UN3902: Economics of Public Policy Seminar
Week 5: Health

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Outline

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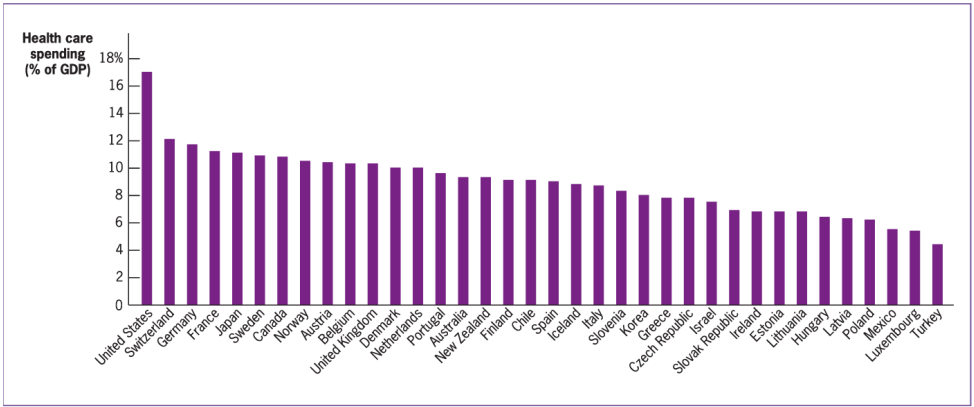
Health Improvements and Health Spending

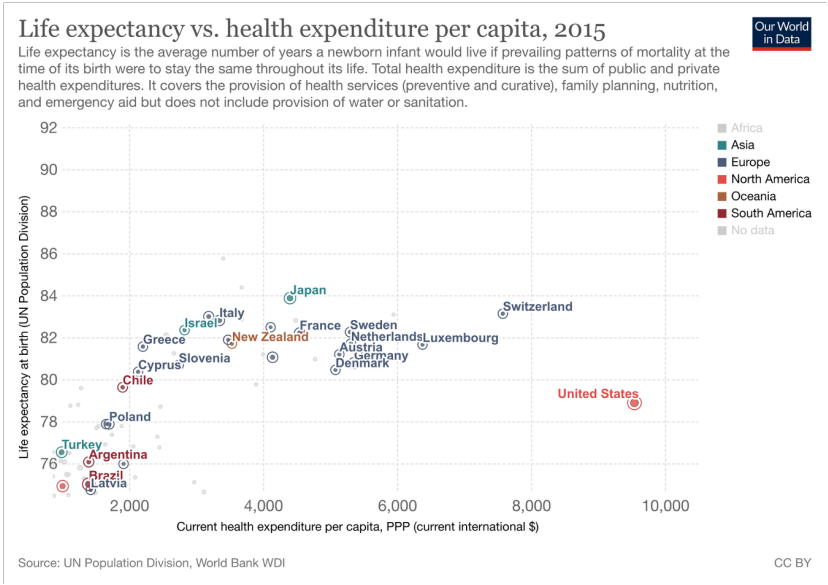
- Since 1950:
  - Medical technology has improved dramatically.
  - Heart attack mortality fell by 70%, infant mortality fell by 80%.
  - Health spending grew from 5 to 17% of GDP.
- Yet all is not well for the U.S. healthcare system.
  - There are huge disparities in medical outcomes.
  - The United States is the only major industrialized nation without universal access to health care.
  - The Affordable Care Act attempts to address the gaps in health care in the United States, but many are still without coverage.

Health Care Spending in the OECD Nations, 2019

- Health care spending is much higher in the United States than in the typical industrialized nation.

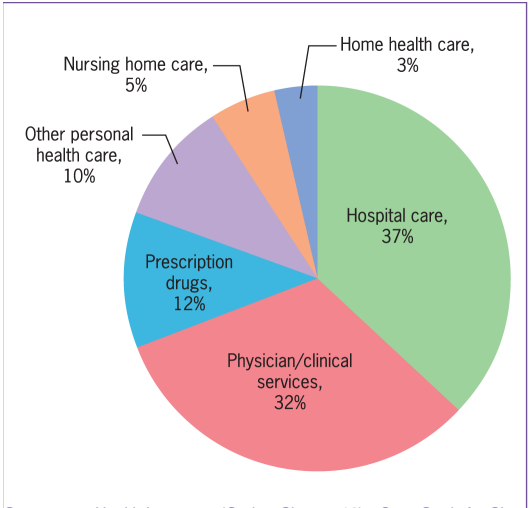


Health Spending and Health Outcomes



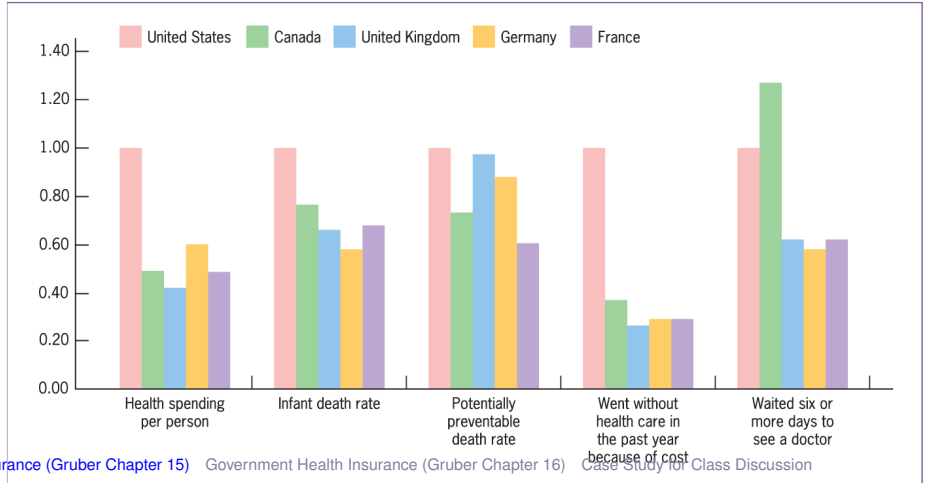
Distribution of Health Expenditures in the United States, 2019

- Together, hospital and physician spending accounted for almost two-thirds of all health care spending.



APPLICATION: Finding the Inefficiency in U.S. Health Care: U.S. Rankings in Health System Outcomes

- The United States is a major outlier in international terms when it comes to health care spending.

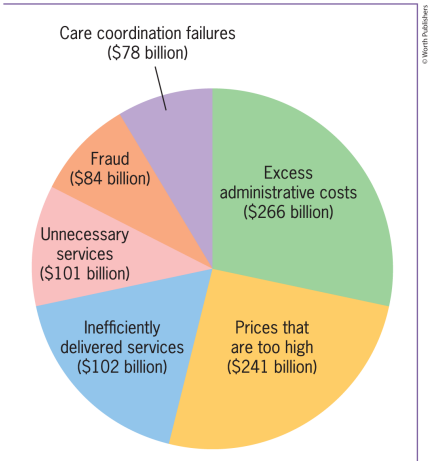


APPLICATION: Finding the Inefficiency in U.S. Health Care: Comparison to Other Countries

- The United States lags behind other countries internationally.
- The United States has the highest per-person health care costs of this set of countries.
- The United States has the highest rate of infant mortality.
- The United States has the highest rate of preventable death.
- The United States has the highest rate of going without care over the past year because of cost.

APPLICATION: Finding the Inefficiency in U.S. Health Care: Breakdown of Health Care Overspending

- The three largest sources of wasteful spending are high prices, excess administration costs, and unnecessary or inefficiently delivered services.

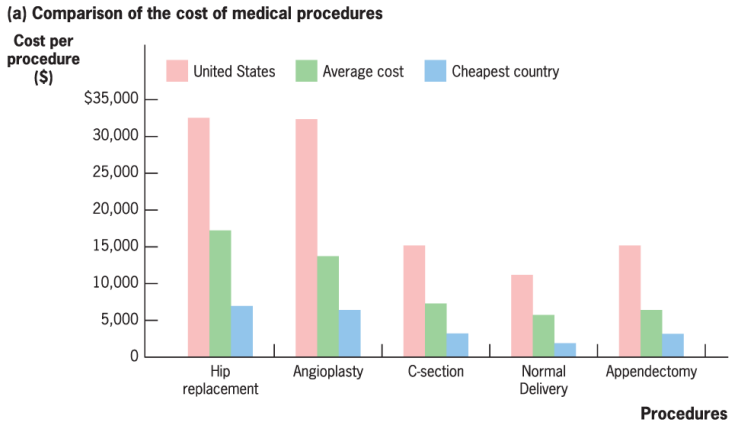


APPLICATION: Finding the Inefficiency in U.S. Health Care: Wasted Administrative Spending

- Arises primarily from the fragmented nature of our health care insurance and delivery system.
  - The administrative costs of private insurance in the United States average about 12%, considerably higher than other developed nations.
  - Health care providers that have different private and public owners and have to deal with multiple private and public health care payers spend a huge amount in billing and collecting payments.
  - A study by Himmelstein et al. (2014) found that hospitals spend 1.43% of GDP on administrative costs.

APPLICATION: Finding the Inefficiency in U.S. Health Care: High Prices

- The United States pays higher prices on average for services and drugs.



How Health Insurance Works: The Basics

- Individuals, or firms on their behalf, pay monthly premiums to insurance companies.
- In return, the insurance companies pay the providers of medical goods and services for most of the cost of goods and services used by the individual.
- There are three types of patient payments:
  1. Deductibles—limit to cost individual pays
  2. Copayment—fixed payment individual pays
  3. Coinsurance—percentage of each bill individual pays

Distribution of the U.S. Population Across Health Insurance Types

	People (millions)
Total population	**324.6**
Private	220.8
Employment-based	183.0
Direct purchase	33.2
Public	110.7
Medicare	58.8
Medicaid	55.9
Tricare/CHAMPVA	3.2
The uninsured	26.1
Data from: Keisler-Starkey and Bunch (2020), Table 1.	

Private Insurance

- In 2019, about 68.5% of the U.S. population had private health insurance.
- Private insurance is provided by employers and by the nongroup insurance market.
- Nongroup insurance market: The market through which individuals or families buy insurance directly rather than through a group, such as the workplace.

Why Employers Provide Private Insurance, Part I: Risk Pooling

- One reason employers provide insurance is to pool risks.
  - Risk pool: The group of individuals who enroll in an insurance plan.
- The goal of all insurers is to create large insurance pools with a predictable distribution of medical risk.
- The law of large numbers helps achieve this goal.
- By pooling all employees, employer-provided health insurance also avoids adverse selection.

Why Employers Provide Private Insurance, Part II: The Tax Subsidy

- Employers also provide insurance because it is subsidized.
- Tax subsidy to employer-provided health insurance: Workers are taxed on their wage compensation but not on compensation in the form of health insurance, leading to a subsidy to health insurance provided through employers.
- While Nigel's private insurance is cheaper, Khadija ends up with more income after taxes due to the subsidy to employer-provided insurance.

	Marginal Product, Wage	Employer Health Insurance Spending	Pre-Tax Wage	After Tax Tax Wage	Personal Health Health Spending	After-Tax, After-Health Insurance Income
Nigel	$30,000	0	$30,000	$20,000	$4,000	$16,000
Kim	$30,000	$5,000	$25,000	$16,666	0	$16,666

The Other Alternative: Nongroup Insurance

- The nongroup insurance market was traditionally not a well-functioning market.
- Nongroup insurance was not always available.
- Those in the worst health were often unable to obtain coverage (or obtain it only at an incredibly high price).
- A central feature of the ACA was an effort to reduce these barriers to the nongroup insurance market.
  - Banned pre-existing conditions exclusions and disallowed higher charges for less healthy enrollees.
  - Provided tax credits that subsidize the cost of insurance.

Medicare

- **Medicare:** A federal program that provides health insurance to all people over age 65 and disabled persons under age 65.
- Every citizen who has worked for 10 years in Medicare-covered employment (and their spouse) is eligible for Medicare at age 65.
- Medicare is financed by a payroll tax on employees and employers.

Medicaid

- **Medicaid**: A federal and state program that provides healthcare for the poor.
- Medicaid benefits are targeted at several groups:
  - Those who qualify for cash welfare programs
  - Most low-income children in the United States
  - Most low-income pregnant women
  - All very low-income families (in states that expanded the program to this group under ACA.)
  - The low-income elderly and disabled (for expenses not covered by Medicare).

The Uninsured

- Who are they?
- There are 26 million in the United States without any insurance coverage.
- The uninsured have low-than-average incomes.
- In 2019, nearly three quarters of the nonelderly uninsured came from families where one or more members were full-time workers.
- About 14.2% of the uninsured are children.

Why Are Individuals Uninsured?

- They may be counting on uncompensated care.
  - Uncompensated care: The costs of delivering health care for which providers are not reimbursed.
- Insurance may cost too much, given risks and prices.
- Insurers may be unwilling to insure the worst risks because of fears of adverse selection.
- They are not appropriately valuing insurance coverage.

Why Care About the Uninsured? 1

- There are several reasons to care about the uninsured.
- There are physical externalities associated with communicable diseases.
- There is a significant financial externality imposed by the uninsured on the insured.
- Care is not delivered appropriately to the uninsured.
- Paternalism and equity motivations.

Why Care About the Uninsured? 2

- A final reason for caring about the uninsured is that becoming uninsured is a concern for millions of individuals who currently have insurance.
  - Job lock: The unwillingness to move to a better job for fear of losing health insurance.
- Health insurance availability may inhibit productivity-increasing job switches.

Outline

How Generous Should Insurance Be to Patients?

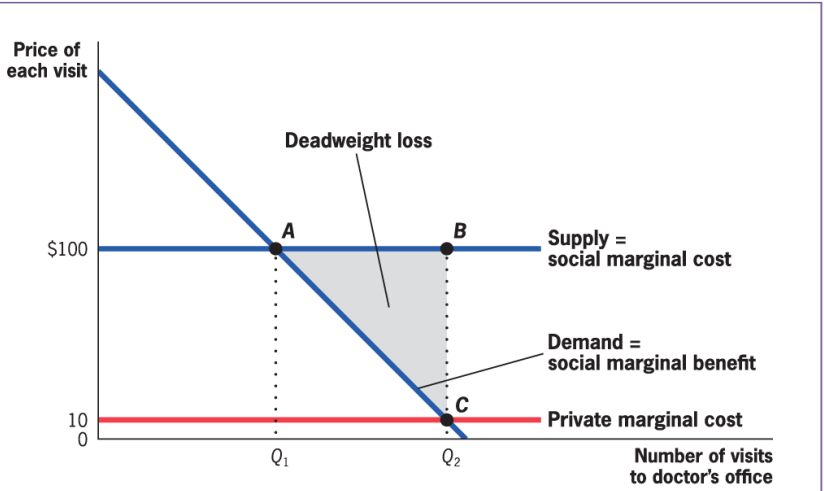
- The generosity of health insurance is measured along two dimensions:
  - Generosity to patients
  - Generosity to providers
- Most generous plans (to patients) provide first-dollar coverage.
  - First-dollar coverage: Insurance plans that cover all medical spending, with little or no patient payment.

Consumption-Smoothing Benefits of Health Insurance for Patients

- The consumption-smoothing benefit from first-dollar coverage of minor and predictable medical events is small for two reasons:
  - Risk-averse individuals gain little utility from insuring a small risk.
  - Individuals are much more able to self-insure such spending than to self-insure large and unpredictable medical events.
- On the other hand, the moral hazard costs are large.

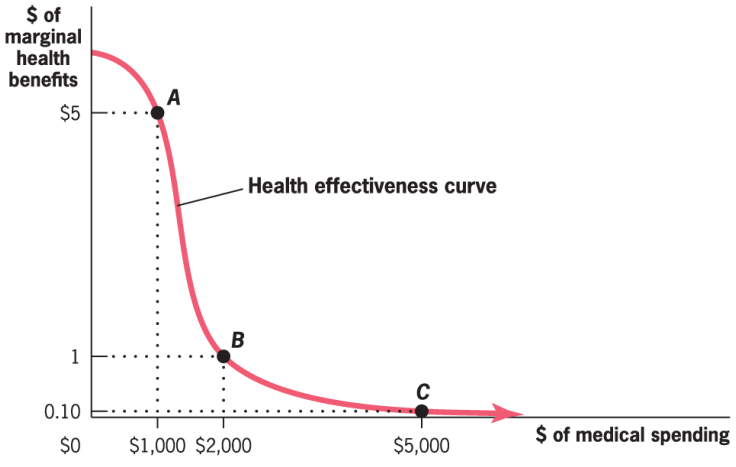
Moral Hazard Costs of Health Insurance for Patients

- Trade-off of health insurance: The gains in terms of consumption smoothing versus the costs in terms of overuse of medical care



The “Flat of the Curve”

- People should not get medical care beyond point B, the point at which each dollar of spending buys a dollar of improved health.

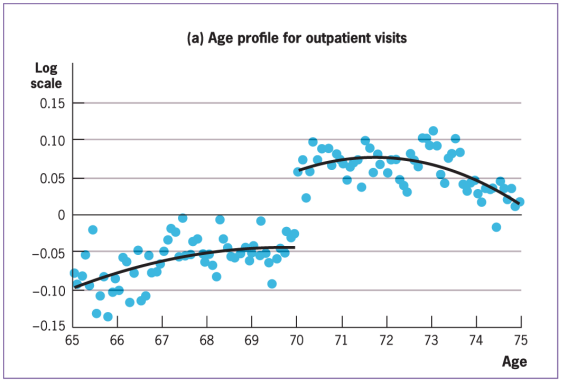


How Elastic Is the Demand for Medical Care? The RAND Health Insurance Experiment

- RAND Health Insurance Experiment (HIE): Evidence on the elasticity of health care demand
- Medical care demand is price sensitive: Free care plan used one-third more care than 95% coinsurance plan.
- Yet more generous plans did not improve health . . .
- except for low-income, chronically ill people.
- These findings largely supported by subsequent quasi-experimental studies.

EVIDENCE: Estimating the Elasticity of Demand for Medical Care

- In Japan, copayments drop dramatically at age 70.
- As the graphs show, this corresponds to a jump in the number of visits to the doctor and hospital admissions.
- Despite this, there is no measurable effect on patient mortality, confirming the “flat of the curve” conclusion from the HIE.



Optimal Health Insurance

- Optimal health insurance:
- Trades off moral hazard against risk protection.
- First-dollar coverage bad for moral hazard, not very valuable risk protection.
- Therefore, optimal health insurance policy:
  - Individuals bear a large share of medical costs within some affordable range.
  - Fully insured only against very large costs.

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Introduction: The Patient Protection and Affordable Care Act

- Fundamental reform of the U.S. health care system has been a constant source of political debate for much of the past century. In 2010, President Barack Obama signed into law a sweeping overhaul of the U.S. health care system.

Introduction: The Patient Protection and Affordable Care Act

- The Patient Protection and Affordable Care Act (ACA) made five fundamental changes to the U.S. health care system.

1. It banned insurers from denying coverage because of pre-existing conditions.
2. It banned insurers from charging different prices to different people based on their health.
3. It mandated all U.S. residents be covered by health insurance.
4. It required the federal government extensively subsidize health insurance coverage for the poor.
5. It took a variety of actions to lower health care costs.

Introduction: The Patient Protection and Affordable Care Act

- This legislation was highly controversial and passed through Congress with a very slim margin in a strictly partisan vote (no Republicans voted for it).
- The right worried that the law would lead to restricted patient choice and a bloated government bureaucracy.
- Those on the left believed that this proposal represented a retreat from the government-run single-payer system that might more efficiently expand coverage and control costs.
  - Single-payer system: A health care system in which all health insurance is provided and paid for by the government.
- President Trump and the Republican Congress were unable to repeal the ACA but took a set of legislative and regulatory actions have significantly weakened the law's impact.

Health Care Reform and the ACA

- There has been an historical impasse over national health insurance.
- Some argue for a single-payer system.
  - Government-provided health insurance for all.
  - Guarantees full coverage.
  - Low administrative costs.
  - Eliminates inequality in care.
  - Straightforward to control costs by budgeting.

Health Care Reform and the ACA

- Public system also has disadvantages:
  - Dramatically increases government expenditures.
  - Budgeting is a blunt instrument.
    - May not allow doctors to use a technology that is worth its high cost.
  - Severe political hurdles from health insurance companies.
- Others push for a private-sector solution, possibly with subsidies.
  - Adverse selection, other market failures remain.
  - No evidence that the private sector can contain costs.

The Massachusetts Experiment with Incremental Universalism

- In 2006, Massachusetts pushed to cover remaining 9% without insurance.
- "Three-legged-stool" approach:
  - Ban pre-existing conditions exclusion, health-based pricing.
  - Individual mandate, avoiding adverse selection.
    - Mandate: A legal requirement for employers to offer insurance or for individuals to obtain some type of insurance coverage.
  - Subsidized/free insurance for low-income families.

The Massachusetts Experiment with Incremental Universalism

- Striking results:
  - Massachusetts uninsurance rate 3%, compared to 18% nationally.
  - Half of the increase in coverage from Medicaid or government subsidized plans.
  - Premiums in the nongroup market have fallen by half relative to national trends.
  - Costs of the reform roughly consistent with projections.
  - Some studies have found the policy has improved health of population.

The Affordable Care Act

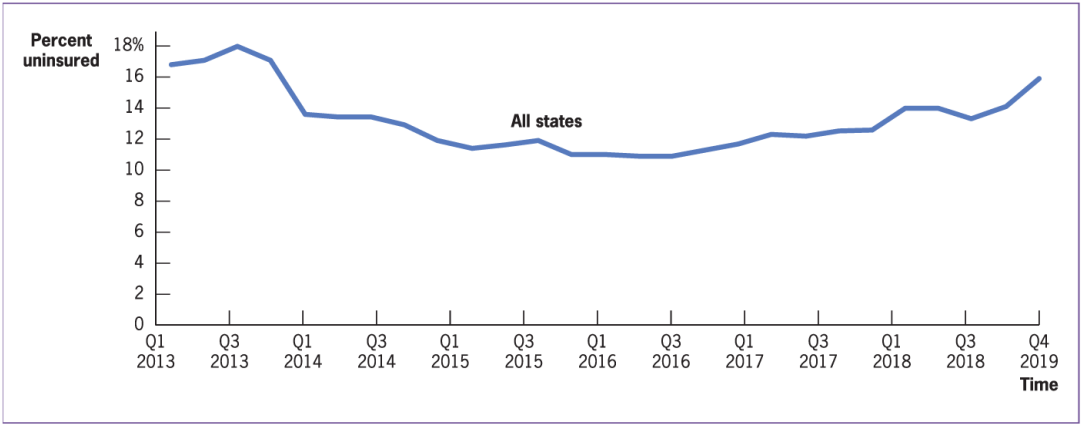
- In 2010, President Obama signed into law the Affordable Care Act, based on the Massachusetts health reform.
- Adopts the “three-legged stool” of Massachusetts:
  - Prices are community rated, not health specific.
  - Individuals are mandated to buy insurance.
  - Medicaid expanded, with subsidies for lower-income people.
- Expected to cost $1 trillion over the next decade.
- Includes substantial efforts to control costs.

Early Evidence on the Effects of the ACA

- Projecting the impacts of a reform as large as the ACA is difficult, but the CBO has attempted to do so, most recently in CBO (2014).
- They projected that these reforms will lead to 26 million newly insured residents by 2019.
- The CBO also projected that the spending cuts and revenue increases in the ACA will more than offset the new spending under the ACA so that the law will reduce the deficit by more than $100 billion over the first decade and more than $1 trillion over the next.

Trends in Uninsurance for Adults Ages 18 to 64

- Uninsurance rates among the states declined precipitously from 2014 through 2016 before rising again in 2017.



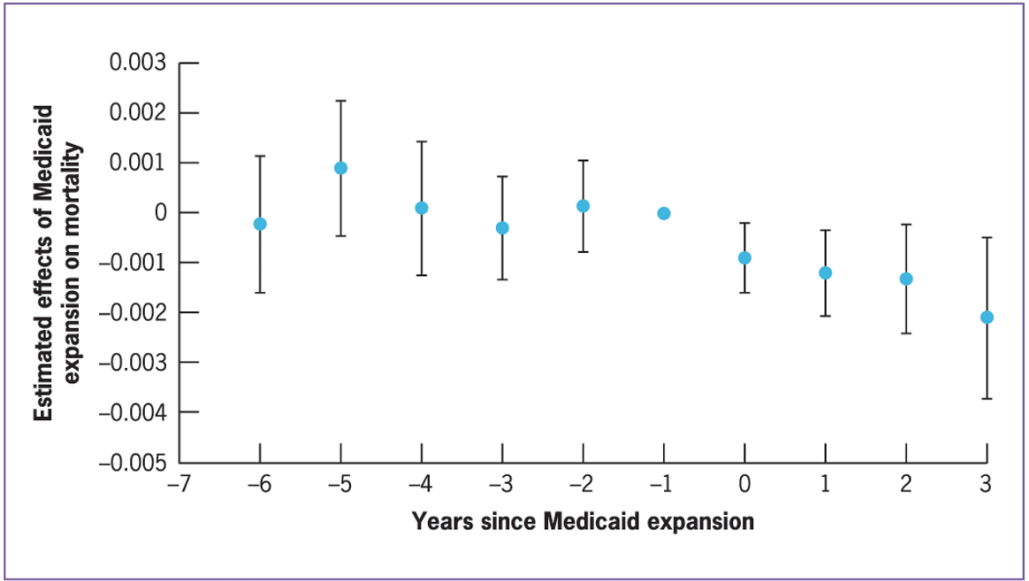
Projected Impacts of the ACA and Early Evidence on Its Effects

- Early evidence on the effects of the ACA appears to support the contentions of the CBO analysis.
- The number of uninsured in the United States has fallen by about 20 million, with the uninsurance rate declining by more than one-third.
- Other studies suggest that this coverage has also improved access to care and self-reported health, decreased emergency room use, and increased use of preventive care.
- Cost growth since the passage of the ACA has been historically low, at a rate of 1.4% in 2013.

Evidence on the Impact of ACA on Mortality

- Recent paper by Miller, Johnson & Wherry (2020) studies impact of Medicaid expansions on mortality of Americans aged 55–64.
- Exploit differences in timing of Medicaid expansions in different states to identify the effect of the expansions on mortality.
- Pursue a dynamic difference-in-differences design, comparing changes in mortality in expansion states to changes in mortality in not-yet-expansion states, before and after the expansions.

Evidence on the Impact of ACA on Mortality



The ACA Runs Into Trouble

- Public support for the ACA was below 50% both before and after passage and remained below 50% even as the law was enacted and the coverage gains took place.
  - This unpopularity was a significant factor in major Republican gains in the 2016 election.
- The ACA's partial reform structure created more opponents than supporters.
  - Many of the benefits were through expanded Medicaid and other mechanisms not directly linked by voters to "Obamacare."
- The Trump administration and Congress took actions that significantly weakened the ACA.
  - Foremost of these actions is the repeal of the individual mandate.

Conclusion

- The ACA held the potential to address many shortcomings in our health insurance system, greatly reducing the ranks of the uninsured.
- Evidence from past insurance expansions suggests that this will provide a cost-effective means of improving health.
- The law failed to achieve widespread popularity and was significantly scaled back by President Trump and Congress.
- Further reform is needed to control costs.

Outline

Case Study for Class Discussion

- In Jan 2026, expanded tax subsidies for health insurance under ACA expired, leading to a large increase in the cost of insurance for millions of Americans.
- Read up on this.
  - https://www.nytimes.com/2026/01/30/upshot/obamacare-subsidies-financial-cliff.html?smid=url-share
  - https://www.cbpp.org/research/health/health-insurance-premium-spikes-imminent-as-tax-credit-enhancements-set-to-e
  - https://www.urban.org/research/publication/48-million-people-will-lose-coverage-2026-if-enhanced-premium-tax-credits
  - https://www.cbpp.org/blog/how-to-evaluate-proposals-to-address-expiring-premium-tax-credit-enhancement
- let's use this google doc to plan an evaluation together! https://docs.google.com/document/d/1UC5z4sPzOZTeC4wy4aErScUNNLexrcniVdQw-1ZkrB0/edit?usp=sharing