Heath Insurance and Market Failures

These notes provide a brief summary of teh discussion on market failures in health insurance markets from Wednesday, September 24.

health insurance is subject to several types of market failure.

i. Relatively healthy people may choose no to buy health insurance which drives up premiums for less healthy people. This is an example of adverse selection.

ii. Having health insurance may incentivize more risky behavior. this is moral hazard.

iii. Providers must, by law, provide emergency treatment regardless of a patient's ability to pay. This may reduce the availability of treatment options. This is a negative externality.

In the United States, there are several providers of health insurance:

a. A large percentage receive health insurance through their employers. This system evolved beginning in the late 1920s and has become entrenched through laws and the tax code. One benefit is that it may reduce adverse selection. one cost is that it may reduce labor force mobility.

b. Medicare is health insurance for the vast majority of the 65+ population. In exchange for paying payroll taxes during their working years, they receive this entitlement. It is jointly funded and administered by states and Federal government.

c. Medicaid is heath insurance for low income households. Qualification requirements vary by state. It is jointly funded and administered by states and Federal government.

d. Others obtain insurance through the private market but unrelated to their employers. this includes many self-employed persons. Adverse selection is particularly prevalent in this part of the market and it drives much of the uninsured rate in the U.S.

In 2010, Congress enacted the Affordable care Act in an attempt tor educe the uninsured rate. The Act expanded eligibility for Medicaid. It also sought to improve the private market by creating health care exchanges that create pooled rates in an effort to reduce adverse selection. It also created subsides to buy private insurance. The act initially included an individual mandate to have health insurance, but this has since been repealed. Since passage, uninsured rates have fallen significantly.

Most developed economies use a single payer system instead of a multi-payer system like the U.S. In a single payer system, the government is the sole provider of health insurance (not necessarily medical services). Instead of paying premiums, households pay higher taxes to fund the system. The basic economic rationale is argument that market failures in health insurance are too profound to be properly addressed by market mechanisms, such as the Affordable care Act.