



Evi Mercado-Lugo Member since 2008

We've always made it our business to save AAA Members money—on and off the road. That's why, in these tough economic times, we're helping you drive every dollar a little bit farther.

For over 100 years we've measured our success by the value we bring to Members' lives. And, as stewards of our Club's resources, we're confident you and each of your 4.3 million fellow Members will continue to find exceptional value in AAA Membership in the year ahead.

While 2010 was indeed a challenging year for so many of us, we're pleased to report that the Club finished the year in a solid financial position, well equipped to bring you still greater value in 2011. Thank you for your continued loyalty to AAA.

AAA EMERGENCY ROAD SERVICE **DISPATCHES**

2008	2,939,169
2009	2,852,046
2010	2,993,447

RECORDED MEMBER SAVINGS WITH AAA DISCOUNTS

2009	\$42,950,000
2010	\$44,300,000
Find Members-or AAA.com/savings	

¢42.0E0.000

MEMBERS CONDUCTING DMV TRANSACTIONS AT AAA BRANCHES

2008	1,290,519
2009	1,419,802
2010	1,494,592

Paul Gaffney, President and CEO

AAA Northern California, Nevada & Utah

Paula F. Downey, President and CEO

Paula F. Davrey

AAA Northern California, Nevada & Utah Insurance Exchange

Board

In 2010, our dedicated Board Members helped guide our progress as we implemented fresh, new ideas. Our Board of Directors is helping to sharpen our focus as we grow to serve Members in new ways. The Board brings a wealth of diverse experience and varied insights to AAA Northern California, Nevada & Utah.

As always, the Board's priorities in 2010 centered on helping us to anticipate Members' needs and adding value to the relationships we build through AAA Insurance, Membership and Travel.

Board Members

Vivian M. Stephenson (Chair) Mary B. Cranston (Vice Chair)

Robert N. Barone Gilbert W. Chester

(Insurance Bureau Board Member)

Kenneth L. Coleman

Paula R. Collins
Paula F. Downey

Edgar H. Grubb

Norma J. Howard

Sylvester Lucena

Wayne R. Moon Kenneth Nilsson

Wendy Paskin-Jordan

Leo Soong Bashir Wada

Shirley A. Ward

Daniel K. Whitehurst

Robert E. Wilcox

Honorary Directors

Rudy V. Balma John M. Bryan Jack Craemer

Harmon K. Howard

Ronald R. James

John T. Kehoe

Frank MacBride, Jr.
Dr. Alistair W. McCrone

Martin C. Nelsen

Patrick O'Melveny William M. Otterson

Jeanne M. Payne

Estelle G. Saltzman

Ivan L. Suess

Stephen H. Wainwright

Jean R. Wente Kline A. Wilson, Jr.

Management Officers

Paula F. Downey,
President and
Chief Executive Officer

Michael S. Day, *Treasurer*

Jamie E. Chung, *Secretary*

Officers

Vivian M. Stephenson, *Chair*

Mary B. Cranston, *Vice Chair*



California State Automobile Association

Consolidated Financial Statements December 31, 2010 and 2009

California State Automobile Association Table of Contents

December 31, 2010 and 2009

	Page(s)
Report of Independent Auditors	1
Consolidated Financial Statements	
Consolidated Statements of Financial Position	2
Consolidated Statements of Operations	3
Consolidated Statements of Changes in Members' Equity	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6–23



Report of Independent Auditors

Board of Directors California State Automobile Association Walnut Creek, California

Pricewaterhouse Coopers LLP

In our opinion, the accompanying consolidated statements of financial position and the related consolidated statements of operations, changes in members' equity, and cash flows presents fairly, in all material respects, the financial position of the California State Automobile Association and its subsidiaries (the Company) at December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

May 18, 2011

California State Automobile Association Consolidated Statements of Financial Position December 31, 2010 and 2009

(in thousands)

	2010			2009
Assets				
Current assets				
Cash and cash equivalents	\$	15,306	\$	19,111
Equity securities (cost: 2010 - \$186,042; 2009 - \$184,830)		196,318		185,355
Bonds (cost: 2010 - \$76,114; 2009 - \$72,363)		79,294		75,349
Accounts receivable, net		9,874		9,973
Related party receivables		7,634		7,618
Other current assets		19,455		19,524
Total current assets		327,881		316,930
Non-current assets				
Property, equipment and software, net		40,064		58,926
Deferred income tax asset non-current, net		6,528		1,167
Other non-current assets		6,244		5,562
Total non-current assets		52,836		65,655
Total assets	\$	380,717	\$	382,585
Liabilities and members' equity Current liabilities				
Unearned membership revenue and enrollment fees	\$	130,790	\$	126,921
Unpaid losses and loss adjustment expenses		23,108		22,015
Accounts payable, accrued expenses and other liabilities		16,491		19,275
Related party payables		14,650		38,919
Federal and state income taxes payable, net		3,168		2,722
Deferred income tax liability current, net		6,606		3,286
Total current liabilities		194,813		213,138
Non-current liabilities				
Unearned membership enrollment fees		11,836		10,403
Related party payables		8,689		7,955
Other non-current liabilities		1,149	-	1,719
Total non-current liabilities Total liabilities		21,674		20,077
	-	216,487		233,215
Commitments and contingencies (Note 7)				
Members' equity		154,300		146,132
Accumulated other comprehensive income		9,930		3,238
Total members' equity		164,230	-	149,370
Total liabilities and members' equity	\$	380,717	\$	382,585

The accompanying notes are an integral part of these consolidated financial statements.

California State Automobile Association Consolidated Statements of Operations For the Years Ended December 31, 2010 and 2009

(in thousands)

	2010		2009	
Revenues Membership Insurance commissions, royalties and brand name fees Travel services Advertising, credit card fees and other income Investment income, including realized gains and losses on investments and real estate income	\$	261,499 125,010 26,889 14,706	\$	247,703 124,339 26,739 21,772
Insurance premiums earned		8,178		7,706
		446,488		443,465
Expenses Emergency road service Sales and services General and administrative expenses Membership services Public services Insurance agency expenses Other		186,002 123,400 56,469 38,229 9,631 13,645 11,162 438,538		170,776 116,084 53,162 43,881 9,520 17,857 9,269 420,549
Income before federal and state income taxes		7,950		22,916
Provision (benefit) for federal and state income taxes		(218)		7,344
Net income	\$	8,168	\$	15,572

California State Automobile Association Consolidated Statements of Changes in Members' Equity For the Years Ended December 31, 2010 and 2009

(in thousands)

	Accumulated Other					
	N	lembers' Equity		prehensive ncome	•	Total
Balances, January 1, 2009	\$	128,317	\$	(4,266)	\$	124,051
Comprehensive income						
Net income		15,572		-		15,572
Cumulative effect of change in accounting principle (Note 2 - Topic 320)		346		(346)		_
Cumulative effect of change in accounting		340		(340)		
principle (Note 2 - Topic 740)		1,897		-		1,897
Other comprehensive income, net of tax						
Net unrealized gain on investments arising during				44.000		44.000
the period		-		11,636		11,636
Less: reclassification adjustment for net realized gain included in net income		-		(3,591)		(3,591)
Less: non-credit other than temporary impairment loss		-		(195)		(195)
Total comprehensive income						25,319
Balances, December 31, 2009	\$	146,132	\$	3,238	\$	149,370
Comprehensive income						
Net income		8,168		-		8,168
Net unrealized gain on investments arising during the period		_		6,786		6,786
Less: reclassification adjustment for net realized		_		0,700		0,700
gain included in net income		-		(94)		(94)
Total comprehensive income						14,860
Balances, December 31, 2010	\$	154,300	\$	9,930	\$	164,230

Accumulated

California State Automobile Association Consolidated Statements of Cash Flow For the Years Ended December 31, 2010 and 2009

(in thousands)

		2010		2009
Cash flows from operating activities				
Net income	\$	8,168	\$	15,572
Adjustments to reconcile net income to cash and cash equivalents				
provided by operating activities		0.4.000		40.000
Depreciation and amortization of property, equipment and software		24,309		19,202
Amortization of premium and discount on debt securities, net		(25)		(76)
Net (gain) loss on sale of investments		241		(6,413)
Net loss on sale of property, equipment and other assets Deferred income taxes		4,471 (5,647)		1,870 2,987
Provision for asset impairments		(5,647) 998		2,907
Changes in assets and liabilities		990		_
Accounts receivable		98		(525)
Related party receivables, net of payables		(23,551)		(21,872)
Other assets		(259)		(298)
Unearned membership revenue and enrollment fees		5,301		10,620
Unpaid losses and loss adjustment expenses		1,094		(1,143)
Accounts payable, accrued expenses and other liabilities		(3,354)		(5,349)
Federal and state income taxes payable		446		118
Net cash and cash equivalents provided by				
operating activities		12,290		14,693
Cash flows from investing activities				
Proceeds from sales and maturities of bonds		39,273		36,933
Proceeds from sales of equity securities		68,308		153,628
Proceeds from sales of other investments		-		4,606
Purchases of bonds		(42,198)		(34,768)
Purchases of equity securities		(70,563)		(228,271)
Purchases of other investments		-		(544)
Proceeds from sales of property and equipment		1,030		58
Capital expenditures		(11,945)	_	(9,672)
Net cash and cash equivalents used in				
investing activities		(16,095)		(78,030)
Net change in cash and cash equivalents		(3,805)		(63,337)
Cash and cash equivalents, beginning of year		19,111		82,448
Cash and cash equivalents, end of year	\$	15,306	\$	19,111
Supplemental disclosures				
Income taxes paid	\$	4,982	\$	4,238
Interest paid	\$ \$	583	\$	965
Accounts payable for fixed asset additions	\$	(183)	\$	(347)

The accompanying notes are an integral part of these consolidated financial statements.

(in thousands)

1. Nature of Operations

The California State Automobile Association (the Association) is a not-for-profit automobile club and the American Automobile Association (AAA) organization member for Northern California, Nevada and Utah. Services provided to members include emergency road service (ERS) and a variety of vehicle and travel-related services.

The Association has the following wholly owned subsidiaries:

- a. Pacific Lighthouse Reinsurance, Ltd. (Pacific Lighthouse), a Bermuda-domiciled insurance company, insures the Association and the California State Automobile Association Inter-Insurance Bureau (the Bureau) for traditional business risks including workers compensation, errors and omissions, directors and officers coverage, as well as commercial automobile, property and general coverage. In addition, Pacific Lighthouse acts as a reinsurer for certain Association member-related insurance products including travel cancellation and trip interruption insurance.
- Auto Partners Inc., a California corporation, provides a full line of towing and roadside assistance services to AAA members and to non-member customers in markets not serviced by the Association, including corporate accounts, commercial businesses and municipalities.
- c. Auto Partners Motor Club Inc. (APMC), a California corporation, is licensed as a motor club in the state of California. APMC fulfills some of the Association's emergency roadside service obligations under roadside assistance programs with AAA and provides a full line of roadside assistance services for commercial businesses.
- d. CSAA Life Insurance Agency of California, a California corporation, produces life and annuity business in California and Nevada.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Association and its wholly owned subsidiaries. All intercompany transactions have been eliminated.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

Revenue Recognition

Membership – Membership dues are recognized as income on a pro rata basis over the 12 month membership period. Membership enrollment fees are recognized as income on a pro rata basis over the life of a membership which is estimated to be 12 years. Membership dues and enrollment fees are recorded on the later of the effective date of membership or receipt. Membership dues and enrollment fees received prior to the effective date of membership are recorded as an advance payment received and included in unearned membership revenue and enrollment fees.

(in thousands)

Insurance Commissions – Insurance commissions represent revenue received from insurance companies, primarily from the Bureau's subsidiaries, for insurance services provided to members. Insurance commissions are based on a percentage of premiums written and are earned as those premiums are written.

Royalties – Royalties are derived from membership list sales to Club Marketing Services, LLC (CMKS), a subsidiary of the Bureau. The Association is the owner of a list of about 4.2 million AAA members in Northern California, Nevada and Utah. CMKS pays the Association royalties based on the number of members, types of membership and insurance products held by members.

Brand Name Fees – Brand name fees represent revenue from the Bureau for the various intangible benefits flowing to the Bureau as a result of its relationship with the Association. Brand name fees are based on a percentage of premiums written and are earned as those premiums are written.

Travel Services – Revenue from travel services provided to members represents commissions from travel service providers and fees from members. Revenue from these services is recognized as the services are provided.

Advertising – Advertising revenue represents sales of print ads in the Association's bi-monthly VIA magazine. Revenue is recognized with the publishing of the magazine containing the advertisement.

Credit Card Fees – Revenue from sponsorship of an affinity credit card is recognized as income over the underlying affinity credit card agreement periods (up to four years). The income related to activation of new accounts, royalties and interchange, processing and brand fees are recorded monthly as earned based on the number of transactions rendered.

Insurance Premiums Earned – Insurance premiums written by Pacific Lighthouse are earned on a pro rata basis over the life of the underlying policies. The liability for unearned premiums is included in accrued expenses and totaled \$350 and \$253 at December 31, 2010 and 2009, respectively.

Cash and Cash Equivalents

Cash and cash equivalents include cash in banks, demand deposits, money market funds and highly liquid investments with original maturities of three months or less. The carrying amount approximates fair value because of the short maturity of these instruments.

Equity Securities and Bonds

Equity securities and bonds are categorized as available for sale. The estimated fair value of these securities is based on quoted market values as provided by independent pricing services and reviewed by management. These pricing services may apply matrix pricing for the same or similar debt securities where no price is observable. Unrealized gains and losses, net of income taxes, are included as a component of members' equity until realized. Declines in the fair value of equity securities deemed to be other than temporary are included in investment income as a realized loss. Subsequent recoveries in fair value are reflected as increases in unrealized gains and included as a component of members' equity. Declines in the fair value of bonds deemed to be other than temporary are included in investment income as a realized loss if the Association intends to sell the security or determines it is more likely than not that it will be required to sell the security before recovery of the amortized cost basis. For bonds that are considered to have an other than

(in thousands)

temporary impairment and that the Association does not intend to sell and will not be required to sell the security prior to recovery of its amortized cost basis, the Association separates the amount of the impairment into the amount that is credit related and the amount due to all other factors. The component of the loss that is credit related is recognized in investment income as a realized loss and equates to the difference between the security's amortized cost basis and the present value of its expected future cash flows. The remaining difference between the security's fair value and the present value of its expected future cash flows is due to factors that are not credit related and is recognized as a loss in other comprehensive income. Realized gains and losses on the sales of investments are included in income based on a specific identification basis. Changes to net unrealized gains or losses on securities sold are also identified on a specific identification basis and recorded as reclassification adjustments to other comprehensive income.

On January 1, 2009, as a result of the issuance of new accounting guidance in Topic 320 *Investments – Debt and Equity Securities*, the Association recognized an opening balance adjustment to reclassify \$533 (\$346 net of tax) from members' equity to accumulated other comprehensive income.

Fair Value Measurements

The Association records certain financial assets at fair value on a periodic basis. These financial assets consist of investment securities available for sale. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Association categorizes its financial assets and liabilities into the following fair value hierarchy:

- Level 1 Financial assets and liabilities with values based on unadjusted quoted prices for identical assets or liabilities in an active market. Level 1 includes active exchange-traded equity securities, regulated investment companies and US treasury securities.
- Level 2 Financial assets and liabilities with values based on quoted prices for similar assets
 and liabilities in active markets, and inputs that are observable for the asset or liability, either
 directly or indirectly, for substantially the full term of the asset or liability. Level 2 includes
 certain unlisted domestic equities, convertible securities, municipal bonds, US corporate
 bonds and international corporate bonds.
- Level 3 Financial assets and liabilities with values based on prices or valuation techniques that require inputs that are both unobservable in the market and significant to the overall fair value measurement. These inputs reflect management's judgment about the assumptions that a market participant would use in pricing the asset or liability, and are based on the best available information, some of which is internally developed. Level 3 includes private investments in limited partnerships.

When determining the fair value measurements for financial assets carried at fair value on a recurring basis, the Association considers the principal or most advantageous market in which it would execute a transaction and considers assumptions that market participants would use when pricing the asset or liability. Whenever possible, active and observable markets are used to price identical assets. When identical assets are not traded in active markets, market observable data for similar assets is used. Nevertheless, certain assets are not actively traded in observable markets and alternative valuation techniques to derive fair value measurements are used.

(in thousands)

Property, Equipment, and Software

Property and equipment are stated at historical cost. Property and equipment is depreciated on a double declining method over the first half of the estimated useful life and a straight-line method over the second half of the estimated useful life, which for buildings is 15 to 45 years and for furniture and equipment is three to eight years. Amortization of leasehold improvements is based on the shorter of the term of the underlying lease or the estimated useful life. Upon retirement or disposition of fixed assets, any gain or loss is included in net income.

Internal and external costs which are directly associated with the development of internal-use software are capitalized. Once the software is ready for its intended use, these costs are amortized over the estimated useful life of the software (five years) on a straight-line basis.

The Association reviews long-lived assets for impairment whenever events or changes in circumstances indicate that carrying values may not be recoverable. Due to changes in circumstances generally arising from a change in the estimated useful lives of assets, during 2010 the Association identified \$2,697 of assets required to be reviewed for impairment and recorded impairment charges of \$998. There were no assets that met the criteria for impairment review in 2009.

Insurance Operations

The liabilities for unpaid losses and loss adjustment expenses of Pacific Lighthouse are based on the estimated ultimate cost of settling claims, using past experience adjusted for current trends and any other factors which, in management's judgment, would modify this experience. Changes in estimates of losses resulting from the continuous review process and differences between estimates and payments for claims are included in operations of the period in which the estimates are changed.

Income Taxes

The Association accounts for income taxes using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax laws and rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

The Association utilizes a recognition threshold and measurement standard for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. This recognition threshold has been applied to all tax positions of the Association as of December 31, 2010. Only tax positions that met the more-likely-than-not recognition threshold on December 31, 2010 are recognized.

Interest expense associated with unrecognized tax benefits is classified as income tax expense in the statements of operations, when applicable. Penalties associated with unrecognized tax benefits are classified as other expense in the statement of income, when applicable. See Note 6 for a tabular reconciliation of the total amount of unrecognized tax benefits for the year.

(in thousands)

On January 1, 2009, as a result of the issuance of new accounting interpretations on Topic 740 *Income Taxes,* the Association recognized an opening balance adjustment of \$1,897 to members' equity.

Variable Interest Entities

In accordance with Topic 810 *Consolidation*, effective January 1, 2010, the Association is deemed to have a controlling financial interest in, and is the primary beneficiary of, a variable interest entity (VIE) if it has both the power to direct the activities of the VIE that most significantly impact the VIE's economic performance and an obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. On an ongoing basis, the Association will assess whether it has a controlling financial interest in and is the primary beneficiary of a VIE. The reassessment process considers whether the Association has acquired or divested the power to direct the activities of the VIE through changes in governing documents or other circumstances. The assessment also considers whether the Association has acquired or disposed of a financial interest that could be significant to the VIE, or whether an interest in the VIE has become significant or is no longer significant. The consolidation status of the VIEs with which the Association is involved may change as a result of such assessments.

The Bureau was determined to be a VIE and due to its servicing agreements with the Association was reviewed under the updated accounting guidance in Topic 810. The Bureau is a reciprocal insurance exchange with approximately \$3 billion in surplus, primarily offering personal lines insurance products to its policyholders for auto and homeowners protection. Through the analysis, the Association determined it was not the primary beneficiary of the Bureau's operating results, nor was it exposed to any loss from the Bureau as there were no contracts obligating the Association to absorb any portion of the Bureau's potential losses. Additionally, control of the Bureau does not rest with the Association. The Association does stand to benefit from the Bureau in years when it performs well as it is entitled to a variable portion of the Bureau's premium revenue (i.e., commissions) giving rise to its variable interests. As of December 31, 2010, the Association has not provided financial support to unconsolidated VIEs nor does it intend to do so. There were no other VIEs identified in which the Association has an interest variable or otherwise. As a result, there are no changes to the Association's consolidated results of operations or financial position after applying Topic 810.

Recent Accounting Pronouncements

In January 2010, the Financial Accounting Standards Board (FASB) updated its guidance in Topic 820 Fair Value Measurements and Disclosures requiring disclosure of gross transfers into and out of Level 3 of the fair value hierarchy and adding a requirement to disclose significant transfers between Level 1 and Level 2 of the fair value hierarchy. The updated guidance also clarifies existing disclosure requirements regarding the level of disaggregation of fair value measurements and inputs, and valuation techniques. Beginning in 2011, this new guidance also will require separate presentation of purchases, issuances and settlements in the Level 3 reconciliation table.

In July 2010, the FASB updated guidance in Topic 310 *Receivables* requiring additional disclosures about a company's allowance for credit losses and the credit quality of the loan portfolio. The additional disclosures include a rollforward of the allowance for credit losses on a disaggregated basis and additional information, by type of receivable, on credit quality indicators including aging and troubled debt restructurings, as well as significant purchases and sales. These new disclosures are effective for nonpublic entities for periods ending on or after December 15, 2011. This new accounting guidance will have no impact on the Association's consolidated results of operations or financial position.

(in thousands)

In December 2009, the FASB updated guidance in Topic 810 *Consolidation*. This update replaces the quantitative-based risks and rewards calculation for determining which reporting entity, if any, has a controlling financial interest in a variable interest entity with an approach focused on identifying which reporting entity has the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and (1) the obligation to absorb losses of the entity or (2) the right to receive benefits from the entity. This approach is expected to be more effective in identifying which reporting entity has a controlling financial interest in a variable interest entity. This update also requires additional disclosures about a reporting entity's involvement in variable interest entities. The update was effective for reporting periods beginning after November 15, 2009 (effective January 1, 2010 for the Association) and resulted in no changes to the Association's consolidated results of operations or financial position.

3. Related Parties

The Association has the following agreements with related parties:

- a. Under a Services Agreement, the Association and the Bureau provide various operating and administrative services to each other and reimburse each other for the cost of these services. The Association provides services to the Bureau including marketing, advertising and related services, real estate and other administrative services of conducting business. The Association receives services from the Bureau including salaries and related benefit services, software and other information systems, advertising, marketing and related services, real estate and other administrative services of conducting business. The Services Agreement's allocation factors between the Association and the Bureau are determined annually by cost studies.
- b. The Bureau funds all costs incurred related to the development of internal-use software and the Association recognizes a liability due to the Bureau for the Association's portion of these costs as they are incurred. Interest on the liability is accrued monthly by the Bureau and is charged to the Association using an agreed upon interest rate (5% in 2010 and 2009). The Association repays its obligation to the Bureau over a period of five years from the date the software is placed in service, on a project by project basis.
- c. The Bureau entered into an agreement with its wholly owned subsidiary, CMKS, under the terms of which CMKS agreed to perform marketing services on behalf of the Bureau. In order to perform such services, CMKS licensed certain intellectual property from the Association, including the Association's right to the use of the AAA brand and the Association's membership list. Royalty fees are paid monthly in arrears by CMKS to the Association based on the ending membership list and the fee is determined by the number and types of membership and insurance products sold to each Association primary member.
- d. The Association receives from the Bureau a brand name fee in consideration of the various intangible benefits flowing to the Bureau as a result of the Bureau's relationship with the Association. The brand name fee is based on 1% of Bureau's direct premium written on most lines of business and is included in insurance commission and brand name fees.
- e. The Bureau has various agreements with third-party vendors of information technology services, including Electronic Data Systems Corporation, Accenture, AT&T and IBM, to perform certain services for the Bureau and the Association. Business services associated

(in thousands)

with information, communication, and data processing are paid by the Bureau and costs are allocated to the Association.

- f. The Association acts as an agent for Western United Insurance Company (WUIC) and ACA Insurance Company (ACAIC), wholly owned subsidiaries of the Bureau. Insurance commissions from WUIC are 11% of direct written premiums for new policies and 8% of direct written premiums for renewals and from ACAIC are 9.5% of direct written premiums for new policies and renewals.
- g. The Association issued a corporate membership to AAA Club Affiliates, Inc (ACA). ACA is a not-for-profit mutual benefit corporation. Its business purpose is to form a company structure in which the Association and other AAA member clubs could participate through the issuance of corporate memberships. AAA member clubs who have elected to become affiliated with ACA will issue a corporate membership in such member clubs to ACA. In exchange for these corporate memberships, ACA will grant an ACA participation interest to such member clubs.
- h. The Association assists in the collection and remittance of payments by and between the Bureau and ACA. The Bureau provides management services to ACA, including allocated salaries and related benefit services, and other administrative services of conducting business. The Bureau also pays ACA an access fee based on 0.25% of the Bureau's direct written premium. The access fee is collected and remitted to ACA by the Association.

(in thousands)

The income statement impact of the above-detailed agreements for the years ended December 31, 2010 and 2009 was as follows:

	2010	2009
Access fee remitted to ACA on behalf of the Bureau (included in Membership services)	\$ 4,500	\$ 4,457
Management fee received from ACA on behalf of the Bureau	\$ 2,001	\$ 2,130
Royalty fees, brand name fees and insurance commission (included in Insurance commissions, royalties and brand name fees) Royalty fees from CMKS Brand name fees from the Bureau Direct premium commission from WUIC Direct premium commission from ACAIC	\$ 68,263 18,002 14,755 11,340	\$ 67,839 17,827 15,309 12,051
·	\$ 112,360	\$ 113,026
Primary services agreement with the Bureau (included in various expense line items) Services provided to the Bureau	\$ 57,460	\$ 60,539
Services provided by the Bureau	\$ 175,857	\$ 187,694

Amounts relating to these agreements on the balance sheets at December 31, 2010 and 2009 were as follows:

		2010	2009		
Payable to the Bureau and its affiliates Payable to ACA	\$	23,339	\$	46,785 89	
Total related party payables	<u>\$</u>	23,339	\$	46,874	
Receivable from CMKS Receivable from WUIC	\$	5,669 1,081	\$	5,674 1,121	
Receivable from ACAIC		836		823	
Receivable from ACA		48		-	
Total related party receivables	<u>\$</u>	7,634	\$	7,618	
Amounts relating to software development					
Capitalized costs in current year	\$	5,487	\$	3,142	
Included in payable to the Bureau	\$	13,051	\$	24,780	
Interest capitalized/expensed in current year	\$	722	\$	1,298	

(in thousands)

4. Investments

The cost or amortized cost and estimated fair value of bonds and equity securities, primarily mutual fund holdings, were as follows:

	Cost or Amortized	Gross Unrealized		Estimated Fair	
	Cost	Gains	Gains Losses		
December 31, 2010					
Asset-backed securities State and municipal bonds Corporate bonds U.S. Government bonds Foreign bonds	\$ 25,589 23,702 13,596 10,241 	\$ 941 898 1,029 565 274	\$ (183) (208) (105) (24) (7)	\$ 26,347 24,392 14,520 10,782 3,253	
Total bonds	\$ 76,114	\$ 3,707	\$ (527)	\$ 79,294	
Equity securities	\$ 186,042	\$ 11,069	\$ (793)	\$ 196,318	
	Cost or Amortized		Inrealized	Estimated Fair	
		Gross U Gains	Inrealized Losses		
December 31, 2009	Amortized			Fair	
December 31, 2009 State and municipal bonds Asset-backed securities U.S. Government bonds Corporate bonds Foreign bonds	Amortized	\$ 1,320 643 411 583		Fair	
State and municipal bonds Asset-backed securities U.S. Government bonds Corporate bonds	\$ 23,678 22,570 14,063 9,600	\$ 1,320 643 411 583 158	\$ (44) (18) (35) (8)	Fair Value \$ 24,954 23,195 14,439 10,175	

The activities related to bonds and equity securities inclusive of other than temporary impairments for 2010 and 2009 were as follows:

	 2010		2009	
Proceeds from sales and maturities of bonds Gross gains realized on sales of bonds	\$ 39,273 850	\$	36,933 923	
Gross losses realized on sales of bonds Realized losses on bonds that were considered other than temporarily impaired in value	(49) -		(38)	
Proceeds from sales of equity securities Gross gains realized on sales of equity securities Gross losses realized on sales of equity securities	\$ 68,308 1,466 (2,509)	\$	153,628 15,163 (8,600)	

(in thousands)

The gross unrealized losses and estimated fair values on investments aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position were as follows:

	12 m	onths	or gre	ater	Less than 12 months			
	Unrea Loss		Estimated Fair Value		Unrealized Losses			stimated air Value
	LUSS	65	Ган	value		3362		ali Value
December 31, 2010								
U.S. government bonds	\$	-	\$	-	\$	24	\$	2,184
Corporate bonds		-		-		105		1,951
State and municipal bonds		-		-		208		7,528
Foreign bonds		-		-		7		267
Asset-backed securities						183	_	5,004
Total bonds	\$	-	\$		\$	527	\$	16,934
Equity securities	\$	-	\$		\$	793	\$	33,887
			or gre			ss than		
	Unrea	lized	Esti	mated	Unre	alized	Es	stimated
		lized	Esti		Unre		Es	
December 31, 2009	Unrea	lized	Esti	mated	Unre	alized	Es	stimated
December 31, 2009 U.S. government bonds	Unrea	lized	Esti	mated	Unre	alized	Es	stimated
·	Unrea Loss	lized	Estii Fair	mated	Unre Los	alized sses	Es <u>Fa</u>	stimated air Value
U.S. government bonds Corporate bonds State and municipal bonds	Unrea Loss	lized ses	Estii Fair	mated Value	Unre Los	alized sses 35 - 42	Es <u>Fa</u>	2,213 - 1,264
U.S. government bonds Corporate bonds State and municipal bonds Foreign bonds	Unrea Loss	ized ses - 8	Estii Fair	mated Value - 142	Unre Los	alized sses 35 - 42 23	Es <u>Fa</u>	2,213 - 1,264 694
U.S. government bonds Corporate bonds State and municipal bonds	Unrea Loss	ized ses - 8	Estii Fair	rmated Value - 142 47	Unre Los	alized sses 35 - 42	Es <u>Fa</u>	2,213 - 1,264
U.S. government bonds Corporate bonds State and municipal bonds Foreign bonds	Unrea Loss	ized ses - 8	Estii Fair	rmated Value - 142 47	Unre Los	alized sses 35 - 42 23	Es <u>Fa</u>	2,213 - 1,264 694

An investment is deemed impaired if the fair value of the investment is less than its carrying value. After the investment is deemed impaired, the Association evaluates whether the decline in value is other-than-temporary. When evaluating whether the impairment is other-than-temporary, the Association takes into consideration whether or not it will receive all of the investment's contractual cash flows based on factors that include, but are not limited to, the length of time and extent that the investment's fair value has been less than its amortized cost and the Association's ability and intent to hold the investment for a sufficient amount of time to recover the unrealized losses. On review of each individual investment in an unrealized loss position, management concluded that none of the investments with unrealized losses at December 31, 2010 had experienced an other-than-temporary impairment. During 2009 the Association recognized other-than-temporary impairment in other comprehensive income of \$195.

As of December 31, 2010 and 2009 there were 59 and 26 securities in unrealized loss positions, respectively.

(in thousands)

The cost or amortized cost and estimated fair value of bonds at December 31, 2010, by contractual maturity, were as follows:

	Cost or Estimate Amortized Fair Cost Value				
Due in one year or less	\$ 2,292	\$	2,176		
Due after one year through five years	13,830		14,512		
Due after five years through ten years	16,093		17,456		
Due after ten years	 18,310		18,803		
	50,525		52,947		
Asset-backed securities	 25,589		26,347		
	\$ 76,114	\$	79,294		

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations.

The Association's investment policy limits concentration of credit risk by diversifying its investment portfolio. Since the portfolio is diversified and issuers of securities are dispersed throughout many industries and geographies, the concentration of credit risk is limited.

The Association also invests a limited amount in alternative investments including high yield limited partnerships, inflation-protected bond funds and private equity funds. These alternative investments are categorized as available for sale and included in other current assets. These investments are carried at estimated fair value as of December 31, 2010 and 2009 and the fund fair values are based on audited financial statements. Because alternative investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investment existed. Such differences could be material to the investment.

The cost or amortized cost and estimated fair value of the alternative investments were as follows:

	Cost or			Gross U	nrealize	ed	Estimated		
	Amortized Cost			Gains	Lo	Losses		Fair Value	
December 31, 2010									
Alternative investments	\$	7,667	\$	2,269	\$		\$	9,936	
December 31, 2009									
Alternative investments	\$	7,667	\$	1,922	\$	(7)	\$	9,582	

On December 31, 2009, the Association sold an alternative investment to the Bureau. The proceeds from the sale of the investment were \$4,606 and the gross gain realized on the sale was \$259.

(in thousands)

The following tables present information with respect to financial assets carried at fair value in the consolidated balance sheets:

	Fair Value Measurements at December 31, 2010 using								
		Quoted Prices in Active Markets Significant Othe for Identical Observable Assets Inputs Total (Level 1) (Level 2)			bservable Inputs	Significant Unobservable Inputs (Level 3)			
Asset-backed securities State and municipal bonds Corporate bonds U.S. government bonds Foreign bonds	\$	26,347 24,392 14,520 10,782 3,253	\$	- - 7,949 742	\$	26,347 24,392 14,520 2,833 2,511	\$	- - - -	
Total bonds	\$	79,294	\$	8,691	\$	70,603	\$		
Equity securities	\$	196,318	\$	196,318	\$		\$		
Alternative investments	\$	9,936	\$		\$	_	\$	9,936	
		Fair Val				cember 31, 20	009 us	ing	
		Fair Val	Quot Acti fo	easurements ted Prices in tve Markets or Identical Assets Level 1)	Sign O	cember 31, 20 ificant Other bservable Inputs (Level 2)	Sig Unol	ing Inificant bservable Inputs Level 3)	
State and municipal bonds Asset-backed securities U.S. government bonds Corporate bonds Foreign bonds	\$		Quot Acti fo	ed Prices in ive Markets or Identical Assets	Sign O	ificant Other bservable Inputs	Sig Unol	nificant bservable nputs	
Asset-backed securities U.S. government bonds Corporate bonds	\$	Total 24,954 23,195 14,439 10,175	Quot Acti fo	ed Prices in ve Markets or Identical Assets Level 1)	Sign	ificant Other bservable Inputs (Level 2) 24,954 23,195 1,889 10,175	Sig Unol I	nificant bservable nputs	
Asset-backed securities U.S. government bonds Corporate bonds Foreign bonds		Total 24,954 23,195 14,439 10,175 2,586	Quoti Acti fo	ted Prices in ive Markets or Identical Assets Level 1)	Sign O	ificant Other bservable Inputs (Level 2) 24,954 23,195 1,889 10,175 1,893	Sig Unol (L	nificant bservable nputs	

(in thousands)

The following tables present activity related to financial assets categorized in Level 3 of the valuation hierarchy:

Fair Value Measurements Using Significant Unobservable Inputs

		Year Ended December 31, 2010										
				Total	Realiz	zed and						
			Uı	nrealize	d Gai	ns (Losses)	Pι	ırchases,				
	Jaı	Fair alue at nuary 1, 2010		orded ncome		ecorded in Other mprehensive Income		suances and ttlements, Net	Int	ansfers to and/or Out of _evel 3	De	ir Value at ecember 1, 2010
Alternative investments	\$	9,582	\$	-	\$	354	\$	-	\$	_	\$	9,936

Fair Value Measurements Using Significant Unobservable Inputs

		Year Ended December 31, 2009										
				Total I	Real	ized and						
				Unrealized	d Ga	ins (Losses)	Р	urchases,				
	Fair Value at January 1, 2009			ecorded Income	Recorded in Other Comprehensive		Issuances and Settlements, Net		Transfers Into and/or Out of Level 3		Fair Value at December 31, 2009	
Equity securities	\$	285	\$	(11)	\$	<u>-</u>	\$	(274)	\$		\$	_
Alternative investments	\$	11,940	\$	(1,153)	\$	2,159	\$	(3,364)	\$	-	\$	9,582

5. Property, Equipment and Software

Property, equipment and software at December 31 consists of the following:

	2010	2009
Furniture and equipment	\$ 73,532	\$ 95,780
Software Buildings and leasehold improvements	60,469 57,689	56,905 58,224
	191,690	210,909
Accumulated depreciation and amortization	(156,682)	(157,144)
Land, at cost	35,008 5,056	53,765 5,161
	\$ 40,064	\$ 58,926

(in thousands)

Depreciation and amortization expenses are as follows:

	_	2010	_	2009
Software	\$	16,310	\$	9,151
Buildings and leasehold improvements		4,284		4,534
Furniture and equipment		3,715		5,517
	\$	24,309	\$	19,202

6. Income Taxes

The provision for income taxes consists of the following:

	201	2009
Current tax provision	ф 4.	450 ¢ 2.740
Federal State	,	452 \$ 3,719 976 824
Claic		428 4,543
Deferred tax (benefit) expense	(5,6	646) 2,801
Total provision for income taxes	<u>\$ (2</u>	218) \$ 7,344

The provision for income taxes is different from that which would be computed by applying the statutory federal income tax rate to income before taxes as follows:

	 2010	_	2009
Pre-tax income (equity eliminated)	\$ 7,941	\$	22,916
Tax at federal statutory rate Tax-exempt investments income State tax rate Settlements and releases from statute expirations, net Other	\$ 2,779 (1,373) 659 (2,383) 100	\$	8,021 (1,433) 638 - 118
	\$ (218)	\$	7,344

(in thousands)

	2010	2009
Tax at federal statutory rate	35.0%	35.0%
Tax-exempt investments income	(17.3)	(6.3)
State tax rate	8.3	2.8
Settlements and releases from statute expirations, net	(30.0)	-
Other	1.2	0.5%
	(2.8)%	32.0%

Deferred income taxes reflect the impact of temporary differences between the amounts of assets and liabilities recorded for financial reporting purposes and such amounts as measured in accordance with tax laws. The sources and related tax (benefit) provision of those temporary differences are presented below:

	2010		2009	
Deferred membership expenses	\$	236	\$	275
NOL and other credit carryforwards		14		3,989
State deferred taxes, net of federal tax benefit		(4)		(621)
Deferred income recognition		(321)		(376)
Investment adjustments		(370)		1,168
Other		(529)		497
Depreciation		(801)		(452)
Software amortization		(3,871)		(1,679)
Deferred income (benefit) tax	\$	(5,646)	\$	2,801

The tax effect of temporary differences that give rise to significant portions of the deferred tax assets and tax liabilities at December 31, 2010 and 2009 are presented below:

(in thousands)

	 2010		2009	
Deferred tax assets				
Depreciation	\$ 5,843	\$	5,042	
Deferred income recognition	4,432		4,112	
Investment adjustments	1,129		759	
Loss reserve discounting	1,099		1,083	
State deferred taxes, net of federal tax benefit	908		904	
Accrued expense	744		548	
Excess capital loss	351		-	
NOL and other credits carryforward	250		264	
Other	 125		125	
	14,881		12,837	
Deferred tax liabilities				
Unrealized appreciation of investments	5,794		2,189	
Software amortization	4,157		8,028	
Deferred membership expenses	3,450		3,214	
Prepaid asset	710		717	
Other	519		372	
Printing supplies expensed for tax	 329		436	
	 14,959		14,956	
Net deferred tax liability	\$ (78)	\$	(2,119)	

The following is a reconciliation of the total amount of unrecognized tax benefits for the year:

Balance at January 1, 2010	\$ 3,061
Increase related to current year tax positions	196
Increase for tax positions for prior years	90
Lapse in statute of limitations	(1,341)
Balance at December 31, 2010	\$ 2,006

Included in the unrecognized tax benefits of \$2,006 at December 31, 2010 was \$1,653 that, if recognized, would impact the Association's annual effective tax rate. The Association accrues interest and penalties related to unrecognized tax benefits in the provision for income taxes. As of December 31, 2010, accruals for the payment of interest and penalties totaled \$353.

Due to the potential lapse of statute of limitations, it is reasonably possible that the balance of gross unrecognized tax benefits could decrease within the next twelve months by a range of \$200 to \$300.

The Association files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. The Association is subject to U.S. federal income tax examinations for the tax years ended 2007 through 2009. The Association is subject to state and local tax examination for tax returns filed for the years ended 2006 through 2009. The Association is currently under examination by the California Franchise Tax Board.

(in thousands)

The Association has tax credits and loss carryforwards available to offset future taxes as follows:

	2	010	 2009
Alternative minimum tax credit General business credit	\$	250 -	\$ 250 14
NOL and other credits carryforward	\$	250	\$ 264

The alternative minimum tax credit can be carried forward indefinitely. The general business credit and the net operating loss can be carried forward for 20 years.

7. Commitments and Contingencies

Certain district offices are leased by the Association under long-term commitments. Some of the leases are noncancelable and others have renewal options for periods up to five years. The Association's total rental expense for leases was \$1,119 and \$1,293 in 2010 and 2009, respectively.

The Association's future minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of December 31, 2010 are as follows:

\$ 849
352
189
169
67
 -
\$ 1,626

The Association is party to various claims and lawsuits arising in the normal course of business. It is the opinion of management, after consultation with legal counsel, that the disposition of these matters is not expected to have a material adverse effect on the financial position or results of operations of the Association.

8. Subsequent Events

Effective January 1, 2011, ACA merged with and into AAA Club Partners, Inc. (ACP). The corporate membership held by ACA in the Association was terminated effective January 1, 2011. Thereafter, the Association issued a new corporate membership to ACP.

In January, 2011, the Association contributed \$774 to ACP for projects, \$580 of which was received from the Bureau for remittance.

(in thousands)

In February, 2011, the Association changed its name to AAA Northern California, Nevada & Utah.

At January 1, 2011 the Association and the Bureau entered into a new economic relationship, reflected in a new Producer Agreement, Marketing Channel Agreement and a number of other agreements. The Association and the Bureau have always been separate entities, however, prior to January 1, 2011 their operations were integrated. In conjunction with the merger of ACA and ACP and related transactions, the Boards of the Association and the Bureau decided to separate operations. The Association will continue to be the primary seller of insurance for the Bureau and will continue to partner with the Bureau in producing business.

There were no other subsequent events through May 18, 2011, which is the date the financial statements were available to be issued, requiring recognition or disclosure in the financial statements for the year ended December 31, 2010.

2010 Insurance Report

CSAA Inter-Insurance Bureau

In 2010, we returned significant value to AAA members across 18 states, restoring order to their lives when natural and manmade disasters struck, and offering an array of products—backed by unparalleled customer service—that provide superior protection and peace of mind.

2010 was a year of unprecedented storms in the western United States, with Arizona experiencing record-setting hail and the worst fall weather in 15 years. Severe spring storms, including multiple tornadoes, pummeled the Midwest. In September, a natural gas line ruptured, causing a deadly explosion and subsequent fire that swept through a large swath of San Bruno, California.

AAA handled incident after incident with efficiency *and* compassion. And we have the financial strength to deliver on our promises—even in large-scale catastrophes. We once again earned an A+ (superior) rating from A.M. Best, a respected credit rating organization that evaluates the insurance industry. The A+ reflects our capital strength, favorable operating earnings and significant market presence. It is one more assurance to policyholders and prospective policyholders that we can be counted on to deliver on our promises, as we have for generations.

Highlights of 2010:

- New Walnut Creek headquarters Recognized for its beautiful design, the building includes features that minimize our environmental impact and promote sustainability. It is the first Walnut Creek office building to receive LEED Gold certification.
- Signature Series automobile product Rolled out in an increasing number of states, this standardized product gives policyholders across the country access to the same high-quality coverage.
- Usage-based automobile insurance—Launched in Nevada, this product rewards low-mileage drivers.
- New suite of AAA specialty insurance products Motorcycle, RV, mobile home, watercraft, snowmobile and collector cars insurance is now available in more states.
- New condominium policy—Launched in California, this policy has an option for repairs or rebuilding to be done with environmentally friendly materials.

We look forward to returning the most value to you, our AAA Members, and to being there for you when you need us.

Note: In March 2011, California State Automobile Association Inter-Insurance Bureau became AAA Northern California, Nevada & Utah Insurance Exchange. You will see the new name on your insurance documents going forward. This is a change in name only and does not affect your insurance coverage.

California State Automobile Association Inter-Insurance Bureau Group Financial Highlights

For the Years Ended December 31, 2010 and 2009 (in millions)	2010	2009	Change
Total admitted assets	\$5,844.2	\$5,576.2	\$268.0
Amortized value of bond portfolio	3,123.4	2,882.2	241.2
Market value of stock portfolio	1,228.9	1,249.9	-21.0
Premiums earned	2,428.3	2,390.5	37.8
Underwriting income (loss)	21.2	(56.0)	77.2
Net investment income	232.4	89.2	143.2
Policyholders' surplus	3,325.7	3,081.6	244.1

Paula F. Downey