

Insurance Exchanges and Adverse Selection

What Is Insurance?

- Insurance = Financial Risk Management.
- Designed for risks that are infrequent, expensive, and unpredictable, in which case, risk pooling is primary means of risk management.
- What if risk is predictable?
- Adverse selection “death spiral”
- Underwriting counters adverse selection, but
 - adds substantial administrative cost, and
 - undermines the whole purpose of health care.
- Competition among plans
 - Adds substantial administrative costs, and
 - Amplifies incentives to avoid the sick and deny care.
- Risk adjustment also would add substantial administrative cost.

PPACA – Insurance Exchanges

- Exchanges are intended to regulate and stabilize individual and small group insurance markets, but bring many problems:
 - Adverse Selection (will require risk adjustment)
 - Achieving “critical mass” to succeed
 - Making competition work
 - Offering choice among plans without complexity
 - Administrative costs (have added 4% in MA)
 - Governance (accountability)
 - Lack cost controls
 - Not viable without individual mandate

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