

BULLETIN 2002-7

DISCRETIONARY CLAUSES PROHIBITED

This bulletin publishes the department's position on discretionary clauses, also known as allocation of authority, interpretation of plan, or similar provisions in accident and health, life, and annuity insurance contracts.

Department Position

Discretionary clauses purport to give an insurer full and final discretion in interpreting benefits in an insurance contract. In the department's view, under Utah Code Annotated (U.C.A.) §31A-21-201(3), those clauses and provisions in accident and health, life, and annuity insurance contracts are inequitable, misleading, deceptive, obscure, unfair, not in the public interest, and otherwise contrary to law, and they encourage misrepresentation and violate a statute.

1. Discretionary clauses are inequitable and unfair because they attempt to give additional power to insurers who are already in a superior bargaining position. The insurer has control when drafting the terms of the contract, as well as industry knowledge and experience far superior to that of the typical individual or corporation seeking insurance coverage. Courts generally recognize that insureds and insurers are in unequal bargaining positions.
2. Discretionary clauses are misleading, deceptive, obscure, and not in the public interest, and they encourage misrepresentation because the clauses lead citizens to believe that the insurer has authority to give a binding and final interpretation of the contract and that they have no other legal recourse. Such language is intimidating and could discourage a policyholder from appealing a claim denial.
3. Discretionary clauses violate a statute because they appear to deprive Utah Courts of jurisdiction to interpret insurance contracts in violation of U.C.A. § 31A-21-314(2). Under U.C.A. § 31A-21-314(2), an insurance policy subject to Chapter 21 cannot contain a provision "depriving Utah courts of jurisdiction over an action against the insurer, except as provided in permissible arbitration provisions." A discretionary clause could have the effect of depriving Utah courts of jurisdiction over an action for determination of benefits.
4. Discretionary clauses are otherwise contrary to law because they attempt to usurp the judicial power to interpret insurance contracts granted by Utah case law.

The department recognizes the recent action of the ERISA Working Group of the Health Insurance (B) Committee of the National Association of Insurance Commissioners (NAIC).

The NAIC adopted a model act "PROHIBITION ON THE USE OF DISCRETIONARY CLAUSES". A primary purpose of the model act is to avoid the

conflict of interest that occurs when an accident and health insurance carrier responsible for providing benefits has unfettered authority to decide what benefits are due. It is the position of the department that policyholders and claimants of accident and health, life insurance policies and annuity contracts be protected from an insurer's potential conflict of interest.

Refiling of Forms

Utah is a "File and Use" state as to policy forms and places responsibility for compliance with the insurer. U.C.A. § 31A-21-201 Insurers are advised to review all accident and health, life, and annuity forms to assure compliance. If any policy contains a discretionary clause, allocation of authority, interpretation of plan or similar provision, then the policy does not comply with Utah law. When reviewing forms insurers are advised to refer to the appropriate Department content standard. If a form does not comply with the content standards, an endorsement should be filed and provided to all existing policyholders. Future filings must not contain such provisions. The content standards, rules and bulletins can be found on the department's website, www.insurance.utah.gov.

DATED this 29th day of July, 2002

MERWIN U. STEWART
Insurance Commissioner

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