



**STATE OF ARIZONA**  
**DEPARTMENT OF INSURANCE**

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**CHARLES R. COHEN**  
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Former Director J. Michael Low issued the following Circular Letter on April 28, 1981:

**DEPARTMENT INVESTIGATION OF WORKERS'  
COMPENSATION INSURANCE REPLACEMENT**

April 28, 1981

On March 31, 1981, the Arizona Department of Insurance conducted a public hearing under Docket No. 3781, styled "In the Matter of the Investigation of Workmen's Compensation Insurance Replacement." The purpose of the investigative proceeding was to examine the legality of certain programs presently being offered to employers as an alternative for workers' compensation insurance. These programs typically provide a package of life and health insurance benefits, including disability income benefits, under group insurance policies covering those employees who choose to reject workers' compensation coverage. The programs are chiefly represented as providing more benefits than workers' compensation insurance at a lower cost to the employer.

My review of the transcript of the public hearing persuades me that there are obvious problems which arise whenever an attempt to replace workers' compensation insurance with a package of life and disability insurance benefits is made. To begin, A.R.S. § 20-443 prohibits the making of any misrepresentation to a policyholder for the purpose of including such policyholder to lapse, forfeit, surrender, retain or convert any insurance policy. Further, A.R.S. § 20-444 provides that no person shall make any statement concerning the business of insurance which is untrue, deceptive or misleading. To my way of thinking, the failure to disclose any material provision in an insurance policy, particularly one relating to deductibles, waiting periods or medical expense limitations, is a deceptive and misleading practice. Additionally, the failure to inform a policyholder of the potential liability that may arise when an employee rejects the workmen's compensation act is an inherently deceptive practice. The disclosures which would at a minimum need to be made in a careful and understandable manner should include:

- 1) The fact that an employee who rejects the compensation benefits can sue an employer for negligence relating to an industrial accident.
- 2) A description of the waiting periods, deductibles and co-insurance provisions of the health insurance coverage.

- 3) An adequate explanation of the "reasonable and customary charges" limitation in an accident and health insurance policy.
- 4) A full description of any and all exclusions for preexisting conditions.
- 5) Any limitation on the definition of "physician" or other health care provider for purposes of obtaining coverage under a health insurance policy.
- 6) A complete description of the requirements for renewal after lapse of coverage.
- 7) Any limitation on disability income after age 65 or any Social Security offset provisions.
- 8) Any limitation on benefits for the recurrence of any existing disability.

The above list is not intended to be exhaustive; still the foregoing represents material facts which would need to be carefully considered in the event a health insurance program was substituted for workers' compensation insurance. Failure to adequately address the limitations that exist in typical health and disability income policies, particularly in the context of a sales solicitation designed to substitute such coverages for workers' compensation insurance, constitutes false and deceptive sales practices which will result in the appropriate disciplinary proceedings.

I do not believe that the Department has the authority to forbid outright any attempt to sell a package of life and health insurance benefits in lieu of workers' compensation coverage if all material disclosures are made in an understandable form. However, I do believe that it is erroneous to view a health and disability income program as being generically similar to the mandatory compensation benefits provided by law. Therefore, it is hoped that this letter will put all interested parties on notice that the Department intends to conduct disciplinary hearings based on any material misrepresentation or material omission of fact that arises in connection with the replacement of a workers' compensation insurance coverage.

J. Michael Low  
DIRECTOR OF INSURANCE