ASSOCIATION EXAMINATION REPORT
ON
SOUTHERN STATES INSURANCE EXCHANGE
Richmond, Virginia
as of
December 31, 2007

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE

ALFRED W. GROSS
COMMISSIONER OF INSURANCE
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE

COMMONWEALTH OF VIRGINIA

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I, Alfred W. Gross, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Southern States Insurance Exchange as of December 31, 2007, is a true copy of the original report on file with this Bureau.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed to the original the seal of the Bureau at the City of Richmond, Virginia this 16th day of October, 2008

Alfred W. Gross

Alfred W. Gross
Commissioner of Insurance

(SEAL)

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Richmond, Virginia
July 23, 2008

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition (E) Committee
Commissioner of Insurance
Commonwealth of Virginia
Richmond, Virginia

Honorable Scott H. Richardson
Secretary-Southeastern Zone, NAIC
Commissioner of Insurance
South Carolina Department of Insurance
Columbia, South Carolina

Dear Sirs:

Pursuant to your instructions and by authority of § 38.2-1317 of the Code of Virginia, a financial examination of the records and affairs of the

SOUTHERN STATES INSURANCE EXCHANGE

Richmond, Virginia

hereinafter referred to as the Exchange, has been completed. The report thereon is submitted for your consideration.

DESCRIPTION

The Exchange is a reciprocal insurer licensed pursuant to Chapter 12 of Title 38.2 of the Code of Virginia and was last examined by representatives from the State Corporation Commission's Bureau of Insurance (Bureau) as of December 31, 2004. The present examination, which was called and conducted under the auspices of the National Association of Insurance Commissioners, was conducted by Examiners from the Bureau representing the Southeastern Zone. This examination covers the period from January 1, 2005, through December 31, 2007.

HISTORY

The Exchange was organized in March 1953 under the provisions of Chapter 16 of Title 38.1 (currently Chapter 12 of Title 38.2) of the Code of Virginia for the purpose of permitting Southern States Cooperative, Inc. (Cooperative), and its subsidiary and affiliated corporations to exchange among themselves contracts of insurance through a duly authorized attorney-in-fact. To accomplish this, the Cooperative organized Southern States Underwriters, Inc. (SSUI) to serve as Attorney-in-Fact and advanced $350,000 to the Exchange to enable it to begin operations.

At the organizational meeting, a subscriber's agreement was adopted which appointed SSUI as Attorney-in-Fact for the Exchange. The agreement also set forth the rights, privileges, and obligations of the subscriber as an underwriter and policyholder and the powers and duties of SSUI. The agreement further provided that SSUI, while acting in such capacity, has the power, on behalf of subscribers, to insure and accept reinsurance on property and insurable interest therein, and to issue contracts of insurance. The lines of insurance specified in this agreement include: fire, miscellaneous property, water damage, burglary and theft, glass, boiler and machinery, elevator, animal, collision, workers' compensation and employers' liability, fidelity and surety, credit, marine, and contingent and consequential losses.

After making application and filing the required declarations with the Bureau, a license was granted to the Exchange on April 8, 1953. Operations commenced on May 1, 1953.

By 1982, the Exchange had expanded its homogeneous subscriber base to include independent agricultural businesses that are not organized as cooperatives ("private dealers") and agricultural cooperatives ("independent cooperatives"). Together, these two categories of subscribers are referred to as "independent markets." In 1991, the Exchange began to increase its independent markets business. By 2002, approximately 133 of these businesses had become subscribers.

On April 22, 1987, by resolution, SSUI executed a Power of Attorney to appoint the Clerk of the State Corporation Commission and his successor in office as agent of the Exchange upon who may be served all lawful process against the Exchange.

On April 26, 1988, by resolution, several modifications were made to the Subscriber's Agreement and Power of Attorney. These modifications included entitling Class I subscribers to just one vote on all matters which the Class I subscribers are entitled to vote. This change to voting rights became effective July 1, 1988. Also modified were the procedures for the payment of equities to withdrawn subscribers and the calculation of the management fee.

On April 28, 2003, by resolution, the Subscriber's Agreement and Power of Attorney was amended to increase the management fee paid to SSUI from 10% of direct earned premiums to 15% of direct earned premiums.

MANAGEMENT AND CONTROL

Supervision of the affairs of the Exchange is vested in an Advisory Committee of not less than 6, nor more than 15 persons who are elected by the subscribers at their annual meeting. No less than 3/4 of the members of the committee may be composed of Class I subscribers or representatives of the Class I subscribers, other than SSUI or any person employed by, representing, or having a financial interest in SSUI. The Class I subscribers consist exclusively of subscribers that are cooperative associations. All other subscribers are deemed Class II subscribers. The Subscriber's Agreement and Power of Attorney, among other things, specifies the powers and duties of both the committee and SSUI.

The Cooperative represents a majority of the subscribers and owns all of the outstanding stock of SSUI, thereby giving the Cooperative apparent control over the Exchange.

At December 31, 2007, the Members of the Advisory Committee and its officers were as follows:

Advisory Committee	Principal Business Affiliation
Ashley S. Brooks	Associate General Counsel Southern States Cooperative Richmond, Virginia
Francis M. Crowley	President Hilb Rogal & Hobbs Company Richmond, Virginia
G. Turner Gravitt	Sales Manager, Independent Markets Southern States Cooperative Richmond, Virginia
Floyd T. Grigsby	President Wetsel, Inc. Harrisonburg, Virginia

Advisory Committee (continued)	Principal Business Affiliation
Rex P. Honodel	President Southern States Underwriters, Inc. Richmond, Virginia
Frederic Jezouit	Treasurer and Vice President of Finance Southern States Underwriters, Inc. Richmond, Virginia
Philip W. Miller	Vice President and Controller Southern States Cooperative, Inc. Richmond, Virginia
Leslie T. Newton	Executive Vice President and Chief Financial Officer Southern States Underwriters, Inc. Richmond, Virginia
Norman R. Wenger	General Manager Rockingham Cooperative Farm Bureau Harrisonburg, Virginia

Officers

Leslie T. Newton	Chairman
Philip W. Miller	Vice Chairman
Rex P. Honodel	Secretary

The board of directors and officers of SSUI were as follows at December 31, 2007:

Directors
Rex P. Honodel
Leslie T. Newton

Officers	
Rex P. Honodel	President
Wendy K. Tate	Vice President
Robert G. Waters, Jr.	Secretary and Treasurer
Diane D. Sexton	Assistant Treasurer

COMPENSATION OF ATTORNEY-IN-FACT

SSUI is authorized to pay all expenses and disbursements of every kind and character incident to the Exchange's administration and the exchange of insurance contracts from the funds of the Exchange. However, SSUI must use its own funds to pay all customary office and business expenses and all expenses incurred in connection with bonds and other legal requirements affecting the ability of SSUI to serve as Attorney-in-Fact. SSUI is also authorized to receive from the funds of the Exchange an annual management fee, to the extent and at such times expressly permitted by the Advisory Committee. Unless otherwise rescinded by mutual agreement of the Advisory Committee and SSUI, the management fee shall be fixed at 15% of direct earned premiums, net of returned premiums, and is to be paid monthly. In April 2003, the Advisory Committee received approval from the Bureau to increase this fee from 10%. A final year-end adjustment, subject to the limits established by the Subscribers' Agreement, is to be made promptly after a final determination has been made of revenue received and accrued for the calendar year. The management fee for 2005, 2006 and 2007 was $2,035,688, $2,080,418 and $2,199,937, respectively.

Joint Sales and Marketing Agreement

On January 4, 1994, the Exchange entered into a joint sales and marketing agreement with SSC Insurance Agency, Inc. (SSCIA), an affiliate of SSUI. This agreement provides for SSCIA to assist the Exchange in marketing insurance products to certain of its existing and potential Class I subscribers located in the states of Virginia, North Carolina, Kentucky, West Virginia, Maryland, Delaware, Pennsylvania, Georgia, Alabama and South Carolina. The majority of Class I subscribers are written direct except for 13 independent cooperatives. The agreement further provides assistance in the marketing of insurance products to certain of its existing and potential Class II subscribers located in the states of Virginia, North Carolina, Kentucky West Virginia, Maryland, Delaware, Pennsylvania, Georgia, Alabama and South Carolina. This agreement further provides that, in no event, shall SSCIA have authority to bind insurance coverage or issue insurance policies on behalf of the Exchange. As compensation for SSCIA's assistance in developing new business as provided by the agreement, the Exchange will pay commissions to SSCIA as specified by the agreement. The Exchange paid commissions of $918,820, $898,001 and $821,024 to SSCIA during 2005, 2006 and 2007, respectively.

FIDELITY BOND

SSUI was a named insured on two policies that provided fidelity coverage at December 31, 2007. The first policy was issued by the Exchange and has a $100,000 policy limit with a $5,000 deductible. The second policy, issued by a commercial insurer, has a $3,000,000 limit of liability and is subject to a $100,000 deductible.

TERRITORY AND PLAN OF OPERATION

The Exchange was authorized to operate in the following states at December 31, 2007, as evidenced by licenses in its possession:

Alabama	North Carolina
Delaware	Pennsylvania
Georgia	South Carolina
Kentucky	Virginia
Maryland	West Virginia

In Virginia, the Exchange was licensed to write the following insurance coverages at December 31, 2007:

Fire	Water Damage
Miscellaneous Property and Casualty	Burglary and Theft
Commercial Multiple Peril	Liability Other Than Auto
Automobile Physical Damage	Automobile Liability
Ocean Marine	Fidelity
Inland Marine	Surety
Workers' Compensation and Employers' Liability	

Organized as a reciprocal, or interinsurance exchange, the Exchange provides policy contracts to its subscribers through an Attorney-in-Fact. Its subscribers consist of the Cooperative; 62 (plus 16 branch locations) independent local farm cooperatives operated by the Cooperative under management agreements; 13 independent local cooperatives not operated by management agreement; and approximately 119 other agribusinesses.

The Subscriber's Agreement and Power of Attorney has a contingent liability provision that is not joint, but several. The liability is limited to not more than one additional annual premium on any policy during the calendar year.

Effective July 1, 1989, the Exchange began writing commercial automobile and comprehensive general liability insurance for the Cooperative and its managed affiliates. Liability coverages are now offered to all subscribers.

In 1991, the Exchange began offering all coverages to additional agribusinesses, including private dealers of the Cooperative. In order to qualify for coverage, each individual prospective insured must meet certain underwriting criteria.

Accounts are maintained for each subscriber which includes accumulated figures for premiums earned, dividends paid, and subscriber savings accounts (equity in the surplus of the Exchange). After providing for operating expenses, which includes a management fee to the Attorney-in-Fact, amounts are occasionally set aside as a reserve for contingencies. Upon authorization of the Advisory Committee, the remaining savings are paid to each subscriber as dividends or applied as credits to their individual subscriber savings accounts. Distributions of prior years' subscriber savings were made to subscribers in 2005, 2006 and 2007. Such distributions, combined with dividends paid to policyholders, are included in the Growth of the Exchange section of this report. Additionally, subscribers are entitled to their remaining savings upon withdrawal from the Exchange by March 15 of the following year after their withdrawal as a subscriber.

GROWTH OF THE EXCHANGE

The following data, obtained from annual statements filed with the Bureau and from examination reports, indicates the growth of the Exchange for the ten-year period ending December 31, 2007:

Year	Admitted Assets	Liabilities	Subscriber Savings Accounts	Unassigned Funds
1998	$52,172,182	$23,272,978	$20,181,982	$8,717,222
1999	55,394,542	25,426,424	23,780,070	6,188,048
2000	49,460,359	22,140,358	25,470,933	1,849,068
2001	50,197,951	22,368,067	25,346,023	2,483,861
2002	35,757,616	24,533,877	9,775,975	1,447,764
2003	33,583,660	19,043,050	10,984,579	3,556,031
2004	31,517,847	16,976,847	10,501,801	4,039,199
2005	33,923,250	19,382,250	10,309,566	4,231,434
2006	34,403,439	19,862,439	10,674,298	3,866,702
2007	36,321,076	20,821,076	12,664,358	2,835,642

	Premiums Earned	Losses and Loss Adjustment Expenses Incurred	Other Underwriting Expenses	Net Underwriting Gain
1998	$8,907,668	$5,042,894	$1,449,054	$2,415,720
1999	9,446,325	5,200,232	1,556,263	2,689,830
2000	9,030,793	5,249,282	1,437,307	2,344,204
2001	10,044,237	5,293,084	1,329,001	3,422,152
2002	9,557,070	5,113,653	2,168,799	2,274,618
2003	9,788,537	4,473,986	2,739,126	2,575,425
2004	9,619,540	6,629,452	2,982,170	7,918
2005	10,788,092	7,155,820	3,227,960	404,312
2006	11,366,444	6,624,636	3,369,808	1,372,000
2007	11,509,696	7,909,669	3,544,427	55,600

	Management Fees Incurred	Equities and Dividends Paid to Subscribers
1998	$1,066,176	$5,333,334
1999	1,134,661	6,828,124
2000	1,109,463	6,829,753
2001	1,483,684	5,430,530
2002	1,432,872	18,336,342
2003	1,828,904	7,432,467
2004	1,881,886	2,500,015
2005	2,035,688	922,822
2006	2,080,418	1,785,995
2007	2,199,937	3,405,767

REINSURANCE

At December 31, 2007, the Exchange had the following reinsurance coverage in force:

Type of Agreement	Types of Policies Covered	Limit of Reinsurance
Combined Excess of Loss	Property	$750,000 excess of $250,000 per risk, subject to $2,250,000 limit any one loss occurrence
	Workers' Compensation, and Employers' Liability	$750,000 excess of $250,000 each loss occurrence
	Automobile Liability, Commercial General Liability, and Garage Liability	$750,000 excess of $250,000 each loss occurrence
		In the event of a combined loss recoverable of all of the above, $500,000 each occurrence excess of $250,000 each loss occurrence

Type of Agreement	Types of Policies Covered	Limit of Reinsurance
First Property Per Risk Excess of Loss	Property	$4,000,000 each and every loss, each and every risk excess of $1,000,000 each and every loss, each and every risk, subject to a limit of $12,000,000 any one loss occurrence
Second Property Per Risk Excess of Loss	Property	$5,000,000 each and every loss, each and every risk excess of $5,000,000 each and every loss, each and every risk, subject to a limit of $15,000,000 any one loss occurrence
Second Casualty Excess of Loss	Workers' Compensation and Employers' Liability, Automobile Liability, Commercial General Liability, and Garage Liability	$4,000,000 each occurrence excess of $1,000,000 each loss occurrence
Workers' Compensation Excess of Loss	Workers' Compensation and Employers' Liability	$9,000,000 each loss occurrence excess of $1,000,000 each loss occurrence; maximum policy limit for employer's liability is $1,000,000
First Property Catastrophe Excess of Loss	Property	$500,000 first loss occurrence subject to limit of $500,000; $375,000 each subsequent occurrence subject to a limit of $625,000 any one occurrence; $1,125,000 all loss occurrences

Type of Agreement	Types of Policies Covered	Limit of Reinsurance
Second Property Catastrophe Excess of Loss	Property	$2,000,000 each and every loss occurrence excess of $1,000,000 each and every loss occurrence; $4,000,000 all loss occurrences
Third Property Catastrophe Excess of Loss	Property	$2,000,000 each and every loss occurrence excess of $3,000,000 each and every loss occurrence; $4,000,000 all loss occurrences
Umbrella Facultative Excess of Loss	Commercial Liability	90% up to $1,000,000 of ultimate net loss, each loss occurrence, each policy; 100% of $4,000,000 excess of $1,000,000 each loss occurrence, each policy

The Exchange also had an equipment breakdown treaty reinsurance agreement to cover losses in excess of stated amounts for policies issued under the Exchange's equipment breakdown coverages.

The reinsurance agreements contain insolvency and guarantee of intermediary credits clauses.

SCOPE

This is a full scope financial condition examination initiated and conducted under the provisions of Article 4, Chapter 13 of Title 38.2 of the Code of Virginia. The examination covers the period from January 1, 2005, through December 31, 2007. Assets were verified and liabilities were established at December 31, 2007. A review of income and disbursements for the period was made to the extent deemed necessary.

The items comprising the Balance Sheet for which Specific Risk Analyses (SRA) were required had medium or low risk assessments as determined from the *National Association of Insurance Commissioners Examiners Handbook.* Analytical review procedures were applied for non-SRA items.

The services of AMI Risk Consultants, Inc. were employed pursuant to the provisions of Code of Virginia § 38.2-1318.E. This engagement was made to provide an actuarial report as to the reasonableness of the Exchange's loss and loss adjustment expense reserves reported as of December 31, 2007.

In addition, the following items were reviewed, several of which are discussed separately under their respective captions in this report.

History
Management and Control
Records of the Exchange
Compensation of Attorney-in-Fact
Fidelity Bond and Other Insurance
Territory and Plan of Operation
Growth of the Exchange
Reinsurance
Accounts and Records
Financial Statements
Conflict of Interest

FINANCIAL STATEMENTS

There follows a statement of financial condition of the Exchange at December 31, 2007, a statement of income for the year ending December 31, 2007, a reconciliation of surplus for the period under review and a statement of cash flow for the year ending December 31, 2007. The financial statements are presented in accordance with Statutory Accounting Principles.

ASSETS

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$21,301,426		$21,301,426
Common stocks	10,136,164		10,136,164
Cash and short-term investments	923,814		923,814
Investment income due and accrued	258,288		258,288
Premiums and considerations:			
Uncollected premiums and agents' balances in the course of collection	288,063	87,454	200,609
Deferred premiums, agents' balances and installments booked but deferred and not yet due	2,909,616		2,909,616
Amounts recoverable from reinsurers	20,470		20,470
Net deferred tax asset	1,445,339	996,617	448,722
Guaranty funds receivable or on deposit	53,254		53,254
Electronic data processing equipment and software	244,788	244,788	
Aggregate write-ins for other than invested assets	118,482	49,769	68,713
Totals	$37,699,704	$1,378,628	$36,321,076

LIABILITIES, SURPLUS AND OTHER FUNDS

Losses		$12,949,390
Loss adjustment expenses		1,893,376
Other expenses		355,290
Taxes, licenses and fees		122,031
Unearned premiums		4,780,566
Dividends declared and unpaid		55,351
Ceded reinsurance premiums payable		99,112
Funds held by company under reinsurance treaties		5,530
Reserve for return of subscriber saving accounts		560,430
Total liabilities		$20,821,076
Subscriber saving accounts	$12,664,358	
Unassigned funds (surplus)	2,835,642	
Surplus as regards policyholders		15,500,000
Totals		$36,321,076

UNDERWRITING AND INVESTMENT EXHIBIT
STATEMENT OF INCOME

UNDERWRITING INCOME

Premiums earned	$11,509,696
Deductions:	
Losses incurred	$5,871,215
Loss expenses incurred	2,038,454
Other underwriting expenses incurred	3,575,608
Aggregate write-ins for underwriting deductions	(31,181)
Total underwriting deductions	$11,454,096
Net underwriting gain	$55,600

INVESTMENT INCOME

Net investment income earned	$1,018,945
Net realized capital gains	1,557,958
Net investment gain	$2,576,903

OTHER INCOME

Non-underwriting income	$37,729
Total other income	$37,729
Net income before dividends to policyholders	$2,670,232
Dividends to policyholders	55,351
Net income	$2,614,881

RECONCILIATION OF CAPITAL AND SURPLUS FOR PERIOD UNDER REVIEW

	2005	2006	2007
Surplus as regards policyholders, December 31, previous year	$14,541,000	$14,541,000	$14,541,000
Net income	$1,207,153	$2,446,359	$2,614,881
Change in net unrealized capital gains or (losses)	158,608	(348,296)	(866,919)
Change in net deferred income tax	8,209	(14,369)	119,555
Change in nonadmitted assets	25,418	4,104	(323,763)
Change in provision for reinsurance		(28,400)	28,400
Aggregate write-ins for gains and losses in surplus:			
Increase in contingency reserve		22,229	11,668
Decrease in subscriber savings accounts	(1,399,388)	(2,081,627)	(624,822)
Change in surplus as regards policyholders for the year	$0	$0	$959,000
Surplus as regards policyholders, December 31, current year	$14,541,000	$14,541,000	$15,500,000

CASH FLOW

Cash From Operations

Premiums collected net of reinsurance	$12,136,094
Net investment income	1,035,925
Miscellaneous income	37,729
Total	$13,209,748
Benefits and loss related payments	$5,644,002
Commissions, expenses paid and aggregate write-ins for deductions	4,564,241
Dividends paid to policyholders	1,363,561
Total	$11,571,804
Net cash from operations	$1,637,944

Cash From Investments

Proceeds from investments sold, matured or repaid:	
Bonds	$6,473,472
Stocks	16,856,872
Net gains on cash and short-term investments	2
Total investment proceeds	$23,330,346
Cost of investments acquired (long-term only):	
Bonds	$6,041,552
Stocks	16,191,914
Miscellaneous applications	357,437
Total investments acquired	$22,590,903
Net cash from investments	$739,443

Cash From Financing and Miscellaneous Sources

Cash provided (applied):	
Other cash applied	($2,373,662)
Net cash from financing and miscellaneous sources	($2,373,662)
Net change in cash and short-term investments	$3,725

RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS

Cash and short-term investments:	
Beginning of year	$920,089
End of year	923,814
Net change in cash and short-term investments	$3,725

RECOMMENDATION FOR CORRECTIVE ACTION

During the review of loss adjustment expenses, it was noted the Exchange was classifying such expenses as either direct loss adjustment expenses or unallocated loss adjustment expenses. Pursuant to the NAIC Accounting Practices and Procedures Manual, SSAP No. 55-Unpaid Claims, Losses and Loss Adjustment Expenses states loss adjustment expenses should be classified as either defense and cost containment or adjusting and other. The Examiners recommend the Exchange correctly classify their loss adjustment expenses.

CONCLUSION

The courteous cooperation extended by the Attorney-in-Fact's officers and employees during the course of the examination is hereby gratefully acknowledged.

In addition to the undersigned, Jennifer K. Crawley, CFE, Mario A. Cuellar, CFE, and Theresa C. Lewis, CFE of the Bureau participated in the work of the examination.

Respectfully submitted,

T. Bradford Earley, Jr., CFE, CPCU, AIAF
Insurance Principal Financial Analyst
Commonwealth of Virginia
Representing the Southeastern Zone, NAIC

Southern States Insurance Exchange

Southern States Insurance Exchange

Southern States Underwriters, Inc., Attorney-in-Fact
6606 West Broad Street, Richmond, Virginia 23230 • Switchboard (804) 281-1525 • Facsimile (804) 281-1042

September 23, 2008

Mr. David H. Smith, CFE, CPA, CPCU
Chief Examiner
State Corporation Commission
Bureau of Insurance
P. O. Box 1157
Richmond, Virginia 23218

RE: Southern States Insurance Exchange
Examination Report as of December 31, 2007

Dear Mr. Smith:

I appreciate the courteous and professional manner in which Mr. Earley and his team conducted the recent examination. Please provide us with fifteen copies of the report.

We are taking the following actions in response to your recommendation:

Loss Adjustment Expenses

Recommendation: During the review of loss adjustment expenses, it was noted that the Exchange was classifying such expenses as either direct loss adjustment expenses or unallocated loss adjustment expenses. Pursuant to the NAIC Accounting Practices and Procedures manual, SSAP No. 55-Unpaid Claims, Losses and Loss Adjustment Expenses states loss adjustment expenses should be classified as either defense and cost containment or adjusting and other. The Examiners recommend the Exchange correctly classify their loss adjustment expenses.

Response: The responsible personnel fully understand the requirements and in the future the Exchange will correctly classify its loss adjustment expenses.

Sincerely

Rex P. Honodel

Rex P. Honodel, CPCU, AIAF, CIC
President of Attorney-in-Fact