REPORT OF EXAMINATION

OF THE

AAA NORTHERN CALIFORNIA, NEVADA

& UTAH INSURANCE EXCHANGE

AS OF

DECEMBER 31, 2011

Filed June 25, 2013

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San Francisco, California
May 10, 2013

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

AAA NORTHERN CALIFORNIA, NEVADA & UTAH INSURANCE EXCHANGE

(hereinafter also referred to as the Exchange) at its home office located at 3055 Oak Road, Walnut Creek, California 94597.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Exchange. The previous examination of the Exchange was made as of December 31, 2008. This examination covers the period from January 1, 2009 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 Exchange's financial condition, to identify prospective risks, and to obtain information about the Exchange, 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 Exchange were considered in accordance with the risk-focused examination process.

The examination was a coordinated examination with participation from the Pennsylvania Insurance Department and New Jersey Department of Banking and Insurance, and was conducted concurrently with the examinations of other insurance entities in the holding company group, including Keystone Insurance Company, AAA Mid-Atlantic Insurance Company, and AAA Mid-Atlantic Insurance Company of New Jersey.

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

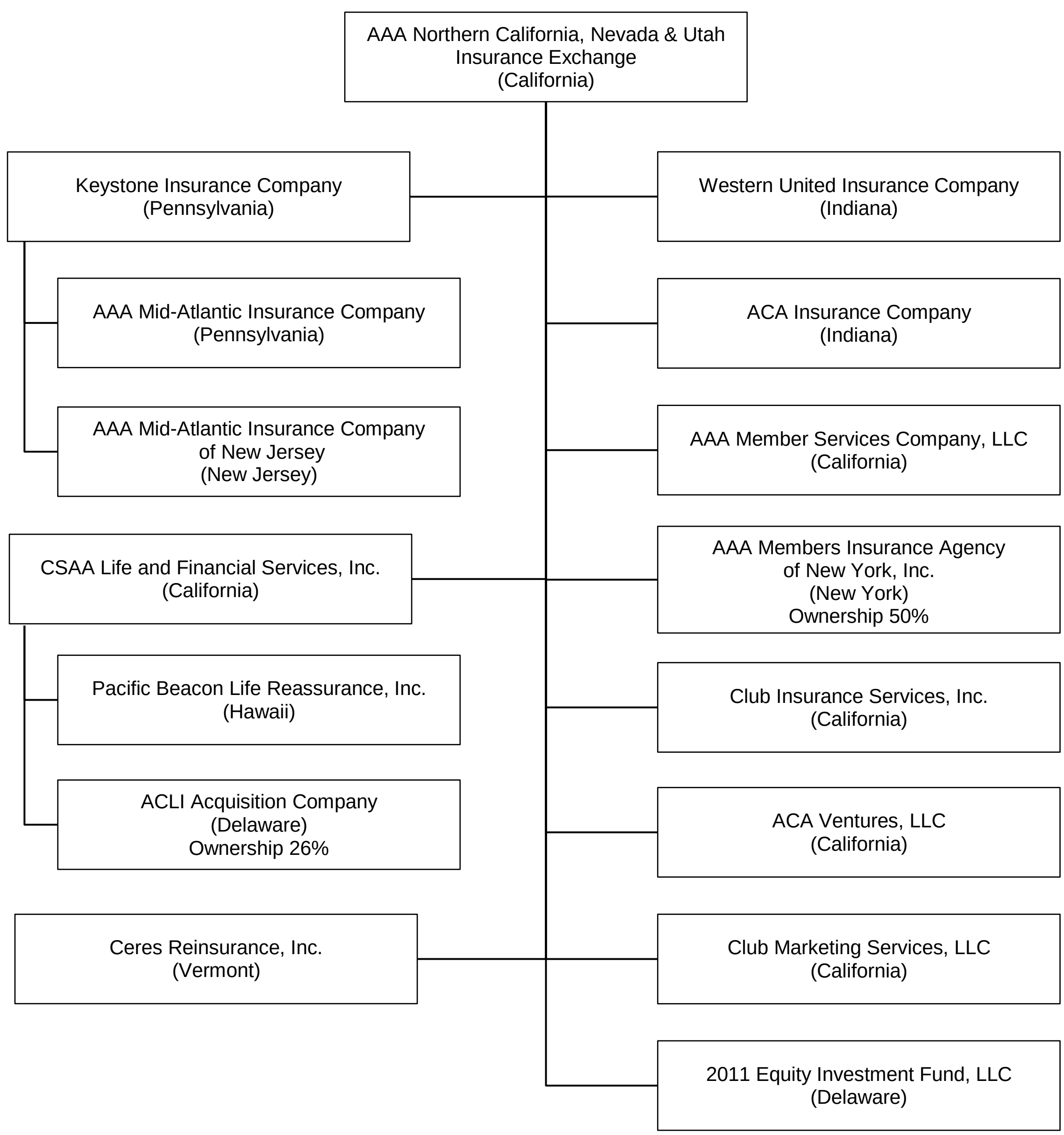
EXCHANGE HISTORY

The Exchange is a reciprocal exchange which was organized on June 20, 1914 and commenced business on August 14, 1914. It was sponsored by interests allied with the California State Automobile Association (CSAA), now called AAA Northern California, Nevada & Utah (Club), a motor club incorporated in 1907. The Exchange was created to offer insurance to members of the Club. The Exchange primarily writes private passenger automobile and homeowner coverages.

On January 1, 2011, the Club and the Exchange separated its management and Board of Directors. The separation of the employees and operations between the two entities occurred over the course of the year, with the majority of the separations occurring on July 1, 2011. On February 11, 2011, the California Department of Insurance (CDI) approved a Certificate of Authority changing the Exchange's name to AAA Northern California, Nevada, & Utah Insurance Exchange from California State Automobile Association Inter-Insurance Bureau.

MANAGEMENT AND CONTROL

As a reciprocal insurer, the Exchange has no shareholders and is not directly owned by any party. As of December 31, 2011, the Exchange is the ultimate parent of a holding company system with eleven directly owned and five indirectly owned subsidiaries. The following chart depicts the entities the Exchange had interrelationships with during the examination period (all ownership is 100% unless otherwise indicated):



The Exchange's Insurance Board consists of eleven members. Previously, nine of the members were independent and elected by the Board of Directors of AAA Northern California, Nevada & Utah (Club). The Chief Executive Officer of the Exchange and the Chief Executive Officer of AAA Club Partners, Inc. also serve as the ex officio voting members of the Insurance Board.

Under the amended Rules and Regulations dated July 26, 2011 that were filed with the California Department of Insurance (CDI), the members of the Insurance Board shall be elected by the Insurance Board (self-appointed). The members of the Board are elected annually.

Following are members of the Board and principal officers of the Exchange serving at December 31, 2011:

<u>Directors</u>

Name and Residence	Principal Business Affiliation
Robert N. Barone Reno, Nevada	Principal Ancora West Advisors
Jack E. Brown Cincinnati, Ohio	Retired
David C. Carney Jamison, Pennsylvania	Retired
Gilbert W. Chester Phoenix, Arizona	Principal WestCor Development Partners
Kenneth L. Coleman Los Altos Hills, California	Chairman Accelrys
Mary B. Cranston San Francisco, California	Senior Partner Pillsbury Winthrop Shaw Pittman LLP
Allen J. DeWalle Williamsburg, Virginia	Retired

Directors (continued)

Name and Residence	Principal Business Affiliation
Paula F. Downey Walnut Creek, California	President and Chief Executive Officer AAA Northern California, Nevada & Utah Insurance Exchange
Edgar H. Grubb, Chair Walnut Creek, California	Retired
James R. Pouliot Diablo, California	Chief Executive Officer AAA Club Partners, Inc.
Vivian M. Stephenson San Francisco, California	Retired

Principal Officers

Name	Title
Paula F. Downey*	President and Chief Executive Officer
Michael S. Day*	Chief Financial Officer and Treasurer
Michael J. Zukerman*	General Counsel and Secretary
Steven A. George	Chief Operating Officer
Stephen J. O'Connor	Chief Information Officer
Marie L. Andel	Chief Administrative Officer
Mary D'Agostino[a]	(Interim) Chief Marketing Officer

*Also served as Attorney-in-Fact

The following changes in management occurred subsequent to the examination date:

[a] Debora Tomlin was hired as the Chief Marketing Officer in August 2012.

Related Party Agreements

Intercompany Chargeback Agreement: Effective January 1, 2012, the agreement was entered into between the Exchange and the following subsidiaries: AAA Mid-Atlantic Insurance Company (AAA MAIC), AAA Mid-Atlantic Insurance Company of New Jersey (AAA MAICNJ), ACA Insurance Company (ACAIC), Keystone Insurance Company

(KIC), and Western United Insurance Company (WUIC). Under the terms of the agreement, the Exchange provides certain policy administration services and claims administration services for policies issued by the subsidiaries. The Exchange will be reimbursed at cost for such services to its subsidiaries. The agreement is pending approval from the CDI.

Secondment Agreement: Effective January 1, 2012, the agreement was entered into between the Exchange and its subsidiary, AAA Member Services Company, LLC (AAA MSC). Under the terms of the agreement, employees transferred from the Exchange to AAA MSC will provide call center services to WUIC and ACAIC. The agreement is pending approval from the CDI.

Transition Services Agreement: Effective July 1, 2011, the agreement was entered into between the Exchange and AAA Northern California, Nevada & Utah (Club). The agreement provides for the winding down and transition of certain services provided by the Exchange to and from the Club or its designees. The Transition Services Agreement supersedes the two 1988 Service Agreements and the subsequent amendments entered between the Exchange and the Club. The agreement was not filed with the CDI at least 30 days prior to the effective date pursuant to California Insurance Code (CIC) Section 1215.5(b)(4).

Employee Transfer Agreement: Effective June 8, 2011, the agreement between the Exchange and the Club sets forth the terms and conditions regarding the transfer of employees and related matters resulting from the separation of the two entities. Under the agreement, the Exchange and the Club will continue as members of a single controlled group for Employee Retirement Income Security Act (ERISA) and tax qualified plan purposes. Specified employees will be transferred to the Club upon the separation of the two entities. On or after the transfer date (July 1, 2011), the Club's employees will continue to participate in the Exchange's retirement plans until December 31, 2011. The agreement was not filed with the CDI at least 30 days prior to the effective date pursuant to CIC Section 1215.5(b)(4).

Agreement on Branch Offices: Effective June 8, 2011, the agreement was entered into between the Exchange and the Club. Under the terms of this agreement, the Club agrees to lease or sublease offices that are either owned or leased by the Exchange. The agreement was not filed with the CDI at least 30 days prior to the effective date pursuant to CIC Section 1215.5(b)(4).

Producer Agreement: Effective January 1, 2011, the agreement was entered into between the Exchange and the Club. Under the terms of this agreement, the Exchange appoints the Club as its exclusive producer to procure and submit applications for insurance policies underwritten by the Exchange. The agreement was not filed with the CDI at least 30 days prior to the effective date pursuant to CIC Section 1215.5(b)(4).

Marketing Channel Agreement/Joint Marketing & Services Agreement: Effective January 1, 2011, the agreement was entered into between the Exchange and the Club. The agreement allows the Exchange to market in territories only with the Club's prior approval. The Exchange shall not implement any campaigns for direct sales without the Club’s approval. The agreement was not filed with the CDI at least 30 days prior to the effective date pursuant to CIC Section 1215.5(b)(4).

On February 29, 2012, the Exchange filed with the CDI a Disclaimer of Affiliation with the Club, which is currently being reviewed. If the Disclaimer of Affiliation is disallowed, it is then recommended the Exchange file the above five agreements with the CDI pursuant to CIC Section 1215.5 (b)(4).

Third Amended Restated Intercompany Services Agreement: Effective January 1, 2011, the third amendment to the agreement was entered into with the following subsidiaries: CSAA Life and Financial Services, Inc. (CSAA L&FS), ACAIC, WUIC, Pacific Beacon Life Reassurance, Inc., Ceres Reinsurance Company (Ceres Re), ACA Ventures, LLC, Club Marketing Services, LLC, Club Insurance Services, Inc., AAA MSC, The Innovation Fund, L.P., KIC, AAA MAIC, and AAA MAICNJ. The agreement outlines services to be provided by the Exchange to the subsidiaries including: personnel, facilities, accounting, tax, auditing, underwriting, claims, investments and other functional support services. Reimbursement is based on allocated costs plus a reasonable charge for overhead. The agreement was originally in effect as of January 1, 2007, with a second amendment restated as of December 1, 2009. The agreement was approved by the CDI on January 5, 2011.

Second Amended Restated Tax Allocation Agreement: Effective January 1, 2011, the agreement was entered into between the Exchange and the following subsidiaries and affiliates: CSAA L&FS, ACAIC, WUIC, Pacific Beacon Life Reassurance, Inc., Ceres Re, Club Insurance Services, Inc., KIC, AAA MAIC, and AAA MAICNJ. The agreement allocates federal income taxes among the companies on a separate company basis. The agreement replaced the Restated Intercompany Tax Allocation Agreement which was approved by the CDI on August 1, 2005. The purpose of this amendment was to add KIC, AAA MAIC, and AAA MAICNJ as participants to the tax allocation agreement. The amendment did not require filing with the CDI pursuant to CIC Section 1215.5(b)(4).

Second Amendment to Claims Administration Services Agreement: Amended March 15, 2010, the agreement was entered between the Exchange and ACAIC. Under the terms of this agreement, the Exchange agrees to perform claims services for homeowner policies underwritten by ACAIC in states other than Alaska. The agreement was terminated and superseded by the Intercompany Chargeback Agreement, effective January 1, 2012.

Second Amendment to Restated Claims Administration Services Agreement: Amended March 15, 2010, the agreement was entered between the Exchange and WUIC. Under the terms of this agreement, the Exchange performs claims services for homeowner policies underwritten by WUIC. The agreement was terminated and superseded by the Intercompany Chargeback Agreement, effective January 1, 2012.

First Amendment to Brand Agreement: Originally effective January 1, 1999, and amended August 1, 2009, the agreement was entered into between the Exchange and the Club. The Exchange agrees to pay the Club 1% of the direct premiums written for all lines of business for the use of the AAA brand. The amendment was not filed with the CDI at least 30 days prior to the effective date pursuant to CIC Section 1215.5(b)(4). This agreement was terminated on January 1, 2011.

First Amendment to Service Agreements: There were two separate agreements, both effective January 1, 1988, covering the provision of services between the Exchange and the Club. In one agreement, the Club provided services to the Exchange, which included operation and management of district offices, and related administrative services. In the second agreement, the Exchange provided the following services to the Club: accounting, programming, data processing, real estate development, personnel management, and other related administrative and consultation services. All services were provided at cost. The agreements were amended August 1, 2009 to change the interval of payments. These agreements have been superseded by the Transition Services Agreement that became effective as of July 1, 2011.

Service Agreement: Effective February 15, 2007, the agreement was entered into between the Exchange and AAA MSC. Under the terms of the agreement, AAA MSC is to operate a call center to respond to routine telephone inquiries from policyholders of the Exchange and its affiliated insurers. The agreement was approved by the CDI on February 9, 2007.

Services and Investment Management Agreement: Effective February 12, 2007, the agreement was entered into between the Exchange and AAA MSC. The agreement calls for the Exchange to provide facilities, personnel, and other administrative services to AAA MSC. The agreement was approved by the CDI on February 9, 2007. This agreement was superseded by the Intercompany Services Agreement referenced above.

Development Agreements, Reorganization Agreements and Partner Club Agreements: The Exchange was party to a number of Development Agreements with motor clubs which are members of the American Automobile Association (AAA). The purpose of the agreements was to provide access to insurance to members of these motor clubs, using the Exchange's insurance subsidiaries as direct writers. It was noted in the prior Report of Examination that one of the Development Agreement did not meet the standards for CIC Section 1215.5 because it did not make clear which of the affiliated parties was subject to the agreement and what their individual obligations were, as all references to the Exchange included its insurer subsidiaries. That Development Agreement had a duration of five years and has now lapsed.

The Exchange and ACA Holdings, Inc. (ACA Holdings), which changed its name in 2008 to AAA Club Affiliates, Inc., were parties to a number of Reorganization Agreements during the examination period with other auto clubs. ACA Holdings was formed by the Club in 2004 as a California mutual benefit corporation in order to form alliances with other auto clubs. The Reorganization Agreements provided that the Exchange would pay a brand fee to ACA Holdings as mutually agreed. However, no agreement to pay such a brand fee was reached. In addition, the Reorganization Agreements also provided that the Exchange would form an investment company to fund projects related to product innovation. The investment company was formed but is now dormant. Lastly, a series of Partner Club Agreements were formed between ACA Holdings and other auto clubs, which indirectly involve the Exchange. The Partner Club Agreements set forth rules and guidelines for each auto club's corporate membership in ACA Holdings, as well as offering cash investments to the auto clubs.

Effective January 1, 2011, ACA Holdings merged with AAA Club Partners (ACP), ACP being the surviving entity. All Reorganization Agreements and Partner Club Agreements were then amended and restated. The Exchange is not a party to any of these Reorganization Agreements or Partner Club Agreements.

TERRITORY AND PLAN OF OPERATION

The Exchange primarily writes private passenger automobile and homeowners coverages for members of the AAA Northern California, Nevada & Utah (Club) in its assigned territory of Northern California, Nevada, and Utah. Direct premiums written in 2011 were $1.8 billion (99.99%) in California and $0.17 million (0.01%) in Nevada. Major lines of business included private passenger auto liability (38.4%), auto physical damage (34.8%), and homeowner multiple peril (24.8%). Business is developed through the sales agents of the Club who serve as exclusive representatives of the Exchange.

On January 1, 2011, the Exchange purchased 100% of the issued shares of capital stock of Keystone Insurance Company (KIC), AAA Mid-Atlantic Insurance Company, and AAA Mid-Atlantic Insurance Company of New Jersey, collectively known as the AAA Mid Atlantic Insurance Group (MAIG), from AAA Mid-Atlantic, Inc. The acquisition of MAIG will foster opportunities for significant growth in the Mid-Atlantic region, providing the Exchange the ability to expand and diversify its insurance product offerings and geographic footprint outside of California.

REINSURANCE

Reinsurance Pooling Agreement

Effective January 1, 2011, the Exchange entered into a pooling agreement with five of its subsidiaries: Western United Insurance Company (WUIC), ACA Insurance Company (ACAIC), Keystone Insurance Company (KIC), AAA Mid-Atlantic Insurance Company (AAA MAIC), and AAA Mid-Atlantic Insurance Company of New Jersey (AAA MAICNJ). Under the terms of this agreement, the Exchange is the lead insurer and each company cedes 100% of its premiums written, unearned premiums, losses and loss adjustment expenses incurred and other underwriting expenses incurred to the Exchange. The Exchange then retrocedes a prorated amount to each company based on its pool participation percentage. All business written, including all underlying assumed and ceded by entity by each of the pool participants is subject to the intercompany pooling arrangement. This pooling agreement was approved by the California Department of Insurance (CDI) on March 7, 2012 and terminated the Exchange's prior reinsurance agreements with WUIC and ACAIC, respectively. As of 2011, the pooling percentage is as follows:

Company Name	Percentage of Participation
The Exchange	94.1%
Western United Insurance Company	3.0%
ACA Insurance Company	0.5%
Keystone Insurance Company	1.5%
AAA Mid-Atlantic Insurance Company of New Jersey	0.6%
AAA Mid-Atlantic Insurance Company	0.3%
Total	100%

Assumed

The Exchange participated in a portfolio participation program of global catastrophe risks, whereby it assumes catastrophe reinsurance from Renaissance Reinsurance Limited (Ren Re), a Bermuda insurer and Renaissance Reinsurance of Europe, Dublin, and Ireland. This program is also known as Catastrophe Portfolio Participation (CPP) program, a variable quota share reinsurance contract. The Exchange has a maximum liability of $250 million per contract year, and ceding commissions and profit commissions at 28% and 32.5%, respectively. Premiums assumed from Ren Re in 2011 were $83.3 million. The largest components of catastrophic events insured during the examination period were the tsunami in Japan and the earthquake in New Zealand.

Ceded

The Exchange is party to a four-layer catastrophe excess of loss treaty and cedes to various subscribing reinsurers, brokered through AON Benfield, for business defined as

Homeowners Multiple Peril (property only), Automobile Physical Damage (comprehensive only), Earthquake, Fire, and Inland Marine. Other than amounts ceded under the Reinsurance Pooling Agreement, and minor amounts to the National Flood Insurance Program, the Exchange had no ceded losses at December 31, 2011. The following is a summary of the principal ceded reinsurance treaty in-force as of December 31, 2011:

Line of Business and Type of Contract	Reinsurer's Name	Exchange's Retention	Reinsurer's Limit
Catastrophe Excess of Loss Covers catastrophic property loss on homeowner multiple peril (property sections), auto physical damage, earthquake, fire and inland marine.	27 reinsurers with varying participations	<u>1st Layer:</u> 30% of $50 million excess of $200 million per occurrence	<u>1st Layer:</u> 70% of $50 million excess of $200 million per occurrence, limited to $100 million aggregate during the term
		<u>2nd Layer:</u> 25% of $100 million excess of $250 million per occurrence	<u>2nd Layer:</u> 75% of $100 million excess of $250 million per occurrence, limited to $200 million aggregate during the term
		<u>3rd Layer:</u> 15% of $150 million excess of $350 million per occurrence	<u>3rd Layer:</u> 85% of $150 million excess of $350 million per occurrence, limited to $300 million aggregate during the term
		<u>4th Layer:</u> 15% of $250 million excess of $500 million per occurrence	<u>4th Layer:</u> 85% of $250 million excess of $500 million per occurrence, limited to $500 million aggregate during the term

ACCOUNTS AND RECORDS

During the course of the examination, a review was made of the Exchange's general controls over its information systems. As a result of this review, deficiencies were noted in controls over the areas of logical security, change management, and other deficiencies. These findings were presented to the Exchange along with recommendations to strengthen its controls. Many of the issues have been remediated at the time of this report. It is recommended that the Exchange continue to address the recommendations made regarding its information systems controls.

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, 2008 through December 31, 2011

Statement of Financial Condition
as of December 31, 2011

Assets	Ledger and Nonledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$3,057,755,635	$	$ 3,057,755,635	
Preferred stocks	153,032,451		153,032,451	
Common stocks	1,437,458,555		1,437,458,555	
Properties occupied by the Exchange	248,561,138		248,561,138	
Properties held for the production of income	16,310,533		16,310,533	
Cash and short-term investments	102,713,144		102,713,144	
Other invested assets	260,228,455	56,563,170	203,665,285	
Receivable for securities	10,134,755		10,134,755	
Aggregate write-ins for invested assets	105,523		105,523	
Investment income due & accrued	34,399,521		34,399,521	
Uncollected premiums and agents' balances in course of collection	241,653,650	4,188,340	237,465,310	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	493,324,931		493,324,931	
Amount recoverable from reinsurers	10,416,468		10,416,468	
Current federal and foreign income tax recoverable and interest thereon	36,543,863		36,543,863	
Net deferred tax asset	165,257,306		165,257,306	
Electronic data processing equipment and software	96,530,721	96,103,480	427,241	
Furniture and equipment	43,261,161	43,261,161	0	
Receivable from parent, subsidiaries and affiliates	53,195,977		53,195,977	
Aggregate write-ins for other than invested assets	398,704,434	374,014,521	24,689,913	
Total assets	$6,859,588,221	$ 574,130,671	$ 6,285,457,549	

Liabilities, Surplus and Other Funds			
Losses		$ 967,578,621	(1)
Reinsurance payable on paid losses and loss adjustment expenses		58,476,508	
Loss adjustment expenses		183,223,233	(1)
Commissions payable, contingent commissions and other similar charges		18,038,076	
Other expenses		105,144,329	
Taxes, licenses and fees		3,574,853	
Current federal and foreign income taxes		28,881,089	
Borrowed money		18,603,750	
Unearned premiums		1,238,579,854	
Advance premiums		13,619,830	
Ceded reinsurance premiums payable		519,570	
Amounts withheld or retained by Exchange for account of others		194,262,590	
Remittances and items not allocated		5,395,016	
Drafts outstanding		112,473	
Payable for securities		3,751,913	
Aggregate write-ins for liabilities		5,170,992	
Total liabilities		2,844,932,697	
Aggregate write-ins for special surplus funds	$ 200,228,030		
Unassigned funds (surplus)	3,240,296,822		
Surplus as regards policyholders		3,440,524,852	
Total liabilities, surplus and other funds		$ 6,285,457,549	

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

Statement of Income

Underwriting Income		
Premiums earned		$2,551,293,520
Deductions:		
Losses incurred	$ 1,517,623,024	
Loss adjustment expenses incurred	287,070,537	
Other underwriting expenses incurred	785,859,915	
Total underwriting deductions		2,590,553,476
Net underwriting loss		(39,259,956)
Investment Income		
Net investment income earned	165,452,507	
Net realized capital gain	104,095,808	
Net investment gain		269,548,315
Other Income		
Net loss from agents' or premium balances charged off (amount recovered $1,297,448 amount charged off $7,658,710)	(6,361,262)	
Finance and service charges included not included in premiums	13,014,405	
Aggregate write-ins for miscellaneous income	(10,377,391)	
Total other income		(3,724,248)
Net income before federal and foreign income taxes		226,564,111
Federal and foreign income taxes incurred		15,478,251
Net income		$ 211,085,860

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2010		$3,325,738,630
Net income	$ 211,085,860	
Change in net unrealized capital losses	(68,923,455)	
Change in net unrealized foreign exchange capital loss	(7,771,055)	
Change in net deferred income tax	26,425,779	
Change in nonadmitted assets	(46,411,605)	
Aggregate write-ins for gains in surplus	380,698	
Change in surplus as regards policyholders for the year		114,786,222
Surplus as regards policyholders, December 31, 2011		$3,440,524,852

Reconciliation of Surplus as Regards Policyholders from December 31, 2008 through December 31, 2011

	Gain in Surplus	Loss in Surplus	
Surplus as regards policyholders, December 31, 2008 per Examination			$2,737,510,784
Net income	$ 524,524,140	$	
Net unrealized capital gains	176,080,956		
Change in net foreign exchange capital losses		6,460,250	
Change in net deferred income tax	17,428,660		
Change in nonadmitted assets		7,024,345	
Aggregate write-ins for gains and losses in surplus		1,535,093	
Total gains and losses	$ 718,033,756	$ 15,019,688	
Net increase in surplus as regards policyholders			703,014,068
Surplus as regards policyholders, December 31, 2011, per Examination			$3,440,524,852

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on an analysis by a Senior Casualty Actuary for the California Department of Insurance, the Exchange's losses and loss adjustment expense reserves as of December 31, 2011 were found to be reasonably stated and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Management and Control – Related Party Agreements (Page 5): If the Disclaimer of Affiliation with AAA Northern California, Nevada & Utah (Club) is disallowed, it is then recommended the Exchange file the following agreements with the California Department of Insurance (CDI) pursuant to California Insurance Code (CIC) Section 1215.5(b)(4).

- Transition Services Agreement
- Employee Transfer Agreement
- Agreement on Branch Offices
- Producer Agreement
- Marketing Channel Agreement/Joint Marketing & Services Agreement

Accounts and Records (Page 14) - It is recommended that the Exchange continue to address the recommendations made regarding its information systems controls.

<u>Previous Report of Examination</u>

Management and Control – Related Party Agreements, Amended Restated Intercompany Services Agreement (Page 6): It was recommended the Exchange file the Amended Restated Intercompany Services Agreement effective January 1, 2007 with the CDI pursuant to CIC Section 1215.5(b)(4). This agreement was superseded by the Third Amended Restated Intercompany Services Agreement.

Management and Control – Related Party Agreements, Development Agreements (Page 8): It was again recommended the Exchange revise its Development Agreement to specify which insurer subsidiaries are party to the agreement, and what their individual obligations are, or file for an exemption under CIC Section 1215.5(i). The agreement had a duration of five years and has now lapsed.

Management and Control – Related Party Agreements (Page 9): It was recommended that the Exchange treat ACA Holdings, Inc. as a member of the holding company system and provide the required disclosures and notifications pursuant to CIC Section 1215.4 and 1215.5. It was also recommended that the Exchange file the various Development, Reorganization, and Partner Club Agreements with the CDI pursuant to CIC Section 1215.5(b)(4), or file for an exemption pursuant to CIC Section 1215.5(i). The Reorganization Agreements and Partner Club Agreements were since amended and restated. The Exchange is no longer a party to these agreements.

Management and Control – Related Party Agreements (Page 9): It was recommended that the Exchange implement procedures to properly report and disclose all affiliated and other agreements as required by CIC Section 1215.4 and 1215.5. It was also recommended the Exchange develop a more comprehensive system of tracking its inventory of existing agreements, including amendments and amounts spent pursuant to those agreements. The Exchange has partially complied with this recommendation and is in the process of implementing an online agreement library.

Accounts and Records – Information Systems Controls (Page 12): It was recommended that the Exchange continue to address the recommendations made regarding its information systems controls. The Exchange is in the process of addressing the current examination recommendations made regarding its information systems controls.

Accounts and Records – Premiums and Agents' Balances in the Course of Collection (Page 12): It was recommended the Exchange follow the National Association of Insurance Commissioners' Annual Statement Instructions for reporting installment premiums. It was also recommended the Exchange revise its premium system to include policy-level aging of uncollected premiums. The Exchange has complied with these recommendations.

ACKNOWLEDGMENT

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

Respectfully submitted,

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Kyo S. Chu, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California