Comentario para la XLVI Reunión Anual de la AAEP
“Collusion in a One-Period Insurance Market with Adverse Selection”
escrito por Alexander Alegría y Manuel Willington

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This paper contributes to the well-known literature dealing with the existence of equilibrium in competitive insurance markets under adverse selection (Rothschild and Stiglitz, 1976) by analyzing the case in which insurers face capacity constraints and a minimum premium constraint. The model presented features two types of consumers (high and low risk) who must buy insurance, and a number of homogeneous risk-neutral, capacity-constrained insurers subject to a regulation that imposes both a minimum premium and coverage.

The main finding here is that, under certain conditions, there exists a range of equilibria, most of which result in positive profits for all firms – profits that entry does not dissipate. The intuition is easiest to grasp by considering the case in which a deviating offer intends to attract both type of consumers (Inderst and Wambach, 2001): to obtain a profit on low-risk individuals, the offer must specify a higher coverage than the Rothschild-Stiglitz contract, but such an offer would be most attractive to high-risk types – given the expected level of congestion at the deviating firm, low risks will not apply for the offer, implying that the deviator would make a loss. The imposition of a minimum premium constrains further the kinds of deviations that would be considered and facilitates more collusive outcomes in which firms obtain positive profits.

I like the general idea of the paper of extending the analysis to consider the case of premium regulation, and find it original and compelling as a story that may not apply to all insurance markets, but to some, and may be practically very relevant in those cases. However, I also have some concerns and comments about the paper:

1. I disagree with the statement that “the standard R&S’s zero-profit separating equilibrium” is the “unique equilibrium” in Inderst and Wambach (2001). Their proposition clearly states that “there exists an equilibrium”, while the proof begins with “one possible equilibrium strategy of firms” (emphasis added). Moreover, in the Conclusion I&W claim that “the derived equilibrium is, however, not unique under capacity constraints” and refer to Peters (1984) for the case of complete information in which there exist “equilibria where firms make positive profits”. I am not fully cognizant of this literature, but may a more proper claim of the contribution of your paper be that you demonstrate the existence of multiple equilibria with positive profits under incomplete information?

2. Given that your main departure from I&W is the imposition of the minimum-premium constraint, I would suggest motivating better that assumption. This is done somewhat lightly in the paper, and I believe it deserves a more organized discussion.

3. In a related vein, the introduction of the Chilean antitrust case is promising, but it leaves one wanting a deeper discussion of how it relates to the assumptions or results in your paper. What are the policy recommendations or remedies that come out of your analysis? There is some of this in the concluding section (like the discussion of the role of the public insurer on page 27 – which should probably appear earlier in the paper), but I would have liked to see more discussion of these matters.
4. My first intuition about your results was that premium regulation acts as a coordinating device for firms, making it easier for them to sustain less-than-competitive outcomes in a setup in which premia are strategic complements. Whether right or wrong, I would have liked to see some of this discussion in the paper. Can we infer from your analysis that it would pay firms to invest in limiting capacity?

5. Doesn’t the mandatory insurance assumption amount to assumption A.1 (that the search cost is sufficiently low that no one chooses to stay uninsured) in I&W?

6. Expositional comments:
   a. Please number pages.
   b. The discussion of what you qualify as “collusion” in pages 5 and 6 can certainly be cut down.
   c. There are too many footnotes, many of which are too long.

References: