Bargaining in Markets with Exclusion: An Analysis of Health Insurance Networks

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Abstract

Health insurance companies regularly exclude certain hospitals from the network of hospitals their enrollees may visit. Many healthcare insiders argue that one reason insurance companies exclude hospitals is because exclusion provides leverage in contract negotiations with hospitals. This paper formalizes and explores the implications of that story.

Data from the Affordable Care Act exchanges in the market around Denver, Colorado, show 65 percent of consumers are enrolled in plans that exclude at least 40 percent of hospitals in the market. For those plans, consumers pay 10 percent lower premiums and insurers reimburse hospitals at 20 percent lower rates for the same services. To formalize this story, I incorporate exclusion into a bargaining model between many insurers and many hospitals. An important feature of this model is that exclusion is an equilibrium outcome; even though exclusion reduces consumers willingness-to-pay for the insurance plan, insurers make up for the lost revenue by paying lower negotiated prices to hospitals.

After estimating the model, in a counterfactual analysis, I find that laws that restrict the ability of insurers to exclude would increase the negotiated prices insurance companies pay by 15 percent. I contrast my model's counterfactual results with the standard model used in the insurer-hospital bargaining literature. The standard model has opposite signed counterfactual results, decreasing negotiated prices by 29 percent.

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