

Department of Legislative Services
Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE
Revised

House Bill 1085 (Delegate Pena-Melnyk, *et al.*)

Health and Government Operations

Finance

Disability Insurance Policies - Discretionary Clauses - Prohibition

This bill prohibits insurers and nonprofit health service plans (carriers) from selling, delivering, or issuing a disability insurance policy that contains a clause that purports to reserve sole discretion to the carrier to interpret the terms of the policy, or to provide standards of interpretation or review that are inconsistent with the laws of the State.

The bill applies to disability insurance policies sold, delivered, issued, or renewed in the State on or after October 1, 2011.

Fiscal Summary

State Effect: Minimal special fund revenue increase for the Maryland Insurance Administration (MIA) in FY 2012 from the \$125 rate and form filing fee. The bill's requirements can be handled by MIA with existing budgeted resources.

Local Effect: Potential minimal increase in expenditures for disability insurance policies to the extent insurance companies pass on any additional costs in the form of higher insurance premiums.

Small Business Effect: Potential minimal increase in expenditures for disability insurance policies to the extent insurance companies pass on any additional costs in the form of higher insurance premiums.

Analysis

Current Law: Maryland law is silent on the use of discretionary clauses in disability policies (as well as life and health insurance policies).

Background: Discretionary clauses in insurance contracts generally give the insurance carrier full discretion to determine when insurance benefits are due.

As stated by the U.S. Supreme Court in *Firestone Tire v. Bruch* (1989), under the federal Employee Retirement Income Security Act of 1974 (ERISA), insureds who believe they have been wrongfully denied benefits may sue in federal court. The court determines the standard of review by checking for the presence of a discretionary clause. Such a clause might read: “Insurer has full discretion and authority to determine the benefits and amounts payable and to construe and interpret all terms and provisions of the plan.” If an insurance contract has a discretionary clause, the decisions of the insurance company are reviewed under an “abuse of discretion” standard. Absent a discretionary clause, review is *de novo*.

Under the *de novo* standard, a court may consider all available evidence and issue a decision based on its own judgment, which gives claimants a better chance of receiving the benefits in their policies. An “abuse of discretion” standard limits the court to only issuing a ruling different from the carrier’s decision if the carrier’s decision is found to have been unreasonable and an abuse of discretion.

The National Association of Insurance Commissioners (NAIC) has advocated prohibition of discretionary clauses in life, health, annuity, and disability insurance contracts by promulgating a model law, which has been adopted by several states. Other states have established regulatory rules and administrative authority to prohibit discretionary clauses. States that have restricted the use of discretionary clauses include California, Hawaii, Illinois, Indiana, Maine, Michigan, Minnesota, Montana, New Jersey, New York, Oregon, and Utah.

NAIC’s model law is intended to help ensure that health insurance benefits and disability-income protection coverage are contractually guaranteed and avoid the conflict of interest that occurs when the carrier responsible for providing benefits has discretionary authority to decide what benefits are due.

Additional Information

Prior Introductions: HB 236 of 2008, an MIA departmental bill which was similar to this bill, was heard by the House Health and Government Operations Committee but later withdrawn.

Cross File: None.

Information Source(s): Department of Health and Mental Hygiene, Maryland Insurance Administration, Department of Legislative Services

Fiscal Note History: First Reader - March 9, 2011
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Analysis by: Jennifer B. Chasse

Direct Inquiries to:
(410) 946-5510
(301) 970-5510