



**STATE OF NEW YORK
INSURANCE DEPARTMENT**
25 BEAVER STREET
NEW YORK, NEW YORK 10004

George E. Pataki
Governor

Howard Mills
Superintendent

**Circular Letter No. 8 (2006)
March 27, 2006**

TO: All Insurers Licensed to Write Accident and Health Insurance in New York State ("Commercial Insurers"), Article 43 Corporations, and Health Maintenance Organizations ("HMOs").

RE: Discretionary Clauses in Health Insurance Policies and Contracts including Disability Income Insurance

STATUTORY REFERENCE: Sections 3201 and 4308 of the Insurance Law

Discretionary clauses are contract provisions that grant a commercial insurer, Article 43 corporation or an HMO the unrestricted authority to determine eligibility for benefits and to interpret terms and provisions of the policy or contract. Examples of discretionary clauses are: "the company has full, exclusive, and discretionary authority to determine all questions arising in connection with the policy, including its interpretation", and "when making a benefit determination under the policy, the company has the discretionary authority to determine your eligibility for benefits and to interpret the terms and provisions of the policy."

Historically, such provisions were permitted as a recapitulation of the insurer's, Article 43 corporation's or HMO's rights subject to independent judicial review. However, the Department has re-examined whether the use of discretionary clauses in accident and health insurance policies and subscriber contracts complies with New York Insurance Law, in light of recent federal cases that have interpreted discretionary clauses under ERISA as constricting the ability of the courts to exercise de novo review of policy provisions contained in the insurance policy or contract. The courts apply an arbitrary and capricious standard, whereby the courts would be required to uphold the insurer's, Article 43 corporation's or HMO's claim decisions unless they were found to be "arbitrary and capricious". Such wide latitude in the insurer's, Article 43 corporation's or HMO's discretion serves to negate essential features of policies and contracts, as well as statutorily required appeal rights. As a result, policies and contracts may be rendered illusory by nullifying the insurer's, Article 43 corporation's or HMO's responsibility to pay.

The Department has determined that the use of discretionary clauses violates Sections 3201(c) and 4308(a) of the Insurance Law in that the provisions "encourage misrepresentation or are unjust, unfair, inequitable, misleading, deceptive, or contrary to law or to the public policy of this state." Additionally, the Department believes that the

use of discretionary clauses is an unfair or deceptive act or practice, within the meaning of Article 24 of the Insurance Law. Consequently, in accordance with Sections 3201 and 4308 of the Insurance Law, discretionary clause provisions in accident and health insurance policies and in subscriber contracts will no longer be approved by the Department.

Insurers, Article 43 corporations and HMOs must remove discretionary clauses from existing policies and contracts. Every insurer, Article 43 corporation and HMO shall, within 30 days of this letter, provide to Stephen L. Rings, at the address below, a statement of whether it has discretionary clause provisions in its policies or contracts, identify its policies and contracts that contain these provisions and set forth its plan for appropriate revision. If policies and contracts are not revised voluntarily, the Department may proceed under Section 3110 of the Insurance Law to withdraw approval of the policies and contracts identified as containing discretionary clause provisions and Article 24 of the Insurance Law to determine whether the use of discretionary clause provisions is a determined violation. Pursuant to Article 24, upon such a determination, the Superintendent may seek an injunction to enjoin the use of policy forms containing the provisions.

Any questions on this Circular Letter may be directed to:

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New York Insurance Department
One Commerce Plaza
Albany, New York 12257
(518) 474-4899

Or by e-mail to [Mr. Rings](mailto:Stephen.L.Rings@ins.state.ny.us)

Very truly yours,

Charles Rapacciuolo
Assistant Deputy Superintendent and
Chief, Health Bureau