

【長崎大学経済学部ディスカッション・ペーパー・シリーズ】

DISCUSSION PAPER SERIES

Faculty of Economics, Nagasaki University

No.2012-01 (Feb. 2012)

The Relationship between Moral Hazard and Insurance Fraud

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Abstract:

This research addresses an insurance market in which moral hazard and insurance fraud coexist. It yields several interesting results. First, the effort conducted by policyholders to lower accident probability is a weakly monotone decreasing function of the insurance firm's investment in preventing insurance fraud. Second, the insurance firm's investment in preventing insurance fraud depends on whether it wants to give an additional incentive to policyholder's effort in exchange for realizing the possibility of insurance fraud. Third, unlike in previous moral hazard models, policyholder chooses a strictly positive amount of effort even in the full insurance case.

Keywords: Moral hazard, Insurance fraud, Economic model