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Information and consumer choice: The value of publicized health plan ratings

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Abstract

We use data on the enrollment decisions of federal annuitants to estimate the influence of publicized ratings on health plan choice. We focus on the impact of ratings disseminated by the National Committee for Quality Assurance (NCQA), and use our estimates to calculate the value of the information. Our approach exploits a novel feature of the data—the availability of nonpublic plan ratings—to correct for a source of bias that is inherent in studies of consumer responsiveness to information on product quality: since publicized ratings are correlated with other quality signals known to consumers (but unobserved by researchers), the estimated influence of ratings is likely to be overstated. We control for this bias by comparing the estimated impact of publicized ratings to the estimated impact of ratings that were never disclosed. The results indicate that NCQA's plan ratings had a meaningful influence on individuals' choices, particularly for individuals choosing a plan for the first time. Although we estimate that a very small fraction of individual decisions were materially affected by the information, for those that were affected the implied utility gains are substantial.

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1. Introduction

Consumers often choose between products whose qualities or characteristics are ex ante uncertain. The reliability of a car, for example, cannot be fully known at the time of purchase, and the quality of a restaurant isn't known until after one has dined there. For some products, the presence of such uncertainty has given rise to markets for information: for example, companies like Edmunds and Consumer Reports publish automobile ratings, and publications like Zagat provide restaurant reviews. The profitability of such information enterprises indicates that the information is valuable—but exactly how valuable is it? In some cases, government or nonprofit consumer-interest agencies have assumed the role of information provider. Does the information benefit consumers enough to warrant the costs of its acquisition and dissemination?

In this paper, we attempt to answer these questions in the context of employee health plan decisions. For employees choosing from a menu of health plan options, how valuable are publicized plan ratings in making the decision? The National Committee for Quality Assurance (NCQA), an independent nonprofit agency that serves as a “watchdog for the managed care industry”, collects and actively disseminates information about health insurance plans. The ratings and statistics are used by large employers to inform their employees about plans, and for a period of time in the late 1990's summaries of the ratings were published in a major national news magazine, *U.S. News & World Report*. Using enrollment data for a large sample of U.S. government annuitants, we measure the impact of the health plan ratings on individuals' choices, and use our estimates to calculate the value (to consumers) of the information.

This study is not the first to analyze consumer responses to health plan quality information. Wedig and Tai-Seale (2002) examine data on federal employees in 1995 and 1996, when health plan report cards were first provided, and report evidence that plan ratings significantly influenced individuals' decisions. Beaulieu (2002) examined the health plan choices of Harvard University employees and found that the provision of quality information in 1997 had a small but significant effect. Scanlon et al. (2002) use employee data from General Motors to study health plan decisions; they find that employees respond to overall quality indices but not to specific quality measures. Using the same dataset, Chernew et al. (2004) estimate the parameters of a Bayesian learning model, in which reported plan ratings cause individuals to update their prior beliefs about plan quality. Their findings confirm the positive value of information, but also suggest that much of the information in reported ratings was already known.

Relative to the previous literature, the key contribution of this paper lies in its ability to correct for an important source of bias in estimating the quantitative impact of publicized ratings. A fundamental challenge for this study and all its predecessors is that published information may be highly correlated with quality signals consumers can obtain through informal channels. In general, this correlation between observed product ratings and unobserved product quality will cause econometric estimates of the ratings' impact to be biased. In the present context, if health plan ratings simply mirror information about plan quality that was already known to consumers (but not the econometrician), then high market shares for plans with high ratings could be incorrectly interpreted as evidence that the ratings were influential. This is obviously a critical concern if one's objective is to determine the value

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