



THE STATE
of **ALASKA**
GOVERNOR MICHAEL J. DUNLEAVY

Department of Commerce, Community,
and Economic Development

DIVISION OF INSURANCE

550 West Seventh Avenue, Suite 1560
Anchorage, AK 99501-3567
Main: 907.269.7900
Fax: 907.269.7910

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

STATE OF ALASKA
DEPARTMENT OF COMMERCE, COMMUNITY AND
ECONOMIC DEVELOPMENT
DIVISION OF INSURANCE
550 WEST 7TH AVENUE, SUITE 1560
ANCHORAGE, AK 99501-3567

Order FE 18-01)
In the Matter of Examination of)
ARECA Insurance Exchange)

FINDINGS OF FACT

1. A report of examination of ARECA Insurance Exchange, domiciled in the State of Alaska, has been issued by the State of Alaska, Division of Insurance, to ARECA Insurance Exchange.
2. The Report of Examination of ARECA Insurance Exchange (FE 18-01) has been transmitted to Brenda Mead, Chief Financial Officer of ARECA Insurance Exchange (Examinee), and Examinee has been accorded at least 30 days opportunity to review and comment on this Report of Examination. A response from the examinee was received on June 3, 2019.
3. The Director of the Division of Insurance has fully considered and reviewed the report, the examinee response and any relevant portions of the examiner's work papers to the extent she considered necessary.

CONCLUSIONS OF LAW

1. The written Report of Examination referred to in Finding of Fact No. 1 was issued in accordance with Alaska Statute (AS) 21.06.150(b).

2. The actions set forth in Finding of Fact No. 2 were conducted in accordance with AS 21.06.150(b).

3. The Director of the Division of Insurance has reviewed the Report of Examination, the examinee response and any other relevant work papers as set forth in Finding of Fact No. 3 to the extent she considered necessary in accordance with AS 21.06.150(b).

ORDER

IT IS ORDERED

1. Pursuant to AS 21.06.150(b)(1), the Report of Examination of ARECA Insurance Exchange (FE 18-01) is approved as filed.

2. Pursuant to AS 21.06.060, the Report of Examination shall be kept in the Office of the Director of the Division of Insurance and be open to public inspection.

This order is effective June 14, 2019.

Dated this 14th day of June, 2019 in Anchorage, Alaska.



Lori Wing-Heier, Director
State of Alaska
Division of Insurance

Statutory Financial Examination of
ARECA INSURANCE EXCHANGE

FE 18-01

As of
December 31, 2017

Issued by
STATE OF ALASKA
DEPARTMENT OF COMMERCE, COMMUNITY, AND
ECONOMIC DEVELOPMENT
DIVISION OF INSURANCE

NAIC Company Code: 16926
NAIC Group Code: N/A

FINAL REPORT:
May 23, 2019

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June 14, 2019

Lori Wing-Heier, Director
Division of Insurance
Department of Commerce, Community
and Economic Development
State of Alaska
550 West 7th Avenue, Suite 1560
Anchorage, AK 99501-3567

Dear Director Wing-Heier:

In accordance with your instructions and authorizations, and in accordance with statutory requirements, an examination has been made of the financial condition and business affairs of:

ARECA Insurance Exchange (the Exchange)
703 West Tudor Road
Anchorage, AK 99503

(NAIC CoCode 16926)

SCOPE OF EXAMINATION

We have performed our full-scope single-state examination of ARECA Insurance Exchange covering the three-year period of January 1, 2015 through December 31, 2017. Transactions subsequent to the full-scope examination period were reviewed where deemed appropriate. The last examination covered the period of January 1, 2012, through December 31, 2014.

We conducted our examination in accordance with the NAIC *Financial Condition Examiners Handbook* (Handbook). The Handbook requires that we plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and

evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as required by AS 21.06.150, and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g. subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

SUMMARY OF EXAMINATION FINDINGS

Significant Finding

The examination team noted there was no discussion captured in the minutes regarding the approval of the external auditors at the Joint Audit Committee meetings.

DESCRIPTION OF COMPANY

Company History

The Exchange is an Alaska-domiciled insurance company organized pursuant to Title 21, Chapter 75, of the Alaska Statutes. The Exchange is an unincorporated reciprocal exchange for assessable policies that was formed to provide workers' compensation, property, boiler and machinery, general, and automotive liability insurance to members of the Alaska Power Association (APA), formerly known as the Alaska Rural Electric Cooperative Association. ARECA Insurance Management, Inc. (AIM) is the wholly-owned attorney-in-fact for the Exchange. The Exchange received a Certificate of Authority, #D-1530, from the State of Alaska on December 30, 1983, authorizing them to transact the business of property, casualty, surety, boiler and machinery, marine and transportation, and health insurance. As of December 31, 2017, the Exchange was licensed only in Alaska.

Management and Control

The Exchange is an unincorporated association of subscribers that insure the other subscribers in the Exchange. Membership in the Exchange is effective following the execution and approval of a Subscriber's Agreement between the Exchange and each member. Each subscriber has a contingent assessment liability, as provided in the subscribers' agreement, for payment of actual losses and expenses incurred while the subscriber's policy was in force. Subscribers may be required to make contributions to surplus of the Exchange from time to time as required by the Trustees in order to maintain adequate levels of surplus. Pursuant to the bylaws no one subscriber shall be assessed an aggregate liability in any one calendar year in excess of an amount equal to the direct premiums for such a policy during the year.

The Exchange has a subscribers' advisory committee (Board of Trustees) that consists of one person selected by the governing body of each member. The Board of Trustees elects the Chairman of the Board of Trustees, and any other officers as the business of the Exchange may require. Following is a list of officers so elected/appointed for the Exchange as of December 31 of each year covered by this examination, as reported in the minutes of the Board of Trustees.

| NAME | TITLE | December 31, | | |
|-----------------|---------------|--------------|------|------|
| | | 2015 | 2016 | 2017 |
| Meera Kohler | Chairman | X | X | X |
| Rick Schikora | Vice Chairman | X | X | X |
| Jodi Mitchell | Treasurer | X | X | X |
| Crystal Enkvist | Secretary | X | X | X |

Pursuant to the management agreement dated December 16, 1983, the affairs of the Exchange are handled by the attorney-in-fact, AIM, which is a wholly owned subsidiary of the Exchange. A Services Contract between the Exchange and the Alaska Power Association dated February 26, 2014, requires that the attorney-in-fact receives reimbursement of proportionate employee costs from the Exchange.

Pursuant to the bylaws of AIM, the attorney-in-fact shall have seven directors from the members of the governing bodies of the subscribers of the Exchange, and no subscriber shall provide more than one director. Any subscriber credited with more than 20% of capital and surplus of the Exchange shall be entitled to designate one director to the Board of Directors of the attorney-in-fact.

Related Party Activity

Conflict of Interest

The Exchange has established a formal code of conduct outlining procedures for disclosure of potential conflicts of interest. Annual conflict of interest disclosure questionnaires are to be completed by all officers and directors. They are submitted to the Company's Secretary and reviewed by the Board of Trustees for resolution of any potential conflict. These statements identify any material interest or affiliation which may conflict with the duties of such person on behalf of the Exchange.

Territory and Plan of Operation

The Exchange is authorized to transact the following lines of business: property, casualty, surety, health, marine, and transportation policies. As of December 31, 2017, they were licensed only in Alaska. The Exchange's marketing strategy utilized appointed agents to increase the number of its subscribers.

Based on the lines of business for which the Exchange is licensed, and pursuant to the requirements of AS 21.09.070, the Exchange is required to maintain minimum policyholders' surplus of \$4,125,000.

Reinsurance

The Exchange has reinsured its cumulative and individual risks through excess-of-loss per-occurrence and facultative reinsurance agreements through placements with various reinsurers.

As of December 31, 2017, the Exchange had a maximum retention per occurrence of \$500,000 on workers' compensation, automobile liability and general liability and \$750,000 retention on property. Automobile liability and general liability were reinsured up to \$2,000,000 in losses and workers' compensation was reinsured up to \$30,000,000 in losses. Excess-of-loss property reinsurance covers 100% of losses up to \$50,000,000 excess of \$750,000 of all physical perils excluding earthquake and flood and equipment breakdown. Earthquake and flood and equipment breakdown are reinsured 100% up to \$50,000,000. Commercial umbrella liability and directors, officers and managers liability are reinsured 100% up to \$20,000,000.

The Exchange does not assume any reinsurance.

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Exchange with the Alaska Division of Insurance and present the financial condition of the company for the period ending December 31, 2017. The accompanying comments on financial statements should be considered an integral part of the financial statements.

FINANCIAL STATEMENTS
STATEMENT OF ASSETS, LIABILITIES and SURPLUS
As of December 31, 2017

| | As Reported 12/31/2017 |
|---|---------------------------|
| <u>Assets</u> | |
| Bonds | \$ 23,422,321 |
| Common stocks | 1,567,130 |
| Properties occupied by the company | 153,415 |
| Properties held for the production of income | 156,057 |
| Cash, cash equivalents and short-term investments | 2,362,556 |
| Total cash and invested assets | 27,661,479 |
| Investment income due and accrued | 151,481 |
| Uncollected premiums and agents' balances in the course of collection | 9,256 |
| Deferred premiums, agents' balances and installments booked but deferred | 580,537 |
| Amounts recoverable from reinsurers | 6,508 |
| Other amounts receivable under reinsurance contracts | 5,802 |
| Current federal income tax recoverable | 10,000 |
| Total Admitted Assets | \$ 28,425,062 |
| <u>Liabilities, Surplus, and Other Funds</u> | |
| <u>Liabilities</u> | |
| Losses | \$ 4,976,141 |
| Loss adjustment expenses | 1,073,436 |
| Commissions payable, contingent commissions and other charges | 1,028 |
| Other expenses | 286,745 |
| Taxes, licenses and fees | 26,552 |
| Unearned premiums | 1,566,593 |
| Advance premium | 79,777 |
| Ceded reinsurance premiums payable | 9,332 |
| Payable to parent, subsidiaries and affiliates | 92,658 |
| Aggregate write-ins for liabilities | 25,236 |
| Total Liabilities | \$ 8,137,498 |
| <u>Surplus</u> | |
| Aggregate write-ins for other-than-special surplus funds | 225,893 |
| Unassigned funds | 20,061,671 |
| Total surplus | \$ 20,287,564 |
| Total Liabilities and Surplus | \$ 28,425,062 |

FINANCIAL STATEMENTS
STATEMENT OF OPERATIONS
As of December 31, 2017

| | <u>As Reported</u> <u>12/31/2017</u> |
|--|---|
| <u>Underwriting Income</u> | |
| Premiums earned | <u>\$ 3,646,143</u> |
| <u>Deductions</u> | |
| Losses incurred | \$ 1,463,470 |
| Loss adjustment expenses | 667,985 |
| Other underwriting expenses incurred | <u>1,696,296</u> |
| Total underwriting deductions | <u>\$ 3,827,751</u> |
| Net underwriting gain or (loss) | <u>\$ (181,608)</u> |
| <u>Investment Income</u> | |
| Net investment income earned | \$ 557,719 |
| Net realized capital gains | <u>72,189</u> |
| Net Investment gain or (loss) | <u>\$ 629,908</u> |
| <u>Other Income or (Loss)</u> | |
| Finance and service charges not included in premiums | \$ 2,195 |
| Aggregate write-ins for miscellaneous income | <u>1,528</u> |
| Net Other Income or (loss) | <u>\$ 3,723</u> |
| Net income before federal income tax | \$ 452,023 |
| Federal income taxes incurred | <u>-</u> |
| Net income (loss) | <u>\$ 452,023</u> |

FINANCIAL STATEMENTS
RECONCILIATION OF CAPITAL AND SURPLUS
As of December 31, 2017

| | Gross Paid-in and Contributed Surplus | Surplus Allocated to Policyholders | Unassigned Surplus (Deficit) | Total Policyholders' Surplus |
|--|---|--|------------------------------------|------------------------------------|
| Balance at December 31, 2014 | \$ 19,937,923 | \$ 2,622,707 | \$ (687,936) | \$ 21,872,694 |
| Net income - 2015 | | | 616,051 | 616,051 |
| Allocation of current year net gain to policyholders | | 616,051 | (616,051) | - |
| Change in net unrealized capital gains | | | (276,004) | (276,004) |
| Change in non-admitted assets | | | 10,981 | 10,981 |
| Transfers to surplus | 2,622,706 | | | 2,622,706 |
| Prior year gain allocated to policyholders | | (2,622,706) | | (2,622,706) |
| Surplus paid to policyholders | (593,419) | | | (593,419) |
| Surplus paid to discontinued policyholders | (1,279,276) | | | (1,279,276) |
| Other adjustments | 70 | | (65,828) | (65,758) |
| Balance at December 31, 2015 | \$ 20,688,003 | \$ 616,052 | \$ (1,018,786) | \$ 20,285,269 |
| Net income (loss) - 2016 | | | 1,019,831 | 1,019,831 |
| Allocation of current year net gain to policyholders | | 1,019,831 | (1,019,831) | (1) |
| Change in net unrealized capital gains | | | (42,926) | (42,926) |
| Change in non-admitted assets | | | (28,156) | (28,156) |
| Transfers to surplus | 616,051 | | | 616,051 |
| Prior year gain allocated to policyholders | | (616,051) | | (616,051) |
| Surplus paid to policyholders | | | (142,634) | (142,634) |
| Surplus paid to discontinued policyholders | | | (548,180) | (548,180) |
| Balance at December 31, 2016 | \$ 21,304,055 | \$ 1,019,831 | \$ (1,780,682) | \$ 20,543,204 |
| Net income - 2017 | | | 452,023 | 452,023 |
| Change in net unrealized capital gains | | | 227,316 | 227,316 |
| Change in non-admitted assets | | | (20,669) | (20,669) |
| Surplus paid to policyholders | | | (200,285) | (200,285) |
| Surplus paid to discontinued policyholders | | | (714,025) | (714,025) |
| Reclassification adjustments | (21,078,162) | (1,019,831) | 22,097,993 | - |
| Balance at December 31, 2017 | \$ 225,893 | \$ 0 | \$ 20,061,671 | \$ 20,287,564 |

**ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS
RESULTING FROM THE EXAMINATION**

No adjustments to the financial statements filed as of December 31, 2017 were made to surplus as a result of the examination.

COMMENTS ON FINANCIAL STATEMENTS

There were no recommendations to be made within the scope of this report of examination.

SUBSEQUENT EVENTS

There were no subsequent events that occurred between the end of the valuation period of this examination and the date of this report to be of significance for comment.

SUMMARY OF RECOMMENDATIONS

Finding – External Auditor Review

The examiners determined in a review of the Joint Audit Committee (JAC) meeting minutes that no discussion of External Auditors is captured. The CFO, who is authorized to sign the letter, receives the Engagement Letter and reviews it. The Engagement Letter is signed by both the CFO and the JAC Chair. As per 3 AAC 21.720 (k) the audit services must be preapproved by the board of directors; however, under 3 AAC 21.720 (l) the Board of Directors or Audit Committee may delegate a member(s) the authority for preapproval. If so, "the decisions of any member to whom this authority is delegated must be presented to the full board of directors or audit committee at each of its scheduled meetings". No record of approval was found in review of the JAC meeting minutes thus a violation of 3 AAC 21.720 (l).

CLOSING

This examination was conducted in accordance with practices and procedures promulgated by the NAIC. This examination also includes a compliance review of applicable Alaska Statutes and Regulations.

In addition to the undersigned, the following examiners participated in the examination from the Alaska Division of Insurance: Insurance Financial Examiner II Wallace R. Thomas, Actuary Michael D. Ricker, FCAS, MAAA, Insurance Financial Examiner I Laura L. Hancock and Insurance Financial Examiner I Jeffery A. Bethel. Also participating in the examination were contract examiners from Risk and Regulatory Consulting, LLC, as follows: John Humphries, CFE, ASA, MAAA, CISA, AES; Darlene Lenhart-Schaeffer, CISA, CFE; and Joshua J. Johnson, CFE.

We wish to express our appreciation for the courteous cooperation and assistance extended to us by the management and staff of ARECA Insurance Exchange during the course of this examination.

This report is respectfully submitted,



Cathie A. Stewart, CPA, CFE
Examiner-in Charge
Risk and Regulatory Consulting, LLC



W. David Phifer, CFE
Chief Financial Examiner
State of Alaska

AFFIDAVIT

Tucson, Arizona)
June 14, 2019)
STATE OF ARIZONA)
COUNTY OF PIMA)

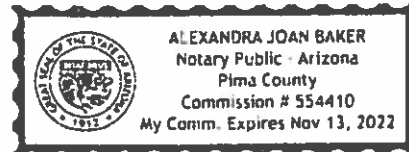
I, the undersigned, being duly sworn, do verify that the report of examination as of December 31, 2017, of ARECA Insurance Exchange, an Alaska-domiciled company holding Certificate of Authority #D-1530, is true to the best of my knowledge and belief.

Cathie A. Stewart
Cathie A. Stewart, CPA, CFE
Examiner-in-Charge
Risk and Regulatory Consulting, LLC

Subscribed and sworn to before me this 14 day of June, 2019.

Alexandra Joan Baker
Notary Public for the State of Arizona

My commission expires: 11-13-2022



AFFIDAVIT

Anchorage, Alaska)
June 14, 2019)
STATE OF ALASKA)
THIRD JUDICIAL DISTRICT)

I, the undersigned, being duly sworn, do verify that the report of examination as of December 31, 2016, of Alaska National Insurance Company, an Alaska-domiciled company holding Certificate of Authority #D-1285, is true to the best of my knowledge and belief.

David Phifer

W. David Phifer, CFE
Chief Financial Examiner
State of Alaska

Subscribed and sworn to before me this 14th day of June, 2019.

[Signature]

Notary Public for the State of Alaska

My commission expires: with office

