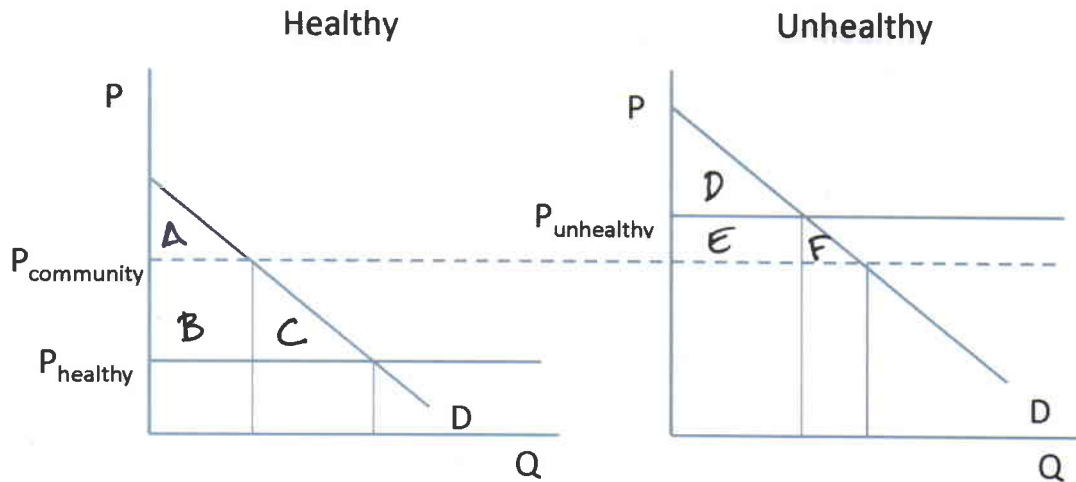


Name Solutions
Midterm 2

1. (20 points) Use the following graphs to show what happens to consumer surplus if a regulation is introduced which requires health insurance companies to charge the same premium to all customers. $P_{healthy}$ and $P_{unhealthy}$ represent the premium charged per customer under experience rated insurance, $P_{community}$ represents the premium charged per customer under community rated insurance, and Q represents the number of customers. List one benefit and one drawback of the community rating regulation. Overall, does it look like total consumer surplus is higher or lower under the community rating regulation?



	Experience Rated		Community Rated	
	Healthy	Unhealthy	Healthy	Unhealthy
CS:	A+B+C	D	A	D+E+F
D:	-B-C			+E+F

Benefit of CR: more unhealthy are insured b/c it is more affordable.
 Drawback of CR: many healthy people will go without insurance (adverse selection).

B/c B & C look bigger than E & F, it appears that consumer surplus is lower under CR.