



**STATE OF NEW YORK  
INSURANCE DEPARTMENT**  
ONE COMMERCE PLAZA  
ALBANY, NY 12257

George E. Pataki  
Governor

Howard Mills  
Superintendent

**Circular Letter No. 14 (2006)**  
**June 29, 2006**

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

**RE: Discretionary Clauses in Accident and Health (including Disability Income) Insurance Policies, Life Insurance Policies, Annuity Contracts and Subscriber Contracts.**

**STATUTORY REFERENCE: Sections 3201 and 4308 and Article 24 of the Insurance Law.**

This Circular Letter supersedes Circular Letter No. 8 (2006), Supplement 1 to Circular Letter No. 8 (2006), and Supplement 2 to Circular Letter No. 8 (2006), which are withdrawn, and sets forth the Department's position regarding the use of discretionary clauses in accident and health insurance policies, life insurance policies, annuity contracts and subscriber contracts.

Discretionary clauses are contract provisions that grant a commercial insurer, Article 43 corporation, HMO or administrator the unrestricted authority under an insurance policy, annuity contract or subscriber contract to determine eligibility for benefits and to interpret terms and provisions of the policy, contract or certificate. 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, these 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 insurance policies, annuity contracts and subscriber contracts complies with New York Insurance Law, in light of recent federal cases that have interpreted discretionary clauses under the federal Employee Retirement Income Security Act (ERISA) as constricting the ability of the courts to exercise *de novo* review of policy provisions contained in the insurance policy, contract or certificate. 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 the policies, contracts and certificates, as well as statutorily required appeal rights. As a result, policies, contracts and certificates may be rendered illusory by nullifying the insurer's, Article 43 corporation's or HMO's responsibility to pay.

The Superintendent may disapprove any accident and health insurance policy form, life insurance policy form, annuity contract form or subscriber contract if "the same contains any provision...which is likely to mislead the policyholder, contract holder or certificate holder." The Superintendent may disapprove any life insurance policy form, or any form of annuity contract or group annuity certificate, if "its issuance would be prejudicial to the interests of policyholders or members or it contains provisions which are unjust, unfair or inequitable." The Superintendent may disapprove any accident and health insurance policy forms, or subscriber contracts that "encourage misrepresentation or are unjust, unfair, inequitable, misleading, deceptive, or contrary to law or to the public policy of this state." See New York Insurance Law Sections 3201(c) and 4308(a). Additionally, pursuant to Article 24 of the Insurance Law, no person shall engage in this state in any unfair or deceptive act or trade practice. The Department believes that the use of discretionary clauses are contrary to Sections 3201(c) and 4308(a) and Article 24. Accordingly, the Department is drafting regulations that would prohibit the use of discretionary clauses in all new and existing accident and health insurance policies, life insurance policies, annuity contracts and subscriber contracts upon renewal, modification, alteration or amendment on or after the effective date of the regulation.

In the interim, in accordance with Sections 3201 and 4308 and Article 24 of the Insurance Law, the Department suggests that commercial insurers, Article 43 corporations and HMOs remove discretionary clauses from policies, contracts and certificates that are submitted for review and approval. Any policy, contract or certificate that is submitted containing a discretionary clause will be reviewed in accordance with the opinion expressed herein. Accordingly, any life insurance policy or annuity contract form containing a discretionary clause may not be submitted to the Department for approval under a certified procedure.

Any questions on discretionary clauses in accident and health policies may be directed to:

Stephen L. Rings  
Health Bureau  
New York Insurance Department  
One Commerce Plaza  
Albany, New York 12257  
(518) 474-4899

Or by e-mail to [Stephen L. Rings](mailto:Stephen.L.Rings)

Any questions on discretionary clauses in life insurance policies or annuity contracts may be directed to:

Kate Powers  
Life Bureau  
New York State Insurance Department  
One Commerce Plaza  
Albany, New York 12257  
(518) 474-4552

Or by e-mail to [Kate Powers](mailto:Kate.Powers)

Very truly yours,

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Charles Rapacciuolo  
Assistant Deputy Superintendent  
and Chief, Health Bureau

Jeffrey Angelo  
Assistant Deputy Superintendent  
and Chief, Life Bureau