THE HAMILTON PROJECT

Advancing Opportunity, Prosperity, and Growth

**NEW PAPERS ON INNOVATION IN THE HEALTH CARE SECTOR**

*For Release on October 7, 2015*

Looking past the Affordable Care Act debates on expanding health insurance coverage and incorporating cost-effective approaches to delivering health care services, there are enduring policy challenges around consumer decision-making, medical innovation and the affordability of new technologies, and the structure of the health care market—in particular, the hospital sector. The Hamilton Project has commissioned three papers from some of the nation's leading health care economists working at the intersection of health care economics, industrial organization, and behavioral economics. These papers' innovative and forward-looking proposals move the policy conversation forward in exciting, productive directions.

**Getting the Most from Marketplaces: Smart Policies on Health Insurance Choice**
*Authors:* Ben Handel (University of California, Berkeley) and Jonathan Kolstad (University of California, Berkeley)

Health insurance coverage is at the heart of health care delivery in the United States and a core component of the recently passed Affordable Care Act's (ACA) efforts to change health care access and delivery. Consumers in state-based health exchanges, Medicare Part D, Medicare Advantage, and employer exchanges typically shop from a large set of insurance options with complex and varying features. These features—both financial and non-financial—are crucial determinants of the quality and quantity of health-care services that consumers receive as well as the extent to which insurance contracts protect consumers from financial risk. The recent literature on choice in health insurance markets documents that consumers face substantial difficulties in weighing these features, and as a result often make poor individual decisions given the available options. These choice frictions have important implications for (i) positive market outcomes, (ii) the fiscal burden of health programs, and (iii) social welfare. This paper will discuss and propose policy solutions focused on decision support tools, active market management, and default policies.

**A Floor-and-Trade Proposal to Improve the Delivery of Charity-Care Services by U.S. Nonprofit Hospitals**
*Authors:* David Dranove (Northwestern, Kellogg), Craig Garthwaite (Northwestern, Kellogg), and Christopher Ody (Northwestern, Kellogg)

The vast majority of private hospitals in the United States are non-profit organizations. In exchange for this tax-preferred status, non-profit hospitals are expected to provide a "community benefit." Historically, this was defined as providing medical services without compensation, although the definition was expanded in 1969 to include other activities such as teaching or providing unprofitable services. The authors note that the supply of and demand for charity care are not well-aligned geographically. Non-profit hospitals in high-income areas tend to receive the largest tax benefits, but hospitals in the poorest communities face the largest demand for such care. To address this mismatch, the authors propose that charity care be quantified and assigned a tradable credit through a "floor and trade" system similar to the cap and trade approach to air pollutants. States will specify a minimum floor amount for hospitals' charity-care provisions, and will allow hospitals to trade credits for providing care. This system will allow hospitals that receive a large number of uninsured patients to receive compensation for these patients from other non-profit hospitals where the provision of charity care is much lower. The design of the system will provide incentives for hospitals to provide services that might not be profit maximizing but contribute to social welfare.

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**Correcting Signals for Innovation in Health Care**

*Authors:* Nicholas Bagley (University of Michigan), Amitabh Chandra (Harvard University), and Austin Frakt (Department of Veterans Affairs)

Technology adoption accounts for 30 to 50 percent of health-care spending growth. A central challenge to getting the most out of health-care spending is encouraging more high-value innovation and less low-value innovation that pushes up costs but results in meager health benefits. The structure of insurance plans is a key determinant of medical technology developers' incentives to innovate, but that structure does not currently promote high-value innovation. The authors propose three policy reforms that move the system away from encouraging inefficient innovation without requiring drastic regulatory changes: in particular, eliminating the tax subsidy for health insurance for high-paid employees by replacing the tax exclusion with a tax credit, reforming Medicare's coverage determination process, and introducing reference pricing for certain therapies.