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November 2, 1995

Mr. Mark Hobratschk
Cochlear Corporation
Suite 200
61 Inverness Drive East
Englewood, Colorado 80112

Re: The Exclusion of Cochlear Implants from Employer-provided Health Insurance Plans

Dear Mr. Hobratschk:

You requested that we address the applicability of the Americans With Disabilities Act ("ADA"), 42 U.S.C. § 12101 et. seq. (Supp. 1992), to the exclusion of Cochlear Implants from employer-provided health insurance plans. Specifically, you asked whether, under the ADA, an employer could legally offer health insurance coverage to its employees which expressly excludes coverage for Cochlear Implants.

The ADA, 42 U.S.C. § 12112(a), prohibits a "covered entity" from discriminating against a qualified individual with a disability in regard to that individual's "terms, conditions, and privileges of employment." A covered entity is defined as "an employer, employment agency, labor organization, or joint labor-management committee." 42 U.S.C. § 12111(2). (Emphasis added.) Regulations promulgated by the Equal Employment Opportunity Commission ("EEOC") to implement the ADA confirm that fringe benefits, including health insurance, are covered by the Act. 29 C.F.R. § 1630.4(f). See also Carparts Distribution Center, Inc. v. Automotive Wholesaler's Ass'n. of New England, No. 93-1954, 1994 WL 543530, at *3 (1st Cir. Oct. 12, 1994). Consequently, an employer discriminates when it provides health insurance benefits to its employees that discriminate against that employer's disabled employees. An employer also "discriminates" against its disabled employees when it "participat[es] in a contractual . . . relationship that has the effect of subjecting a covered entity's . . . employee with a disability to . . . discrimination . . . . (Such a relationship includes a relationship

with . . . an organization providing fringe benefits to an employee of a covered entity.)" 42 U.S.C. § 12112(b)(2). This provision makes it clear that an employer cannot contract with a third party to provide discriminatory health insurance benefits that the employer itself would be prohibited by statute from offering.

The ADA does contain a savings clause applicable to insurance:

> Subchapters 1 through 3 of this Chapter and Title 4 of this Act shall not be construed to prohibit or restrict
>
> > (1) an insurer, hospital or medical service company, health maintenance organization, or any agent, or entity that administers benefit plans, or similar organizations from underwriting risks, classifying risks, or administering such risks that are based on or not inconsistent with state law; or
> >
> > (2) a person or organization covered by this Act from establishing, sponsoring, observing or administering the terms of a bona fide benefit plan that are based on underwriting risks, classifying risks, or administering such risks that are based on or not inconsistent with state law; or
> >
> > (3) a person or organization covered by this act from establishing, sponsoring, observing, or administering the terms of a bona fide benefit plan that is not subject to state laws that regulate insurance.
>
> Paragraphs (1), (2), and (3) shall not be used a subterfuge to evade the purposes of [the ADA].

42 U.S.C. § 12201(c) ("501(c)"). By incorporating this section into the ADA, Congress intended to permit the health insurance industry to continue employing traditional underwriting procedures, which, by their nature, discriminate against high-risk groups, so long as these procedures are not used as a "subterfuge" for disability discrimination, i.e., the disability discriminated against fails to pose a greater insurance risk.

On June 9, 1993, the EEOC issued its Interim Guidance on Application of ADA to Health Insurance ("Interim Guidance") to provide a framework within which health insurance plans may be analyzed. Under these guidelines, the burden is first on the plaintiff to demonstrate that a health-related term or provision creates a disability-based distinction. Once the Plaintiff satisfies this burden, the defendant must prove that the plan is bona fide, and complies with state law (if applicable), and that the distinction is not being used as a "subterfuge" to evade the purposes of the ADA. Although the EEOC's interpretations of the ADA are not binding upon courts, its opinions are entitled to great deference. To date, the courts have adopted the framework identified by the EEOC in its Interim Guidance. See, Inter alia, EEOC v. Tarrant Distributors, Inc., Civil Action No. H-94-3001 (S.D. Tex. Oct. 12, 1994); U.S. v. State of Illinois, 3 A.D. Cas. (BNA) 1157 (N.D. Ill. 1994); Holmes v. City of Aurora, 3 A.D. Cas. (BNA) 23 (N.D. Ill. 1993); Mason Tenders v. Donaghey, 2 A.D. Cas. (BNA) 1745 (S.D.N.Y. 1993).

A. Disability Based Distinctions.

Not all insurance distinctions which impact more heavily upon individuals with a disability are "disability-based". Typically, broad-based distinctions which apply to a range of disorders are not disability-based, even though the distinctions may in fact disparately impact disabled individuals. The EEOC's Interim Guidance states:

> Coverage limits on medical procedures that are not exclusively, or nearly exclusively, utilized for the treatment of a particular disability are not distinctions based on disability.

[Guidance at 2.] For example, it is not a violation of the ADA for an employer to limit the number of covered blood transfusions on an annual basis, even if this limit has a disparate impact on individuals with certain disabilities, including hemophiliacs. Likewise, refusing to cover renal dialysis will not violate the ADA, even if the refusal impacts employees with kidney failure more heavily, because renal dialysis is used to treat other ailments.

By contrast, a distinction that singles out a specific disability and refuses coverage for treatment associated exclusively or almost exclusively with that disability is probably a disability-based distinction, and may violate the ADA. For example, the EEOC has brought suit against several employers whose health benefit plans cap lifetime coverage for treatments associated with AIDS more rigorously than the lifetime coverage for other illnesses, on grounds that such distinctions are "disability-based". See EEOC v. Tarrant Distributors, supra. In its Interim Guidance, the EEOC illustrates other coverage

distinctions that it considers to be "disability-based", including deafness. [See Guidance, at 2.]

Where an insurance plan expressly excludes coverage for Cochlear Implants, that provision is a disability-based distinction. Unlike treatments which serve a variety of purposes, only some of which are directed towards individuals with disabilities, Cochlear Implant devices are used exclusively for the treatment of individuals who are profoundly hearing-impaired. Therefore, unless the exclusion of coverage for these devices falls within the protective ambit of § 501(c), it is likely that this provision will violate the ADA.

B. Exemption Under § 501(c).

42 U.S.C. § 12201(c) permits an employee benefit plan to continue employing disability-based distinctions so long as the plan is bona fide, and the distinction in question is not a "subterfuge" for discrimination.

(a) Bona Fide Plan. Reliance upon § 501(c) requires a defendant to prove that the health insurance plan is either a bona fide insured plan which is not inconsistent with state law, or a bona fide self-insured plan. A plan is bona fide if it exists, its terms have been accurately communicated to eligible employees, and it pays benefits. [See Guidance, at 3.]

(b) Subterfuge. Even if a health insurance plan is bona fide, a disability-based distinction is not permitted under the ADA if the distinction is a subterfuge for discrimination. 42 U.S.C. § 12201(c). To prove no subterfuge exists, the defendant must prove that the disability-based distinction has a business/insurance justification. In its Interim Guidance, the EEOC identified four non-exclusive methods for proving a business justification:

(i) The disability-based distinction is justified by legitimate actuarial data, i.e., the distinction is attributable to the application of legitimate risk classification and underwriting procedures to the increased risks of the disability;

(ii) The disability-based distinction is necessary to insure that the plan does not become so expensive as to cause it to become financially insolvent;

(iii) The disability-based distinction is necessary to prevent an "unacceptable change" in coverage or premiums;[1] or

(iv) The treatment at issue provides no medical benefit.

[Id.]

It does not appear that actuarial data will support a decision to deny coverage for Cochlear Implants. As defined by the EEOC, an actuarial defense is allowable if "conditions with comparable actuarial data and/or experience are treated in the same fashion." [See Guidance, at 3.] To justify the omission of Cochlear Implants from coverage, the defendant must demonstrate that all other medical conditions with similar costs and rates of prevalence are also omitted from coverage. It will be the defendant's burden to come forth with proof on this issue.

Likewise, it is unlikely that the second or third justification identified by the EEOC will apply. Cochlear Implants would probably make up an extremely small portion of claims to the benefit plan of an individual employer. Other insurance companies cover the costs associated with Cochlear Implants. Consequently, it will be difficult to demonstrate that the coverage of Cochlear Implants would either cause an insurance plan to become insolvent or create an unacceptable change in an insurance plan. For these reasons, a court should find that an employee benefit plan's exclusion of Cochlear Implants violates the ADA. The exclusion is one that is likely disability-based and it does not appear that the exclusion can be supported by any cost justification.

[1] An "unacceptable" change is one that would either make the plan effectively unavailable to a significant number of employees, make the plan so unattractive that significant adverse selection results, or make the plan so unattractive that the employer cannot compete for workers.

Please be certain to contact us if you have any questions or comments. This letter involves legal advice to you, our client. Because analyses of unsettled areas of the law may vary, no third parties may rely upon the opinions or evaluations set forth in this letter. Rather, said persons must obtain their own counsel before taking action with respect to the matters addressed herein.

Very truly yours,

ROTHGERBER, APPEL, POWERS & JOHNSON

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