

CORE DISCUSSION PAPER
2006/5

**THE OPTIMALITY OF HOSPITAL FINANCING SYSTEM:
THE ROLE OF PHYSICIAN-MANAGER INTERACTIONS**

David CRAINICH¹, Hervé LELEU² and Ana MAULEON³

February 2006

Abstract

In a paper published by Ma (1994) it was argued that the prospective payment system in the hospital industry was superior to the cost based reimbursement system to achieve both cost reduction and quality improvement objectives. In the analysis, it was assumed that quality and costs decisions were made by a single agent. Our paper compares these two financing systems assuming that the main decisions taken within the hospital are shared between physicians (quality of treatment) and hospital managers (cost reduction). If Ma's conclusions hold in the US context (where the hospital managers bear the whole cost of treatment), we show that the ability of a prospective payment system to achieve both objectives is very depending of the type of interaction between the agents when physicians bear a part of the treatment cost as it is the case in many European countries. **Keywords:** hospital's financing system, strategic interaction, prospective payment system.

JEL Classification: H51, I18, D21.

¹CRESGE/LEM/FLSEG, Université catholique de Lille, France.
E-mail: dcrainich@cresge.fr

²CNRS and CORE, Université catholique de Louvain, Belgium and LEM, Université catholique de Lille, France. E-mail: leleu@core.ucl.ac.be

³FNRS and CEREC, Facultés Universitaires Saint-Louis and CORE, Université catholique de Louvain, Belgium. E-mail: mauleon@fusl.ac.be

This paper presents research results of the Belgian Program on Interuniversity Poles of Attraction initiated by the Belgian State, Prime Minister's Office, Science Policy Programming. The scientific responsibility is assumed by the authors.