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The Moral Hazard Effects of Consumer Responses to Targeted Cost-Sharing

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Abstract

This paper examines the effects of the reference pricing program implemented by the California Public Employees Retirement System (CalPERS) in 2012. The program uses targeted cost-sharing to incentivize patient price shopping. We find that the program leads to a 10.3% increase in the use of low-price providers and reduces the average cost per procedure by 12.5%. We further estimate that the program reduces price-margin medical spending by $218.8 per procedure, which we estimate is approximately 53.7% of the excessive spending that is due to patient choice of higher price providers caused by insurance coverage, at the expense of a $94.3 (or 12.5%) reduction in consumer surplus. The cost savings from the reference pricing program is about two to three times as large as the reduction from implementing a high-deductible health plan while the accompanying consumer surplus reduction is much smaller under reference pricing. (JEL codes I11, and I13)

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