

# STATE OF MISSOURI



## DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

P.O. Box 690, Jefferson City, Mo. 65102-0690

RE: Examination Report of Delta Dental of Missouri

### ORDER

After full consideration and review of the report of the financial examination of Delta Dental of Missouri for the period ended December 31, 2009, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, John M. Huff, Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 374.205.3(3)(a), RSMo., adopt such report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, the findings and conclusions of the examination report are incorporated by reference and deemed to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo.

Based on such findings and conclusions, I hereby ORDER, Delta Dental of Missouri to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed by such report: (1) implement, and verify compliance with each item, if any, mentioned in the Comments on Financial Statement Items and/or Summary of Recommendations section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions.

So ordered, signed and official seal affixed this 25<sup>th</sup> day of May, 2011.



A handwritten signature in black ink, appearing to read "John M. Huff".

John M. Huff, Director  
Department of Insurance, Financial Institutions  
and Professional Registration

REPORT OF  
FINANCIAL EXAMINATION

# Delta Dental of Missouri

As of:  
DECEMBER 31, 2009

**FILED**  
JUN 04 2011  
DIRECTOR OF INSURANCE &  
FINANCIAL INSTITUTIONS &  
PROFESSIONAL REGISTRATION



STATE OF MISSOURI  
DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS  
AND PROFESSIONAL REGISTRATION  
JEFFERSON CITY, MISSOURI

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March 17, 2011

Honorable Joseph Torti III, Superintendent  
Division of Insurance Regulation  
State of Rhode Island  
Chairman, Financial Condition (E) Committee, NAIC

Honorable Stephen Robertson, Commissioner  
Department of Insurance  
State of Indiana  
Secretary, Midwestern Zone, NAIC

Honorable John M. Huff, Director  
Missouri Department of Insurance, Financial  
Institutions and Professional Registration  
301 West High Street, Room 530  
Jefferson City, Missouri 65101

Dear Sirs:

In accordance with your financial examination warrant, a comprehensive financial examination has been made of the records, affairs and financial condition of

#### **Delta Dental of Missouri**

hereinafter referred to as such or as "DDM" or as the "Company." The Company's statutory home office is located at 12399 Gravois Road, St. Louis, MO 63127, telephone number (314) 656-3000. This examination began on December 6, 2010 and concluded on the above date.

#### **SCOPE OF EXAMINATION**

##### **Period Covered**

The last full scope association financial examination of Delta Dental of Missouri was made as of December 31, 2005, by examiners from the state of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC) with no other zones participating.

The current full scope financial examination covers the period from January 1, 2006, through December 31, 2009, and was conducted by examiners from the state of Missouri representing the Midwestern Zone of the NAIC with no other zones participating. This examination also included material transactions or events occurring subsequent to December 31, 2009.

## **Procedures**

This examination was conducted using guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Department of Insurance, Financial Institutions and Professional Registration ("DIFP") or statutes of the state of Missouri prevailed. The Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating systems controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The following key activities were identified: Investments, Treasury, Reserves, Claims Handling, Premiums, Underwriting, and Intercompany.

The examiners relied upon information and workpapers provided by the Company's independent auditor, BKD LLP, for its audit covering the period from January 1, 2009, through December 31, 2009. Such reliance included fraud risk analysis, internal control narratives and tests of internal controls.

## **SUMMARY OF SIGNIFICANT FINDINGS**

### **Intercompany Service Agreements**

The examination determined that intercompany services were provided between affiliates without DIFP approved agreements. The most significant activities identified by the examination that were not supported by an agreement included services provided by Deniserv, LLC to DDM.

### **Fidelity Bond**

The Company is a named insured on a financial institution bond which provides \$750,000 in coverage with a \$10,000 deductible. This coverage does not equal the minimum amount of fidelity insurance recommended by the NAIC of \$900,000.

## **SUBSEQUENT EVENTS**

On February 4, 2010, the Company acquired 100% of the membership interest in Allied EyeCare, LLC (dba Advantica EyeCare), a specialty managed eye care company. The purchase price was \$11,000,000, with a potential earn-out of an additional \$3,000,000.

## **COMPANY HISTORY**

### **General**

Delta Dental of Missouri was incorporated as a not-for-profit entity on November 10, 1958, as Missouri Dental Service, and was licensed as a health services corporation under

the provisions of Chapter 354 RSMo (Health Service Corporations). The Company changed its name to Delta Dental Plan of Missouri on February 23, 1985.

On July 1, 1990, the DIFP issued a Certificate of Authority for the Company to operate as a prepaid dental plan pursuant to Sections 354.700 to 354.723 RSMo (Prepaid Dental Plans). In 2005, the Company changed its name to Delta Dental of Missouri, its current name.

#### **Capital Stock and Paid-In Surplus**

The Company has no common capital stock or paid-in surplus. The Company does maintain segregated surplus of \$150,000 in compliance with Section 354.710.1 RSMo (Reserve requirements).

#### **Dividends**

The Company has paid no dividends.

#### **Acquisitions, Mergers and Major Corporate Events**

Effective December 31, 2007, Delta Dental of Missouri formed a new subsidiary, Essex Holding Company ("EHC"), and transferred all former direct subsidiaries into EHC. EHC was subsequently renamed Advantica Holding Company, Inc.

#### **Surplus Debentures**

None

### **CORPORATE RECORDS**

The Company's articles of incorporation and bylaws were reviewed. There were no amendments to the articles of incorporation during the exam period. In 2007, the bylaws were amended to clarify and separate the roles of "Secretary of the Board" and "Secretary of the Corporation," and to eliminate the Building Committee.

The minutes of the board of directors and committee meetings were reviewed and appear to properly support and approve the corporate transactions and events for the period under examination.

### **MANAGEMENT AND CONTROL**

#### **Board of Directors**

The management of the Company is vested in a board of 13 directors authorized by the Company's bylaws. The directors serving at December 31, 2009, were as follows:

<u>Name and Address</u>	<u>Principal Occupation and Business Affiliation</u>
Guy P. Bates Jr. Springfield, MO	Dentist
Brian W. Berglund Saint Louis, MO	Attorney Bryan, Cave LLP

<u>Name and Address</u>	<u>Principal Occupation and Business Affiliation</u>
Melvin M. Bloom Chesterfield, MO	Retired Partner Hochschild, Bloom & Co.
Ollie C. Fisher Saint Louis, MO	Dentist
Steve P. Gaal III Saint Louis, MO	Retired (2010) President Delta Dental of Missouri
Richard J. Haffner Saint Louis, MO	Dentist
Dee A. Joyner Clayton, MO	Senior Vice President Commerce Bank
Shanon T. Kirchhoff Cape Girardeau, MO	Dentist
H.R. Redohl Saint Louis, MO	Retired AAIM Management
Edward C. Robison Warrensburg, MO	Dentist
Robert M. Tait Grandview, MO	Dentist
William J. Tunney Jr. Chesterfield, MO	Retired Boyd
Kenneth L. Worley Fortuna, MO	Retired UAW

### Officers

The officers of the Company serving and reported on the Jurat page of the Annual Statement at December 31, 2009, were as follows:

<u>Name</u>	<u>Position</u>
David Haynes	President
Janice Lees	Secretary
David Haynes	Treasurer
Richard Klassen	Vice President of Marketing
Alcides Martinez	Vice President of Compliance
Pamela Martin	Vice President of Operations

<u>Name</u>	<u>Position</u>
Karl Mudra	Vice President IT

### **Committees**

In accordance with the bylaws, the board has established various committees with responsibility for managing the Company's affairs between meetings of the board. Quarterly, the full board reviews and approves the actions of the committees.

Established committees include the following:

#### Executive Committee

Richard J. Haffner, Chairperson  
 Robert M. Tait  
 Dee A. Joyner  
 William J. Tunney Jr.  
 Melvin M. Bloom  
 H.R. Redohl  
 Steve P. Gaal III  
 Staff Liaison – Janice Lees

#### Compensation Committee

Brian W. Berglund, Chairperson  
 H.R. Redohl  
 Robert M. Tait  
 Kenneth L. Worley  
 Staff: Jane Stanhaus

#### Finance and Audit Committee

Melvin M. Bloom, Chairperson  
 Dee A. Joyner  
 Guy P. Bates Jr.  
 Brian W. Berglund  
 Staff Liaison –David Haynes

#### Governance Committee

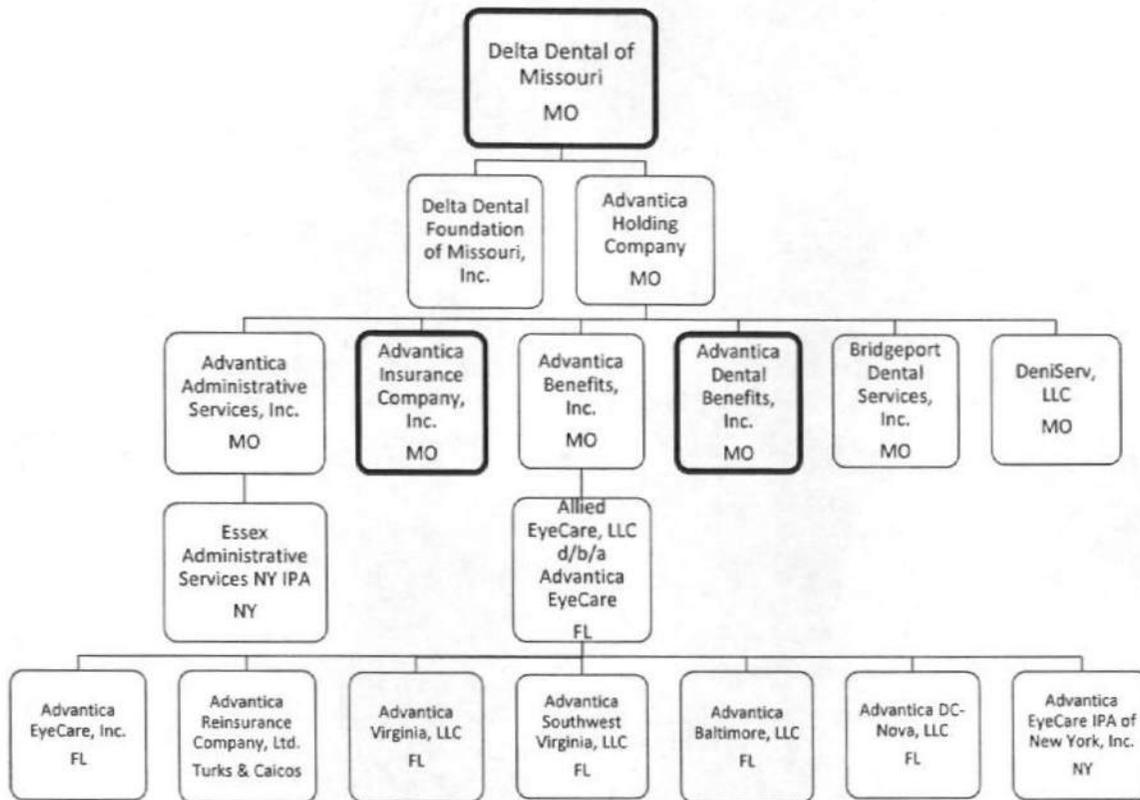
H.R. Redohl, Chairperson  
 Brian W. Berglund  
 Melvin M. Bloom  
 Guy P. Bates Jr.  
 William J. Tunney Jr.  
 Staff: Janice Lees

### **Holding Company, Subsidiaries and Affiliates**

The Company is the ultimate controlling entity of an Insurance Holding Company System as defined by Section 382.010 RSMo (Definitions).

### **Organization Chart**

The following organizational chart depicts the Company within the current holding company system. All subsidiaries shown are wholly owned.



### Affiliated Transactions

The Company enters into various agreements with affiliates. Active agreements are discussed below:

#### 1) Management Agreement

Parties: Advantica Dental Benefits, Inc., Advantica Insurance Company, Inc., DeniServ, LLC, and Delta Dental of Missouri.

Effective: January 1, 2007, non-disapproved by DIFP on July 31, 2007

Terms: DDM will provide various administrative services to the other parties to include human resources, financial services, accounting services, information systems services, marketing services and purchasing services.

Rate(s): Fees charged under the Agreement are equal to the cost incurred to render such services to the other parties.

#### 2) Guaranty Agreement

Parties: Delta Dental of Missouri, Bridgeport Dental Services, Inc., and Children's Mercy Family Health Partners, Inc.

Effective: June 1, 2008, non-disapproved by DIFP on December 2, 2008

Terms: The agreement guarantees prompt performance and payment by Bridgeport Dental Services, Inc., of all obligations to Children's Mercy

Family Health Partners, Inc. (replaces obligation to maintain a \$275,000 performance bond originally effective February 1, 2002).

Rates: None.

Intercompany services were provided between affiliates without agreements governing those transactions. The most significant activities identified by the examination that were not supported by an agreement included services provided by Deniserv, LLC to DDM.

The Company should execute all necessary intercompany service agreements and file them for approval with the DIFP.

#### **FIDELITY BOND AND OTHER INSURANCE**

The Company is a named insured on a financial institution bond which provides \$750,000 in coverage with a \$10,000 deductible. This coverage does not meet the minimum amount of fidelity insurance recommended by the NAIC of \$900,000.

The Company should obtain additional fidelity coverage to comply with the amount recommended by the NAIC.

The Company is also a named insured on policies that provide the following coverages: property, general and excess, auto, directors and officers, fiduciary, and workers' compensation. The Company's insurance coverages, other than the financial institution bond, appear adequate.

#### **PENSIONS, STOCK OWNERSHIP AND INSURANCE PLANS**

The Company provides the following benefits to full time employees: various types of leave, holidays, cafeteria plan, group life, short-term disability, long-term disability, employee group health plan, educational assistance, 401(k) savings plan and a defined contribution retirement plan. In addition, the Company has a nonqualified, defined benefit, deferred compensation plan for its officers.

#### **TERRITORY AND PLAN OF OPERATION**

The Company is licensed as a not-for-profit prepaid dental plan in Missouri under Chapter 354 RSMo (Health Service Corporations – Health Maintenance Organizations - Pre-paid Dental Plans). At year end 2009, the Company was also licensed in the state of South Carolina.

DDM is a member plan of the Delta Dental Plan Association that operates in all 50 states, Guam, Puerto Rico and the Virgin Islands. DDM provides dental insurance benefits to over 1.2 million members through over 1,500 employer group contracts. Employer groups pay a fee to DDM and, in turn, DDM then pays dental claims for their employees. National employer groups can access a nationwide provider panel and local procedure fees via the national association.

DDM also processes and pays claims for self-funded employers who reimburse DDM for the claims processed on their behalf. These employers are referred to as ASC –

Administrative Service Contracts. For this service, DDM receives administrative fees on a per member per month basis or a percentage of claims basis. The fees are billed and collected from each employer group monthly.

### GROWTH OF COMPANY

The Company's premium continued to grow over the examination period in spite of the economic crisis. However, increased costs attributed to increased utilization in the bad economy resulted in lower margins in 2009.

<u>Year</u>	<u>Direct Premium Written</u>	<u>Capital and Surplus</u>	<u>Direct Premium Written to Capital and Surplus</u>
2009	130,448,910	56,576,697	231%
2008	119,732,693	51,769,221	231%
2007	106,581,087	42,656,271	250%
2006	98,752,836	35,328,182	280%

### LOSS EXPERIENCE

The following exhibit reflects the Company's claims unpaid and medical expense experience over the examination period. As noted above, utilization increased substantially as a result of the economic downturn, especially in 2009.

<u>Year</u>	<u>Claims Unpaid</u>	<u>Medical Benefits</u>
2009	6,176,757	109,694,003
2008	6,294,504	97,202,656
2007	5,813,655	84,960,251
2006	6,290,280	77,398,291

### REINSURANCE

The Company has no reinsurance.

### ACCOUNTS AND RECORDS

#### General

The Company's financial statements were prepared using Sage MAS 500 financial accounting software.

Reserves and related actuarial items as of December 31, 2009, were reviewed and certified by F. Ray Martin, FSA, MAAA, president and owner of MarACon, LLC.

The company is planning to replace the functions of its current premium administration system, Wisddm, with an existing, but unused, Finance Manager module of the customized commercial software, aQDen, which has been used for claims, eligibility and

enrollment administration since 1999. Testing of the premium administration system will take place sometime in 2011.

**Independent Auditor**

The Company's financial statements for the period January 1, 2006 to December 31, 2009, were audited by BKD LLP, Certified Public Accountants. The workpapers and reports of the most recent independent audit were reviewed for this examination. These workpapers and reports were used in the course of this examination as deemed appropriate.

**Information Systems**

In conjunction with this examination, Andrew Balas, AES, Information Systems Financial Examiner with the DIFP, conducted a review of the Company's information systems. His evaluation did not identify any significant weaknesses.

**STATUTORY DEPOSITS**

**Deposits with the State of Missouri**

The funds on deposit with the Missouri Department of Insurance, Financial Institutions and Professional Registration as of December 31, 2009, are reflected below. These deposits had sufficient par and market values to meet the deposit requirement for the state of Missouri per Section 354.707 RSMo (Capital, surplus, security required).

<u>Type of Security</u>	<u>Par Value</u>	<u>Market Value</u>	<u>Statement Value</u>
US Treasury Notes	\$ 205,000	\$ 204,221	\$ 205,025

**Deposits with Other States**

The Company also has funds on deposit with the state of South Carolina to satisfy its statutory deposit requirements. Those funds on deposit as of December 31, 2009, were as follows:

<u>State</u>	<u>Security</u>	<u>Par Value</u>	<u>Market Value</u>	<u>Statement Value</u>
South Carolina	US Treasury Note	\$ 150,000	\$ 149,954	\$ 149,965

## **FINANCIAL STATEMENTS**

The following financial statements, with supporting exhibits, present the financial condition of the Company as of December 31, 2009, and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Comments on the Financial Statements," which follow the financial statements.

There may have been additional differences found in the course of this examination, which are not shown in the "Comments on the Financial Statements." These differences, if any, were determined to be immaterial in relation to the financial statements, and therefore were only communicated to the Company and noted in the workpapers for each individual annual statement item.

## ASSETS

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$ 24,323,785	\$	\$ 24,323,785
Stocks	10,180,263	1,905,141	8,275,122
Real estate - properties occupied by the company	2,224,509		2,224,509
Cash, cash equivalents and short-term investments	28,138,201		28,138,201
Investment income due and accrued	304,068		304,068
Uncollected premiums	2,295,036		2,295,036
Amounts receivable relating to uninsured plans	6,885,108		6,885,108
EDP equipment	168,282	30,988	137,294
Furniture and equipment	108,499	108,499	
Receivables from parent, subsidiaries and affiliates	4,984,273	3,649,889	1,334,384
Prepaid expenses	285,906	285,906	
Other assets	2,529,110		2,529,110
Total assets	\$ 82,427,040	\$ 5,980,423	\$ 76,446,617

## LIABILITIES, CAPITAL, AND SURPLUS

	Current Year
Claims unpaid	\$ 6,176,757
Unpaid claim adjustment expenses	563,749
Premiums received in advance	2,205,025
General expenses due or accrued	10,531,462
Retention reserves and advance deposits	392,927
Total liabilities	\$ 19,869,920
Required statutory surplus	150,000
Unassigned funds (surplus)	56,426,697
Total capital and surplus	\$ 56,576,697
Total liabilities, capital and surplus	\$ 76,446,617

## STATEMENT OF REVENUE AND EXPENSES

	Current Year
Net premium income	\$ 130,395,112
Other income	53,798
Total revenues	\$ 130,448,910
Hospital/medical benefits	\$ 109,694,003
Claims adjustment expenses	5,971,114
General administrative expenses	10,833,750
Total underwriting deductions	\$ 126,498,867
Net underwriting gain (loss)	\$ 3,950,043
Net investment income earned	\$ 1,795,858
Net realized capital gain (loss) less capital gains tax	1,014,239
Net investment gains	\$ 2,810,097
Net income (loss) after capital gains tax and before federal income tax	\$ 6,760,140
Federal income tax	\$
Net income	\$ 6,760,140

## CAPITAL AND SURPLUS

	Current Year
Capital and surplus prior reporting year	\$ 51,769,221
Net income	\$ 6,760,140
Change in net unrealized capital gains (losses)	(794,462)
Change in nonadmitted assets	(1,177,795)
OTTI common stock	19,593
Net change in capital and surplus for the year	\$ 4,807,476
Capital and surplus, December 31 current year	\$ 56,576,697

## COMMENTS ON THE FINANCIAL STATEMENTS

There are no comments on the Company's financial statements.

## SUMMARY OF RECOMMENDATIONS

### Intercompany Service Agreements

The examination determined that intercompany services were provided between affiliates without DIFP approved agreements. The most significant activities identified by the examination that were not supported by an agreement included services provided by Deniserv, LLC to DDM. The Company should execute all necessary intercompany service agreements and file them for approval with the DIFP.

### Fidelity Bond

The Company is a named insured on a financial institution bond which provides \$750,000 in coverage with a \$10,000 deductible. This coverage does not equal the minimum amount of fidelity insurance recommended by the NAIC of \$900,000. The Company should obtain additional fidelity coverage to comply with the minimum amount recommended by the NAIC.

