Discretionary Clauses in ERISA Health and Disability Plans—Are They Still Viable?

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(for Bloomberg BNA)Following the Supreme Court's issuance of Firestone Tire & Rubber Company v. Bruch in 1989, Employee Retirement Income Security Act (ERISA) plan administrators, including insurers that underwrite health, life and disability insurance plans subject to ERISA, have been able to insulate their decisions from exacting judicial scrutiny by including discretionary clauses in their plans. As of 2015, however, nearly 25 states either have or are in the process of banning discretionary clauses in insurance policies subject to ERISA. This effort to ban discretionary clauses has led to legal challenges; however, the court rulings have uniformly favored state efforts to ban discretionary clauses. In general, a discretionary clause is a plan provision that grants the plan administrator authority to interpret the terms of the plan and to resolve all questions arising under the plan, including the determination of eligibility to receive benefits. ERISA plan administrators and insurers rely on discretionary clauses to gain deferential court review should a plan participant file a lawsuit challenging the denial of a claim for benefits. The Firestone decision made it clear that in the absence of an effective discretionary clause, a court deciding a benefit disputes utilizes the de novo standard of adjudication that favors neither party. When states ban or prohibit insurers from including discretionary clauses in their products, the discretionary standard of review, which is highly prized by insurers, is eliminated. In 2004, the National Association of Insurance Commissioners (NAIC) promulgated a proposed rule that would ban discretionary clauses in insurance products, including policies governed by ERISA plans.2 The NAIC took the position that discretionary clauses are unfair to insureds because they insulate plan insurers from meaningful judicial review. The regulatory association's effort to ban or prohibit these clauses was aimed at leveling the playing field between plan insurers and participants. Following the NAIC's lead, several state adopted some form of the proposed rule by legislation, regulation, or directive of the state insurance commissioner. In 2009, two federal appeals courts examined state insurance laws that ban discretionary clauses and ruled in favor of the states.3 Dozens of lower court rulings in Illinois, Colorado, Washington, and most recently, in California, have likewise upheld state bans on discretionary clauses.As the legal scales have tipped in

favor of the states, some have predicted that other states will likewise enact statutes or issue rules or regulations that prohibit discretionary clauses. Plan insurers, on the other hand, are expected to continue their opposition to the laws and argue that states run afoul of ERISA when they attempt to regulate the language in ERISA plans; however, the Supreme Court's refusal to hear an appeal from the Morrison ruling suggests that such efforts are unlikely to succeed.