

REPORT OF EXAMINATION
OF THE
ALLIANCE UNITED INSURANCE COMPANY
AS OF
DECEMBER 31, 2011

Filed March 12, 2013

TABLE OF CONTENTS

	<u>PAGE</u>
SCOPE OF EXAMINATION.....	1
SUBSEQUENT EVENT	2
COMPANY HISTORY	2
MANAGEMENT AND CONTROL:	3
Management Agreements	5
TERRITORY AND PLAN OF OPERATION	6
REINSURANCE:	6
Assumed.....	6
Ceded	6
FINANCIAL STATEMENTS:.....	7
Statement of Financial Condition as of December 31, 2011	8
Underwriting and Investment Exhibit for the Year Ended December 31, 2011.....	9
Reconciliation of Surplus as Regards Policyholders from December 31, 2007 through December 31, 2011	10
COMMENTS ON FINANCIAL STATEMENT ITEMS:.....	11
Losses and Loss Adjustment Expenses.....	11
Taxes, Licenses and Fees	11
SUMMARY OF COMMENTS AND RECOMMENDATIONS:.....	11
Current Report of Examination.....	11
Previous Report of Examination.....	11
ACKNOWLEDGMENT.....	13

Los Angeles, California
December 21, 2012

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

ALLIANCE UNITED INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 5300 Adolfo Road, Suite #200, Camarillo, California 93012.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2007. This examination covers the period from January 1, 2008 through December 31, 2011. The examination was conducted in accordance with the National Association of Insurance Commissioners' Financial Condition Examiners' Handbook. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, to identify prospective risks, and to obtain information about the Company, including corporate governance, identification and assessment of inherent risks, and the evaluation of the system controls and procedures used to mitigate those risks. The examination also included an assessment of the principles used and the significant estimates made by management, as well as an evaluation of the overall financial statement presentation, and management's compliance with Statutory Accounting Principles and Annual Statement instructions. All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; pensions; stock ownership and insurance plans; growth of company; loss experience; accounts and records; statutory deposits; and sales and advertising.

SUBSEQUENT EVENT

During 2012, the Company received \$14.5 million in capital contributions from its parent, Alliance United Group (AUG). California Bank & Trust loaned AUG \$15 million in July 2012. The loan was secured by a general collateralization of AUG's assets.

On July 1, 2012, the Company amended its quota share reinsurance agreement with Maiden Reinsurance Company by decreasing its participation from 45% to 30%.

The Company has been under a Regulatory Agreement with the California Department of Insurance (CDI) since August 15, 2006. The agreement requires the Company to maintain a net premium-to-surplus ratio of not greater than 3-to-1. On January 11, 2012, the Company filed corporate application with the CDI requesting a termination of the Regulatory Agreement. In July 2012, the Company withdrew its application and replaced it with a new corporate application requesting to amend the ratio from 3-to-1 to 3.5-to-1. The CDI approved the application on December 21, 2012.

COMPANY HISTORY

The Company was incorporated in California on December 17, 1997 as Millennium Insurance Company and commenced business on June 30, 1998. On January 1, 2004, Alliance United Group (AUG) purchased the Company from GuideOne Financial Group, Inc., and changed the name of the Company to its current name.

On December 23, 2005, Platinum Group of Companies (Platinum) and Mr. David Mandel, the ultimate controlling individual of Platinum, requested approval from the California Department of

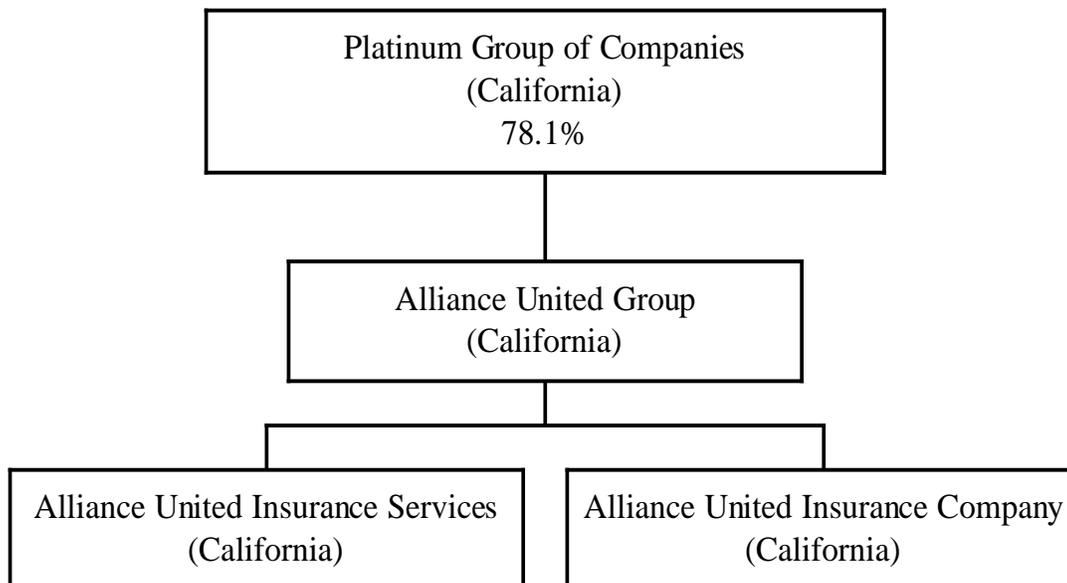
Insurance (CDI) to acquire indirect control of the Company through a purchase of 42,932 shares, or 56%, of the authorized but unissued class A common stock of AUG. On August 15, 2006, the CDI approved this request and concurrently entered into a Regulatory Agreement with Mr. Mandel, Platinum, and the Company, setting conditions for control of the Company. These conditions include, but are not limited to: maintaining a risk based capital of 300% or greater; maintaining a premium to surplus ratio of not greater than 3 to 1; no dividends can be declared by the Company during the first three years following the acquisition of control; the Company may not write any business other than automobile insurance without prior consent from the CDI in each instance; and the Company must attempt to retain the services of its senior management for the five years following the acquisition of control.

During 2008, 2009, 2010, and 2011, the Company authorized stock repurchase programs that brought his total holding to 49,718 shares or 78% of the outstanding stock of AUG.

As of December 31, 2011, Platinum owned 78% of the outstanding shares of AUG. The Company is wholly owned by AUG and ultimately controlled by Platinum. The capital contributions received from AUG were \$1.5 million, \$1.5 million, \$500 thousand and \$2.2 million for 2008, 2009, 2010, and 2011, respectively.

MANAGEMENT AND CONTROL

The following abridged organizational chart, which is limited to the Company's ultimate parent along with its subsidiaries, depicts the Company's relationship within the holding company system:



(*) All ownership is 100% unless otherwise noted.

Management of the Company is vested in a six-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2011 follows:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Kjell Paul Austad Encino, California	Secretary and Vice President Alliance United Insurance Company
David Earl Beck Northridge, California	Board Member Los Angeles Office of Managed Care
Louis Craig Borstelmann Northridge, California	Chief Financial Officer and Treasurer Alliance United Insurance Company
Philip Brad Hinkle Newbury Park, California	Vice President Alliance United Insurance Company
David Mandel Chatsworth, California	President and Chief Executive Officer Platinum Group of Companies

Name and Residence

Principal Business Affiliation

Jeffrey Carl Molino
Camarillo, California

Underwriting and Compliance Manager
Alliance United Insurance Company

Principal Officer

Name

Title

David Mandel
Phillip Bradley Hinkle
Kjell Paul Austad
Louis Craig Borstelmann

President and Chief Executive Officer
Vice President
Secretary and Vice President
Chief Financial Officer and Treasurer

Management Agreements

Administrative Services Agreement: The Company has an Administrative Services Agreement, effective January 1, 2004, with its affiliate, Alliance United Insurance Services (AUIS). Under the terms of the agreement, AUIS provides facilities, insurance administrative, and management support services continuously for the Company to conduct its business. The services include, but is not limited to, financial reporting, tax, treasury services, budget and cost accounting, human resources, payroll, electronic fund transfers, legal, office services, actuarial, investment management, computer, marketing and corporate affairs and graphic arts. AUIS also provides office space to the Company. The Company reimburses AUIS for actual expenses incurred on a monthly basis. Payments made to AUIS for 2008, 2009, 2010, and 2011, were \$140,918, \$241,587, \$349,429, and \$836,477, respectively. The California Department of Insurance (CDI) approved this agreement on February 12, 2004. On November 18, 2011, the Company amended this agreement to sublease the office space from AUIS in Camarillo, California. The amendment was approved by the CDI on November 18, 2011.

Tax Reimbursement Agreement: The Company and its affiliates are parties to a consolidated federal income tax agreement with its parent, Alliance United Group dated January 1, 2004. Under the terms of the agreement, allocation of taxes is based upon separate return calculations with inter-company tax balances settled in the quarter subsequent to the filing of the consolidated return. The CDI approved this agreement on February 12, 2004. On March 9, 2009, the Company amended this

agreement by replacing its previous name, Millennium Insurance Company, with its current name.

Agency Agreement: Effective January 1, 2004, the Company entered into an agency agreement with AUIS. Under the terms of the agreement, AUIS has authority to process policies, collect premiums and perform responsibilities typical of a servicing general agent. Premium settlements are made within 30 days after each month of collection. The CDI approved the agreement on February 12, 2004. The Company made an amendment to have its previous name, Millennium Insurance Company, replaced with its current name. The amendment was approved by the CDI on March 20, 2008.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to write Fire, Marine, Disability, Plate Glass, Liability, Common Carrier Liability, Boiler and Machinery, Burglary, Sprinkler, Team & Vehicle, Automobile, and Miscellaneous coverage in the State of California.

The business is produced by a network of insurance agencies through its affiliated general agent, Alliance United Insurance Service (AUIS), a wholly owned subsidiary of AUG. In 2011, the Company wrote \$105 million of direct premiums. Of the direct premium written, 74.5% was non-standard private passenger auto liability and 25.5% was physical damage.

REINSURANCE

Assumed

The Company does not assume any reinsurance.

Ceded

The following is a summary of the principal ceded reinsurance treaties inforce as of December 31, 2011:

Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Limits
Quota Share	Maiden Reinsurance Company	55% per Occurrence	45% per occurrence up to \$100K
Excess of Loss	Maiden Reinsurance Company	Bodily Injury \$100,000 per Occurrence	Bodily Injury \$250,000 excess of \$100,000 per occurrence
		Physical Damage \$100,000 per occurrence	Physical Damage \$1 million excess of \$100,000 per occurrence

Maiden Reinsurance Company is an authorized reinsurer. As of December 31, 2011, reinsurance recoverables for all ceded reinsurance totaled \$4.5 million.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2011

Underwriting and Investment Exhibit for the Year Ended December 31, 2011

Reconciliation of Surplus as Regards Policyholders from December 31, 2007 through December 31, 2011

Statement of Financial Condition
as of December 31, 2011

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 48,521,937	\$	\$ 48,521,937	
Preferred stocks	493,751		493,751	
Common stocks	30,731		30,731	
Cash and short-term investments	3,293,195		3,293,195	
Investment income due and accrued	369,548		369,548	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	13,177,522		13,177,522	
Amount recoverable from reinsurers	4,484,289		4,484,289	
Current federal and foreign income tax recoverable and interest thereon	178,932		178,932	
Net deferred tax asset	1,341,408	226,239	1,115,169	
Receivables from parent, subsidiaries and affiliates	1,352,437		1,352,437	
Aggregate write-ins for other than invested assets	<u>49,357</u>	<u>49,356</u>	<u>0</u>	
Total assets	<u>\$ 73,293,107</u>	<u>\$ 275,596</u>	<u>\$ 73,017,511</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 19,831,655	(1)
Loss adjustment expenses			8,329,001	
Commissions payable, contingent commissions and other similar charges			8,197,235	
Other expenses			579,964	
Taxes, licenses and fees			337,060	(2)
Unearned premiums			10,687,962	
Ceded reinsurance premiums payable			5,143,056	
Aggregate write-ins for liabilities			<u>116,029</u>	
Total liabilities			53,221,962	
Common capital stock		\$ 2,600,000		
Gross paid in and contributed surplus		18,900,000		
Unassigned funds (surplus)		<u>(1,704,451)</u>		
Surplus as regards policyholders			<u>19,795,549</u>	
Total liabilities, surplus and other funds			<u>\$ 73,017,511</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2011

Statement of Income

Underwriting Income

Premiums earned		\$ 57,972,478
Deductions:		
Losses	\$ 38,735,643	
Loss expenses incurred	13,920,071	
Other underwriting expenses incurred	<u>8,987,147</u>	
Total underwriting deductions		<u>61,642,861</u>
Net underwriting loss		(3,670,383)

Investment Income

Net investment income earned	\$ 1,390,073	
Net realized capital gain	<u>284,905</u>	
Net investment gain		1,674,978

Other Income

Aggregate write-ins for miscellaneous income	<u>\$ (13,297)</u>	
Total other income		<u>(13,297)</u>
Net income before federal income taxes		(2,008,702)
Federal income taxes incurred		<u>(799,910)</u>
Net loss		<u>\$ (1,208,792)</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2010		\$ 18,692,478
Net income	\$ (1,208,792)	
Change in net unrealized capital gains	(12,058)	
Change in net deferred income tax	43,485	
Change in nonadmitted assets	80,436	
Surplus adjustments: Paid in	<u>2,200,000</u>	
Change in surplus as regards policyholders for the year		<u>1,103,071</u>
Surplus as regards policyholders, December 31, 2011		<u>\$ 19,795,549</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2007 through December 31, 2011

Surplus as regards policyholders, December 31, 2007 per Examination				\$ 12,084,900
		<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$	1,017,446	\$	
Change in net unrealized capital losses			116,746	
Change in net deferred income tax		917,542		
Change in non-admitted assets		192,407		
Surplus adjustments: Paid-in		<u>5,700,000</u>		
Total gains and losses	\$	<u>7,827,395</u>	\$	<u>116,746</u>
Net increase in surplus as regards policyholders				<u>7,710,649</u>
Surplus as regards policyholders, December 31, 2011, per Examination				<u>\$ 19,795,549</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on the analysis by a Senior Casualty Actuary from the California Department of Insurance (CDI), the Company's December 31, 2011 reserves for losses and loss adjustment expenses were determined to be deficient by \$656,000. No adjustment to the Company financials is necessary as the amount is immaterial.

(2) Taxes, Licenses and Fees

The Company did not report the fees received from the insured for finance and administrative charges in its 2010 and 2011 premium tax returns. It is recommended that the Company file amended premium tax returns for 2010 and 2011 with the CDI, and report all fees received during 2010 and 2011.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Comments on Financial Statement Items – Taxes, Licenses and Fees (Page 11): It is recommended that the Company file amended premium tax returns for 2010 and 2011 with the California Department of Insurance.

Previous Report of Examination

Management and Control - Management Agreements - Tax Sharing Agreement (Page 4): It was recommended that the tax sharing agreement be amended to include the current names of all participants. The Company has complied with the recommendation.

Corporate Records - (Page 5): It was recommended that the Company obtain conflict of interest

statements from its officers, directors, and key employees on an annual basis. It was also recommended that the Company prepare detailed board of directors' minutes during each of its meetings. The Company has complied with the recommendation.

Accounts and Records - (Page 7): It was recommended that the Company maintain documentation to support all financial statement accounts. The documentation should be prepared in sufficient detail as to allow for a full and complete audit trail from the Annual Statement to individual records. The Company has complied with the recommendation.

Accounts and Records - Information System Controls (Page 7): It was recommended that the Company prepare a written disaster recovery plan for its information systems. The Company has complied with the recommendation.

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

_____/S/_____
Millie Cao, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California