cure

## Mark Harrison; Alex Robson

- Excellent emphasis on the fact that health does compete with other objectives in our lives
- Authors rightly point out that prevention is a *risky* investment
- It has a *certain* cost but an *uncertain* payoff because the probability of future ill health is only reduced, never eliminated
- Indeed, given full insurance coverage, zero prevention effort is optimal unless the individual is not interested in wealth only (Zweifel et al., 2009, ch. 6.4)



# 1. Preventive Health No Cure

## Mark Harrison; Alex Robson

- The authors drive home the fact that from an efficiency point of view, public intervention is only justified in the presence of *externalities*
- (Food for thought: What are the negative externalities of obesity?)
- They could have applied the „Marginal Cost (MC) equal to Marginal Benefit (MB)“ rule also to policy effort at internalizing a health externality
- MB of internalization is zero at 100% internalization by definition, while MC is  $> 0$  for sure
- Thus, full internalization is welfare-decreasing (even when it comes to health effects of ambient smoke)



## 2. Impacts of the Health Insurance Rebate and the Medicare Levy Surcharge

Alex Robson; Henry Ergas, Francesco Paolucci

- Very nice grounding in microeconomic theory (including insurance theory)
- The authors could have emphasized that the true price of insurance is not the premium but only the loading for administrative expense and profit
- They show that both a rebate and a levy *conditioned* on a minimum amount of private health insurance (PHI) coverage reduce the price elasticity of demand
- Yet this would be even more true without conditioning because the demand curve would shift out globally



## 2. Impacts of the Health Insurance Rebate and the Medicare Levy Surcharge

Alex Robson; Henry Ergas, Francesco Paolucci

- The case for subsidizing PHI depends on whether privately and publicly financed health care services are complements or substitutes
- If *complements*, a decrease in the net price thanks to PHI coverage induces more demand for Medicare-financed services as well: PHI should be *taxed!*
- If *substitutes*, there is a case for a rebate and/or tax relief for purchasers of PHI
- Recent U.S. evidence by Hsu et al. (2006, NEJM) and Chandra et al. (2010, AER) does point to substitution, creating 'fiscal externalities'



# 3. Removing Duplication in Public/Private Health Insurance

Jim Butler; F. Paolucci, Wynand van de Ven

- The authors review the arguments proffered in favor of subsidizing the purchase of PHI
- Justifiably, they find them unconvincing in the presence of a comprehensive public scheme
- They might have emphasized the one exception – relief of the public purse as a positive externality
- The condition is that *substitution* prevails (see above)
- The authors show that it takes ,opting out for good‘ to make PHI-financed and Medicare-financed health care services ,true‘ *substitutes*



# 3. Removing Duplication in Public/Private Health Insurance

Jim Butler; F. Paolucci, Wynand van de Ven

- They convincingly argue that risk-rated premiums combined with subsidies would re-establish the „price equal (expected) MC“ rule
- The whole machinery of risk adjustment could be done away with
- But why introduce premium bands?
- True, a few individuals will pay extremely high premiums, cashing in extremely high subsidies
- However, these individuals also would burden Medicare most so provide the most relief through purchasing PHI



# 4. Introducing Risk Equalization into the Health Australian Health Insurance Market

Francesco Paolucci; Amir Shmueli

- The authors have great merit in showing how a risk equalization (RE) scheme could be constructed for Australia using published data only
- They note that the RE formula needs to reflect insurers' risk selection behavior
- However, finding a favorable risk / dumping an unfavorable risk is a (risky) investment
- Therefore, basing RE on annual (let alone quarterly) data will not suffice to neutralize insurers' risk selection incentives (Beck et al. 2010, JHE)



# 4. Introducing Risk Equalization into the Health Australian Health Insurance Market

Francesco Paolucci; Amir Shmueli

- Also, payments into/from the RE scheme may be heavily influenced by the precise choice of formula (Schoder et al. 2010, IJEcBus)
- The most fundamental problem with RE, however, is that „it takes two to tango“
- A payment into RE is like an indirect tax on favorable risks: *Paid* by the insurer but *borne* at least in part by the consumer (as an extra loading)
- The single instrument ‚RE payment‘ cannot neutralize both the insurer’s and the consumer’s incentive to strike a ‚mutually beneficial‘ contract



# References (1)

- Beck, Konstantin; Trottmann, Maria; Zweifel, Peter (2010). Risk Adjustment in Health Insurance and its Long-term Effectiveness. *Journal of Health Economics* 29: 489-498.
- Chandra, Amitabh; Gruber, Jonathan; McKnight, Robin (2010). Patient Cost-sharing and Hospitalization Offsets in the Elderly. *American Economic Review* 100(1): 193–213.
- Eugster, Patrick; Sennhauser, Michèle; Zweifel, Peter (2010). Capping Risk Adjustment? *Journal of Health Economics* 29: 499-507.
- Hsu, John; Price, Mary; Huang, Jie; Brand, Richard; Fung, Vicki; Hui, Rita; Fireman, Bruce; Newhouse, Joseph P.; Selby, Joseph V. (2006). Unintended Consequences of Caps on Medicare Drug Benefits. *New England Journal of Medicine* 354: 2349–59.



## References (2)

- Schoder, Johannes; Sennhauser, Michèle; Zweifel, Peter (2010). Fine-Tuning of Health Insurance Regulation – Unhealthy Consequences for an Individual Insurer. *International Journal of the Economics of Business* 17(3), 313-327.
- Zweifel, Peter; Breyer, Friedrich; Kifmann, Mathias (2009). *Health Economics*, 2<sup>nd</sup> ed. Boston: Springer.

