Lessons Learned from Behavioral Finance: Implications for Consumerism in Health Care

EBRI Policy Forum

The Future of Employment-Based Health Benefits:
Will Employers Reach a Tipping Point?
December 6, 2007
Introduction

Questions:
- How Rational Are Human Employees?
- How Well Does Education Influence Better Decision Making?
- How Well Do Employer Incentives Work?
- How are Decisions Affected by Choices Offered?

Opportunities for Future Behavioral Research
How Rational Are Human Employees?

Inertia

Loss Aversion

Framing Effects

Cognitive Overload

Herding

Status Quo Bias

“Hello, Mum... the Doc wants to know if I have difficulty making decisions. What do you think?”
How Well Does Education Help?

Not very well….

Financial Education and 401(k) Savings

<table>
<thead>
<tr>
<th></th>
<th>Seminar Attendees</th>
<th>Non-Attendees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Planned Change</td>
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<tr>
<td>Actual Change</td>
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<tr>
<td>Actual Change</td>
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</tr>
<tr>
<td><strong>Non-Participants</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Enroll in 401(k) Plan</td>
<td>100%</td>
<td>14%</td>
</tr>
<tr>
<td><strong>Participants</strong></td>
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<td></td>
</tr>
<tr>
<td>Increase contribution rate</td>
<td>28%</td>
<td>8%</td>
</tr>
<tr>
<td>Change fund selection</td>
<td>47%</td>
<td>15%</td>
</tr>
<tr>
<td>Change asset allocation</td>
<td>36%</td>
<td>10%</td>
</tr>
</tbody>
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Source: Choi, Laibson, Madrian and Metrick
Employer contributions not a panacea

- 20% to 30% of non-highly compensated employees don’t respond to employer matching contributions
- In one study of seven companies, 54% of employees younger than 59 1/2 did not take full advantage of the match
- Research results are mixed on the impact of match threshold and rate on employee contribution rates

Generally, it’s the existence and level, not the rate that matters.
How are Decisions Affected by Choices Offered?

Status Quo Bias: The Tried and True

Too Much Information, More Choices
- Lower Satisfaction
- Less Action
- More Reliance on Simple Rules of Thumb

Simultaneous vs. Sequential Choices
Choice and Utility Not Perfectly Correlated

- The Menu at Charlie Trotter’s
  - Grand Menu ($115)
  - Vegetable Menu ($100)

- Yet, diners indicated it's their favorite restaurant (Zagat, 2001).
The Paradox of Choice

% Visiting  40%  60%
% Buying    30%   3%
More Choices, Less Participation

Figure 10
Number of Funds Offered and Predicted Participation Rates

Source: Iyengar, Jiang, and Huberman
Opportunities for Future Behavioral Research

How are plan design features influencing employee decision making?

How can behavioral interventions influence compliance?

How can framing techniques positively influence decision making?