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**OLR Bill Analysis****HB 6307*****AN ACT REGULATING THIRD-PARTY ADMINISTRATORS.*****SUMMARY:**

This bill requires third-party administrators (TPA) to be licensed by the Insurance Department, file audited financial statements, submit to examination by the department, and pay application and annual fees. With certain exceptions, a TPA is one who directly or indirectly (1) underwrites; (2) collects charges or premiums; or (3) adjusts or settles claims on Connecticut residents with respect to life, annuity, or health coverage offered or provided by an insurer. Entities that are exempt from TPA licensure but that perform similar services must annually register with the insurance commissioner.

The bill requires a TPA to have a written agreement with an insurer or other person using its services before performing duties on the insurer's or person's behalf and hold certain funds in a fiduciary capacity. It requires a TPA to maintain books and records of transactions made on the customer's behalf and make them available to the customer for inspection for at least five years after creation. The customer owns any record the TPA generates pertaining to it.

The bill authorizes the insurance commissioner to suspend or revoke a TPA's license, or issue a cease and desist order if the TPA does not have a license, after notice and hearing. It also authorizes him to adopt implementing regulations.

EFFECTIVE DATE: October 1, 2011

**§ 1 — DEFINITIONS*****Third-Party Administrator Exceptions***

The bill excludes from the definition of TPA:

1. an employer administering its employee benefit plan or that of

- an affiliated employer under common management and control;
2. a union administering a benefit plan on its members' behalf;
  3. an insurer licensed in Connecticut or acting as an authorized insurer with respect to insurance lawfully issued to cover a Connecticut resident, and its sales representatives;
  4. an insurance producer licensed to sell life, annuity, or health coverage in Connecticut, whose activities are limited exclusively to selling insurance;
  5. a creditor acting on its debtors' behalf with respect to insurance covering a debt between the creditor and its debtors;
  6. a trust and its trustees and agents acting pursuant to a trust established under federal law that restricts financial transactions with labor organizations;
  7. a tax-exempt trust (see BACKGROUND) and its trustees, or a custodian and the custodian's agents acting pursuant to an account meeting federal requirements for custodial accounts and contracts treated as qualified trusts;
  8. a mortgage lender, credit union, or financial institution subject to supervision or examination by federal or state banking authorities, when collecting or remitting premiums to licensed insurance producers, limited lines producers, or authorized insurers in connection with loan payments;
  9. a credit card company advancing or collecting insurance premiums or charges from its credit card holders who have authorized collection;
  10. an attorney adjusting or settling claims in the normal course of his or her practice or employment who does not collect charges or premiums in connection with life, annuity, or health coverage;

11. an adjuster licensed in Connecticut or not subject to state license requirements whose activities are limited to adjusting claims;
12. an insurance producer licensed in Connecticut and acting as a managing general agent whose activities are limited exclusively to those specified in law;
13. a business entity affiliated with an insurer licensed in Connecticut that undertakes activities as a TPA only for the direct and assumed insurance business of the affiliated insurer;
14. a consortium of state-funded federally qualified health centers that only provide services to recipients of programs administered by the Department of Social Services;
15. a pharmacy benefits manager registered with the insurance commissioner;
16. an entity providing administrative services to the Health Reinsurance Association; and
17. a nonprofit association or one of its direct subsidiaries that provides access to insurance as part of the benefits or services the association or subsidiary makes available to its members.

***Underwriting***

The bill defines “underwriting” as (1) accepting applications from employers or individuals for coverage in accordance with the written rules of the insurer or self-funded plan and (2) the overall planning and coordination of a benefits program.

***Adjuster***

The bill defines “adjuster” as an independent or contracted person who investigates or settles claims, excluding an insurer’s employee who investigates or settles claims incurred under insurance contracts the insurer or an affiliated insurer writes.

***Insurer***

The bill defines an “insurer” as a person or people doing insurance

business, including a captive insurer, a licensed insurance company, a medical or hospital service corporation, an HMO, or a consumer dental plan, that provides employee welfare benefits on a self-funded basis. It excludes a fraternal benefit society.

## **§ 2 — LICENSE REQUIREMENT**

The bill prohibits a person (including an entity) from offering to act as a TPA in Connecticut unless licensed or exempt from licensure under the bill. This requirement does not apply to a TPA's employee to the extent that his or her activities are under the TPA's supervision and control. But, the bill does not exempt a TPA's employees from the licensing requirements regarding public adjusters, casualty adjusters, motor vehicle physical damage appraisers, certified insurance consultants, surplus lines brokers, or any other insurance-related occupation for which the commissioner deems a license necessary. (See § 11 - TPA Licensing Process below for more details.)

### ***License Exemption***

A licensed insurer that underwrites, collects premiums or charges, or adjusts or settles claims, except for its policyholders, subscribers, and certificate holders, is exempt from the bill's requirements. These insurers must (1) be subject to the Connecticut Unfair Insurance Practices Act, (2) respond to all complaint inquiries received from the Insurance Department within 10 days of receiving them, and (3) obtain a customer's prior written consent for advertising mentioning the customer.

### ***ERISA Plans***

The bill specifies that it does not authorize the commissioner to regulate a self-insured plan subject to the federal Employee Retirement Income Security Act (ERISA). The commissioner is authorized to regulate activities an insurer undertakes for such plans that do not relate to the benefit plan and that comport with his authority under ERISA to regulate the business of insurance.

### ***Written Agreement***

Under the bill, a TPA must have a written agreement with the

insurer (hereafter, insurer includes another person using the TPA's services). The agreement must be kept as part of the official records of both the TPA and the insurer until five years after the contract ends. The agreement must contain all of the following provisions, except those that do not apply to the functions the TPA performs:

1. a statement of activities that the TPA must perform on the insurer's behalf;
2. the lines, classes, or types of insurance the TPA is authorized to administer;
3. a provision requiring the TPA to render an accounting, on an agreed frequency, detailing all transactions it performs pertaining to the insurer's underwritten businesses;
4. the procedures for any withdrawals to be made, including remittance, deposits, transfers to and deposits in a claims-paying account, payment to a group policyholder, payment to the TPA for commissions, fees, or charges, and remittance of return premiums;
5. procedures and requirements for required disclosures; and
6. termination provisions and dispute resolution procedure.

***Termination and Disputes Regarding Lawful Obligations***

A TPA or insurer may, with written notice, terminate the written agreement for cause as provided in the agreement. The insurer may also suspend the TPA's underwriting authority while any dispute regarding the cause for the agreement's termination is pending. In a dispute between the TPA and the insurer regarding the fulfillment of a lawful obligation with respect to a policy or plan subject to the written agreement, the insurer must fulfill the obligation.

**§ 3 — PAYMENTS TO INSURERS**

The bill specifies that insurance premiums or charges paid to a TPA by an insured party or on its behalf are deemed to have been received

by the insurer. "Return premium" or claim payments the insurer forwards to the TPA are not deemed to have been paid to the insured party or claimant until the insured party or claimant receives them. The bill specifies that it does not limit an insurer's rights to bring suit against the TPA resulting from the TPA's failure to pay the insurer, insured parties, or claimants.

#### **§ 4 — BOOKS AND RECORDS OF TRANSACTIONS PERFORMED ON PAYOR'S BEHALF**

The bill requires a TPA to maintain and make available to an insurer with which it contracts complete books and records of all transactions performed on the insurer's behalf. The TPA must maintain the books and records (1) in accordance with prudent standards of insurance recordkeeping and (2) for at least five years after they were created.

Under the bill, the insurer owns any records the TPA generates pertaining to the insurer. But the TPA retains the right to access the books and records to fulfill its contractual obligations to insured parties, claimants, and the insurer.

If a written agreement is terminated, the TPA may, by a separate written agreement with the insurer, transfer all books and records to a new TPA. The new TPA must acknowledge to the insurer, in writing, that it is responsible for retaining the books and records of the prior TPA.

#### ***Insurers Affiliated with Certain Business Entities***

An insurer that is affiliated with a business entity (i.e., a for-profit or nonprofit corporation, a limited liability company, or similar form of business organization) is responsible for the acts of that business entity to the extent of the entity's activities as a TPA for such insurer. Upon the commissioner's request, the insurer is responsible for furnishing the books and records of all transactions performed on behalf of the insurer to the commissioner.

#### ***Access to Books and Records***

The commissioner must have access to examine, audit, and inspect

books and records maintained by a TPA. Any documents, materials, or other information in the possession or control of the commissioner that are furnished by a TPA, insurer, insurance producer, or employee or agent acting on behalf of any of them, or obtained by the commissioner in an investigation are (1) confidential by law and privileged, (2) not subject to disclosure under the Freedom of Information Act, (3) not subject to subpoena, and (4) not subject to discovery or admissible in evidence in any private civil action. The commissioner may use these documents, materials, or other information in any regulatory or legal action brought as a part of the commissioner's official duties.

Neither the commissioner nor anyone who receives documents, materials, or other information may testify or be required to testify in any private civil action concerning them.

The commissioner may share and receive documents, materials, or other information deemed confidential and privileged with other state, federal, and international regulatory agencies; the National Association of Insurance Commissioners (NAIC) or its affiliates or subsidiaries; and state, federal, and international law enforcement authorities, provided the recipient of such documents, materials, or other information agrees to maintain their confidentiality and privileged status. He may also enter into agreements governing the sharing and use of information.

Disclosure to the commissioner or sharing documents, material, or other information does not waive any applicable privilege or claim of confidentiality. The bill does not prohibit the commissioner from releasing final, adjudicated actions, including for cause terminations of licenses issued to TPAs, to a database or other clearinghouse service maintained by the NAIC or its affiliates or subsidiaries.

#### **§ 5 — ADVERTISING BY A TPA**

The bill requires a TPA who advertises on an insurer's behalf to use only advertising that the insurer approved, in writing, before its use. A TPA that mentions any customer in its advertising must obtain the

customer's prior written consent.

## **§ 6 — ADMINISTRATION OF BENEFITS**

Each insurer is responsible for determining the benefits, premium rates, underwriting criteria, and claims payment procedures for the lines, classes, or types of insurance the TPA is authorized to administer, and for securing reinsurance. The insurer must provide to the TPA, in writing, procedures pertaining to administration of benefits, premium rates, underwriting criteria, and claims payment. Each insurer is responsible for the competent administration of its benefit and service programs.

If the TPA administers benefits for more than 100 certificate holders on behalf of an insurer, the insurer must, at least semiannually, conduct a review of the TPA's operations. At least one such review must be an on-site audit.

## **§ 7 — FIDUCIARY CAPACITY**

The bill requires the TPA to hold in a fiduciary capacity (1) all insurance charges and premiums it collects on behalf of or for an insurer and (2) return premiums received from an insurer.

The bill requires that funds be (1) immediately returned to the person entitled to them or (2) deposited promptly in a fiduciary account the TPA establishes and maintains in a federally insured financial institution. The TPA must provide a periodic accounting to the insurer, detailing all transactions it performed pertaining to the insurer's business.

### ***Record Maintenance***

The bill requires the TPA to keep clear records of deposits and withdrawals and copies of all records of any fiduciary account it maintained or controlled on an insurer's behalf and, at an insurer's request, give the insurer copies of the deposit and withdrawal records.

### ***Paying Claims***

The bill prohibits a TPA from paying any claim by withdrawing

funds from a fiduciary account in which premiums or charges are deposited. Withdrawals from such an account must be made as provided in the TPA's written agreement.

The bill requires that all claims a TPA pays from funds collected on behalf of or for an insurer must be paid only by drafts or checks of, and as authorized by, the insurer.

#### **§ 8 — COMPENSATION**

The bill prohibits a TPA from entering into an agreement or understanding with an insurer that makes or has the effect of making the TPA's commissions, fees, or charges contingent upon savings achieved by the adjustment, settlement, or payment of losses covered by the insurer's obligations.

The bill specifies that this prohibition does not prevent a TPA from receiving performance-based compensation for providing auditing services. It also does not prevent a TPA's compensation from being based on premiums or charges collected or the number of claims paid or processed.

#### **§ 9 — NOTICE AND DISCLOSURE**

The bill requires that when a TPA's services are used, the TPA must provide a written, insurer-approved notice to covered individuals advising them of its identity and the relationship among the TPA, policyholder, and insurer.

The bill requires a TPA, when it collects premiums, charges, or fees, to inform the insured person of the reasons for each. Additional charges are prohibited to the extent the insurer has paid for the services.

The bill requires the TPA to disclose to the insurer all charges, fees, and commissions that it receives for services it provides the insurer, including any fees or commissions paid by insurers providing reinsurance or stop loss coverage.

#### **§ 10 — PROMPTLY DELIVER WRITTEN COMMUNICATIONS**

The bill requires a TPA to promptly deliver written communications on the insurer's behalf. The TPA must deliver, promptly after receiving instructions from the insurer, any policies, certificates, booklets, termination notices, or other written communications the insurer delivers to the TPA for delivery to insured parties or covered individuals.

### **§ 11 — TPA LICENSING PROCESS**

The bill requires a TPA applying for a license to (1) submit a completed application to the commissioner (by using the current version of the "NAIC's Uniform Application for Third Party Administrators") and (2) pay the required fee.

The application must include or be accompanied by the following information and documents:

1. the applicant's basic organizational documents, including any articles of incorporation or association; partnership, trust, or shareholder agreement; trade name certificate; and other applicable documents;
2. the bylaws, rules, regulations, or similar documents regulating the applicant's internal affairs;
3. an NAIC biographical affidavit for the people responsible for the applicant's affairs, including (a) all members of the board of directors, board of trustees, executive committee, or other governing board or committee; (b) the principal officers in the case of a corporation, or the partners or members in the case of a partnership, association, or limited liability company; (c) any shareholder or member directly or indirectly holding 10% or more of its stock, securities, or interest; and (d) any other person who exercises control or influence over the applicant's affairs;
4. audited annual financial statements or reports for the two most recent fiscal years that prove the applicant has a positive net worth (see below);

5. a statement describing the business plan, including (a) information on staffing levels and activities proposed in Connecticut and nationwide and (b) details of the applicant's capability for providing a sufficient number of experienced and qualified personnel for claims processing, recordkeeping, and underwriting; and
6. other pertinent information the commissioner may require.

***Applicants in Existence for Less than Two Fiscal Years***

If the applicant has been in existence for less than two fiscal years, the uniform application must include financial statements or reports for any completed fiscal years and for any month during the current fiscal year for which these have been completed. The statements or reports must be certified by an officer of the applicant and prepared according to generally accepted accounting principles. An audited statement or report prepared on a consolidated basis must include a "columnar consolidating or combining worksheet" that includes the following:

1. amounts shown on the consolidated audited financial report;
2. amounts for each entity, stated separately;
3. explanations of consolidating and eliminating entries; and
4. other information the commissioner may require to review the applicant's current financial condition.

***Access to Records***

The bill requires a TPA applying for a license to make available for the commissioner's inspection copies of all contracts with insurers or others using the TPA's services. The TPA must produce its accounts, records, and files for examination and make its officers available to give information concerning its affairs, as often as the commissioner reasonably requires.

***License Refusal***

The commissioner may refuse to issue a license if he determines that:

1. the TPA or any individual responsible for conducting its affairs is not competent, trustworthy, financially responsible, or of good personal and business reputation;
2. the TPA has had an insurance or a TPA certificate of authority or license denied or revoked for cause by any jurisdiction; or
3. any of the grounds relating to the bill's enforcement requirements exist with respect to the TPA (see § 14).

### ***Miscellaneous Requirements***

A license issued to a TPA is in force until September 30<sup>th</sup> in each year, unless revoked or suspended before that date. The commissioner, at his discretion, may renew a TPA license upon receiving payment of the required fee without having the TPA reapply.

A TPA licensed or applying for a license must immediately notify the commissioner of any material change in its ownership, control, or other fact or circumstance affecting its qualification for a license.

A licensed TPA or applicant that administers or will administer self-insured government or church plans must maintain a surety bond, for use by the commissioner and the insurance regulatory authority of any other state in which the TPA is authorized to conduct business, to cover people who have remitted premiums, insurance charges, or other money to the TPA in the course of the TPA's business. The bond must be equal to the greater of (1) \$100,000 or (2) 10% of the aggregate total amount of self-funded coverage under government or church plans handled in Connecticut and all additional states in which the TPA is authorized to conduct business.

## **§ 12 — REGISTRATION REQUIREMENT**

A person who is not required to be licensed as a TPA but who directly or indirectly underwrites, collects charges or premiums from, or adjusts or settles claims for Connecticut residents in connection with

a self-insured life, annuity, or health coverage plan must annually register with the commissioner by October 1 on a form he designates. This does not apply if the self-insured plan is a government or church plan.

### **§ 13 — ANNUAL REPORT**

The bill requires each licensed TPA to file an annual report with the commissioner for the preceding calendar year by July 1 each year or within a time extension the commissioner grants for good cause. The annual report must include a financial statement audited by an independent certified public accountant. The bill requires that an audited annual financial statement or report prepared on a consolidated basis must include a “columnar consolidating or combining worksheet” that must be filed with the report and include the following:

1. amounts shown on the consolidated audited financial report;
2. amounts for each entity, stated separately; and
3. explanations of consolidating and eliminating entries.

The commissioner prescribes the form and contents of the report. At least two officers of the TPA must verify it.

The annual report must include the complete names and addresses of all insurers with which the TPA had agreements during the preceding fiscal year. The TPA must pay the required filing fee when it files the annual report.

The bill requires the commissioner to review each TPA’s most recently filed annual report by September 1. After its review, the commissioner must issue a certification to the TPA, or update the NAIC’s electronic database, indicating (1) that the annual report shows it has a positive net worth as evidenced by audited financial statements and that it is currently licensed and in good standing or (2) any deficiencies found in the annual report or financial statements.

**§ 14 — ENFORCEMENT**

The bill requires the commissioner to suspend or revoke a TPA's license or issue a cease and desist order if the TPA does not have a license, after notice and hearing, if he finds that the TPA:

1. is financially unsound;
2. is using methods or business practices that render its further business in Connecticut hazardous or injurious to insured persons or the public; or
3. failed to pay any judgment rendered against it in Connecticut within 60 days after the judgment became final.

The bill authorizes the commissioner to suspend or revoke a TPA's license or issue a cease and desist order if the TPA does not have a license, after notice and hearing, if he finds that the TPA:

1. has violated any (a) lawful rule or order of the commissioner or (b) provision of applicable Connecticut insurance laws;
2. has refused to be examined or produce its accounts, records, and files, or any individual responsible for its affairs for examination;
3. has, without just cause, (a) refused to pay proper claims or perform its contractual services or (b) caused covered individuals to accept less than the amount due or employ attorneys or bring suit against the TPA to secure full payment or settlement of the claims;
4. fails at any time to meet any license qualification that would have been grounds for the commissioner to refuse to issue a license;
5. has a person responsible for its affairs who has been convicted of or pled guilty or no contest to a felony, without regard to whether adjudication was withheld;

6. is under license suspension or revocation in another state; or
7. has failed to file an annual report in a timely manner.

The commissioner may, without advance notice and before a hearing, issue an order immediately suspending a TPA's license, or a cease and desist order if the TPA does not have a license, if he finds that:

1. the TPA is insolvent or impaired;
2. another state has started a proceeding for receivership, conservatorship, rehabilitation, or other delinquency proceeding regarding the TPA; or
3. the TPA's financial condition or business practices pose an imminent threat to the public health, safety, or welfare of Connecticut residents.

When the commissioner issues an order suspending a license or a cease and desist order, he must notify the TPA that it may request a hearing within 10 business days of receiving the order. If a hearing is requested, the commissioner must schedule it within 10 business days of receiving the request. If a hearing is not requested and the commissioner does not choose to hold one, the order remains in effect until the commissioner modifies or vacates it.

#### **§ 15 — ADOPTION OF REGULATIONS**

The bill authorizes the insurance commissioner to adopt implementing regulations.

#### **§ 16 — MARKET CONDUCT EXAMINATION**

The bill authorizes the commissioner, as often as he deems it expedient, to examine the market conduct of any TPA doing business in Connecticut. He already has this authority with respect to insurance companies, HMOs, and fraternal benefit societies.

#### **§ 17 — FEES**

The bill establishes the following fees that the insurance

commissioner must collect from a TPA:

1. \$500 for each license issued,
2. \$350 for each license renewal, and
3. \$100 for each annual report filed.

## **BACKGROUND**

### ***Internal Revenue Code § 501***

Section 501 of the Internal Revenue Code establishes categories of tax-exempt entities, including charities; fraternal benevolent societies; certain retirement funds; recreational clubs; state-sponsored health coverage organizations; civic leagues; religious and apostolic organizations; and qualified pension, profit-sharing, and stock bonus plans.

## **COMMITTEE ACTION**

Insurance and Real Estate Committee

Joint Favorable

Yea 20 Nay 0 (03/03/2011)