



## TRANSITION GUIDE

### *Health Insurance, Second Edition*

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Rather than focus on the day-to-day operations of insurers, *Health Insurance* looks in from the outside and explains the role that private health insurance plays in the United States. Noted health economist Michael Morrissey presents a rigorous but intuitive examination of the issues raised by insurance and how the market and the government have dealt with these issues. His emphasis is on understanding the underlying problems from an economics perspective and then applying the empirical literature to provide insight into the impact and effectiveness of the solutions. As such, this book serves as a basis for understanding and predicting the effects of the Patient Protection and Affordable Care Act (ACA). This updated edition includes new chapters covering the ACA and the structure, conduct, and performance of the insurance market. Additional resources in each chapter include recent research articles and classic insurance papers that give readers further information on each topic.

## Chapter Breakdown

Each chapter now contains two to four end-of-chapter references “for the interested reader.” These readings may be classic insurance papers or, more typically, are recent research papers that make significant contributions to the topics covered in the chapter.

### **Chapter 1 – History of Health Insurance in the United States**

The chapter adds new material on industrial sickness funds that pre-date the progressive era and provide better context for the lack of acceptance of compulsory insurance in the 1920s. A major new section discusses the political development of Medicare and Medicaid beginning with the Truman administration and concluding with the creation of the “three layer cake” of Wilber Mills. The end of the chapter contains an expanded discussion of consumer directed health plans.

### **Chapter 2 – A Summary of Insurance Coverage**

This chapter has been totally updated with the most current data on coverage. A new section on the effects of the “great recession” on coverage has also been added.

### **Chapter 3 – The Patient Protection and Affordable Care Act (PPACA)**

This entirely new chapter summarizes the major insurance components of the law: the individual mandate, the Medicaid expansion and Supreme Court decision, the penalties and subsidies for coverage, the exchanges, and the requirements for small and large employers. The revenue sources for

the law, new taxes and reductions in Medicare funding, are described as are the spending projections. The last CBO estimates before the vote on the legislation are used.

#### **Chapter 4 – The Demand for Insurance**

This chapter is essentially unchanged from the first edition.

#### **Chapter 5 – Adverse Selection**

This chapter is largely unchanged. However, new work on the favorable selection effects in Medicare Advantage plans and on adverse selection in employer-sponsored health insurance is now included. In addition, there is a brief concluding section suggesting the adverse selection issues inherent in the PPACA. This sets the stage for discussions in later chapters.

#### **Chapter 6 – Underwriting and Rate Making**

This chapter is largely unchanged. However, greater attention is paid to insurers administrative costs and the Medical Loss Ratio under the PPACA is introduced. Finally, after the discussion of self-insured plans, there is a discussion of the potential that some small employers may self-insure to avoid the premium implications of participating in the insurance exchanges.

#### **Chapter 7 – Risk Adjustment**

The substance of this chapter is unchanged. The relevant values used in the example of paying Medicare Advantage plans under the Hierarchical Condition Categories (HCCs) have been updated as has the review of the literature on the predictive power of risk adjustment. More importantly, the chapter now has new motivation relating to the requirement under PPACA that the insurance exchanges. A section on the effectiveness of the introduction of the HCCs on reducing favorable selection is now included.

#### **Chapter 8 – Moral Hazard and Prices**

This chapter has been expanded. The discussion of the effects of health insurance on health outcomes has been expanded and the dollar effects of various co-insurance, deductible and copay changes have been updated to 2013 terms. The discussion of copays and prescription drugs has been expanded to include new research. The concept of “value based insurance design” is also introduced with a brief discussion of the state of the empirical literature. The chapter concludes with discussions of recent challenges to the RAND Health Insurance Experiment and Finkelstein’s work exploring whether large scale expansions of insurance coverage, e.g., the introduction of Medicare, had effects consistent with the RAND experiment.

#### **Chapter 9 – Utilization Management**

The chapter is largely unchanged. However, there is now an expanded discussion of the effectiveness of disease management and intensive case management programs. A discussion of prevention services reducing health care utilization and spending has also been added.

#### **Chapter 10 – Selective Contracting**

This chapter continues to focus on managed care plans and hospitals but now includes selected materials on managed care plans and physicians that previously constituted a separate chapter. In addition to general updates the chapter now includes a discussion of Medicaid managed care. The chapter concludes with a discussion of “reference pricing” and “centers of excellence pricing” as new examples of selective contracting.

### **Chapter 11 – Managed Care Backlash, Provider Consolidation, and Monopsony Power**

This chapter has been substantially redesigned. It focuses on the consequences of the backlash and provider consolidation on selective contracting success. The discussion of hospital consolidation has been expanded and new research of the effects of actual hospital mergers on managed care prices is reviewed. New literature on the effects of physician market power and managed care contractual form is also presented. The chapter concludes with a discussion of the distinction between hospital monopoly power and insurer monopsony power. The discussion of “most favored nation clauses” has been moved to a new Chapter 12.

### **Chapter 12 – Insurance Market Structure, Conduct, and Performance**

This new chapter examines the nature of private insurance markets. It reports on the conversions of many Blue Cross and Blue Shield plans to for-profit status and examines the profitability of the largest health insurers. It then examines reports of the concentration of insurers in various segments of the market. This is followed by a review of the new research examining the effects of insurer concentration and of insurer mergers on premiums and provider prices. This is followed by the discussion of most favored nation clauses that was found in the first edition.

### **Chapter 13 – Premium Sensitivity for Health Insurance**

This chapter is much the same as in the first edition. The major change is the reworking and expansion of the evidence on the decision of workers to take-up coverage offered by an employer.

### **Chapter 14 – Compensating Differentials**

This chapter continues to provide a comprehensive overview of compensating differentials in employer-sponsored health insurance. The key new material focuses on the effects of obesity and smoking on money wages. This research argues that the mechanism for lower wages flows through higher health insurance claims and, therefore, a compensating wage differential.

### **Chapter 15 – Taxes and Employer-Sponsored Health Insurance**

Two new features have been added to this chapter. First, proposals to replace the current tax treatment of ESHI are considered and the simulation results presented. Second, the “Cadillac Tax” on ESHI required by the PPACA is discussed and the simulations of its effect are discussed. The chapter also includes updated tax tables and a re-written discussion of out-of-pocket premium contributions.

### **Chapter 16 – Employers as Agents**

Updated data on employee satisfaction with the wage-benefit tradeoff and new research on worker – employer matching is presented. New discussion of “defined contribution health insurance” analogous to defined contribution pension plans has been added.

### **Chapter 17 – Health Savings Accounts and Consumer-Directed Health Plans**

This chapter has been updated with recent data on enrollment. Significant new research on the effects of high deductible plans on health care spending is presented. The interplay of the PPACA and high deductible plans is discussed.

### **Chapter 18 – The Small-Group Market**

The chapter provides updated estimates of the size and nature of the small group market. Considerable attention is given to the effects that the PPACA is likely to have on this segment. The discussion of the role of managed care in this market has been reduced with expanded emphasis on the role of high deductible health plans. A new section on the roles of agents and brokers has been added.

### **Chapter 19 – The Individual Insurance Market**

This chapter has been updated to include discussions of the PPACA. It examines the availability of coverage for young adults under their parent's policy and the early effects of the medical loss ratio on the individual market. Extensive discussion of the exchanges is deferred to a new Chapter 22. A new section reviews new empirical work on the price sensitivity in the individual market. Another new section explores the effects of the availability of charity care on the purchase of individual coverage. The discussion of prices of individual coverage available through the internet has been fully updated.

### **Chapter 20 – Health Insurance Regulation**

Most of this chapter remains intact. Two major expansions deal with the new research examining the effects of specific insurance mandates on use of services, and the research on the effects that interstate competition would have on insurance coverage. This is presented here, because the effects are driven by differences in state level insurance regulation.

### **Chapter 21 – High-Risk Pools**

This chapter is largely unchanged although the data on coverage and premiums in selected state plans has been updated. Importantly, the details of the temporary "preexisting condition insurance plan" under the PPACA is discussed. The chapter remains in the text because high risk pools are often considered a key component of any non-PPACA reforms.

### **Chapter 22 – Health Insurance Exchanges**

This new chapter describes the health insurance exchanges in some detail. State vs. federal default exchanges are discussed in the context of their differential scope of activities and the number of states choosing each approach. The role and structure of the exchanges is presented along with the distribution of states taking each alternative approach. Governance options and the required functions of the exchanges are described. Essential health benefits and benchmark plans are discussed. The subsidies are described in some detail with examples of the size of such subsidies to eligible individuals and small firms. There is also a discussion of the implications for the exchanges if a state does not expand its Medicaid program. The risk adjustment and other mechanisms that the exchanges must use to account for adverse plan selection are discussed. Financing of the exchanges is discussed using cost and fee estimates for the Alabama exchange. Finally, the chapter presents simulation results on the number of people likely to be enrolled in the exchanges and the size of premiums that are likely to result from the underwriting provisions required by the PPACA.

### **Chapter 23 – An Overview of Medicare**

This chapter updates the deductibles, copays and premium contributions for Medicare from the first edition. It adds a discussion of higher Part B premiums for higher income seniors both as a matter of substance, but also to allow a discussion of potential future changes to Medicare. The discussion of Medicare Advantage plans has been moved to this chapter from the retiree coverage chapter as it seems a more natural home. The discussion of Medicare Part D has been expanded significantly. The implications of the PPACA on Medicare both in terms of changes to the program and tax law changes are discussed. A new section on the effects of Medicare on health spending and health status has been added. There is also a discussion of Medicare "premium support" as a reform alternative to traditional Medicare.

### **Chapter 24 – Retiree Coverage**

The descriptive data in this chapter have been updated and there is somewhat less attention devoted to employer sponsored retiree coverage. More attention is given to Medigap plans particularly focusing on the changes in the plans available for purchase.

### **Chapter 25 – Medicaid, Crowd-Out, and Long-Term Care Insurance**

The chapter devotes more attention to describing the Medicaid program and expands its discussion of the Children's Health Insurance Plans (CHIP). It introduces new research on the effects of premium contributions and copayments on children's use of services in these programs. The discussion of Medicaid managed care has also been expanded. A major new section examines the states' option to expand their Medicaid program under the PPACA. This section replaces the earlier discussion of the future of Medicaid.