

JUN 30 1995

## STATE OF ARIZONA

## DEPARTMENT OF INSURANCE

DEPARTMENT OF INSURANCE  
By *llc*

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2  
3 In the Matter of )  
4 DENTAL HEALTH CLUBS, INC.; )  
5 NELSON C. KRUM, JR.; WALTER J. )  
6 VENERABLE, JR., )  
7 Respondents. )

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Docket No. 95-097-F

**ORDER**

8           On May 5, 1995, the Director issued a Cease and Desist  
9 Order against Dental Health Clubs, Inc., Nelson C. Krum, Jr., and  
10 Walter J. Venerable, Jr. ("Respondents"). On May 8, Respondents'  
11 counsel, Frederick A. Schaffer, Jr., filed with the Arizona  
12 Department of Insurance (the "Department") a Demand for Hearing.  
13 The Department issued a Notice of Hearing dated May 9, 1995 which  
14 was mailed/delivered to the Respondents on May 10, 1995. The  
15 Department issued and mailed/delivered to the Respondents a  
16 Notice of Stay of the Director's Cease and Desist Order on May  
17 10, 1995.

18           On May 30, 1995, a hearing was held in the  
19 above-captioned matter before Administrative Law Judge Lewis D.  
20 Kowal. Assistant Attorney General Gerrie L. Switzer appeared on  
21 behalf of the Department and Augustine Jiminez III appeared on  
22 behalf of the Respondents.

23           Based upon the entire record in this matter, including  
24 all pleadings, motions, testimony, and exhibits admitted during  
25 the hearing of this matter, Administrative Law Judge Lewis D.  
26 Kowal has prepared the following Findings of Fact, Conclusions of  
27 Law, and Order for consideration and approval by the Director of  
28 the Arizona Department of Insurance (the "Director"). The

1 Director adopts and enters the following Findings of Fact,  
2 Conclusions of Law and enters the following Order:

3 FINDINGS OF FACT

4 1. At all times material to this action, Respondent  
5 Dental Health Clubs, Inc. ("DHC") was an Arizona Corporation.

6 2. At all times material to this action, DHC was not  
7 authorized to transact the business of insurance in Arizona as a  
8 Prepaid Dental Plan Organization or otherwise.

9 3. At all times material to this action, DHC was not  
10 operating under a certificate of authority issued by the Director  
11 pursuant to A.R.S. §20-1001 et seq.

12 4. At all times material to this action, Respondent  
13 Nelson C. Krum, Jr. ("Dr. Krum") was a shareholder, director and  
14 the president of DHC.

15 5. At all times material to this action, Respondent  
16 Walter J. Venerable, Jr. ("Dr. Venerable") was a shareholder,  
17 director and the vice-president of DHC.

18 6. On October 12, 1994, Dr. Krum and Dr. Venerable  
19 executed the Articles of Incorporation of DHC which were filed  
20 with the Arizona Corporation Commission on October 18, 1994.

21 7. Since October 18, 1994, Dr. Krum and Dr. Venerable  
22 have operated DHC without obtaining or applying for a certificate  
23 of authority to be issued by the Director.

24 8. In a letter dated November 24, 1993, Assistant  
25 Attorney General Mark Sendrow informed Dr. Krum that his dental  
26 health club concept may be subject to regulation by the  
27 Department pursuant to A.R.S. §20-1001 et seq.  
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1                   9. In a letter dated December 1, 1993, Charles R.  
2 Cohen, Assistant Deputy Director of the Department, advised Dr.  
3 Krum that upon review of certain literature, it appeared that his  
4 dental health club concept may be a prepaid dental plan. Mr.  
5 Cohen further advised Dr. Krum that in order for a prepaid dental  
6 plan to transact business in Arizona, a certificate of authority  
7 must be obtained from the Department.

8                   10. In a letter to Mr. Cohen dated December 7, 1993,  
9 Dr. Krum stated that he had stopped his efforts to develop his  
10 dental office concept in Green Valley, Arizona. Dr. Krum further  
11 stated that he would not continue with those efforts until the  
12 issue of whether his dental office concept falls under the  
13 "supervision of the Department" was resolved.

14                   11. The dental plan concept which Dr. Krum presented  
15 to residents of Green Valley, Arizona is the same dental plan  
16 concept used by DHC.

17                   12. DHC provides certain general dental services to  
18 its members at no additional cost but for the membership fee.  
19 The cost of any required outside lab work is at wholesale cost.  
20 DHC members pay for any outside lab work by either providing  
21 payment to DHC to be forwarded to the lab or by paying the lab  
22 directly. For any other dental services, members are referred  
23 out to specialists.

24                   13. DHC obtains or has obtained income from the  
25 following: a) fee for service patients who are billed at the  
26 usual and customary rates; b) referral plans (American Dental and  
27 Savon Dental) where certain dental services are performed at no  
28 charge to members of the referral plans and other dental services

1 are charged at discounted rates which the member/patient pays  
2 directly to DHC; and c) until March, 1995, DHC had an arrangement  
3 with two capitated plans (National Dental and U.S. Dental) where,  
4 for a capitated monthly amount per patient, DHC agreed to perform  
5 certain types of dental services to the member/patient at no  
6 charge and perform other dental services at a discounted rate.

7 14. Since October, 1994, residents of Arizona have  
8 been solicited to become members of DHC's prepaid dental health  
9 plan.

10 15. DHC currently has approximately 400 members  
11 enrolled in its dental health plan.

12 16. DHC has conducted solicitations of members  
13 directly and through agents, some of whom are licensed insurance  
14 agents.

15 17. Agents who solicit Arizona residents for  
16 membership in DHC receive a 15% commission fee. The membership  
17 fees are paid directly to DHC. After processing, DHC remits the  
18 commission to the agents.

19 18. Since October, 1994, DHC has charged and collected  
20 membership fees and entered into contractual arrangements to  
21 provide general dental services to its members on a prepaid  
22 basis. Because DHC provides 100% of the cost of general dental  
23 services to its members, there is no remaining portion of general  
24 dental services which requires payment or reimbursement.

25 19. Since October, 1994, DHC has distributed or made  
26 available advertising material regarding the operation of DHC and  
27 its services.

28

1           20. DHC has not had its form of membership, sales or  
2 advertising material filed with or approved by the Director.

3           21. Dr. Krum determined the amount of the annual  
4 membership fee of DHC's prepaid dental health plan to be charged  
5 to Arizona residents based upon a review of his Colorado private  
6 practice patient files. Dr. Krum did not use any actuarial  
7 analysis, underwriting guidelines or financial analysis as to the  
8 cost of operating a dental office in Arizona in determining the  
9 amount of the annual membership fee.

10           22. DHC has not established any eligibility  
11 requirements for club membership other than payment of the annual  
12 membership fee or a contractual arrangement for payment of the  
13 annual membership fee.

14           23. DHC does not have a contingency plan to provide  
15 financial security to its members if the membership fees do not  
16 meet the costs of dental services required by its members.

17           24. The Dental Health Club Agency Agreement (Exhibit  
18 #27) which DHC provides to its agents states that the arrangement  
19 entered into between DHC and its members is not an insurance  
20 policy. That statement is untrue, deceptive or misleading  
21 because the dental health plan agreements entered into between  
22 DHC and its members are insurance policies.

23           25. Dental Health Club's brochure (Exhibit #21) states  
24 "Unlimited Dental Services for One Low Fee." That statement is  
25 untrue, deceptive or misleading because DHC does not provide all  
26 dental services for one low fee. DHC only provides general  
27 dental services to DHC members for one low fee.

1 26. Based upon the totality of the facts and  
2 circumstances concerning DHC's formation and operation, DHC has  
3 at all times material to this matter operated as and is a prepaid  
4 dental health plan organization with respect to its club  
5 membership activities.

6 27. Because Dr. Krum and Dr. Venerable erroneously  
7 determined that DHC was not a prepaid dental plan organization  
8 within the meaning of A.R.S §20-1001, Respondents have knowingly  
9 failed to comply with the requirements of A.R.S. §20-1001 et seq.

#### 10 DISCUSSION

##### 11 Issue

12 The key issue in this matter is whether DHC is a  
13 prepaid dental plan organization which must obtain a certificate  
14 of authority issued by the Director in order to transact business  
15 in Arizona.

##### 16 Jurisdiction

17 Pursuant to A.R.S. §20-115, any person or entity that  
18 provides coverage for dental expenses is presumed to be subject  
19 to jurisdiction by the Department "unless the person or other  
20 entity shows that while providing coverage it is subject to the  
21 jurisdiction of another agency of this state, any political  
22 subdivision of this or any other state or the federal government."

23 For the presumption of jurisdiction under A.R.S.  
24 §20-115 to apply, there must be coverage of dental expenses "by  
25 direct payment, reimbursement or otherwise." Through payment of  
26 a membership fee, DHC provides members with general dental  
27 services at no additional cost. Those general dental services  
28 are "covered" by DHC through its compensation of the DHC dentist

1 and other DHC employees and payment of the costs of supplies used  
2 for the general dental services. In the opinion of the  
3 undersigned Administrative Law Judge, this arrangement falls  
4 within the scope of A.R.S. §20-115 because while it is not direct  
5 reimbursement, the arrangement qualifies as the "otherwise" type  
6 of coverage within the meaning of A.R.S. §20-115. Thus, the  
7 Department has jurisdiction over the Respondents pursuant to  
8 A.R.S. §20-115.

9 Prepaid Dental Organization

10 A person who establishes or operates a prepaid dental  
11 organization must obtain and maintain a certificate of  
12 authority. A.R.S. §20-1002. The term "person" is defined as  
13 being "an individual, company, insurer, association,  
14 organization, society, reciprocal or inter-insurance exchange,  
15 partnership, syndicate, business trust, corporation and entity."  
16 A.R.S. §20-105.

17 A prepaid dental plan organization is "any person who  
18 undertakes to conduct one or more prepaid dental plans providing  
19 only dental services." A.R.S. §20-1001(4) (emphasis added). A  
20 prepaid dental plan is "any contractual arrangement whereby any  
21 prepaid dental organization undertakes to provide directly or to  
22 arrange for prepaid dental services and to pay or make  
23 reimbursement for any remaining portion of such prepaid dental  
24 services on a prepaid basis through insurance or otherwise."  
25 A.R.S. §20-1001(3).

26 Respondents admit that DHC provides prepaid dental  
27 services. Dr. Krum testified that he formed DHC to provide  
28 prepaid dental services to DHC members. Although the statutory

1 definition of a prepaid dental plan states that a prepaid dental  
2 organization directly provide or arrange prepaid dental services  
3 and pay or reimburse of any remaining portion of the dental  
4 services, for purposes of being a prepaid dental plan  
5 organization the prepaid dental plan must provide only dental  
6 services.

7           By virtue of an annual membership fee, DHC members are  
8 provided certain general dental services at no additional cost.  
9 DHC has been structured so that there is no "remaining portion"  
10 to be paid or reimbursed because 100% of the cost of the prepaid  
11 dental services is assumed by DHC.

12           The Department contends that pursuant to A.R.S.  
13 §20-1002, DHC is a prepaid dental organization which must obtain  
14 and maintain a certificate of authority. In its interpretation  
15 of the term "prepaid dental plan," the Department maintains that  
16 a prepaid dental organization qualifies as a prepaid dental plan  
17 even if there is no remaining portion of prepaid dental services  
18 to be paid or reimbursed by insurance or otherwise.

19           Respondents contend that the Legislature established a  
20 two-pronged test within definition of prepaid dental plan:  
21 1) that the prepaid dental organization must directly provide or  
22 arrange prepaid dental services; and 2) that there must be  
23 payment or reimbursement of the remaining portion of the prepaid  
24 dental services on a prepaid basis.

25           Respondents assert that there is no remaining portion  
26 to be paid or reimbursed because all general dental services are  
27 covered through club membership. Therefore, Respondents claim  
28



1 that the second prong within the definition of prepaid dental  
2 plan is not satisfied.

3 Respondents interpret A.R.S. §20-1001(3) to mean that  
4 if the terms of a plan which provides directly or arranges for  
5 prepaid dental services eliminates the existence of any amount  
6 owed for those services after payment of a membership fee, the  
7 plan does not constitute a prepaid dental plan.

8 The plain reading of A.R.S. §20-1001(3) indicates the  
9 Legislature intended to regulate plans that purport to satisfy  
10 all of a member's financial obligation in connection with the  
11 prepaid dental services. The statute further indicates the  
12 Legislature's intent to also regulate plans that satisfy only a  
13 portion of the member's financial obligation in connection with  
14 those dental services whose remaining portion is paid or  
15 reimbursed by insurance or otherwise.

16 The language used in A.R.S. §20-1001(3) clearly shows  
17 that intent by inclusion of the phrase "for any remaining  
18 portion" (emphasis added). If no remaining portion exists, then  
19 the need for additional payment or reimbursement also does not  
20 exist. Thus, the use of the term "any" qualifies the term  
21 "remaining portion" and can only mean that to the extent that any  
22 remaining portion exists, in order to be a prepaid dental plan,  
23 the plan must provide for payment or reimbursement of the  
24 remaining portion.

25 DHC's financial structure and its ability to be  
26 profitable flows from the premise that not all members will  
27 require dental services and that the membership fees collected  
28 will exceed the volume of dental services needed. However, if

1 that target membership level is never reached or if all or a  
2 majority of members require extensive general dental services,  
3 DHC does not guarantee that it will be able to provide its  
4 members the services required or that DHC will have the financial  
5 resources to provide membership refunds to DHC members.

6 This situation appears to be exactly what the  
7 Legislature intended to regulate when it delegated authority to  
8 the Department to regulate prepaid dental organizations. The  
9 Legislature intended to ensure coverage to members of prepaid  
10 dental plan organizations for dental services regardless of  
11 whether the coverage paid all of the costs of the dental service  
12 or made or arranged for reimbursement of any remaining portion.  
13 The legislative intent would be defeated if a dental plan  
14 organization could avoid regulation by structuring the dental  
15 plan in a manner so no remaining portion exists.

16 Based upon the above analysis, it is determined that  
17 DHC is a prepaid dental organization within the meaning of A.R.S.  
18 §20-1001(4).

#### 19 CONCLUSIONS OF LAW

20 1. The Director has jurisdiction over this matter  
21 pursuant to A.R.S. §§20-161 and 20-401.02.

22 2. The Department has jurisdiction over the  
23 Respondents Dental Health Clubs, Inc., Nelson C. Krum, Jr., and  
24 Walter J. Venerable, Jr., pursuant to A.R.S. §§20-115 and 20-161.

25 3. Respondent Dental Health Clubs, Inc. is a prepaid  
26 dental organization within the meaning of A.R.S. §§20-1001(4) and  
27 20-1002(A).

1                   4. Respondent Dental Health Clubs, Inc. has been  
2 established and is operating in Arizona as a prepaid dental plan  
3 organization without obtaining and maintaining a certificate of  
4 authority issued by the Director in violation of A.R.S. §20-1001  
5 et seq.

6                   5. Respondents Dental Health Clubs, Inc., Nelson C.  
7 Krum, Jr., and Walter J. Venerable, Jr. are transacting the  
8 business of insurance within the meaning of A.R.S. §§20-103,  
9 20-106, 20-107 and 20-401.01.

10                   6. Respondents Dental Health Clubs, Inc., Nelson C.  
11 Krum, Jr., and Walter J. Venerable, Jr. have violated and are in  
12 violation of the provisions of A.R.S. §§20-107 and 20-401.01.

13                   7. Based upon all of the above Findings of Fact  
14 contained in paragraphs 1 through 27, Respondents Dental Health  
15 Clubs, Inc., Nelson C. Krum, Jr., and Walter J. Venerable, Jr.  
16 have knowingly failed to comply with the provisions of A.R.S.  
17 §20-1001 et seq.

18                   8. Pursuant to A.R.S. §§20-401.02 and 20-456, the  
19 Director has the authority to issue a cease and desist order  
20 against Respondents Dental Health Clubs, Inc., Nelson C. Krum,  
21 Jr., and Walter J. Venerable, Jr.

22                   9. Respondent Dental Health Clubs, Inc. has violated  
23 A.R.S. §§20-443 and 20-444 by making, issuing or circulating or  
24 causing the making, issuance, circulation or placement before the  
25 public, of untrue, deceptive or misleading material within the  
26 meaning of A.R.S. §§20-443 and 20-444.

27 . . .

28 . . .

ORDER

IT IS ORDERED that:

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3 1. The Director's Cease and Desist Order dated May  
4 5, 1995 remain in full force and effect and the Stay of the Cease  
5 and Desist Order issued pursuant to A.R.S. §20-162(A) is no  
6 longer in effect.

7 2. Respondents Dental Health Clubs, Inc., Nelson C.  
8 Krum, Jr., and Walter J. Venerable, Jr. shall cease and desist  
9 from violating the provisions of A.R.S. §§20-107, 20-401.01 and  
10 20-1001 et seq.

11 3. Pursuant to A.R.S. §20-456, Respondent Nelson C.  
12 Krum, Jr. shall pay a civil penalty to the Arizona Department of  
13 Insurance in the amount of \$5,000.00 within 20 days of the date  
14 of this Order.

15 4. Pursuant to A.R.S. §20-456, Respondent Walter J.  
16 Venerable, Jr. shall pay a civil penalty to the Arizona  
17 Department of Insurance in the amount of \$5,000.00 within 20 days  
18 of the date of this Order.

19 5. Pursuant to A.R.S. §20-456, Respondent Dental  
20 Health Clubs, Inc. shall pay a civil penalty to the Arizona  
21 Department of Insurance in the amount of \$15,000.00 within 20  
22 days of the date of this Order.

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6. Respondent Dental Health Clubs, Inc. shall remit to the Arizona Department of Insurance all taxes due together with interest and penalties pursuant to A.R.S. §§20-1010 and 20-225.

EFFECTIVE this 30th day of June, 1995.

*Chris Herstam*

CHRIS HERSTAM  
Director of Insurance

*Lewis D. Kowal*

LEWIS D. KOWAL  
Administrative Law Judge

NOTIFICATION OF RIGHTS

The aggrieved party may request a rehearing with respect to this Order by filing a written petition with the Administrative Law Division within 30 days of the date of this Order, setting forth the basis for such relief pursuant to A.A.C. R20-6-114(B).

The final decision of the Director may be appealed to the Superior Court of Maricopa County for judicial review pursuant to A.R.S. § 20-166.

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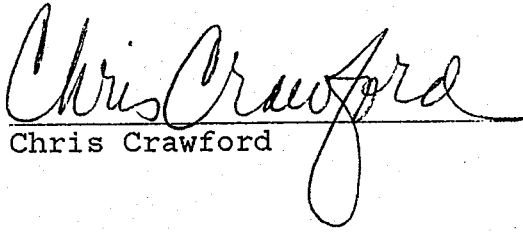
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COPY of the foregoing mailed/delivered  
this 30th day of June, 1995, to:

Gay Ann Williams, Deputy Director  
Charles R. Cohen, Executive Assistant Director  
Erin H. Klug, Executive Assistant  
Gary A. Torticill, Assistant Director  
Catherine O'Neil, Assistant Director  
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