REPORT OF EXAMINATION
OF THE

CALIFORNIA FAIR PLAN ASSOCIATION

AS OF
SEPTEMBER 30, 2009

Filed January 12, 2011

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Los Angeles, California
December 10, 2010

Honorable Steve Poizner
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

CALIFORNIA FAIR PLAN ASSOCIATION

(hereinafter also referred to as the Association) at the primary location of its books and records, 3435 Wilshire Boulevard, Suite 1200, Los Angeles, California 90010.

SCOPE OF EXAMINATION

The previous examination of the Association was made as of September 30, 2005. This examination covers the period from October 1, 2005 through September 30, 2009. The examination included a review of the Association's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of September 30, 2009, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Association's operations were reviewed including the following areas that require no further comment: association history; corporate records; fidelity bonds and other insurance; officers', and employees' welfare and pension plans; growth of association; business in force by states; accounts and records; and sales and advertising.

MANAGEMENT AND CONTROL

A thirteen-member governing committee manages the Association. Nine members are elected annually from member companies and are voting members. Four members are appointed by the Governor for an indefinite term and are nonvoting members. The representation on the Governing Committee is specified in California Insurance Code Section 10094 and in the Association's Plan of Operations. A listing of the governing committee members serving as of September 30, 2009 follows:

Voting Members

Name	Company	Representing
Fred Strauss Chairman	Allstate Insurance Company	Other Stock Insurers
Kevin Stockton Vice Chairman	State Farm Insurance Companies	At-large Insurance companies
Brian Braddock Secretary	Farmers Insurance Group	Other Non-Stock Insurers
Joseph Evleth	Interinsurance Exchange of the Automobile Club	At-large Insurance companies
William Martin	The Hartford	American Insurance Association
Jack McGraw	Pacific Specialty Insurance Company	At-large Insurance companies
Anne McLeod	Liberty Mutual Group	The Alliance of American Insurers
James McMasters	Fireman's Fund Insurance Companies	At-large Insurance companies
Joseph Muenzen	California Casualty Group	The National Association of Independent Insurers

Nonvoting Members

Name	Company	Representing
Howard King	Modern Corporation	Public
Wes Bannister*	Bannister and Associates	Insurance Brokers
Vacant**		Insurance Agents
Vacant**		Surplus Lines

*Wes Bannister passed away on December 10, 2009.

**The Association has contacted the Governor regarding the vacancies and is waiting for the Governor's appointment of the three members.

George Yen, Chief, Rate Specialist Bureau, is the designated liaison for the California Department of Insurance.

The following schedule shows the management staff responsible for the daily operation of the Association as of September 30, 2009:

Name	Title
Anneliese Hart	President
Victor R. Natividad	Vice President - Finance
Alfred Hess	Vice President - Claims
John Boeder	Vice President - Underwriting and General Operation
Michael Harris	Vice President - Public Affairs
Cesar Flores	Vice President - Information Systems

TERRITORY AND PLAN OF OPERATION

The Association writes fire, extended coverage, vandalism and malicious mischief, and commercial sprinkler leakage on risks located in urban areas designated by the California Insurance Commissioner. It also writes in certain specified geographical areas or hazardous brush areas as designated by the Insurance Services Office. One-year policies are issued and premium rates are based upon the Association's (FAIR Plan) experience.

The purpose of the Association is to provide coverage in areas where applicants have been unable to obtain coverage in the normal markets. However, no active procedure is currently used by the Association to determine if any attempts have been made by applicants to place the risk in the regular market. It is assumed that producers would not attempt to place business in the Association if comparable coverage was available in the regular market.

The Association is not an insurer, but a mechanism to spread the risk, premiums, losses and expenses among the participating insurers. The Association is a separate joint venture of all insurance companies (participants or participating insurers) holding certificates of authority from the California Department of Insurance for each class of business. The Association's Plan of Operations provides that the policies of insurance written and issued by them are on behalf of its participating insurers and that the respective liabilities of the insurers are several and not joint, and each such insurer is considered to be a direct insurer for its share in such writing.

All activity of the Association is on behalf of its participating insurers. For this reason, it does not have a certificate of authority as an insurance company. Likewise, it does not have a producer's license as it is composed of its participating insurance companies. Therefore, producers are not appointed agents of the Association, and they cannot bind coverage. All producers licensed by the State of California are eligible to produce business for the Association.

The Association writes its own policies and collects premiums, pays return premiums, commissions, and various general expenses. The Association contracts with and assigns independent adjusters to adjust claims filed and pay claims and related loss adjustment expenses. Unallocated general expenses are apportioned between claims and underwriting. Each participating insurer includes its portion of the Association's written premiums with its direct business and pays the associated premium tax.

Member insurers' participation percentages are reduced proportionately by the amount that they voluntarily write in designated brush areas and certain urban areas.

The maximum limit of liability that may be placed through the Association is as follows:

Description of Coverage	**Maximum Limit Amount**
Dwelling Buildings and Contents	$1.5 million per one location
Commercial Buildings	$3 million
Commercial Building Contents	$1.5 million maximum for each tenant
The maximum cumulative coverage for all tenants' contents, which can be insured in a single commercial building, will be $3 million, unless the following conditions are met:	
1. $3 million and up to $5 million contents coverage if the building is protected 24 hours by a guard service on the premises.	
2. $5 million to $10 million contents coverage if the building is protected 24 hours by a guard service on the premises and an automatic sprinkler system approved by the Insurance Services Office.	

A Business Owners' Policy (BOP) is available to certain commercial property owners and to small to medium sized business operators. The BOP provides a package of coverages for eligible risks, which includes mandatory property and liability coverages, with burglary and robbery offered as optional coverage. The BOP comprises approximately 3% of the total Association writings.

In December 1996, the California Earthquake Authority (CEA) was created by the California State Legislature to help resolve the insurance availability crisis in California following the 1994 Northridge earthquake. The Association participated in the CEA and made a $15 million capital contribution. The participation was designed to limit the Association's earthquake exposure. As of September 30, 2009, the Association has a 0.83% share of the total CEA market and has a maximum exposure to earthquake loss of approximately $23 million. Future assessments in the event of a catastrophe are dependent upon the Association's CEA earthquake market share, the amount of the earthquake losses and the financial status of the CEA.

Effective May 30, 2001, the California Insurance Commissioner issued an order expanding the geographic areas eligible for coverage to provide relief to those who live in high risk areas with no insurance options, and who were formerly ineligible for Association coverage. In order to obtain coverage, the applicants must provide confirmation that they have been rejected from three insurers.

LOSS EXPERIENCE

The following chart depicts the Association's operation results from the 2006 through 2009 fiscal years and highlights the recent underwriting and net losses in the 2008 through 2009 fiscal years:

Fiscal Year	**Member's Equity or (Deficit)**	**Net Underwriting Gain or (Loss)**	**Net Income or (Loss)**
2006	44,311,920	26,862,337	34,982,263
2007	71,017,318	25,043,319	31,097,495
2008	44,573,209	(27,732,962)	(24,459,045)
2009	$ (14,033,899)	$ (53,734,109)	$ (53,278,156)

The Association provides fire coverage in brush and wildfire areas throughout the State of California. These areas are subject to the environmental hazard of catastrophic wildfires. The operating and net losses in fiscal years 2008 and 2009 are attributed to significant fire activity during these two periods. In October and November 2007, a series of wildfires resulted in approximately $46 million in losses and severely affected the financial results of fiscal year 2008. In addition, a succession of wildfires occurred in November 2008, May and August 2009 and resulted in losses of approximately $74 million for fiscal year 2009. The combined losses of approximately $120 million from these wildfires were settled without a need for cash assessments from participating member companies, but severely reduced the Association's available funds for operations.

Pursuant to California Insurance Code Section 10094, upon an approval from the Governing Committee, the Association is empowered to assess participating companies their pro rata share of losses incurred in a pool year. The Association's Governing Committee has evaluated the Association's liquidity position and the current policy for making assessment, and determined that no special assessment will be collected for the 2008 and 2009 pool years.

REINSURANCE

Assumed

The Association did not assume reinsurance during the examination period.

Ceded

As of September 30, 2009, the Association's ceded reinsurance consists of a catastrophe excess of loss reinsurance agreement with Lloyd's of London, the largest participant (41.75%), along with other participants covering catastrophic brush fire losses in areas subject to brush and wild fires. The Association's retention is $100 million and the reinsurer's maximum limit of liability is $100 million. This agreement was first effective on February 1, 1999 and has been renewed annually. As of September 30, 2009, there have been no ceded losses under the reinsurance agreement.

Effective February 15, 2010, the Association entered into a Property Catastrophe Aggregate Excess of Loss Reinsurance Agreement with Lloyd's of London, the largest participant (26%), along with other participants, where the Association will be indemnified at the net aggregate liability as a result of one or more loss occurrences. The Association's retention is $100 million and the reinsurer's maximum limit of liability is $100 million.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of September 30, 2009

Statement of Income and Member's Equity for the Year Ended September 30, 2009

Reconciliation of Member's Equity
from September 30, 2005 through September 30, 2009

Statement of Financial Condition
as of September 30, 2009

Assets	Ledger and Nonledger Assets		Net Admitted Assets	Notes
Cash and short-term investments	$ 60,428,736		$ 60,428,736	
Premiums receivable	4,064,186		4,064,186	
Accrued investment income	51,313		51,313	
Total assets	$ 64,544,235		$ 64,544,235	
Liabilities and Members' Equity				
Unpaid losses			$ 27,697,316	(1)
Unpaid loss adjustment expenses			2,249,637	(1)
Commissions payable			750,576	
Accrued expenses			371,624	
Unearned premiums			35,692,177	
Advance and unapplied premiums			2,853,010	
Other liabilities – post-retirement benefit accrual			5,966,712	
Distributions due to members			2,997,082	
Total liabilities			78,578,134	
Total members' deficit			(14,033,899)	(2)
Total liabilities, and members' equity			$ 64,544,235	

Statement of Income and Members' Equity
for the Year Ended September 30, 2009

Statement of Income

Underwriting Income		
Premiums earned		$ 67,200,369
Deductions:		
Losses incurred	$ 98,354,843	
Loss expense incurred	5,391,629	
Other underwriting expenses incurred	17,188,006	
Total underwriting deductions		120,934,478
Net underwriting loss		(53,734,109)
Investment Income		
Net investment income earned		455,953
Net loss		$ (53,278,156)

Members' Equity

Members' equity, September 30, 2008		$ 44,573,209
Net loss	$ (53,278,156)	
Change in assets not admitted	(407,856)	
Distribution of equity	(2,993,639)	
Change in minimum pension liability	(1,927,457)	
Change in equity		(58,607,108)
Members' deficit, September 30, 2009		$ (14,033,899)

Reconciliation of Members' Equity
from September 30, 2005 through September 30, 2009

Members' equity, September 30, 2005, per Examination			$ 40,460,893
	Gain in Equity	Loss in Equity	
Net loss	$	$ 11,657,443	
Change in nonadmitted assets		665,626	
Assessments from member companies	25,434		
Distribution to member companies		44,667,612	
Aggregate write-ins for gains in surplus	2,470,455		
Totals	$ 2,495,889	$ 56,990,681	
Net decrease in members' equity for the examination period			(54,494,792)
Members' deficit, September 30, 2009, per Examination			$ (14,033,899)

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Unpaid Losses and Unpaid Loss Adjustment Expenses

The liabilities for unpaid losses and unpaid loss adjustment expenses include an amount determined from individual case estimates and loss reports and an amount, based on past experience, for losses incurred but not reported. Losses incurred are directly allocated to pool years based upon the effective date of the policy. Allocated loss adjustment expenses are allocated to pools directly and unallocated loss adjustment expenses are allocated to pools by a ratio of claims paid.

Pursuant to California Insurance Code Section 10094, the Association is empowered to assess member companies their proportional share of losses incurred in a pool year. The Association's Governing Committee must approve all assessments. Assessments are allocated to pool years based upon the effective date of the policy covering the event deemed to have caused the pool year loss. During the four-year examination period the Association assessed member companies a total of $25,434.

The Association is not required to prepare an Analysis of Losses and Loss Expenses (Schedule P), or to provide an actuarial opinion.

Based on an analysis by a Casualty Actuary for the California Department of Insurance, the Association's unpaid losses and unpaid loss adjustment expenses as of September 30, 2009 were found to be reasonably stated and have been accepted for purposes of this examination.

(2) Members' Equity

The Association reviews pool years annually to determine if a distribution of members' equity is appropriate. Upon approval of the Governing Committee, the Association will issue a preliminary distribution with subsequent yearly adjustments to the pool year until unpaid losses permit a final settlement of members' equity and the pool year is closed. The Governing Committee is empowered to reduce the distributions by deficits incurred in other pool years. In fiscal year 2009, the Governing

Committee approved the closure of 2006 pool year except for Business Owners' Policy (BOP) and approved the closure of 2008 pool year for BOP. During the four-year examination period the Association distributed a total of $44.7 million to member companies.

The Association's Members' Equity as of September 30, 2009 reported a deficit of $14 million. As mentioned in the Loss Experience section of this report, the two years of significant losses from a succession of wildfires in 2008 and 2009 severely affected the Association's financial result. However, based on the Governing Committee's evaluation on the Association's current cash flow position and the open status of the 2008 and 2009 pool years for brush and wild fire, it was determined that no early assessment will be collected for the 2009 pool year.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None.

Previous Report of Examination

None.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Association's officers and employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

/S/

Sayaka T. Dillon, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California