

REPORT ON EXAMINATION

OF

DELTA DENTAL OF NEW YORK, INC.

AS OF

DECEMBER 31, 2015

DATE OF REPORT

JULY 5, 2018

EXAMINER

TOMMY KONG, CFE, PIR

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Maria T. Vullo
Superintendent

July 5, 2018

Honorable Maria T. Vullo
Superintendent of Financial Services
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and acting in accordance with the instructions contained in Appointment Number 31548, dated November 21, 2016, attached hereto, I have made an examination into the condition and affairs of Delta Dental of New York, Inc., a dental expense indemnity company licensed pursuant to the provisions of Article 43 of the New York Insurance Law, as of December 31, 2015, and respectfully submit the following report thereon.

The examination was conducted at the main administrative office of Delta Dental of New York, Inc. located at One Delta Drive, Mechanicsburg, Pennsylvania.

Wherever the designations “DDNY” or the “Plan” appear herein, without qualification, they should be understood to indicate Delta Dental of New York, Inc.

Wherever the designation the “Department” appears herein, without qualification, it should be understood to indicate the New York State Department of Financial Services.

1. SCOPE OF THE EXAMINATION

Delta Dental of New York, Inc. was previously examined as of December 31, 2011. This examination of the Plan was a combined (financial and market conduct) examination and covered the four-year period from January 1, 2012 through December 31, 2015. The financial component of the examination was conducted as a financial examination, as defined in the National Association of Insurance Commissioners (“NAIC”) *Financial Condition Examiners Handbook, 2016 Edition* (the “Handbook”). The financial examination was conducted observing the guidelines and procedures in the Handbook. Where deemed appropriate by the examiner, transactions occurring subsequent to December 31, 2015 were also reviewed.

The financial portion of the examination was conducted on a risk-focused basis in accordance with the provisions of the Handbook, which provides guidance for the establishment of an examination plan based on the examiner’s assessment of risk in DDNY’s operations and utilizes that evaluation in formulating the nature and extent of the examination. The examiner planned and performed the examination to evaluate DDNY’s current financial condition, as well as to identify prospective risks that may threaten the future solvency of the Plan.

The examiner identified key processes, assessed the risks within those processes and assessed the internal control systems and procedures used to mitigate those risks. The examination also included an assessment of the principles used and significant estimates made by management, an evaluation of the overall financial statement presentation, and determined management’s compliance with the Department’s statutes and guidelines, Statutory Accounting Principles, as adopted by the Department, and NAIC annual statement instructions.

Information concerning DDNY's organizational structure, business approach and control environment were utilized to develop the examination approach. The examination evaluated the Plan's risks and management activities in accordance with the NAIC's nine branded risk categories. These categories are as follows:

- Credit
- Legal
- Liquidity
- Market
- Operational
- Pricing/Underwriting
- Reputational
- Reserving
- Strategic

The examination also evaluated the Plan's risks and management activities in accordance with the NAIC's ten critical risk categories. These categories are as follows:

- Appropriateness/Adequacy of Reinsurance Program
- Appropriateness of Investment Portfolio and Strategy
- Capital Management
- Liquidity Considerations
- Reinsurance Reporting and Collectability
- Related Party/Holding Company Considerations
- Reserve Adequacy
- Reserve Data
- Underwriting and Pricing Strategy/Quality
- Valuation/Impairment of Complex or Subjectively Valued Invested Assets

The Plan was audited annually, for the years 2012 through 2015, by the accounting firm Armanino McKenna LLP ("AM"). DDNY received an unmodified opinion from AM for each of those years. Certain audit workpapers of AM were reviewed and relied upon in conjunction with this examination. A review was also made of the Plan's internal audit function and enterprise risk management program.

A review was also made to ascertain what actions were taken by DDNY with regard to the comments and recommendations contained in the prior report on examination. The results of the examiner's review are contained in Item No. 5 of this report.

This report on examination is confined to financial statements and comments on those matters which involve departures from laws, regulations or rules, or which are deemed to require an explanation or description.

2. DESCRIPTION OF THE PLAN

The New York Dental Service Corporation, which was organized by the Dental Society of New York, was licensed in 1963 by the Department, under the provisions of New York Insurance Law Section 252 (currently Section 4302), as a dental expense indemnity corporation. On March 30, 1994, the New York Dental Service Corporation changed its name to Delta Dental of New York, Inc. The purpose of the Plan is to establish, maintain and operate a non-profit dental service plan, whereby dental care is furnished by dentists, duly licensed to practice under the laws of New York State, who have contracted with the Plan to provide dental care to its subscribers.

A. Corporate Governance

Pursuant to DDNY's by-laws, management of the Plan is to be vested in a board of directors consisting of not less than thirteen (13) members. As of December 31, 2015, the directors of DDNY were comprised of the following fourteen (14) members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Michael C. Alfano, DMD, PhD New York, New York	Executive Vice President, New York University
Anthony L. Dimango, DDS Brooklyn, New York	Dentist
Thomas M. Halton, DMD Sag Harbor, New York	Retired
George S. Karalekas New York, New York	President, Karalekas & Company
Barbara R. Katersky New York, New York	Retired
Andrew S. Levine, DDS Saratoga Springs, New York	Dentist
Francine Y. Lopez Long Island City, New York	VP, Director of Benefits Finance & Administration, Publicis
Stacy A. Mazza Chestnut Ridge, New York	Assistant VP, Corporate Benefits, Ascena Retail Group, Inc.
Thomas J. McCartin Rockville Centre, New York	Advertising Agency Executive, McCartin Advertising
Lynette A. Metz Latham, New York	Director, NYSUT Member Benefits Trust
Alan M. Patrignani, DDS Naples, Florida	Retired
James E. Spencer, DDS Woodcliff Lake, New Jersey	Retired
Jozef C. Verbraeken Sarasota, Florida	Treasurer & Secretary, Delta Dental of New York, Inc.
Thomas H. Wismuller Ogunquit, Maine	President, Wismuller Corporation

The minutes of all meetings of the board of directors and committees thereof held during the examination period were reviewed. The review indicated all board and committee meetings were well attended, with all board members attending at least one-half of the meetings they were eligible to attend. It was also noted that the board met four times during each calendar year covered by the examination period.

The principal officers of DDNY, as of December 31, 2015, were as follows:

<u>Name</u>	<u>Title</u>
Anthony S. Barth	President
Michael J. Castro	Chief Financial Officer
Michael G. Hankinson, Esq.	Chief Legal Officer
Jozef C. Verbraeken	Treasurer & Secretary

B. Enterprise Risk Management

As of December 31, 2015, the Plan has a formal enterprise risk management program in place, as required by Insurance Regulation No. 203 (11 NYCRR 82) and Insurance Circular Letter No. 14 (2011).

C. Territory and Plan of Operation

DDNY is licensed to sell dental insurance in all counties of New York State. The Plan's total revenues (net of reinsurance) for each year of the examination period were as follows:

<u>Calendar Year</u>	<u>Total Revenues</u>	<u>% Increase</u>
2012	49,471,560	—
2013	53,888,990	8.9%
2014	69,712,823	29.4%
2015	81,264,486	16.6%

As of December 31, 2015, the Plan wrote \$161,539,924 in total direct premium. The majority of DDNY's premiums were written in the following five (5) New York State counties:

<u>County</u>	<u>Enrollment</u>	<u>Premiums</u>	<u>Percentage</u>
Albany	201,680	\$50,822,092	31.5%
New York	116,015	\$48,707,288	30.2%
Erie	75,933	\$ 6,860,007	4.2%
Nassau	19,697	\$ 6,005,423	3.7%
Suffolk	16,168	\$ 5,834,656	3.6%

The chart below depicts the total enrollment and the increase or decrease for the years covered by this examination:

<u>Year</u>	<u>Enrollment</u>	<u>Increase</u>
2012	388,685	—
2013	458,686	18.0%
2014	529,151	15.4%
2015	562,293	6.3%

As a result of enrollment growth and rate increases, total revenues in the Plan's non-retention and retention contracts increased each year during the examination period.

DDNY offers dental indemnity and managed dental care contracts. The Plan's managed dental care contract is offered under DeltaCare USA, a dental maintenance product, available to both individuals and groups. With this type of contract, DDNY pays a monthly capitation fee to contracted providers that provide services to enrolled members who pay a fixed co-payment at the time of service. While the dentists who participate in this program accept some risk, the risk is mitigated through the Plan's "Chair Hour Guarantee" program, which guarantees that providers will receive a certain income based upon the relative value units of the procedure(s) performed.

The Plan also acts as a third party administrator for Cost Plus Contracts (administrative service provided only), wherein purchasers are billed for all of the claims that are paid, plus an administrative fee, which is either a percentage of claims paid or a fee per eligible enrollee.

The Plan sells its policies using an internal sales force, as well as independent brokers.

D. Significant Operating Ratios

The following ratios have been computed, as of December 31, 2015, based upon the results of this examination. The ratios presented below are on an earned-incurred basis and encompass the four-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Claims (net of reinsurance recoveries)	\$152,700,635	60.0%
Claims adjustment expenses	31,552,751	12.4%
General administrative expenses	58,022,821	22.8%
Net underwriting gain	<u>12,061,652</u>	<u>4.8%</u>
Premiums earned	<u>\$254,337,859</u>	<u>100.0%</u>

As of December 31, 2015, the Plan's total adjusted capital was \$25,507,136. This amount was well above the Plan's authorized control level risk-based capital of \$3,129,124.

E. Reinsurance

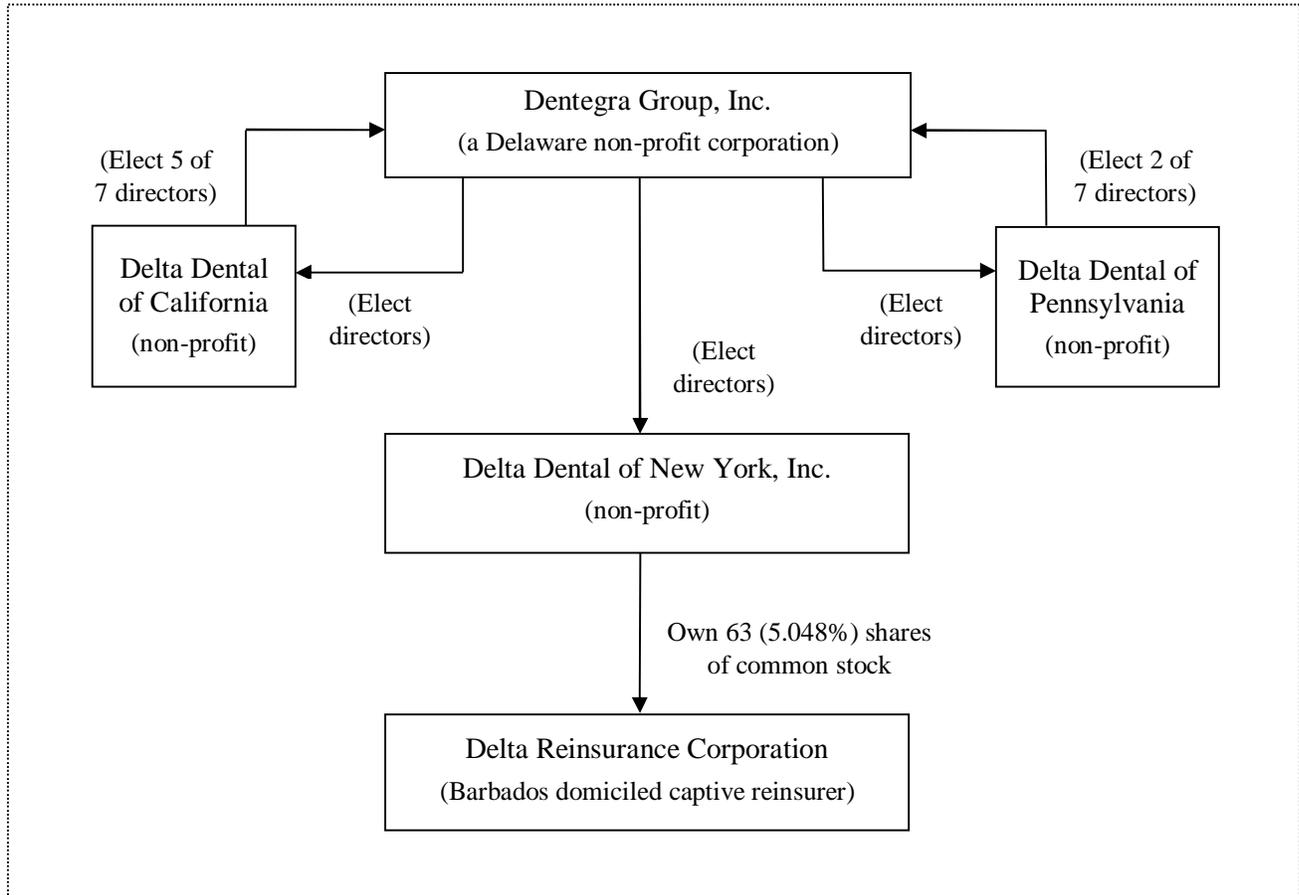
DDNY maintained two quota share reinsurance treaties with Delta Reinsurance Company Inc. ("DRC"), an unauthorized reinsurer. Treaty No. 3-1-1-88 provides that DRC reinsure DDNY's traditional and discounted fee-for-service programs, Delta Premier, and Delta Preferred Option. Under Treaty No. 10-1-1-98, DRC reinsured DDNY's emergency, specialist, and Chair Hour Guarantee payments from the DeltaCare product. Prior to July 1, 2014, these treaties

called for DDNY to cede 75% of the risk for all policies issued. Effective July 1, 2014, the cession was reduced to 60%, as a result of continued improvement in DDNY's business.

As of December 31, 2015, the Plan reported a reinsurance deposit in the amount of \$3,050,000 from DRC for the maintenance of a statutory net credit for unauthorized reinsurance.

F. Holding Company System

The following chart depicts, as of December 31, 2015, the Plan's relationship with core members of its holding company system.



The Plan's operations are managed through a General Agency Agreement ("GAA") between Delta Dental of Pennsylvania ("DDP") and two other affiliates, PaCa Management, LLC and Delta Dental Insurance Company ("DDIC"). Under the terms of the GAA, DDP provides general administration services to the Plan for an administration fee.

Under a separate administrative services agreement, all of DDP's commitments to the Plan were passed to PaCa Management, LLC ("PaCa"), a limited liability company organized

under the laws of the State of Delaware, with its principal office in Wilmington, Delaware. PaCa, which is jointly owned by DDP and DDIC, was formed to administer and support DDNY.

The Plan is also a party to the DeltaCare USA Administration Agreement (“DAA”) with DDIC, whereby DDIC administers the management of the DeltaCare USA (“DUSA”) product, a dental maintenance product. Enrollees in the DUSA product can visit participating providers and pay only a fixed co-payment. Under DAA, the administrator can sell capitated coverage to groups outside of New York State. In many cases, those groups have members within New York State. For those members, PaCa has been paying a fee to the Plan, in return for which the Plan covers dental services to those New York members through its capitated network.

3. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, and surplus as of December 31, 2015, as contained in the Plan's 2015 filed annual statement, a condensed summary of operations, and a reconciliation of the surplus account for each of the years under review.

Armanino McKenna LLP ("AM") was retained by the Plan to audit the Plan's combined statutory basis statements of financial position as of December 31st of each year in the examination period, and the related statutory-basis statements of operations, surplus, and cash flows for the year then ended.

AM concluded that the statutory financial statements presented fairly, in all material respects, the financial position of the Plan at the respective audit dates. Balances reported in these audited financial statements were reconciled to the corresponding years' annual statements with no discrepancies noted.

A. Balance Sheet

Assets

Bonds	\$32,405,762
Common stocks	2,965,172
Cash and short-term investments	(2,964,989)
Investment income due and accrued	379,167
Uncollected premiums in course of collection	1,700,873
Amounts recoverable from reinsurers	6,768,708
Other amounts receivable under reinsurance contracts	1,772,497
Amounts receivable relating to uninsured plans	8,727,209
Receivables from parent, subsidiaries and affiliates	251,251
Aggregate write-ins for other than invested assets	<u>18,893</u>
Total assets	<u>\$52,024,543</u>

Liabilities

Claims unpaid (net of reinsurance)	\$ 3,130,174
Unpaid claims adjustment expenses	375,000
Premiums received in advance	960,836
General expenses due or accrued	4,549,037
Ceded reinsurance premiums payable	7,303,312
Amounts withheld or retained for the account of others	117,601
Remittances and items not allocated	30,197
Amounts due to parent, subsidiaries and affiliates	327,904
Funds held under reinsurance treaties	7,469,834
Liability for amounts held under uninsured plans	1,081,908
Aggregate write-ins for other liabilities	<u>1,171,604</u>
Total liabilities	<u>\$26,517,407</u>

Surplus

Aggregate write-ins for special surplus funds	\$ 1,236,646
Section 1307 loans	1,360,000
Aggregate write-ins for other than special surplus funds	10,203,944
Unassigned funds	<u>12,706,546</u>
Total surplus	\$25,507,136
Total liabilities and surplus	<u>\$52,024,543</u>

Note: The Internal Revenue Service has not conducted any audits of the federal income tax returns filed on behalf of the Plan through tax year 2015. The examiner is unaware of any potential exposure of the Plan to any tax assessments, and no liability has been established herein relative to such contingency.

Note: No liability appears on the above statement for the Section 1307 loans in the amount of \$1,360,000. As of December 31, 2015, accrued interest on these loans was \$0. The Plan requested and received approval from Delta Dental of Pennsylvania for the forgiveness of all accrued interest. The loans were granted pursuant to the provisions of Section 1307 of the New York Insurance Law. As provided in Section 1307, repayment of principal and interest shall only be made out of free and divisible surplus, subject to the prior approval of the Superintendent of Financial Services.

B. Statement of Revenue and Expenses and Surplus

Surplus increased \$17,149,675 during the four-year examination period, January 1, 2012 through December 31, 2015, detailed as follows:

Revenue

Premium	\$253,535,456	
Change in unearned premium reserves and reserve for rate credits	(714,170)	
Risk revenue	<u>1,516,573</u>	
Total revenue		\$254,337,859

Expenses

Claims (net of reinsurance recoverable)	\$152,700,635	
Claims adjustment expenses	31,552,751	
General administrative expenses	<u>58,022,821</u>	
Total underwriting deductions		<u>242,276,207</u>
Net underwriting gain		\$ 12,061,652
Net investment income		2,605,844
Net realized capital gains		25,229
Net gain from agents' or premium balances charged off		26,235
Aggregate write-ins for other expenses		<u>(58,922)</u>
Net income		<u>\$ 14,660,038</u>

Change in Surplus

Surplus, per report on examination, as of December 31, 2011		\$ 8,357,461
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Gains in Surplus

Net income	\$14,660,038	
Change in net unrealized capital gains	2,319,792	
Change in non-admitted assets	<u>169,845</u>	
Net change in surplus		<u>17,149,675</u>
Surplus, per report on examination, as of December 31, 2015		<u>\$25,507,136</u>

4. MARKET CONDUCT ACTIVITIES

In the course of the examination, a review was made of the manner in which the Plan conducts its business practices and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the more precise scope of a market conduct examination. The review was directed at the practices of the Plan in the following areas:

- A. Grievances
- B. Claims processing

A. Grievances

A sample of the Plan's grievances was randomly selected for review. It was noted from a review of the sampled items that the Plan's determination letters did not provide procedures for how to file an appeal to an adverse determination.

As a best practice, it is recommended that DDNY include in its grievance determination letters the procedures on how to file an appeal to an adverse determination.

B. Claims Processing

A claims review was performed using a statistical sampling methodology, covering claims adjudicated during the period of January 1, 2015 through December 31, 2015, to evaluate the overall accuracy and compliance of DDNY's claims processing. A random statistical sample size of 167 claims was drawn, for review, for each claims population of paper, electronic, and denial. A review of the paper claims sample of 167 discovered that there were 38 claims that were adjudicated incorrectly and noted as "*Adjust as Delta error.*" In one instance, a claim was

processed incorrectly for \$45 when it should have been for \$450. In another instance, a claim was processed incorrectly as a “PPO” claim instead of a “Premier” claim. A review of the electronic claims sample of 167 claims uncovered that there were 14 claims that were adjudicated incorrectly and noted as “*Adjust as Delta error.*” One claim was processed incorrectly as a restoration when it should have been for a sealant. Another claim was processed incorrectly under the primary insured when it should have been the secondary insured. A review of the denial claims sample of 167 claims uncovered that there were 17 claims that were adjudicated incorrectly and noted as “*Adjust as Delta error.*” In one instance, a claim was denied incorrectly but was later reprocessed because the insured was eligible for the services.

The reasons for such errors were due to system errors and/or human errors, (e.g., the optical control reader application may have captured incorrect information during the document scanning process, a manual entry error was made during the data review function or an error was made by the claims specialist during adjudication.).

It is recommended that DDNY improve the claims adjudication processes to ensure that claims are adjudicated correctly.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination, as of December 31, 2011, contained the following eight (8) comments and recommendations (page number refers to the prior report on examination):

<u>ITEM NO.</u>		<u>PAGE NO.</u>
	<u>Corporate Governance</u>	
1.	It is recommended that the Plan adhere to the guidance promulgated under the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing by insuring that the Internal Audit Enterprise reports functionally to the Audit Committee, with informal reporting to the Plan's management.	8
	<i>The Plan has complied with this recommendation.</i>	
2.	It is recommended that the Board of Directors adopt written procedures that require the Board to obtain annual certifications from either the Plan's director of internal audit or independent CPA that the responsible officers have implemented procedures adopted by the Board, and from the Plan's general counsel, a statement that the Plan's current claims adjudication procedures, including those set forth in current claims manual, are in accordance with applicable New York State statutes, rules and regulations, as mandated by Department Circular Letter No. 9 (1999).	8
	<i>The Plan has complied with this recommendation.</i>	
3.	It is also recommended that the Plan's Board of Directors obtain annual certifications from its third-party claims administrators that claims are being processed in accordance with the Plan's current claims manual and applicable New York State statutes, rules and regulations, as mandated by Department Circular Letter No. 9 (1999).	9
	<i>The Plan has complied with this recommendation.</i>	
	<u>Holding Company System</u>	
4.	It is recommended that the Plan file with the Department, the DeltaCare USA Administration Agreement, pursuant to the requirements of by Section 1505(d)(3) of the New York Insurance Law.	14
	<i>The Plan has complied with this recommendation.</i>	

ITEM NO.**PAGE NO.**Complaint Log

5. It is recommended that the Plan maintain its complaint logs fully in the manner prescribed by Department Circular Letter 11 (1978). 20

The Plan has complied with this recommendation.

Record Retention

6. It is recommended that DDNY maintain the application/enrollment forms of its groups for at least 6 calendar years after the date the policy is no longer in force or until after the filing of the report on examination in which the record was subject to review, whichever is longer, as required by Section 243.2(b)(1)(ii)(8) of Department Regulation 152 (11 NYCRR 243.2). 21

The Plan has complied with this recommendation.

Prompt Pay Law

7. It is recommended that the Plan take steps to ensure compliance with Section 3224-a(a) of the New York Insurance Law. 24

The Plan has complied with this recommendation.

8. It is recommended that the Plan take steps to ensure compliance with Section 3224-a(b) of the New York Insurance Law regarding the denial of its claims. 25

The Plan has complied with this recommendation.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A.	<u>Grievances</u>	
	As a best practice, it is recommended that DDNY include in its grievance determination letters the procedures on how to file an appeal to an adverse determination.	15
B.	<u>Claims Processing</u>	
	It is recommended that DDNY improve the claims adjudication processes to ensure that claims are adjudicated correctly.	16

Respectfully submitted,

Tommy Kong, CFE, PIR
Financial Services Examiner 2

STATE OF NEW YORK)
)SS.
)
COUNTY OF NEW YORK)

Tommy Kong, being duly sworn, deposes and says that the foregoing report submitted by him is true to the best of his knowledge and belief.

Tommy Kong, CFE, PIR

Subscribed and sworn to before me
this ____ day of _____ 2018

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

I, MARIA T. VULLO, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:

Tommy Kong

as a proper person to examine the affairs of

Delta Dental of New York, Inc.

and to make a report to me in writing of the condition of said

Plan

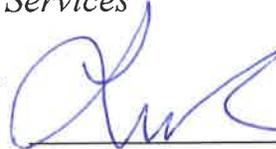
with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed my name
and affixed the official Seal of the Department
at the City of New York

this 21st day of November, 2016

MARIA T. VULLO
Superintendent of Financial
Services

By:



Lisette Johnson
Bureau Chief
Health Bureau

