

**EXAMINATION REPORT  
ON  
SOUTHERN STATES INSURANCE EXCHANGE  
Richmond, Virginia  
as of  
December 31, 2016**

**COMMONWEALTH OF VIRGINIA  
STATE CORPORATION COMMISSION  
BUREAU OF INSURANCE**

# COMMONWEALTH OF VIRGINIA

SCOTT A. WHITE  
COMMISSIONER OF INSURANCE  
STATE CORPORATION COMMISSION  
BUREAU OF INSURANCE



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I, Scott A. White, 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, 2016, 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 9<sup>th</sup> day of March 2018

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Scott A. White  
Commissioner of Insurance

(SEAL)

TABLE OF CONTENTS

Scope of the Examination ..... 1

History ..... 2

Management and Control ..... 3

Compensation of Attorney-in-Fact..... 5

Territory and Plan of Operation ..... 5

Reinsurance ..... 7

Growth of the Exchange..... 10

Financial Statements ..... 11

Subsequent Event ..... 11

Acknowledgement..... 18

Richmond, Virginia  
December 5, 2017

Honorable Jacqueline K. Cunningham  
Commissioner of Insurance  
Commonwealth of Virginia  
Richmond, Virginia

Dear Madam:

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.

**SCOPE OF THE EXAMINATION**

The last examination of the Exchange was made by representatives of the State Corporation Commission's Bureau of Insurance (Bureau) as of December 31, 2013. The current examination covers the three-year period from January 1, 2014 through December 31, 2016.

The examination was conducted in accordance with the NAIC *Financial Condition Examiners Handbook* (Handbook). The Handbook requires that the Bureau plan and perform the examination to evaluate the Exchange's financial condition, assess corporate governance, identify current and prospective risks of the Exchange, 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 Exchange 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.

The services of Merlinos & Associates, Inc. were employed to provide an actuarial report as to the reasonableness of the Exchange's loss and loss adjustment expense reserves as of December 31, 2016.

This examination report includes significant findings of fact 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 Exchange.

## **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. (name changed to Southern States Underwriters, LLC, hereinafter referred to as SSU) 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 SSU 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 SSU. The agreement further provided that SSU, 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 referred to as "dealers". In 1991, the Exchange began to increase its dealers business. By 2016, approximately 180 of these businesses had become dealers.

On April 22, 1987, by resolution, SSU 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 SSU 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 SSU or any person employed by, representing, or having a financial interest in SSU. 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 SSU.

The Cooperative represents a majority of the Class 1 voting subscribers and owns all of the outstanding stock of SSU, thereby giving the Cooperative apparent control over the Exchange.

At December 31, 2016, the Members of the Advisory Committee and its officers were as follows:

<u>Advisory Committee</u>	<u>Principal Business Affiliation</u>
Kevin M. Brown	President Southern States Underwriters, LLC Richmond, Virginia
Anne M. Clingenpeel	Vice President Retail Operations Southern States Cooperative Richmond, Virginia
William T. Didlake, Jr.	Senior Vice President and Controller Southern States Cooperative Richmond, Virginia

Frederic Jezouit	Executive Vice President and Chief Financial Officer Southern States Cooperative Richmond, Virginia
Robert H. Mauck, Jr.	President Scott Insurance Richmond, Virginia
Alfie Q. Parker, III	Manager Southern States Farmers Cooperative Farmville, Virginia
Wayne D. Wayland	Manager Southern States Orange-Madison Cooperative, Inc. Madison, Virginia
Norman R. Wenger	General Manager Rockingham Cooperative Farm Bureau Harrisonburg, Virginia
Samuel G. Williams	Manager Southern States Bedford Cooperative, Inc. Bedford, Virginia

Officers

Frederic Jezouit	Chairman
Kevin M. Brown	Secretary

The board of directors and officers of SSU were as follows at December 31, 2016:

Directors

Kevin M. Brown  
Frederic Jezouit

Officers

Kevin M. Brown	President
Denise L. Husted	Secretary and Treasurer
Diane D. Sexton	Assistant Treasurer

## COMPENSATION OF ATTORNEY-IN-FACT

SSU 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, SSU 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 SSU to serve as Attorney-in-Fact. SSU 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 SSU, 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 2014, 2015 and 2016 was \$3,009,434, \$3,040,042 and \$3,299,555, respectively.

### Joint Sales and Marketing Agreement

On January 1, 2009, the Exchange amended its joint sales and marketing agreement with SSC Insurance Agency, LLC. (SSCIA), an affiliate of SSU. 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, South Carolina and Tennessee. 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 \$597,798, \$661,531 and \$749,323 to SSCIA during 2014, 2015 and 2016, respectively.

## TERRITORY AND PLAN OF OPERATION

The Exchange was authorized to operate in the following states at December 31, 2016, as evidenced by licenses in its possession:

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



In Virginia, the Exchange was licensed to write the following insurance coverages at December 31, 2016:

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; 48 independent local farm cooperatives operated by the Cooperative under management agreements; 11 independent local cooperatives not operated by management agreement; and approximately 178 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. 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 2014, 2015 and 2016. Such distributions, combined with dividends paid to policyholders, are included in the Growth of the Exchange section of this report. Additionally, subscribers receive their remaining savings upon withdrawal from the Exchange, generally by March 15 of the following year after their withdrawal as a subscriber.

**REINSURANCE**

At December 31, 2016, the Exchange had the following reinsurance coverage in force:

<u>Type of Agreement</u>	<u>Types of Policies Covered</u>	<u>Limit of Reinsurance</u>
Combined Excess of Loss	Property	\$700,000 excess of \$300,000 per risk, subject to \$2,100,000 limit any one loss occurrence
	Workers' Compensation, and Employers' Liability	\$700,000 excess of \$300,000 each loss occurrence
	Automobile Liability, Commercial General Liability, and Garage Liability	\$700,000 excess of \$300,000 each loss occurrence
		In the event of a combined loss recoverable of all of the above, \$600,000 each occurrence excess of \$300,000 each loss occurrence
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

<u>Type of Agreement</u>	<u>Types of Policies Covered</u>	<u>Limit of Reinsurance</u>
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 \$27,000,000
Workers Compensation Facultative	Workers' Compensation and Employers' Liability	\$175,000,000 per occurrence excess of \$14,000,000 per occurrence
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

<u>Type of Agreement</u>	<u>Types of Policies Covered</u>	<u>Limit of Reinsurance</u>
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
Umbrella Excess of Loss Facultative	Commercial Liability	\$5,000,000 each loss occurrence excess of \$5,000,000 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.

### 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, 2016:

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Subscriber Savings Accounts</u>	<u>Unassigned Funds</u>
2007	\$36,321,076	\$20,821,077	\$12,664,358	\$2,835,641
2008	33,036,908	19,608,075	13,280,794	148,039
2009	37,438,376	21,438,376	13,646,429	2,353,571
2010	39,662,477	23,412,477	12,586,946	3,663,054
2011	41,367,702	24,867,702	12,644,680	3,855,320
2012	43,377,291	26,627,291	11,646,963	5,103,037
2013	42,410,562	25,410,562	10,632,490	6,367,510
2014	42,909,990	25,659,990	10,782,134	6,467,866
2015	41,799,469	24,299,469	11,497,074	6,002,926
2016	41,983,066	24,233,066	11,581,308	6,168,692

	<u>Premiums Earned</u>	<u>Losses and Loss Adjustment Expenses Incurred</u>	<u>Other Underwriting Expenses</u>	<u>Net Underwriting Gain</u>
2007	\$11,509,696	\$7,909,669	\$3,544,427	\$55,600
2008	12,064,822	8,024,201	3,432,792	607,829
2009	12,788,820	7,093,703	3,306,981	2,388,136
2010	12,423,429	7,533,301	3,013,431	1,876,697
2011	13,099,114	8,503,825	3,006,419	1,588,870
2012	13,989,919	8,794,427	3,174,266	2,021,226
2013	13,707,265	8,740,333	3,300,827	1,666,105
2014	14,011,008	7,703,661	3,402,007	2,905,340
2015	14,547,539	8,430,047	3,419,405	2,698,087
2016	15,457,500	10,428,283	4,219,660	809,557

	<u>Management Fees Incurred</u>	<u>Equities and Dividends Paid to Subscribers</u>
2007	\$2,199,937	\$3,405,767
2008	2,316,521	615,782
2009	2,470,617	0
2010	2,463,830	2,377,372
2011	2,688,997	3,488,830
2012	2,914,125	2,640,984
2013	2,909,955	4,181,834
2014	3,009,434	4,014,881
2015	3,040,042	4,093,307
2016	3,299,555	3,196,183

### **FINANCIAL STATEMENTS**

The following statutory financial statements present the financial condition of the Exchange for the period ending December 31, 2016. No examination adjustments were made to the statutory financial statements filed by the Exchange with the Bureau for the period ending December 31, 2016.

**ASSETS**

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$22,181,792		\$22,181,792
Common stocks	9,291,704		9,291,704
Cash and short-term investments	1,500,215		1,500,215
Investment income due and accrued	158,610		158,610
Premiums and considerations:			
Uncollected premiums and agents' balances in the course of collection	141,085	15,564	125,521
Deferred premiums, agents' balances and installments booked but deferred and not yet due	6,989,878		6,989,878
Amounts recoverable from reinsurers	875,435		875,435
Net deferred tax asset	1,209,573	387,847	821,726
Guaranty funds receivable or on deposit	25,431		25,431
Aggregate write-ins for other than invested assets	12,754		12,754
	<u>12,754</u>	<u>387,847</u>	<u>12,754</u>
Totals	<u>\$42,386,477</u>	<u>\$403,411</u>	<u>\$41,983,066</u>

**LIABILITIES, SURPLUS AND OTHER FUNDS**

Losses		\$11,754,068
Loss adjustment expenses		1,768,941
Commissions payable, contingent commissions and other similar charges		66,154
Other expenses		552,821
Taxes, licenses and fees		156,017
Unearned premiums		7,231,259
Advance premium		48,532
Dividends declared and unpaid		750,000
Ceded reinsurance premiums payable		275,465
Provision for reinsurance		37,000
Aggregate write-ins for liabilities		<u>1,592,809</u>
 Total liabilities		 \$24,233,066
 Aggregate write-ins for other than special surplus funds:		
Subscriber saving accounts	\$11,581,308	
Unassigned funds (surplus)	<u>6,168,692</u>	
 Surplus as regards policyholders		 <u>17,750,000</u>
 Totals		 <u><u>\$41,983,066</u></u>



**UNDERWRITING AND INVESTMENT EXHIBIT**  
**STATEMENT OF INCOME**

UNDERWRITING INCOME

Premiums earned	\$15,457,500
Deductions:	
Losses incurred	\$8,607,613
Loss adjustment expenses incurred	1,820,670
Other underwriting expenses incurred	4,219,660
Total underwriting deductions	\$14,647,943
Net underwriting gain	\$809,557

INVESTMENT INCOME

Net investment income earned	\$603,686
Net realized capital gains	571,795
Net investment gain	\$1,175,481

OTHER INCOME

Aggregate write-ins for miscellaneous income	(\$3,982)
Total other income	(\$3,982)
Net income before dividends and federal income taxes	\$1,981,056
Dividends to policyholders	750,000
Net income after dividends and before federal income taxes	\$1,231,056
Federal income taxes incurred	(282,608)
Net income	\$1,513,664

**RECONCILIATION OF CAPITAL AND SURPLUS**  
**FOR PERIOD UNDER REVIEW**

	<u>2014</u>	<u>2015</u>	<u>2016</u>
Surplus as regards policyholders, December 31, previous year	<u>\$17,000,000</u>	<u>\$17,250,000</u>	<u>\$17,500,000</u>
Net income	\$3,499,383	\$3,412,422	\$1,513,664
Change in net unrealized capital gains or (losses)	(70,453)	(1,103,500)	111,240
Change in net deferred income tax	(53,326)	(68,144)	47,490
Change in nonadmitted assets	(52,015)	456,381	44,035
Change in provision for reinsurance			(37,000)
Aggregate write-ins for gains and (losses) in surplus	<u>(3,073,589)</u>	<u>(2,447,159)</u>	<u>(1,429,429)</u>
Change in surplus as regards policyholders for the year	<u>\$250,000</u>	<u>\$250,000</u>	<u>\$250,000</u>
Surplus as regards policyholders, December 31, current year	<u><u>\$17,250,000</u></u>	<u><u>\$17,500,000</u></u>	<u><u>\$17,750,000</u></u>

**CASH FLOW****Cash From Operations**

Premiums collected net of reinsurance	\$15,844,149
Net investment income	510,719
Miscellaneous income	(3,982)
Total	<u>\$16,350,886</u>
Benefits and loss related payments	\$7,925,995
Commissions, expenses paid and aggregate write-ins for deductions	5,550,795
Dividends paid to policyholders	1,000,000
Federal income taxes paid	11,951
Total	<u>\$14,488,741</u>
Net cash from operations	<u>\$1,862,145</u>

**Cash From Investments**

Proceeds from investments sold, matured or repaid:	
Bonds	\$6,648,514
Stocks	7,296,233
Miscellaneous proceeds	140,338
Total investment proceeds	<u>\$14,085,085</u>
Cost of investments acquired (long-term only):	
Bonds	\$6,833,051
Stocks	8,148,548
Miscellaneous applications	175,120
Total investments acquired	<u>\$15,156,719</u>
Net cash from investments	<u>(\$1,071,634)</u>

**Cash From Financing and Miscellaneous Sources**

Cash provided (applied):	
Other cash provided	<u>(\$2,421,653)</u>
Net cash from financing and miscellaneous sources	<u>(\$2,421,653)</u>
Net change in cash and short-term investments	<u>(\$1,631,142)</u>

**RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS**

Cash and short-term investments:	
Beginning of year	\$3,131,357
End of year	1,500,215
Net change in cash and short-term investments	<u>(\$1,631,142)</u>

**SUBSEQUENT EVENT**

A review of the Cooperative's financial statements as of June 30, 2016 resulted in the Bureau expressing concern regarding the financial condition of the Cooperative. As the Cooperative is the Exchange's largest subscriber, management of the Exchange provided information to the Bureau relating to the Cooperative's plans for corrective actions, as well as a detailed plan of operation, including proforma financial statements, for the Exchange should the Cooperative cease to be an insured of the Exchange.

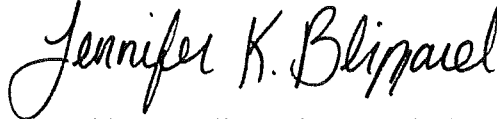
On September 22, 2017, the Cooperative refinanced its credit facility agreement that will be effective through September 22, 2022. The need for refinancing resulted from initiatives developed to assist in the improvement of the Cooperative's capital structure. The Cooperative will be able to alleviate some of its long-term debt with the proceeds from the sale of the agronomy retail and wholesale facilities and of its animal feed manufacturing business. The completion of this agreement and the addition of the sales allowed the independent auditors to issue an unqualified opinion for the Cooperative's June 30, 2017 financial statements

**ACKNOWLEDGEMENT**

The courteous cooperation extended by the Attorney-in-Fact's officers and employees during the course of the examination was sincerely appreciated.

In addition to the undersigned, Mario A. Cuellar, CFE, T. Bradford Earley, Jr., CFE, CPCU, AIAF, and Benjamin B. MacKercher, of the Bureau participated in the work of the examination.

Respectfully submitted,

A handwritten signature in black ink that reads "Jennifer K. Blizzard". The signature is written in a cursive, flowing style.

Jennifer K. Blizzard, CFE, AIAF, AIM  
Senior Insurance Examiner



## *Southern States Insurance Exchange*

Southern States Underwriters, LLC, Attorney-in-Fact  
6606 West Broad Street, Richmond, Virginia 23230 • Switchboard (804) 281-1525 • Facsimile (804) 281-7704

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February 28, 2018

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, 2016

Dear Mr. Smith,

This letter is to provide you with written acknowledgement of receipt of two draft copies of the Examination Report as of December 31, 2016 for Southern States Insurance Exchange. We have reviewed the report and have no issues with any matter contained in the report.

In order to meet the Exchange's present and future needs, please provide us with twenty copies of the final report.

Thank you for your assistance.

Sincerely,

A handwritten signature in black ink, appearing to read "Kevin M. Brown".

Kevin M. Brown  
President