



# Illinois Department of Insurance

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PAT QUINN  
Governor

June 29, 2012

ANDREW BORON  
Director

Thomas Firouz Montamed  
President  
Rick Ehlers  
Vice-President & Associate General Counsel  
Continental Causality Company  
NAIC # 20443  
And  
Affiliates and Subsidiaries  
CNA Plaza  
333 W Wabash Avenue, 43S  
Chicago, IL 60604

Dear Messrs. Montamed and Ehlers:

A Market Conduct Examination of your company was conducted by authorized examiners designated by the Director of Insurance pursuant to Illinois Insurance Code Sections 132 and 401 of the Illinois Insurance Code. The examination concerns CNA's Defense Base Act coverage.

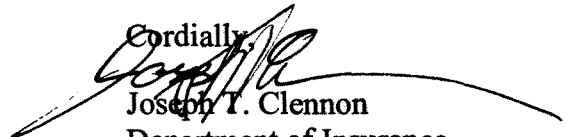
As required by Illinois Insurance Code Section 132, please find attached a copy of the verified examination report. This Department is providing your company an opportunity to make a written submission or rebuttal with respect to any matters in the attached report. Please provide any such written submission or rebuttals to the undersigned by close of business, Friday, June XX, 2012.

Illinois Insurance Code Section 132 provides that the Director of Insurance must afford your company an opportunity to demand a hearing with reference to the facts and other evidence contained in this report. Section 132 further provides that your company may request a Hearing within ten (10) days after receipt of the above Report by giving the Director of Insurance written notice of such request together with a statement of your objections. The deadline to request a hearing is hereby extended until June 5, 2012.

Please note that on September 9, 2011, DOI enter an Order to Produce concerning certain documents that CNA claimed to be confidential. CNA cooperated with the Illinois Department of Insurance and provide all documents requested. Please review the exhibits to the Exam Report, which are contained on the enclose Compact Disc to ensure that none of the exhibits are considered by CNA to be confidential.

Please contact me if you have any questions.

Cordially,



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Enclosures: CD and Exam Report

STATE OF Pennsylvania )  
 ) ss# 343-38-3421  
COUNTY OF Montgomery County )

Alexander T. Farley, being first duly sworn upon his/her oath, deposes and says:

That he was appointed by the Director of Insurance of the State of Illinois (the "Director") as Examiner-In Charge to examine the insurance business and affairs of the Transportation Insurance Company and Continental Casualty Company (collectively, the "Company") of Chicago Illinois.

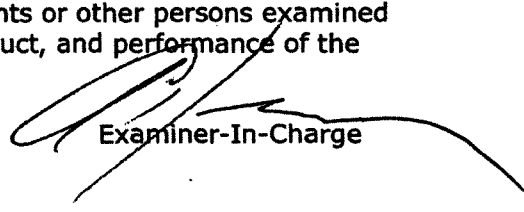
That the Examiner-In-Charge was directed to make a full and true report to the Director of the examination with a full statement of the condition and operation of the business and affairs of the Company with any other information as shall in the opinion of the Examiner-In-Charge be requisite to furnish the Director with a statement of the condition and operation of the Company's business and affairs and the manner in which the Company conducts its business;

That neither the Examiner-In-Charge nor any other persons so designated nor any members of their immediate families is an officer of, connected with, or financially interested in the Company, nor any of the Company's affiliates other than as policyholders, and that neither the Examiner-In-Charge nor any other persons so designated nor any members of their immediate families is financially interested in any other corporation or person affected by the examination;

That an examination was made of the affairs of the Company pursuant to the authority vested in the Examiner-In-Charge by the Director of Insurance of the State of Illinois;

That he was the Examiner-in-Charge of said examination and the attached report of examination is a full and true statement of the condition and operation of the insurance business and affairs of the Company for the period covered by the Report as determined by the examiners;

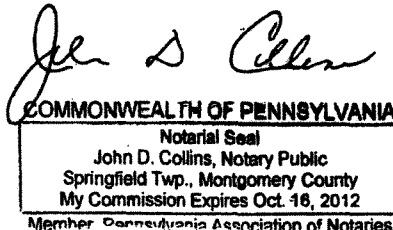
That the Report contains only facts ascertained from the books, papers, records, or documents, and other evidence obtained by investigation and examined or ascertained from the testimony of officers or agents or other persons examined under oath concerning the business, affairs, conduct, and performance of the company.

  
Examiner-In-Charge

Subscribed and sworn to before me

This 4 day of May, A. D. 2012.

Notary Public



***January 5, 2012***

**CNA Special Market Conduct Examination**

***Pursuant to Illinois Department of Insurance  
"Market Examination Warrants" dated May 27, 2011***

***Regarding the  
CNA Defense Base Act Insurance Program for  
Agencies of the United States Government***

***And presented to:  
The Director  
Of The Illinois Department of Insurance***

***Prepared by:  
American Insurance Management Group, Inc.  
709 Bethlehem Pike, Suite C  
Erdenheim, PA 19038***

**This Examination is pursuant to and as authorized by State of Illinois Insurance Code: Sections 401(b) and 132 of the Illinois Insurance Code (215 ILCS 5/401(b) and 132).**

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## **I. Exhibits**

1. Examination Orders
  - a) Illinois Examinations Warrants
  - b) DOI Order on CNA DBA Examination Confidentiality
2. DOL Administrative Law Judge May 12, 2011 Ruling on Sallyport
3. AIM Document Request & CNA Documents (1)
4. CNA Actuarial Report as of 3/31/2011
5. CNA & DOL Communication Documents
6. Rutherford Contract
7. CNA DBA Program Contracts
  - a) United States Army Corp of Engineers Contract
  - b) United States Agency for International Development Contract
  - c) United States Government Security Contract
  - d) Department of State Contract
8.
  - a) CNA DBA Operating Guidelines
  - b) AIM Summary CNA Internal Operations
9. AIM CNA File Selections
  - a) Open Claims Report for AIM Selection
  - b) CNA Claim Denial Lists Pre 2008
  - c) AIM Medical Only File Selection
  - d) CNA Lost Time Claim Listing
10. DOL 2009 WH DFEC Claim Handling Change
11.
  - A. Sallyport MJM 2/5/07 Investigative Report (w/attachments)
  - B. CNA Sallyport Status Email 12.21.2011
  - c. LS 208 and DOL Approval 2.19.2008
12. DOL Inspector General's Report
13. SIGAR Review
  - a) Initial 6/28/11 Report
  - b) CNA 7/14/11 Response to SIGAR Report
  - c) Final SIGAR Report 7/18/11

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<sup>1</sup> Exhibit 3—Because of the volume of material, AIM's Document Request is an electronic folder with an Excel Spreadsheet noting data and information requested. Each request has a hyperlink imbedded that is to pull up a PDF copy of the CNA requested document automatically. Should the link functionality not work, source the documents by title within the master file.

## II. Introduction

This "draft" report prepared by American Insurance Management Group, Inc. (AIM) documents its findings from the Special Examination (Examination) of CNA's<sup>2</sup> Defense Base Act (DBA) insurance program as directed by the Illinois Department of Insurance (DOI). AIM presents herein the "draft" report to the Director of the DOI for consideration and further instruction.

The Examination pertains to CNA's administration and claims management of DBA insurance that the company has contracted to provide on a "program" basis to various agencies of the United States Government as compared to open market insurers that insure contractors on an individually underwritten<sup>3</sup> basis,

The Illinois examination performed by AIM and report of findings herein is pursuant to, and authorized by Sections 401(b) and 132 of the Illinois Insurance Code (215 ILCS 5/401(b) and 132). Exhibit 1 contains copies of the Illinois DOI Warrants issued to CNA.

Without limitation to the DOI's statutory authority and confidentiality of Examination documents as set forth in the Illinois Insurance Code, CNA further asserts that the information provided AIM and the DOI for this examination is (Exhibit 1b).

"CONFIDENTIAL AND/OR TRADE SECRET INFORMATION -- This document, which includes information that CNA ("the company") deems to be confidential, proprietary or trade secret, is being submitted to the Department of Insurance pursuant to its authority under ss. 132, et seq. and 401, et seq. of the Illinois Insurance Code. Pursuant to ss. 132.5(f) and/or 401.5(c) or other applicable law, we request that the document remain confidential and not be subject to public disclosure."

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<sup>2</sup> Including parent, affiliate or subsidiaries as listed in the Exhibits.

<sup>3</sup> A small percent of CNA's DBA business is also written on this basis.

### III. Background

Congress enacted the Defense Base Act in 1941 as a federal law to provide workers' compensation coverage and benefits<sup>4</sup> granted under the Longshore and Harbor Workers' Compensation Act (LHWC – 33 U.S.C. 901 et. seq.) to United States Government contractors and their employees in foreign countries, including contracted foreign nationals.

The Department of Labor (DOL) assisted by its agency the Office of Workers' Compensation Programs (OWCP) is charged with the oversight and compliance of insurers providing DBA insurance. The oversight for CNA providing DBA insurance programs are for its programs with the United States Army Corp of Engineers (USACE); the Department of State (USDOS); the U.S. Agency for International Development (USAID)<sup>5</sup>; the U.S. Government Department of Security; and a nominal amount of "non-program" business from other government agencies. All agencies hiring independent contractors to conduct projects "Outside the Continental United States" (OCONUS) are federally mandated to require the contracted firms to provide DBA insurance for such employees and their sub-contractors.

DBA insurance coverage has traditionally been purchased on an "open-market" basis wherein insurers can reject insuring contractors if, for example, exposures are deemed excessive. On a non-program basis premium rates and terms are negotiated with the broker or agencies' contracting officers and policies issued providing evidence of DBA insurance, necessary for contractors to commence work.

As a specialized and high-risk category of business, only a few insurers offer DBA insurance, which presently includes Chartis, ACE, Zurich, Chubb, AWAC and CNA.

In 1998, CNA was the first insurer to negotiate with a government agency an exclusive agreement to provide DBA insurance on a "program" basis. This was with the U.S. Agency for International Development (USAID)<sup>6</sup> to insure its contractors (and sub-contractors) retained to perform work OCONUS. The government's objective for "program" insurance

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<sup>4</sup> The DBA act provides medical care, lost wages to employees and death benefits to dependents regardless of nationality if injury or death occurs in the scope and course of employment working on federally funded programs. ([www.dol.gov/owcp/olhwc/isdba.htm](http://www.dol.gov/owcp/olhwc/isdba.htm))

<sup>5</sup> A program recently not renewed and with another insurer.

<sup>6</sup> CNA lost the program in 2003 to AWAC when the program contract was up for renewal.



being with a single insurer was to achieve better service, economies of scale and cost control of DBA insurance with one insurer specializing in this business.

The difference in "open-market" insurance and "program" insurance is that in the latter instance CNA would negotiate a contract (most being multiple-year obligations) with a government agency to provide DBA insurance for all contractors the agency engages. Premiums are negotiated with the agency for respective worker classifications and contractually fixed for an agreed period with the agency. Thus, as a program insurer, CNA is obligated to insure all contractors entering into contracts with that specific government agency. CNA has no discretion in selection of risks or premium rates charged, as is otherwise the case with "open-market" insurers.

Since 1998, CNA has negotiated DBA program contracts with three other government agencies in addition to the USAID:

<b>Government Agency</b>	<b>Contract Years<sup>7</sup></b>	<b>Comment</b>
Army Corp of Engineers (USACE)	2005 - 2012	Largest Program
U.S. Department of State (DOS)	DOS 2001 - 2011	High Loss Ratios
U.S. Gov't. Dept. of Security	AIC 2010 - 2012	Low Volume

CNA's DBA written premiums as of June 1, 2011 were \$130 million of which only \$14.3 million is written on an open market basis. Based on CNA's estimated 10% market share of program and non-program business combined, the DBA's total market written premium in 2011 is approximately \$1.3 billion. AIG is the dominant insurer in the market insuring contractors only on an open market basis.

The demand for DBA insurance started to increase rapidly in 2005 with insured exposures. The dramatic increase in the DBA market was driven by the rapid growth of U.S. military operations in Iraq and Afghanistan. Furthermore, the U.S. Government concurrently began increasing the outsourcing of military support services to contractors.

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<sup>7</sup> Represents multiple contract periods

CNA's growth in earned premiums reflects this increase. In 2005, CNA's DBA earned premiums were \$59.8 million and by 2010 had climbed to \$163 million. This is a 270% increase or a 54% annual increase during this five-year period. As a program insurer, CNA was obligated to multiple-year agreements with fixed premiums and no ability to minimize the flow of business to help address the increase in case management sophistication, systems capacity, operational capabilities and staffing needs.

From 2005 through 2009, CNA worked to improve operations with the claim management function being the most impacted by the volume of claims that were also increasingly more complex and time consuming to handle.

The DBA program has been costly for CNA because of high losses incurred. CNA's underwriting performance on a combined ratio<sup>8</sup> basis is below for various time frames:

<b>Period</b>	<b>Earned Premium \$ MM</b>	<b>Combined Ratio</b>	<b>Underwriting Profit (Loss) \$ MM</b>
2005 thru 1 <sup>st</sup> Qrt 2011	\$683.6	106.8%	(\$46.3)
2008 thru 1 <sup>st</sup> Qrt 2011	\$446.5	110.6%	(\$47.2)
1 <sup>st</sup> Qrt 2011	\$34.9	109.9%	(\$3.5)

Exposures causing injury and loss of life of insured employees became increasingly significant and costly. The Army Corp program (USACE), CNA's largest client uses, for example, contractors to build barracks and bridges in hostile areas, forward installations and field hospitals. The Department of State (USDOS) program, CNA's most loss intensive, insures employees of contracted firms to provide security for U.S. military at times, non-military personnel; guard supply transports, and provide interpreters, often foreign nationals who, for example, assist the military in its efforts to train local police for the reconstruction efforts in Iraq and Afghanistan. Exhibit 7 includes copies of CNA's Program contracts.

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<sup>88</sup> Case losses paid and estimated on an incurred but not reported basis (IBNR), loss adjustment expense and underwriting expense.

Management of DBA insurance claims is complex and unique in comparison to other workers' compensation labor classifications. Many factors make DBA claims unique and a challenge to handle. A few such aspects include the complexity of coverage; the circumstances in which injuries or death occur, War Hazard zone casualties in hostile locations that inhibit case management; and cultural barriers that complicate securing the necessary information and documentation to adjudicate claims based on coverage afforded by DBA provisions. The ability to secure information was one of the primary difficulties with respect to the problems that the Sallyport claim presented. Additionally, CNA relies upon contracted firms for that are on-site for loss investigation and obtaining documentation to support benefit decisions.

### **The Sallyport Claims**

On October 29, 2006, 17 Iraqi born<sup>9</sup> interpreters contracted by Sallyport Global Services, Inc. (Sallyport), a U.S. firm, were on a bus in transit to assist in training local police in Basra as part of the U.S.'s Iraqi reconstruction effort.

Insurgents stopped the bus en-route and executed all passengers. CNA proceeded to investigate and adjudicate the claims paying various types of benefits including funeral expense coverage and other benefits to verified claimants and dependents of the deceased translators, which included spouses, sons, daughters and parents.

CNA engaged the services of MJM, Inc.<sup>10</sup> (MJM) for the on-site loss investigation to gather the facts of the incident and documentation as pertained to all potential claims including dependent parent beneficiaries. This included documentation for potential survivorship benefit payments. With this information and in accordance with the DBA benefits available, CNA identified the dependents and survivorship benefits due making payments based on this information and DBA coverage terms.

The Sallyport occurrence was classified as a "War Hazard" zone claim wherein all benefits paid by CNA would be reimbursed by the DOL to CNA plus a 15% claim expense-handling fee in accordance with agreed terms.

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<sup>9</sup> foreign nationals

<sup>10</sup> A U.S. Based company

The claimant subject to this aspect of the DOI examination is the mother of one of the deceased interpreters and the plaintiff subject to the DOL Administrative Law Judge's Court Ruling. This claim was filed with CNA in December 2009 with seven other survivorship dependent parental claims with the same or similar demands.

The mother was paid funeral expense benefits on a timely basis and was not contested. The Court ruling was solely based on the subsequent claim filed by the mother and the seven other claimants in December 2009, which was significantly past the DBA statute of limitations for filing such claim demanding survivorship support benefits. The employer and CNA also stated the information submitted was insufficient, with which AIM concurs based on information provided.

During MJM's original investigation, the mother was found to be only eligible for funeral expense benefits, which was the only benefit sought by the mother at that time. This is based on the records provided AIM by CNA based on MJM's investigation.

AIM's review of the MJM "Final Report" (Exhibit 11) on the matter and supporting documents including CNA's records found that the claim was handled by CNA within DOL guidelines and CNA standards for funeral expense benefits. These benefits were paid on a reasonably timely basis. No dependency was cited in the investigator's report, thus no survivorship dependency benefits appeared to be a consideration. The investigation noted that the mother had three additional sons and two daughters.

The MJM documents reflected typical obstacles in fact determination that AIM had been informed of by CNA and as substantiated in numerous claim files AIM reviewed. For example, the address for the mother of the deceased provided MJM was vague and thus time consuming to locate her, make contact with her to arrange an interview, which took several attempts, and secure documents substantiating funereal expenses incurred and other information deemed pertinent to the case as may come to light during the interview.

The meeting was accomplished with the help of one of her sons, as non-official travel was limited and other difficulties being in a war-zone. In addition, a cultural obstacle is that women often do not have bank accounts as the case with the mother. MJM, as directed by

CNA, assisted the mother in opening a bank account through which CNA could make funeral expense benefit payments and did.

With funeral expense benefits paid (again the only claim identified), CNA filed timely the DOL Form "LS-208 Notice of Final Payment or Suspension of Compensation Payment" with supporting documents. In acceptance of the LS 208 Form and file closure request of CNA. The DOL issued the District Director's October 20, 2008, "Compensation Order" that approved file closure. (Exhibit 11c)

As noted earlier, approximately three years after the 2006 Sallyport event, claims were filed on or about December 2009 by an attorney representing the nine parental dependency cases including the mother's case for dependent survivorship benefits. There was no documentation AIM could identify to verify this as a potential claim in reviewing the files provided by CNA, nor within CNA's paperless claim case file system to which we had unrestricted access to DBA files. Survivorship support claims typically include, for example, regularly cancelled checks from son/daughter's account to parent(s) or regular deposits. The only documentation AIM found supporting plaintiffs' claims of support dependency were affidavits of neighbors and other family members that the parents had been dependent upon their deceased children's income or by household sharing.

As part of the original MJM investigation, there were other Sallyport parental survivorship claims identified and/or filed for support that were investigated and benefits paid based on CNA's claim evaluations.

These parents were not part of the latter claim filing for survivor benefits. This reflects in AIM's opinion that CNA was aware of the category of parental survivorship benefits as potentially part of this incident. CNA was making payments accordingly as investigatory findings and supporting documentation warranted.

With respect to the DOL Administrative hearing on May 12, 2011 (case # 2011-LDA-00002) that pertained to the eligibility of survivor benefits support for the mother, the other claims filed concurrently were included in the ALJ's decision as essentially one class of claimant.

Receiving these claims in 2009, CNA and the employer (Sallyport) ultimately denied benefits asserting the claim(s) was untimely filed being past DBA coverage statute terms

that allow no more than one year to file a claim or an objection to a denial from the date of the incident. The claims also purportedly lacked sufficient documentation for benefits sought though this was not part of CNA's motion denying coverage. The DOL had requested CNA to try to mediate with plaintiffs' counsel. CNA deemed the demands as excessive in light of applicable DBA coverage afforded, despite the claim filing timeliness consideration.

The regional Administrative Judge for the DOL on or about May 26, 2011 ruled in favor of the mother's claim for survivorship support beneficiary status Exhibit 2 – Administrative Court ruling (as well for the other claimants). This ruling, which was the Court's preview to grant despite DBA terms was based on the mitigating circumstance of the event occurring in a war zone wherein the judge identified similar precedent cases wherein untimely filing statutes were "tolled" and the claims were to be paid.

Upon the filing of the ruling, CNA proceeded to adjudicate the amounts due the parties commencing payments accordingly as directed by the ALJ's ruling.

The judge deferred ruling on the criminal misconduct allegations in the plaintiffs Cross Motion against CNA as it was not an administrative matter, and this warranted the authority of a higher court if allegations would be deemed sufficient to be heard. This portion of the case was referred to the DOL's NY District Director for further disposition, which is not yet finalized.

Given the seriousness of the allegations over the mother's denied dependency claim and Illinois being CNA's primary domiciliary state, the Illinois Director of Insurance commenced a Special Examination of CNA in this matter and its DBA program overall.

This examination also addresses subsequent events that include the Deputy Inspector General's report dated March 23, 2011 and the report issued by the Special Investigator General for Afghanistan Reconstruction (SIGAR) dated July 28, 2011.

#### **IV. Scope**

In the Spring of 2011, the Illinois DOI issued Warrants<sup>11</sup> for a special examination of CNA's management of its DBA program with the US Government. Accordingly, the Director instructed AIM as the appointed Special Examiner to:

“..make a full and true report to me (the Director) of the examination of the company's claim settlement and policy administration in connection with contracts with the United States Government and contractors for the United States Government and further including insurance business connected with the Defense Base Act.”

Based on this language, AIM's charge was to conduct a comprehensive management and operations review of all aspects of CNA's administration of its DBA program. Given that the Sallyport incident was a claims management issue, the examination included an in-depth analysis of CNA's DBA claims operations and specifically the handling of the Sallyport claims.

In addition, AIM was directed to include in the examination the two subsequent matters noted, the DOL Inspector General's report and SIGAR report that were critical of CNA's handling of its DBA business.

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<sup>11</sup> Four warrants were issued to numerous CNA subsidiaries, but all with the same wording and instructions.

## **V. Methodology and AIM Review Standards**

### **Methodology**

During the summer of 2011, AIM conducted an examination of all key aspects involving the conduct of CNA's DBA program as directed in the DOI's warrants. This included but was not limited to management oversight and reporting, organizational structure, systems, management information, staffing levels and expertise, claim authority levels and, in particular, the effectiveness of CNA's DBA claim management operations.

Areas of evaluation included the quality and effectiveness of controls, practices and procedures particularly necessary for this unique line of business; use of continuous improvement measures; management responsiveness; span of management responsibilities; and inter-company communication and coordination.

AIM's review included but was not limited to:

- Data Request Exhibits 3 a & b<sup>12</sup>: comprehensive evaluation of critical management and operating documents initially based on AIM's document request and updated as the examination progressed.
- Interviewing key executives, DBA managers and staff that spanned from the President and COO of all Commercial Business to line level claim adjusters.
- The claim file review was an in-depth analysis of 215 DBA claim files of which 198 were randomly selected to provide a statistically valid sample of claims to review enabling AIM to opine on the effectiveness of CNA's DBA claim handling capabilities on an overall basis consistent with the NAIC Chapter 14 Market Regulation Handbook 2010 and CNA's internal claim management guidelines and standards. As detailed below, the claim file review included claim-handling timeliness, case-reserving accuracy, case management practices, follow-up/diary procedures and the

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<sup>12</sup> Because of the volume of material, AIM's Document Request is an electronic folder with an Excel Spreadsheet noting data and information requested. Each request has a hyperlink imbedded that is to pull up a PDF copy of the CNA requested document automatically. Should the link functionality not work source the documents by title within the master file.



general demeanor of claims staff in working with claimants and injured employees based on reviewed file notes.

The balance of claims evaluated included those noted in the DOL's Inspector General's report (Exhibit 13a and Exhibit 13b, the SIGAR report (Exhibit 12a) and 6 of the Sallyport claims including the one giving rise to the adverse publicity last Spring and subject of the USDOL Case # 2011-LDA -2000 (Claimant name redacted) V. Sallyport Global Services (employer) and Continental Casualty Company (carrier), with ruling issued May 12, 2011.

### **AIM Review Standards**

(The following details the basis upon which AIM refers to in this report as "Best Practices" and "Industry Standards, Control, Practices and Procedures")

With respect to "Best Practice" Wikipedia's" definition is as follows:

"A best practice is a method or technique that has consistently shown results superior to those achieved with other means, and that is used as a benchmark. In addition, a "best" practice can evolve to become better as improvements are discovered."

A "Best Practice" is also considered to describe the process of developing and following a standard way of conducting business that multiple organizations use. In this regard, the phrase "Industry Control, Practices and Procedures" is most applicable.

AIM, however, believes a key strategic talent required when applying "best practice" knowledge to evaluating organizations is the ability to balance the unique qualities of an organization and its products or services with the practices that it has in common with others, while also gauging and incorporating the relevance of differences that need to be unique and essential.

This latter point recognizes the unique nature of DBA insurance and an insurer's special operational requirements, such as with CNA, to effectively handle the complexities of DBA insurance and in particular the claims that follow.

While referring in this report to “Best Practices” or “industry standards, controls, practices and procedures”, the comments are based on the aggregation of AIM’s industry experience and that of its examiners who have accumulated recognized expertise and knowledge while evaluating the operations of well over a hundred insurers over the last several decades.

In general, insurance claim management activities that AIM would evaluate for book of workers’ compensation insurance in assessing conformity with industry-recognized standards, controls, practices and procedures and use of “best practices” would include compliance with the insurer’s own documented standards but as well on an industry basis to include but not be limited to the following:

- **Timeliness**

This category addresses the prompt review and response by the claim handler of the file once it has been received by CNA for handling. This includes the examiner’s responses to correspondence and the need for investigation, reserve adjustments, and prompt payments of benefits as required by the DBA. Penalties assessed due to delayed payment of benefits would also be captured in this category.

- **Coverage**

This category addresses the necessity of not only identifying coverage verification for the named contractor but any subcontractors. This area addresses any other available coverage that would respond to the claim (War Hazard, Second Injury Fund). The underwriting file should accompany the claim file and any nuances with respect to coverage terms addressed here.

- **Coding**

This category addresses quality control of data input for policy and claim information. The underwriting files are also reviewed to determine if the agreed rates as defined in the respective government contracts are being utilized. In addition, classification codes, scheduled credit calculations, payroll verification, experience history and premium allocation audited for accuracy.

- Investigation

This category addresses the timely investigation by both CNA and any vendor's assigned to the loss to confirm the injured worker's benefit eligibility as well as dependant eligibility where appropriate. The investigation should include contact with all parties involved and should be completed as soon as possible. Once the initial investigation is completed, additional investigation addressing the injured worker's medical status, return to work and permanent disability will be addressed.

- Evaluation

This category addresses the proper review of information and documentation so that the potential liability exposure can be properly evaluated and appropriate reserves established. The evaluation should identify the information and documentation relied upon to confirm disability and medical needs (physician reports, rehabilitation reports, IME, subrogation, etc.). The claim handler not only identifies and reviews the information but also provides rationale as to how this impacts policy exposure.

- Reserving

This category addresses whether the reserves currently established adequately reflect the injured worker's expected benefits. All aspects of the claim review process (analysis of any legal issues, contract issues, rate adjustments, etc.) should be discussed to support the reserves required to administer the benefits. In addition reserves are reviewed for accurate benefit calculation broken down by benefit level (TTD, TPD, PPD, PTD, Death).

- Litigation Management

This category addresses the claim examiner's review and response to the discovery obtained by defense counsel in litigated cases. It is the claim handler's responsibility to steer litigation strategy and provide guidance to defense counsel regarding appropriate discovery needs. Also evaluated is the examiner's ability to monitor and interact with the attorney to resolve the litigation as efficiently and cost effectively as possible.

- **Medical Management**

This category encompasses the need for nurse case management and vendor review of billings to verify they comport to prevailing rates. A review of whether the claim handler is complying with CNA's Medical Management program is addressed as well as if proactive efforts are demonstrated to control costs and ensure medical is related to industrial injury.

- **Documentation/Reporting**

This category addresses whether there is documentation in the file to support the claim and activity incurred to resolve the loss. Documentation includes all forms of correspondence (i.e. emails, status reports, medical reports, bills, letters, legal documents etc.) and especially examiner generated documents to all involved parties.

- **Settlement/Negotiations**

This category addresses whether the examiner has obtained internal authority approval if required, as well as the claim handlers involvement and/or communication to affect the final disability award, reasons for compromise, etc.

- **Recovery**

This category analyzed the timely pursuit of any potential payment from other responsible parties. This would include, but is not limited to subrogation claims, pursuit of benefit overpayments, Department of Labor reimbursements on War Hazard claims

- **Fraud**

This category is self-explanatory and involves the due diligence of the examiner in identifying claims of a suspicious nature.

- **Management & Supervisory Controls**

This category addresses CNA's supervision of the claims examiner's review and handling of their caseload. Supervision assists the examiner by providing not only additional expertise in claim handling practices, but also another experienced opinion in developing a plan of action to resolve losses. Special attention is

always considered on larger files in excess of the claim handler's authority. In these cases there should be some documentation that management has reviewed the handling of the file at that point in time.

- File Maintenance

This category addresses the condition of both the file order and the system entry applicable to the claim file. Areas of concern involved files not in chronological order, sloppily maintained file documents and files lacking system entries to support the activity on the claim. Specifically it is hoped that there is no mail that has not been reviewed that may affect the action, value and decisions made on the claim. This category also included files noted by the claim examiner to be closed yet they were still open in the system.

- Diary

This category addresses the claim examiners prompt response to necessary activity and regular follow-up thereafter to bring the claim to conclusion. It is important to maintain an active diary to ensure that activities are responded to timely. In the absence of specific dates, our analysis is based upon an appropriate period of time that was consistent with the needed activity on a particular file.

## **VI. Executive Summary**

The two primary objectives of the CNA warrants for the Special Examination issued by the Illinois DOI were:

- Evaluate CNA's claim handling "Compliance" with respect to the Sallyport suit, Case # 2011-LDA-00002.
- Report on CNA's "DBA Program Operations Effectiveness".

### **A. Compliance**

AIM has determined that CNA manages its DBA program business with professionalism and competence in all functional areas<sup>13</sup> and in particular claims management. We are further confident with its organizational structure, expertise and lessons learned from years prior as a leader in DBA "program" insurance that CNA will continue to better handle a patently difficult book of business. CNA has created over-time what AIM considers to be "best practices," which the company has institutionalized and documented since underwriting this line of business in 1998.

CNA has reached this level of competence after a challenging period of rapid growth for DBA insurance and the increasing complexity of claims. Commencing in 2005, the US Government accelerated operations in Iraq and Afghanistan and its reliance on using outsourced support services to contractors, potentially becoming CNA insureds. CNA's operational ability was developed during a period of rapid growth and far more complex tactical claims management issues for essentially what had become a new world for this line of business.

Can a claim happen today similar to the 2006 Sallyport incident, particularly in light of CNA's operational improvements since then? Yes, it can<sup>14</sup>.

The difficulty CNA encountered<sup>15</sup> in the Sallyport case was securing sufficient documentation based on CNA internal claim verification requirements that would also

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<sup>13</sup> Executive oversight, claims management, underwriting, policy and premium administration principally through Rutherford International, corporate ancillary support including actuarial services, and processing and management information systems.

<sup>14</sup> It is noteworthy that CNA paid numerous other dependency claims resulting from the 17 translators killed on the bus.

meet anticipated DOL information needs to determine and verify the mother's dependency with respect to the later demand for survivorship support as a dependent from the decedent, her son. Loss information gathering, particularly to verify parental dependency, was a challenge with the remote location of the claim in a foreign country with significant cultural differences, and often-scarce documentation to source.

While today the case would be managed more proficiently by CNA five years hence with improved operations and more experience, the determination of dependency is still a claim management subjective decision based on available facts (as noted often limited) and the claim handler's experience. However, CNA claim authority levels now elevate such cases to managers and higher if so warranted. Still the facts are not always definitive and ultimately requiring subjective decisions based on professional experience.

Adjudication of similar DBA claims by CNA and other insurers is still the same. It is based on the "experience and judgment" of the claim handler involved and the quality of investigation performed by contracted firms for on-site loss investigation as with MJM. The hardest aspect of determining dependency is again getting documentation needed, if it exists, from remote villages of third world countries. The crux of the issue in this Sallyport claim was that there was initial indication of the mother's dependency and there that there were no set criteria to establish coverage. Once coverage is confirmed, the medical care and benefits are definitive.

### **Sallyport Claim**

CNA had and has no financial self-interest in not paying a dependency claim(s) as it is fully reimbursed by the DOL plus 15% for claim handling expenses as a War Hazard claim. CNA accepted that the documentation secured by its contracted firm, MJM, on the Sallyport case was sufficient. MJM's final report appeared complete and that only funeral expense benefits were due with no surviving dependents. The deceased's mother received funeral benefits on an adequate timely basis. There was no survivorship dependency identified with or asserted by the mother during the on-site investigation based on MJM's "Final Investigation Report" for a claims adjuster to qualify her for

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<sup>15</sup> Including on-site contracted investigators

parental dependency and survivorship support. The insurer's responsibility is to handle claims in accordance with insurance coverage afforded by the DBA and the facts of the event to the extent they can be fully determined and documented.

It is noteworthy that CNA paid other dependent claims wherein parental dependency was verified and survivorship support was paid based on the investigated facts and documents received.

As with many DBA claims overseas, particularly involving foreign nationals, there are material cultural differences such as what circumstances constitute support for dependency and the level of corresponding documentation available in that country.

Therefore, to avoid similar situations occurring in the future, it would be helpful for the DOL to provide more guidance to insurers relative to what documentation is required to determine parental dependency and survivorship benefits.

The losses covered by the CNA DBA program are politically sensitive due to the underlying nature of defense contractor and war hazard claims, as well as the corresponding media attention they elicit. Such publicity against CNA and its claim unit employees is likely to occur from time to time. Therefore, it is important to note, through reading claim file notes during AIM's examination that currently CNA staff, in addition to their exemplary professionalism, when dealing directly with injured parties displayed sensitivity to the handling of the DBA losses considering the often-horrific underlying fact patterns of these claims.

CNA endeavored to find the right management and operational setting in earlier years of the program when the type of DBA exposures were changing with claims escalating due to the expansion of the Iraqi and Afghanistan wars. AIM's review found that after various initiatives to more effectively manage this business, it was in 2009 that CNA found the right organizational setting to achieve the operational improvements and management expertise that is in place today.

It is evident that CNA strives to comply with all regulatory agencies. This is evidenced by (1) CNA's responsiveness in working with the Illinois examination team, (2) review of continuous communications between CNA and the DOL/OWCP; (3) the comprehensive



response submitted by CNA to SIGAR. In the latter matter, CNA's reply addressed accurately, respectfully and factually SIGAR's critical assertions in the report, which AIM evaluated closely. Given this evident cooperation, the reasonably disputed allegations and inaccuracies in the SIGAR report and AIM's file audit findings that CNA meets high standards for handling claims, there is no viable reason or evidence found that any governing entity has cause to assert impropriety or negligence in CNA's management of its DBA program.

In December 2009, nearly three-years after the Sallyport incident, a group of nine parents inclusive of the mother, who were not originally identified as dependents by MJM or CNA, filed claims with the assistance of regional counsel for parental dependent status and survivorship benefits. The benefits sought were in excess of DBA parental survivorship benefit amounts. The primary documents submitted asserting dependency were affidavits from family members and neighbors attesting that this group of decedents had supported each of their parents. Bank records such as copies of cancelled checks or evidence of regular deposit records typically used to substantiate such claims were not in the filing.

This matter resulted in Sallyport/CNA filing for an "Order Granting Partial Summary Decision" based on the claim being untimely filed<sup>16</sup> in accordance with DBA coverage. Again, the case referenced in AIM sourced documents pertained to the mother of the deceased interpreter, Case 2011-LDA-0002 .

Counsel on behalf of the mother filed a "Cross-Motion for Summary Decision", which the Administrative Judge on May 12, 2011 ruled that all DBA coverage filing time restrictions citing other cases were "tolled" based on various factors, in particular the war zone conditions in Iraq. The Judge also determined that for lack of contrary evidence to the mother's claim as a beneficiary he accepted her claim of financial dependency and was due survivorship benefits. As one of the nine claimants that filed concurrently with CNA for these benefits, the Judge also ruled that this decision applied to the other cases as well.

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<sup>16</sup> Pursuant to Section 12 of the Act. Section 33 U.S.C @ 912

It was at that time that with the Court's ruling in favor of the Iraqi parents that publicity about the Sallyport case rose to a national level. Particular attention was drawn to the case by the claimants' other motion that alleged that the employer and insurer committed "fraud and abuse...by intentionally omitting portions of the investigation reports concerning the dependency of the Claimant on the decedent from the submission (LS-208 for file closure Exhibit 11c) to the Department of Labor." The ALJ in determining that this was not an administrative matter within his Court's preview and warranting higher Court authority, if the facts deemed appropriate, referred this aspect of the complaint to the DOL District Director of the OWCP.

Upon issuance of the Order, CNA promptly proceeded to pay dependent survivorship benefits in accordance with DBA benefit guidelines as confirmed by AIM.

No further action as of the writing of this report has been taken by the DOL. Upon AIM recently inquiring about the status of the matter, CNA responded in an email dated December 22, 2011: "We are confident that once the claimant-attorneys' fee issue is resolved that no further issues remain open and the matter will be closed by the DOL <sup>17</sup>" (Exhibit 11b).

Moreover, based on the file review and loss investigation report, AIM found no violations of the Illinois Insurance Code in the handling of this Sallyport claim. Funeral benefits were paid on a reasonably timely basis per DOL requirements with CNA filing the necessary forms with the DOL to close the claim, which occurred. Furthermore, AIM found no evidence in CNA's claim files or MJM's Final Report (Exhibit 11A) of the investigation that there was any information that the deceased's mother was a dependent, nor eligible for survivorship benefits and periodic death benefit payments.

As respects the eight other dependency claims filed as well in December 2009, AIM reviewed the files and assuming all supporting documentation requested of CNA were provided there was little evidence supporting survivorship dependency, except for the affidavits as already referenced. The information typically sought to verify dependency

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<sup>17</sup> Per email dated December 21, 2011 from Rick Ehlers, Vice-President & Associate General Counsel  
CNA Law Department - P&C Legal

and survivorship benefits previously noted were not in the material provided for these other cases as well.

CNA's responsibility is to follow DBA coverage terms and conditions; a necessary component in the government's original DBA Program intent to control costs. It is the Court's purview to "toll" DBA statutes and override DBA terms for timeliness of claim reporting and filing as it found consistent with other precedent setting cases that were cited in the Court ruling.

## **B. DBA Program Operations Effectiveness**

### **Executive & Senior Management**

AIM's interview with Robert Lindemann, P&C Operations President & CEO, was the most senior level interview conducted. The interviews with Mr. Lindemann and other senior managers revealed that executive and senior management fully understood the high profile, complexities and challenges of this unique program. There is a clear understanding of the critical success factors to continue improving the DBA program. Executive direction is evident by the exceptionally qualified senior managers and corporate resources dedicated to the DBA program.

### **Organizational Structure**

CNA has an effective dual governance structure and displays effective communication within inter-company functional areas and profit centers in a cohesive approach to managing the DBA program.

### **Claim File Audit Results**

AIM's in-depth audit of 215 claims<sup>18</sup> included a random claim selection, SIGAR report referenced claims and specific Sallyport cases. CNA's handling of these claim were graded based on 14 selected key metric categories delineated in Section II, "Methodology" that includes considerations such as to timeliness in handling; adjuster's responsiveness to injured parties; coverage application accuracy; quality of investigation;

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<sup>18</sup> Many with long histories and extensive documentation.

adjuster's evaluation; and file documentation. Having conducted many claim reviews, AIM considers a company's compliance scoring average of 80% or higher as adequate.

AIM's compliance rating for CNA is 91%. Each claim was evaluated based on passing or failing anyone of the following; DOL's reporting and handling standards, CNA's stringent<sup>19</sup> "Claim Management Guidelines" and on AIM's assessment based on knowledge of industry "Best Practices".

It is also worthy to note, considering that Sallyport as a single event did not follow the normal complaint filing process with CNA or the DOI, CNA's complaint log provided to AIM had only one entry, which was of minor significance, and did not pertain to claims management, payment of benefits or policy administration.

### **Conclusion**

Based on AIM's thorough examination, which included reliance upon documents requested and provided by the company<sup>20</sup> and based on the on-site investigation report submitted by MJM, CNA handled the Sallyport claims with reasonable effectiveness and did so in compliance with Illinois Insurance Code, DBA/USLHWC Act and DOL procedures and guidelines.

In 2005 military operations in Afghanistan and Iraq with increasing use of contractors for military support services began to increase rapidly as followed the volume of DBA claims. CNA strived to meet the underwriting and claims management needs of the rapidly growing and changing nature of DBA business. In 1999, AIM identified that CNA management began to create the optimum organizational structure and develop "best practices" evident today.

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<sup>19</sup> As determined by AIM

<sup>20</sup> AIM.CNA Data Request Docs (Folder)

## **VII. Defense Base Act Insurance and War Recovery<sup>21</sup>**

The DBA was enacted in 1941 to provide workers compensation benefits to workers of government contractors in foreign countries. As part of this operational and technical review of CNA's handling of the DBA Program and administration of benefits, it is important to understand the benefit structure established by the LHWCA, which the DBA applies to injured or killed employees of government agencies that contract firms to perform services outside the continental United States. For this reason, we list below the benefits paid to qualified injured workers and/or their beneficiaries:

- Temporary Total Disability: 2/3 of the Average Weekly Wage ("AWW") to the current maximum cap of \$1,256.84
- Temporary Partial Disability: 2/3 of employee's loss of wages (pre-injury v post-injury) subject to the maximum cap
- Permanent Partial Disability: 2/3 of loss of earning capacity for unscheduled PPD or a scheduled PPD body part percentage paid at the TTD rate
- Permanent Total Disability: 2/3 of the AWW subject to the maximum cap. Benefit includes annual COLA adjustments set by the Department of labor
- Death:
  - Spouse entitled to 50% of the deceased AWW
  - Dependent child is entitled to 16 2/3% of the AWW
  - If no spouse or children, eligible dependants can receive up to 25% of the deceased's AWW
  - Funeral expenses up to \$3,000

Refer to Exhibit 3b: DBA.CNA Document Summaries (IL DBA A3 "Defense Based Act Overview")

- If CNA concludes a claim is compensable and the method and amount of compensation is agreed to by the claimant (or representative), either the injured worker (or beneficiaries) and CNA can explore options for final resolution,

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<sup>21</sup> All procedural references and guidelines, form references and injury payment or settlement terms can be found on the DOL website at the following web address: (<http://www.dol.gov/owcp/dlhwc>)

including lump sum payments. If such agreements are reached, the agreed to disposition is presented to the DOL for final determination and approval.

- Based on the facts discovered during the claim investigation, the carrier may deny payment of the claim based on its professional experience and conclusion of the investigation claim facts. In this instance, the injured worker has one year from the date of the denial to contest the determination based on DBA terms and conditions.
- When the DOL District Director issues a Compensation Order, payments to the injured worker are to be paid by CNA within 10 days of the DOL Order in accordance with the DOL OWCP DBA Claim Administration Guidelines<sup>22</sup>.
- The DOL may request a conference to discuss the issues of the case after which a DOL 05-01 Bulletin Order is issued with the results of the DOL decision (this conference is required for the processing of war hazard claims by the DOL).
- The carrier and injured worker upon mutual agreement in the course of claim adjudication can enter a DOL/DBA Section 8(if) settlement<sup>23</sup> which is a full lump sum settlement of all benefits (indemnity and medical). Payment is required within 10 days from the order approving the settlement.
- A carrier can pursue A DOL Section 8(f) relief from the Second Injury Fund (SIF) if an earlier injury is deemed to have contributed to the ultimate disability. If the Section 8(f) motion is granted the SIF will assume responsibility to issue payments to the injured worker after 104 weeks of permanent disability has been paid (except in hearing loss cases). There is no SIF relief for medical care.
- A commutation is allowed for a reduced amount (typically set on present value of life benefits) in a lump sum and must be paid within 10 days after the DOL based on DBA terms approves and issues the order.

Not only are the claims of the overseas defense contractors covered under the DBA Act, but those claims filed that occurred as a result of being exposed to a War Hazard (WH) are also

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<sup>22</sup> <http://www.dol.gov/owcp/dlhwc>

<sup>23</sup> <http://www.dol.gov/owcp/dlhwc>

covered. To assist with the understanding of what activities meet the definition of War Hazard (Exhibit 3 – Document Summaries: IL DBA A27a), the DOL has provided the following:

- Discharge of a missile
- Use of a weapon, explosive or other noxious thing by hostile forces
- Combating an attack
- Action of a hostile person without use of specified weapons
- Discharge or explosion of munitions stored for use in a conflict
- Collision of vessels or aircraft during conflict

The DOL has established a process for the carriers relative to the submission of potential WH claims that qualify for 100% recovery from the Federal Government for all contracted United States Citizens and Foreign Nationals injured overseas. In October 2009, the DOL changed the procedures for WH claim management. As before, the process for reimbursement requires the carriers pursuing WH recovery once a WH injured employee reaches maximum medical improvement (MMI) to submit the Compensation Order, commutation, Administrative Law Judge's decision or a DOL approved 8(i) settlement with all supporting documents to the Division of Federal Employees Compensation ("DFEC"). In turn, DFEC will send a voucher followed by a reimbursement check for 100% of payments made by the carrier plus 15% for administrative costs. If denied, the carrier may appeal. This process from the initial filing to actual reimbursement can take a year or more.

However, DFEC will only take over the administrative task of future benefit payments from CNA US citizen approved WH cases that have reached MMI. With respect to Foreign Nationals, the carriers must continue handling the claims and seek at least annually reimbursement for costs incurred plus the 15% expense fee.

Given the complexity of DBA coverage provisions and limited availability of experience in the industry with DBA claim handling particularly earlier on, AIM sought to trace CNA's operational history and effectiveness since 1998 in handling DBA business. A critical component of this review by AIM was to determine efforts CNA undertook to interact with DOL in an effort to gain an understanding of DOL interpretation of DBA coverage and

handling requirements. Unfortunately the majority of CNA personnel handling DBA losses since inception were no longer being with the company to interview. Further, the number of DBA claims did not significantly increase until the United States entered military action on a full conflict basis action in Afghanistan in 2001 and Iraq in 2005. As exposures increase, claims follow usually on a delayed basis as in this case. Thus, the volume of claims began to increase markedly later in 2005 and subsequently.

In time CNA began to experience this change and understand the new demands on its operations to effectively manage the DBA program. This was evident in that the DBA program prior to 2009 had been re-assigned several times to different company operating divisions. Prior to 2009, CNA attempts to effectively provide the service needed and manage its own underwriting performance was not as successful as hoped for and needed. The DBA program for CNA had been and is still unprofitable despite marked improvements.

Although there is significant documentation demonstrating the ongoing interaction between CNA and the DOL on individual cases since program inception, it appears that it wasn't until 2009 that CNA became more proactive in securing operating feedback from the DOL. The frequency and content in communiqués, meetings and discussion notes with the DOL in 2009<sup>24</sup> and thereafter reflects CNA's constructive efforts. This is a direct result of the substantial reorganization of the of the DBA program operations commencing in the latter half of 2009.

Emails authored by Bob Simon, CNA VP – Claims Strategy & Technical Services summarized meetings and conference calls with Richard Robilotti, the DOL NY Deputy District Director, and other DOL staff. Emails directed to Kathy Pagnano, CNA – VP Management Oversight, Todd Lewis, AVP – Claims Strategy & Technical Services and Michael Dower VP – Manager International Underwriting relative to meetings with the DOL in New York on 9/22/09 and 4/27/10 were reviewed. Due to administrative changes and other issues, Deputy Director Robilotti of New York's DOL district office, scheduled meetings with all carriers providing DBA coverage. The DOL selected CNA for the first meeting as Mr. Robilotti perceived that CNA's reporting and compliance with the DOL

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<sup>24</sup> Refer to AIM Data Request Documents: IL DBA A25; 5 Documents



administrative requirements and interpretation of the DBA were the least compliant as compared to the other carriers providing DBA coverage.

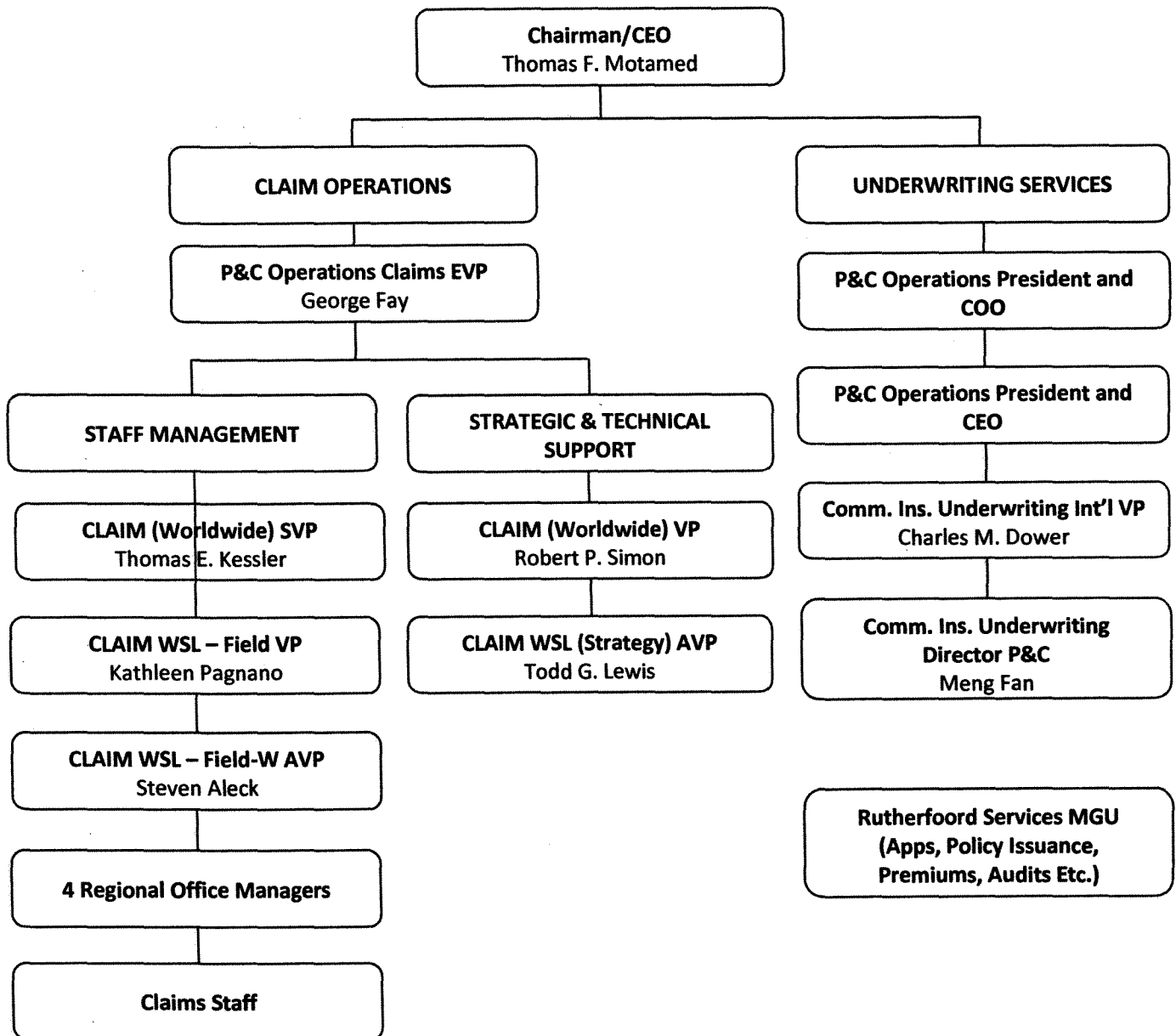
During the meeting, the Deputy Director voiced concerns about CNA's DBA claim handling (most notably the Dallas office) with respect to (A) the need for more timely filing of the LS-202's (first report of injury), (B) the need for better investigative information on disputed claims, and (C) a timeline relative to losses contested due to a need for additional time to investigate (LS-207 Notice of Controversion of Benefits).

A very positive email authored by Kathy Pagnano summarized a 4/27/2010 meeting between CNA representatives Bob Simon and Assistant General Counsel Rick Ehlers and the Deputy Director Robilotti documenting CNA's significant improvements since the initial 9/22/2009 meeting.

## VIII. CNA DBA Insurance Operations<sup>25</sup>

### A. Organizational Structure

CNA has developed an effective organizational structure for the functional operating needs of the DBA program. The DBA program corporate organizational structure is below.



<sup>25</sup> Exhibit 14 - NA Corporate Entities and Subsidiaries

CNA has a dual governance structure that results in effective communication within inter-company functional areas and profit centers in a cohesive approach to managing the DBA program.

The DBA program oversight (as for all lines of business) has two senior managers in the claims area that is most staff intensive; Kathy Pagnano is responsible for staff management and daily operations and Bob Simon is responsible for strategic problem solving, proactive operational direction and technical issue solving. Individuals have strengths typically in differing areas and the span of control at this level if not split would be too broad. CNA's dual claim structure achieves an effective holistic approach on a team basis.

The two primary DBA functional areas are claims and underwriting. Underwriting includes corporate and field actuarial support and front-end policy administration. DBA is a profit center of the International Business Group led by Meng Fan, Underwriting Director, International Commercial P&C Insurance, who we interviewed as well. With established terms when an agency DBA program is effective, there is little or no risk underwriting for the balance of the multiple-year agreement contract. Therefore, underwriting is an intensive onetime effort in developing proposed contract terms and premium rates for work classification tiers during the negotiation process.

Rutherford International, a division of Marsh McLennan, is contracted by CNA to handle parts of the underwriting function including contractor application reviews and approvals, policy issuance, and premium calculation, collection and audit activities. In this capacity, Rutherford is a Managing General Underwriter (MGU) for CNA. Rutherford has been significantly involved in the DBA insurance book as a manager and broker for program and non-program business and is highly experienced as is Rutherford's DBA Manager, Sara Payne, SVP, Government Programs.

CNA has an excellent business partnership with Rutherford. Contractors that seek work for U.S. government agencies in active war zones such as Iraq and Afghanistan are challenging to work with as can be imagined. Historic knowledge of the contractors and how they operate is essential in effectively managing the application process<sup>26</sup>,

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<sup>26</sup> While a contractor cannot be rejected for coverage, coverage and policy issuance can only occur with a fully completed application.

reporting use of sub-contractors, premium management and payroll auditing, particularly if audits result in additional premium to be collected. Rutherford brings this critical expertise to this aspect of the underwriting function and overall management of the DBA program.

### **B. Executive and Senior Management**

AIM's interview with Robert Lindemann, P&C Operations President & CEO, was the most senior level interview conducted. The interview revealed that executive and senior management fully understood the high profile, complexities and challenges of this unique program with a clear understanding of the critical success factors to continue improvement.

Based on our overall findings, executive direction is evident by the exceptionally qualified senior managers assigned the responsibility for the DBA program and the resources applied

### **C. Operations Summary**

Since 2009, the improvements in the claims area have been exceptional as documented by AIM and the DOL. Refer to Exhibit 5 which includes emails first from the DOL in 2009 that CNA was not managing its DBA programs well to emails in 2010 and subsequent noting significant improvement in CNA's DBA program management.

With a substantial amount of fundamental corrective action accomplished, the task of management is to maintain the effort to continuously improve operations particularly with respect to timeliness of claim handling issues (refer to the Claims Operations section and Audit Findings). Also, management needs to maintain sufficient levels of trained and qualified staff as military contract-outsourcing will likely continue to increase for the near-term.

Underwriting is limited as each agency contract is negotiated for a contract period that is typically several years in duration, though recent reductions in contract terms have been negotiated by CNA with various agencies. The USDOS contract that had been a five-year term was re-negotiated with an effective date of July 2011 and only a two-year

term, renewing in June 2013. Higher rates were agreed upon but not to the level CNA actuarial unit perceive is needed to be profitable.

USACE contract renews in the Spring of 2013 as well. If overall underwriting profitability is not achieved by that time, CNA will likely consider whether they should remain a DBA program insurer. In the mean time, it is apparent they are doing everything possible to make this a success.

The following sections address in detail our analysis of underwriting, administrative capabilities, claims management and a review of the AIM claim file audit and findings.

#### **D. DBA Underwriting, Program Administration (Rutherford MGU) and Actuarial Support**

CNA is one of five carriers writing DBA insurance coverage. The other carriers providing coverage are Chartis, ACE, Zurich, AWAC, and CNA. CNA has approximately 10% of the market. DBA business is divided between program and non-program business.

There are four agencies with sole sourced programs (Exhibit 7) with set rates:

- Army Corps of Engineers (Incepted Q2 2005)
- Department of State (Incepted Q2 2002)
- U.S. Government Security (Incepted Q2 2010)
- U.S. Agency for International Development (Incepted Q1 1999 & non-renewed 2009)

The difference in "open-market" insurance and "program" insurance is in the latter instance. CNA would negotiate a contract (most being multiple-year obligations) with a government agency to provide DBA insurance for all contractors the agency engages. Premiums are negotiated with the agency for respective worker classifications and contractually fixed for an agreed period with the agency.

As a program insurer, CNA is obligated to insure all contractors entering into contracts with that government agency. CNA has no discretion in selection of risks or premium rates charged, wherein "open-market" insurers have such discretion.

CNA has been the dominant DBA "program" insurer. The following totals are as of June 1, 2011 (Exhibit 3b IL DBA A3):

<b>Agency</b>	<b># of Active Policies</b>	<b>Written Premium</b>
U.S. Army Corps of Eng	1996	\$56,390,884
Department of State	670	\$59,315,108
U.S. Government Security Non-Program	Not provided	Low volume (# not given)
	310	\$14,295,015

All agencies require the same reporting. Quarterly reports are provided for written premium and audit. Semi-annual and Annual reports are provided for detailed loss experience and War Hazard claims listings.

Management oversight on both corporate and operational levels is depicted in the preceding organizational chart.

The manager of underwriting is Meng Fan whose formal title is Underwriting Director, International Commercial P&C. She has been involved with CNA DBA business (program and non-program) since 1998 when CNA began writing DBA business. She is also the primary liaison with their MGU, Rutherford International with whom CNA initially contracted in 1998.

Rutherford International's government program specialist and manager is SVP, Sara Payne. As commented on previously, Ms. Payne has substantial experience with DBA insurance.

CNA's Meng Fan and Rutherford's Sara Payne possess the most experience each with over 12 years of experience in DBA insurance.

CNA, under Ms. Fan's direction, underwrite non-program business, which is a per risk assessment. CNA's 2011 non-program written premiums as noted above is \$14.3 million (10% of all DBA premiums) for 310 policies in force. Rutherford predominantly brokers the majority of these policies to CNA.

Underwriting performance results were not separated by DBA program or non-program business. It was noted in the interview with Mr. Lindemann that the USACE program is significantly the largest and is profitable. However, also noted was that the USDOS program losses have been so adverse, despite the premium weighting, historic results overall for CNA's DBA business have been in excess of a combined ratio<sup>27</sup> of 108%. It is presumed that the DOS exposures with the "Security" class of business, represents innately to contractor employees far greater frequency and severity of injury including death.

The underwriting results were inclusive of the discontinued USAID program and the USGS program (noted as new and nominal in premium volume).

During our interview with Rutherford's, Sara Payne commented that some contractors unable to get insurance in the "open-market" from non-program agencies for reasons including higher exposures, risk quality and/or safety management weaknesses often pursue business from one of CNA's program agencies. Program business thus can attract more adverse-risk business than expected.

The chart on the next page provided by CNA reflects the underwriting performance of CNA's DBA business that has had combined ratios in excess of 103% since 2007.

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<sup>27</sup> The ratio of ((Ultimate incurred loss and LAE + the underwriting expense ratio)/earned premium.)

# 1. Defense Base Act Underwriting Results

## *All Programs and Non-Program Business*

	2011q1	2010	2009	2008	2007	2006	2005
<b>Earned Premium</b>	<b>34,924</b>	<b>163,689</b>	<b>146,021</b>	<b>101,824</b>	<b>96,334</b>	<b>80,999</b>	<b>59,820</b>
<b>Ultimate L &amp; ALAE %</b>	<b>77.3%</b>	<b>75.8%</b>	<b>77.2%</b>	<b>85.6%</b>	<b>80.1%</b>	<b>68.7%</b>	<b>52.4%</b>
<b>ULAE%</b>	<b>8.5%</b>	<b>8.4%</b>	<b>8.5%</b>	<b>6.9%</b>	<b>6.4%</b>	<b>6.3%</b>	<b>5.0%</b>
<b>Commissions</b>	<b>12.1%</b>	<b>12.2%</b>	<b>12.6%</b>	<b>13.2%</b>	<b>13.7%</b>	<b>14.3%</b>	<b>13.9%</b>
<b>Prem Tax &amp; Other Assessment</b>	<b>7.6%</b>	<b>7.4%</b>	<b>7.9%</b>	<b>8.8%</b>	<b>7.8%</b>	<b>6.8%</b>	<b>5.5%</b>
<b>UW Expense %</b>	<b><u>4.4%</u></b>	<b><u>4.2%</u></b>	<b><u>2.6%</u></b>	<b><u>3.1%</u></b>	<b><u>3.1%</u></b>	<b><u>3.7%</u></b>	<b><u>4.0%</u></b>
<b>Total UW/Acq Expense %</b>	<b>24.1%</b>	<b>23.9%</b>	<b>23.1%</b>	<b>25.1%</b>	<b>24.6%</b>	<b>24.8%</b>	<b>23.4%</b>
<b>UW Profit \$</b>	<b>-3,474</b>	<b>-13,048</b>	<b>-12,776</b>	<b>-17,930</b>	<b>-10,743</b>	<b>149</b>	<b>11,429</b>
<b>Combined Ratio</b>	<b>109.9%</b>	<b>108.0%</b>	<b>108.7%</b>	<b>117.6%</b>	<b>111.2%</b>	<b>99.8%</b>	<b>80.9%</b>

## **Summary**

	2008-2011q1	2005-2011q1
<b>Earned Premium</b>	<b>446,458</b>	<b>683,612</b>
<b>Ultimate L &amp; ALAE %</b>	<b>78.6%</b>	<b>75.3%</b>
<b>ULAE%</b>	<b>8.1%</b>	<b>7.4%</b>
<b>Commissions</b>	<b>12.6%</b>	<b>13.0%</b>
<b>Prem Tax &amp; Other Assessment</b>	<b>7.9%</b>	<b>7.5%</b>
<b>UW Expense %</b>	<b><u>3.5%</u></b>	<b><u>3.5%</u></b>
<b>Total UW/Acq Expense %</b>	<b>23.9%</b>	<b>24.1%</b>
<b>UW Profit \$</b>	<b>-47,228</b>	<b>-46,394</b>
<b>Combined Ratio</b>	<b>110.6%</b>	<b>106.8%</b>

CNA financial liability does not include War Hazard claims.



## **2. Underwriting Review Summary**

Administratively, the CNA / Rutherford relationship is effective and efficient. With characteristically tough insured/contractors, Rutherford is a valuable asset as the gatekeeper for screening and processing incoming contractors.

With the close relationship between CNA and Rutherford, non-program business would need to be underwritten with added care and not on an accommodation basis. The scope of our work did not include testing the underwriting quality of non-program business.

AIM's experience has found that a company's smaller segments of business, specialty programs in particular, can create disproportionately greater losses often due to less management attention and product experience with underwriting and claims handling. This perhaps may have been the case with CNA's DBA program in earlier years. However, with increasing claims costs, it was apparent that management's oversight in 2005 became more focused on the DBA program with an all out effort in 2009, particularly with managing the increasingly complex claims.

CNA as an early specialist in insuring construction risk and knowledgeable in the workers' compensation line of business perceived that DBA program business would be a good fit, particularly with the ACOE. According to management, the ACOE program, its largest, has been profitable. However, its other DBA programs and in particular DOS contract has caused CNA's DBA program business to be quite unprofitable overall as previously illustrated.

## **3. CLUE Reports (Claims Loss Underwriting Evaluation)**

The CLUE report and procedure were established for the Claim Department to communicate with the Underwriting Department pertinent information regarding the risk, the policyholder and other important issues that may influence underwriting decisions. The procedure defines roles and responsibilities for the claim specialist/representative and the underwriting administrator/underwriter. The types of reporting issues, concerns and claims that qualify for a CLUE report are provided in separate charts by line of business as well as given a High, Medium and Low priority status. The following categories are noted for the Workers Compensation Line of Business:

- Fatality
- Unsafe/Unguarded Machinery
- Equipment not complying with safety regulations
- Occupational Disease Exposures
- Injury resulting from use of a controlled substance
- Business closing
- No "Return to Work" program in place
- Employment of minors

This report is an excellent tool connecting underwriting risk exposure with resulting claim experience on a line operating level. While there is less use for DBA as a program line of business, the accumulated information is useful for renewal negotiations. The CLUE reports would be more immediately useful for the non-program business.

The documented controls and procedures utilized in the underwriting and policy administration area are effective and compliance with their use appear to be consistent though a more in depth review would be necessary to verify, which was not in the scope of this engagement being more claim handling focused.

#### **4. Policy and Premium Administrative Controls and Procedures (Rutherford)**

CNA conducts underwriting and premium control audits of Rutherford to insure compliance to Program Administration guidelines set forth in the Rutherford Management Agreement (Exhibit 6). Examples of the Rutherford Underwriting Audit Checklist and Audit Reports were provided (July 2008, 2009, and 2010) with 50 files selected at random providing overall findings, recommendations and responses to the prior year recommendations. The audits focus on application completeness, accurate rate verification, compliance with the Office of Foreign Assets Control (OFAC) documentation overseeing government funding/reimbursement of contractors for DBA insurance, timeliness of policy issuance, and premium collection.

CNA's ACI internal audit team conducts annual audits of the underwriting group to evaluate the effectiveness of the Rutherford oversight by the CNA Program Manager.

Audits conducted in 2008 and 2010<sup>28</sup> were generally satisfactory. The scope of the audits focused on the following areas:

- Program Administrator Rutherford International's adherence with contractual requirements
- Application of rates within each of the programs
- Fiduciary controls over cash receipts, disbursements and premium remittances
- Premium processing and policy issuance, including time service standards
- Receivable monitoring
- Issuance and tracking of premium audits
- Policy number reconciliations
- Regulatory adherence, with focus on proper use of policy forms and rates, verification of broker licensing status, complaint handling, and processing of cancellations and non-renewals
- Coordination between Underwriting, Actuarial and Claim with respect to rate and loss analysis
- Financial stability of the agency
- Handling of WH loss coding by the Claim organization

AIM found that CNA's underwriting function, Rutherford's performance as the MGU, communication between the companies and CNA oversights are effectively conducted.

## **5. DBA Actuarial Support**

Rick Holtz, FCAS, provides CNA's DBA's internal actuarial support. He is a Field Actuarial Team leader with five staff and supports the actuarial reserve setting and product pricing needs of 35 regional CNA offices. He reports to James O'Malley, Vice President and Chief Actuary.

Mr. Holtz was assigned this position in May 2009, when renewal negotiations with the USACE were also underway. This prompted accelerated learning of the unique actuarial challenges presented by the DBA business to accurately establish reserves and the

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<sup>28</sup> 2009 was not conducted ostensibly due to other activities with respect to CNA's overall DBA program reorganization

"Ultimate Incurred Loss and ALAE Ratio (net of WH recoveries), which was determined to be for the USACE negotiations 57.5%.

This ratio established CNA's premium rate tier in the USACE 2009 renewal. CNA's supporting work documents were the ones SIGAR disputed. While AIM perceives that some of CNA's work papers could have been clearer, a function of Mr. Holtz's early familiarity with DBA insurance, the main difficulty SIGAR had was in understanding the concept of IBNR<sup>29</sup>. SIGAR insisted the Loss Ratio should have been 5%, which ignored loss development factors and loss emergence as a statistical reality. Accordingly, SIGAR asserted that CNA's premium rate tiers should have been set at the lowest ACOE contract level and CNA therefore was over charging.

In July 2009, Mr. Holtz led the actuarial component of the file-by-file case reserving adequacy study under the direction of Bob Simon's Claim Strategy and Technical Team. This promoted the overall reengineering of the DBA program's staffing, practices, controls and procedures. Thus, commencing in the latter part of 2009, these efforts began what is today a well-managed book of business. Two outcomes of the study were that 1) case reserves were to be increased dramatically<sup>30</sup> and 2) a management objective should be established whereby the ultimate case reserve for a claim is accurately determined within 12 months from receipt of first report 95% of the time. This measure we (AIM) used in our claim file review.

The increase in understanding of and sophistication in DBA reserve setting and ultimate incurred loss determination is evident in CNA's reserve evaluation work papers as of December 31, 2010 and the Actuarial Opinion<sup>31</sup> Report as of March 31, 2011 (Exhibit 4). During AIM's interview with Rick Holtz, he reviewed the report highlighting how CNA develops paid and incurred loss development factors, which initially includes WH and non-WH claims. The next step separates the War Hazard claims that are fully reimbursed by the government so that ultimate loss projections are then estimated for all Non-WH DBA claims.

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<sup>29</sup> Incurred But Not Reported Losses

<sup>30</sup> Consistent with statutory accounting principles for case reserve adequacy.

<sup>31</sup> While the report indicates that it is an "Opinion," there was no written opinion or analysis discussion that typically accompanies actuarial reports. AIM requested a copy on several occasions, which was not received. Nor, could AIM establish if one had been written for the report.

As learned during the AIM/Holtz interview, it is worthy to note the following:

- Earlier reserving for DBA program reserve setting and pricing included other CNA WC line results as the DBA program did not have sufficient loss history for reserve setting and pricing until more recently.
- Not all perceived WH claims are accepted by the DOL. CNA has developed sufficient experience to presently estimate that 8% of WH claim costs will be denied. This ratio is factored into CNA's pricing; a complaint raised in the SIGAR report.
- WH cases can only be submitted for reimbursement (with substantial documentation) to DOL's DFEC when the injured employee has died or reached Maximum Medical Improvement (MMI), which can take significant time, even years.
- Post Traumatic Syndrome (PTS) is an emerging exposure in DBA claims. PTS claims characteristically take longer to be reported and achieving MMI is often a lengthy process as well.
- CNA's DBA reserving includes their entire book of DBA business, program and non-program business.
- Allocated Loss Adjustment Expense (ALAE) is a bulk estimate and not individually estimated by claim.

The data chart on the following page highlights the March 31, 2011 Actuarial Opinion results.

<b>CNA DBA March 31, 2011 Actuarial Highlights</b>			
	<b>All DBA</b>	<b>DBA X</b>	<b>WH</b>
(\$000's)	(Incl. WH)	WH	Only
Ultimate Premium	734,523	734,523	734,523
Paid Loss & ALAE	294,162	166,666	127,497
Case Loss Reserves	353,980	214,816	139,163
IBNR (L & ALAE)	246,717	142,668	106,954
Total Reserves (Case & IBNR)	600,697	357,485	246,118
Total Ultimate (Incl. Pd.)	894,859	524,151	373,615
Ultimate Net of WH Recoveries*	554,039	524,151	29,889
Gross Loss Ratio net of Recoveries			
2009	72.20%	76.30%	
2010	71.75%	70.90%	
*Assumes a 92% WH Recovery Factor			
Source: CNA Home Foreign DBA Actuarial Study March 31, 2011			

## 6. Data Capture, Systems and Management Information

"MERLIN," which CNA developed internally, is CNA's statistical system data warehouse and the source for statutory financial reporting. The primary claim payment system, ACT, is a legacy system that captures only 'paid' claim amounts which feed into Merlin as do other CNA data capture systems. MERLIN is a robust data warehouse as reflected, for example, in the data and management information that is presented in CLUE and Dashboard reports.

Actuarial services and information needs available through MERLIN effectively support CNA's underwriting function.

## **7. DBA Claim Operations**

A request was made for documents outlining operating guidelines and procedures that presently exist at CNA (Exhibit 8a and Exhibit 8b). To that end, the following documents and applicable subsections AIM received:

- **Workers Compensation Guidelines**
  - Coverage
  - Contact
  - Investigation
  - Reserves including life table and wage loss claims
  - Medical Disability Management
  - File Disposition
  - Litigation Management
  - SIU and Fraud Awareness
  - Recovery/Subrogation Offsets
  - Customer Service
  - Supervisory/Management Input
- **Authority Levels, including Large Loss Report Procedures/Round Table Programs.** Minimum levels \$100,000 for loss time claim handlers to \$750,000 for managers. Officers have authority to \$5 MM and executives to \$25 MM.
- **Internal Audit Process (ACI Group) and Reporting Procedures**
- **Claim Quality Review Process including guidelines, selection process, calibration, scoring and reporting**
- **Vendor Management and Labor Market Surveys**
- **Consumer Complaint Procedures and Log**
- **Diary Requirements**
- **Management Reports**

In 2008 CNA implemented companywide the "Claims Center" system that dramatically improved claims case management in key areas (history, file notes, diary dates, highlighting claim handling action plans and more) and moved CNA closer to its long-term goal of becoming paperless. Thus, with the Claims Center system, DBA claims were capable of being managed more proactively, efficiently and effectively. Due to DBA's growth and management's realization of how much more complicated DBA claims were than more traditional Workers Compensation claims, management recognized the existing staffing limitations and began staffing the DBA unit with more experienced claim professionals. Further, CNA also implemented a parallel organizational re-structure at the VP management level with separate operating functions for "Staff Management" and "Strategy/ Technical Services" (which will be discussed below) as well as a Global Case Management Program for all its International Business.

As is evidenced in the Document Request and Document Review Summary (Exhibits 9 and 1), the review team conducted an in-depth review of the most common management information reports that should exist in a commercial insurance organization to effectively administer and manage the DBA program. AIM findings are that CNA has in place adequate policies and procedures equal to, if not exceeding, industry "Best Practices" standards.

#### **1. Staff**

In the first quarter of 2006, due to increased claim volume, a new specialty unit to handle DBA losses was established in the Diversified Claims Operations Group in the Chicago home office. In addition, two field staff persons were established in Phoenix. In the fourth quarter of 2007 CNA created an additional DBA team in Dallas. In the first quarter of 2008 overall management for DBA claims transferred from Diversified Claims Operations to the Workers' Compensation Claim Line of Business. In the third quarter of 2009 management of the DBA business was transferred Kathy Pagnano, Vice President of the Western Region, Commercial Claims. In the third quarter of 2011 an additional DBA team was established in Lisle, IL.



As far as the reporting structure is concerned, detailed charts are provided in Exhibit 3b - IL DBA 12c. The reporting from CEO Thomas Motamed down to the individuals responsible for the claim handling is as follows:

- P&C EVP Claim George Fay reports to CEO Thomas Motamed
- Bob Simon VP Worldwide Claims, Thomas Kessler SVP Claims Field Operations, and Michael Stapleton SVP Claim Administration report to George Fay
- Todd Lewis AVP Technical & Strategic Claims reports to VP Bob Simon
- Kathy Pagnano VP Claims Field Operations reports to SVP Thomas Kessler
- Steve Aleck AVP Claims reports to Kathy Pagnano
- Claim Managers Nan Husnik - Chicago, Susan Stachewitz - Lisle, Matthew Vigil - Dallas and Michelle Simonson – Phoenix, report to AVP Steve Aleck

Biographies of the entire DBA claims group were provided which demonstrated significant experience levels in both workers compensation claim handling as well as L&H benefit processing. Specifically the breakdown is:

- **Senior Management:** Simon, Pagnano and Aleck average 28 years industry experience
- **Line Management:** Stachewitz, Hasnik, Vigil and Simonson average 24 years industry experience
- **18 Adjusters:** Average 21 years industry experience

In addition, we were provided the overall CNA Claims Organizational Chart showing Bob Simon as VP Worldwide Claims with the following professionals reporting to him:

- Darci Beacom – VP, Claims (Manager)
- Michelle Doss – Director, Operations Analysis Consulting
- James Guidos – Director, Operations Analysis Consulting

- Todd Lewis – AVP, Claims (Manager), primary responsibility for DBA
- Elizabeth Sieks – Director, Operations Analysis Consulting
- Colette Turner – Director, Operations Analysis Consulting

As mentioned above, CNA implemented a parallel organizational re-structure at the VP management level with separate operating functions for “Staff Management” and “Strategy/ Technical Services”. Operationally the DBA unit reports to Kathy Pagnano who is responsible for Staff Management. Ms. Pagnano has \$1.5M in claim reserving and settlement authority, oversees the managers’ field audits of the Claims Quality Review (“CQR”) teams, and addresses staffing adequacy and claim management efficiency such as open/closure rates, error ratios, and claim handling responsiveness.

Relative to the Strategy/Technical Services run by Bob Simon, both Assistant Vice President Todd Lewis and Bob Simon share \$3M authority levels. Todd Lewis reports to George Fay for reserve and settlement authority. Bob Simon assigned DBA to Todd Lewis in March of 2009. Todd approves reserves, settlements, strategy, coverage and litigation.

This dual reporting structure is not uncommon amongst many of the large commercial carriers. Although there is some occasional overlap of specific assignments, the access and required reporting to professionals with exceptional technical skills that exist within the unit run by Bob Simon is a not only a workable and necessary organizational structure, the substantial improvement in the quality of the claim handling since this change was implemented in 2009 is testimony to the effectiveness of this structure.

## 2. Workload

The breakdown of staff by office is:

Number of Staff	Office
4	Chicago
8	Lisle, Ill
3	Phoenix
9	Dallas

A spreadsheet was provided noting pending caseloads in 2009, 2010 and 2011 by individual desk code and office (Exhibit 1 IL DBA A21a). The averages by year are demonstrated below:

Office	2009 Average Count	2010 Average Count	2011 Average Count
Chicago	181	153	137
Dallas	174	162	147
Phoenix	181	150	150

The new Lisle, IL office numbers are still incorporated into the Chicago numbers. The current 2011 claim counts is in line with industry averages for loss time cases.

## 3. Systems

Prior to 2006 the Senator System housed and processed DBA claims. Due to Senator's limited capabilities, DBA claims were then handled in ACT, the primary claim financial system utilized by CNA's domestic claims group (Specialty and Commercial Insurance). In 2007 all claims were converted to Claim Center which is CNA's primary document, data and diary management system (financial transactions continue to be processed in ACT). In the second quarter of 2009 CNA began scanning documents and became "paperless."

Unfortunately legacy information housed in the Senator System was not converted into ACT. As a result, accurate inception to date reports for DBA going back to 1998 cannot be produced. With regard to the ACT system, the system is

cumbersome and not user friendly. Navigation through the system requires an extensive knowledge of codes, function keys, time and patience. CNA has advised the ACT system will be changed in the near future, which can only improve the ease with which a user will be able to access and manipulate data.

#### **4. War Hazard Recovery Operations**

War Hazard Procedures have also been established as part of the DOL's staff counsel operations. In 1995 the staff counsel department moved to Reading, PA. In 2009 staff counsel assumed responsibility for the recovery operation. Ralph Touch manages the Recovery Group. The Recovery Group reports to Senior Vice President Mike Stapleton. The Recovery Group has 30 people (26 in Reading, PA, 3 in Atlanta, and 1 in Syracuse). DBA adjusters make the decisions relative to whether a claim qualifies for WH reimbursement. WH legal verifies if the case has war hazard potential. The Recovery Group processes only recoveries. They verify that all the documentation is complete and the mathematic calculation for recovery is accurate in Claim Center prior to submission to the Department of Labor. Authority levels exist for expense payments. The Recovery Group's performance is measured by the number of submissions and recoveries received, which is collected in a monthly scorecard.

Since the responsibilities for the Recovery Group were transferred to staff counsel operations in 2009 several changes occurred:

- Development of paperless files improved the collection of data
- Efficiencies increased when the collection was farmed out to others
- Reconciliation of amounts due improved the collection process both in dollars received as well as shortened the collection time
- A file referral process was established

A more detailed description of the Recovery Group's operations is provided in Exhibit 1 IL DBA A27. An accurate comparison of the recovery group's performance could not be made due to the changes in the DOL policy removing the eligibility of foreign nationals for WH reimbursement.

## **5. Staff Counsel**

DBA Counsel: Marci Singer-Ruiz and Greg Sujack are the staff attorneys assigned to handle DBA cases for policyholders. Outside panel counsel is used when appropriate. Panel counsel includes Laughlin, Levy & Moresi, Brown & Simms (Michael Quinn), and Dave Smith. Primary outside counsel historically was Laughlin, Levy & Moresi in San Francisco but they are no longer receiving new assignments as all cases are being brought in house for expense reasons. Historically the outside firms were audited annually either onsite or over the phone.

WH Counsel: Jim Andrzejewski is the only staff attorney handling WH recovery. Mr. Andrzejewski reports to Ray Swan. Mr. Swan is the managing trial attorney handling all recovery for CNA countrywide. Mr. Swan reports to Assistant Vice President Brian Granstrand who reports to Vice President Mark Stephens. Mr. Andrzejewski has a very manageable caseload of 120 losses.

## **6. Internal Audit**

A review was made of the July 10, 2009, memo referenced in IL DBA A-20a prepared by Karen Knight from the Audit, Compliance & Investigation (ACI) Department to Todd Lewis. Specifically the unsatisfactory audit opinion noted:

- Deficiencies in management oversight and in file handling controls
- War hazard claim cost recovery processes were inadequate
- Supervisory claim process was ineffective
- Reserving practices were ineffective as evidenced by poor documentation and inappropriate incremental reserve changes
- File controls required improvement as demonstrated by duplicate payments, unsupported post-closing payments, and undocumented use of non-preferred vendors

The work papers relative to the 2009 ACI audit (a 15 page document) were requested and reviewed which did not provide guidance relative to file selection criteria but did provide a more detailed explanation of the deficiencies noted in the summary report (Exhibit 3b IL DBA A-20b). The information was reported in a spreadsheet with headings for Improvement Areas, Agreed upon Action Plans, and Implementation Status. The comments were informative and ran the

spectrum from minor coding issues, to inaccurate benefit calculations to incomplete reserve rationale (to name a few). To assist with the understanding of the auditor's comments references were also made to the appropriate CNA guidelines for the specific category reviewed.

A review was made of the December 13, 2010 memo prepared by Dave Smith from the Audit, Compliance and Investigations (ACI) Department to Bob Simon. This memo was a follow up to a July 10, 2009 ACI review of DBA claims which noted a less than satisfactory audit opinion which is noted below in IL DBA A-20b. Specifically, the report noted significant opportunities for war hazard recovery were being missed due to ineffective oversight. Overall file quality concerns were also identified.

The 2010 memo noted that though improvements had been made, there remained additional concerns surrounding DOL compliance relative to the timely filing of forms and the need for additional management oversight. Apparently, claim management agreed and in 2011 instituted the 90 day supervisory requirement.

## 2. Loss Time File Selection

Based on industry experience, the review team randomly selected 188 (7.8%) loss time files stratified by Desk Code (claim handler/location) and value (Exhibit 9d).

Desk Code	# of WH	# of DBA	\$0-\$100K	\$100-500	\$500k-1M	Over \$1M	Death
DA	2	8	3	3	3	0	1
DB	3	7	3	3	2	1	1
DC	4	8	2	5	3	0	2
DD	0	2	2	0	0	0	0
DJ	5	7	4	2	2	2	2
DK	2	6	3	2	1	1	1
DS	3	9	2	4	3	1	2
DT	3	9	4	5	1	0	2
F2	1	1	1	1	0	0	0
F3	2	3	2	2	1	0	0
F4	4	8	4	3	2	1	2
F5	5	7	5	3	2	0	2
F9	4	7	3	3	2	1	2
FA	4	6	4	2	2	0	2
FB	4	7	4	3	2	0	2
FD	5	8	3	5	2	1	2
FL	3	8	3	4	2	1	1
FM	5	6	3	3	2	0	3
FS	3	9	4	3	1	1	3
<b>Totals</b>	<b>62</b>	<b>126</b>	<b>59</b>	<b>56</b>	<b>33</b>	<b>10</b>	<b>30</b>

### **3. Medical Only File Selection**

In addition, the review team selected 48 medical only files (Exhibit 9e). The medical only claims are primarily handled by one dedicated medical only claims specialist. The breakdown by year is as follows:

<b>Year</b>	<b>Number of files</b>
2008	8
2009	10
2010	2
2011	28

The breakdown by claim handler/desk code is shown below:

<b>Desk Code</b>	<b>Number of files selected</b>
DD	25
DS	2
DK	2
DB	1
DC	5
DT	3
F9	2
FA	3
FB	1
FD	4
<b>Totals</b>	<b>48</b>



#### **4. Sallyport File/Loss Selection**

As this review was prompted by an inquiry into CNA's alleged mishandling of a specific Sallyport loss which occurred on October 29, 2006 involving 17 individuals. AIM requested a review of this specific loss. One of the seventeen claims involved a case where benefit eligibility was challenged. This file was identified as file #HW025061. Of the remaining sixteen, five additional claims were requested (two where benefit eligibility was accepted, and three that were denied). The files are listed below:

HW025059

HW025060

HW025062

HW025063

HW025070

#### **5. SIGAR File Selection**

We reviewed fifteen (15) files which were identified in the SIGAR report.

HW001271 HW025018 HW027512

HW001318 HW025433 HW027967

HW001496 HW025806 HW029342

HW001620 HW026508 HW031264

HW001926 HW026666 HW030114

#### **6. Audit Criteria**

The categories described below are common "Best Practice" areas that the AIM audit team addresses in the claim and underwriting file review. The audit team has provided CNA with the following explanation in an effort to be fully transparent relative to what the reviewer was looking for to determine if the file met requirements in that category. The requirements were established by the audit team based on a review of CNA's own

policies and procedures (See Exhibit 3 IL DBA 1a and b) as well as the audit team's professional experience.

**a) Timeliness**

This category addresses the prompt review and response by the claim handler of the file once it has been received by CNA for handling. This includes the examiner's responses to correspondence and the need for investigation, reserve adjustments, and prompt payments of benefits and filing of LS forms as specified by the DOL. Penalties assessed due to delayed payment of benefits would also be captured in this category.

Specific time frames are shown below:

<b>Action<sup>32</sup></b>	<b>Timeframe</b>
3 Entity Contacts	24 hours from date of notice to CNA
LS-202 filing	10 days from date of knowledge to employer
LS-206 filing	28 days from date of employer knowledge of loss
LS-208 filing	16 days from date of last payment
LS-216 filing	Request from OWCP for additional information is due from CNA within 30 days

A deviation from the above standard was considered relative to the 24 hour contact. Specifically the audit team did allow for one contact within the 24 hour period to be satisfactory because of the time, distance and unavailability of any one or more of the three persons to be contacted. For example, battlefield doctors could not be reached despite adjuster persistence. It did not seem appropriate to impose the time frame provided in the guidelines when attempts were made and only one party was reachable.

**1) Coverage**

This category addresses the necessity of not only identifying coverage verification for the named contractor but any subcontractors. This area also addresses any other available coverage that would respond to the claim (War Hazard, Second Injury

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<sup>32</sup> [www.dpl.gov.owcp/dlhwc/](http://www.dpl.gov.owcp/dlhwc/)

Fund). The underwriting file should accompany the claim file and any nuances with respect to coverage terms are addressed here.

## **2) Claim Denial**

This category addresses whether or not there was documentation to support a denial of the claim by CNA, either wholly or in part, at the time the denial was made. In addition, confirmation of the timeliness of the LS-207 is also reviewed as well as the supporting explanation provided on the form.

## **3) Investigation**

This category addresses the timely investigation by both CNA and any vendor's assigned to the loss to confirm that the injured worker's benefit eligibility as well as dependant eligibility where appropriate. The investigation should have included contact with all parties involved and should have been completed as soon as possible. Once the initial investigation was completed, additional investigation addressing the injured worker's medical status, return to work and permanent disability should have been addressed.

## **4) Evaluation**

This category addresses the proper review of information and documentation so that the potential liability exposure should have been properly evaluated and appropriate reserves established. The evaluation should have identified the information and documentation relied upon to confirm disability and medical needs (physician reports, rehabilitation reports, IME, sub-rosa, etc.). The claim handler should have not only identified and reviewed the information but also provided rationale as to how this might have impacted policy exposure.

## **5) Reserving**

This category addresses whether the reserves currently established adequately reflect the injured worker's expected benefits. All aspects of the claim review process (analysis of any legal issues, contract issues, rate adjustments, etc.) should be discussed to support the reserves required to administer the benefits. In addition, reserves should be reviewed for accurate benefit calculation broken down by benefit level (TTD, TPD, PPD, PTD, and Death).

## **6) Litigation Management**

This category addresses the claim examiner's review and response to the discovery obtained by defense counsel in litigated cases. It is the claim handler's responsibility to steer litigation strategy and provide guidance to defense counsel regarding appropriate discovery needs. Also evaluated was the examiner's ability to monitor and interact with the attorney to resolve the litigation as efficiently and cost effectively as possible.

## **7) Medical Management**

This category encompasses the need for nurse case management and vendor review of billings to verify they comported to prevailing rates. A review of whether the claim handler was complying with CNA's Medical Management program is addressed, as well as if proactive efforts were demonstrated to control costs and ensure medical was related to industrial injury.

## **8) Documentation/Reporting**

This category addresses whether there was documentation in the file to support the claim and activity incurred to resolve the loss. Documentation includes all forms of correspondence (i.e., emails, status reports, medical reports, bills, letters, legal documents, etc.) and especially examiner generated documents to all involved parties.

## **9) Settlement/Negotiations**

This category addresses whether the examiner had obtained internal authority approval if required, as well as the claim handlers involvement and/or communication to impact the final disability award, reasons for compromise, etc.

## **10) Recovery**

This category analyzes the timely pursuit of any potential payment from other responsible parties. This would include, but not limited to subrogation claims, pursuit of benefit overpayments, and Department of Labor reimbursements on War Hazard claims.

### **11) Fraud**

This category is self-explanatory and involves the due diligence of the examiner in identifying claims of a suspicious nature.

### **12) Management & Supervisory Controls**

This category addresses CNA's supervision of the claims examiner's review and handling of their caseload including compliance with CNA's established guidelines (nine month review, etc.). Supervision assists the examiner by providing not only additional expertise in claim handling practices, but also another experienced opinion in developing a plan of action to resolve losses. Special attention is always considered on larger files in excess of the claim handler's authority. In these cases there should be documentation that management has reviewed the handling of the file at that point in time.

### **13) File Maintenance**

This category addresses the condition of both the file order and the system entry applicable to the claim file. Areas of concern involved files not in chronological order or with loose documents and files lacking system entries to support the activity on the claim. Specifically, it is hoped that there is no mail that has not been reviewed that may affect the action, value and decisions made on the claim. This category also included files noted by the claim examiner to be closed yet they were still open in the system.

### **14) Diary**

This category addresses the claim examiners prompt response to necessary activity and regular follow-up thereafter to bring the claim to conclusion. It is important to maintain an active diary to ensure that activities are responded to timely. In the absence of specific dates our analysis was based upon an appropriate period of time that was consistent with the needed activity on a particular file.

## **X. AIM AUDIT FINDINGS – Random Selections**

It is important to note that the handling of DBA claims present unique challenges that most claim departments handling other lines of insurance rarely encounter. The most significant challenges include the following:

- Anti-American sentiment in some countries (especially Afghanistan)
- Unable to speak with widows in some Middle East countries
- Investigators are sometimes thwarted by security checkpoints in war zones
- Legal documentation in some countries is inadequate
- Suicide bombings occur with regularity
- Unable to direct medical care
- Transportation to other countries is sometimes necessary to obtain quality medical care
- Post Traumatic Stress Claims are common
- Zone of Special Danger broadens eligibility as employee does not need to be in the course and scope of their employment to qualify for benefits

“Best Practices” require at a minimum 80% compliance in individual categories. AIM split the analysis between Medical Only versus Loss/Time claims. Attached to this report is a workbook (Exhibit 13) that includes the 253 claims reviewed (4 files from the original selection of 257 were not reviewed) and associated comments relative to those files that did not meet requirements in a certain category separated by Loss Time, Medical Only, and SIGAR. A separate discussion of Sallyport is also included below. The following audit results discussed are broken down as outlined in the file selection categories described above:

### **A. AIM Analysis of Random CNA File Selections (1-17 Criteria)**

#### **1. Open Loss Time**

The following results are based on AIM’s review of 205 files (being 15 SIGAR plus 190 Loss/Time). A recap of the actual files reviewed is noted in the following table for Loss/Time inclusive of the 15 SIGAR files. We separately show the file review results of the SIGAR files below in Section IX C4 of this report.

<b>Area of Review</b>	<b>Loss Time Average Compliance Percentage</b>
Timeliness	73%
Coverage	100%
Investigation	93%
Evaluation	88%
Reserving	89%
Litigation Management	95%
Medical Management	92%
Documentation / Reporting	87%
Settlement/Negotiations	95%
Contribution/Recovery	98%
Fraud	100%
Management & Supervisory Controls	92%
File Maintenance	91%
Diary	95%
<b>Overall Compliance Percentage</b>	<b>91%</b>

Although the attached spreadsheet provides individual claim detail supporting the evaluations in each category, the following is a brief discussion highlighting key points in each category including examples of representative files that are illustrative of the comments.

## 2. Timeliness

75% of the files reviewed met "Best Practices" industry standards. The key area of concern in this category dealt with either delayed 3 point contact and/or delayed action after receipt of information that required response or need for follow up activity. It is understood that the locale and circumstances surrounding these losses present themselves with numerous challenges which impact the receipt of information and amount of time required for the completion of various assignments. However, the concentration of criticism focused on the timeliness of activity within CNA's control.

Examples of not meeting requirements are claims numbers HW001586 and HW001209.

### 3. Coverage

Given the nature and structure of the contracts, it is not surprising that the review demonstrated compliance with "Best Practices" industry standards in 100% of the files reviewed. The Claim Center template provides a coverage field that must be populated. In no instance did the review reveal a file where coverage had not been confirmed.

### 4. Investigation

93% of the files reviewed met "Best Practices" industry standards. CNA utilizes vendors to conduct many of the investigations given the lack of onsite personnel and international field offices. It is remarkable how resourceful the vendors have been in securing information in both remote locations and highly combative and dangerous surroundings. Examples where investigations were incomplete due to circumstances under CNA and/or their vendor's control resulted in a negative review were found in claim numbers HW550235 and HW031995.

### 5. Evaluation

88% of the files reviewed met "Best Practices" industry standards in this category. Evaluations in this book of business can be difficult due to the problematic vocational issues relative to accessibility to meaningful labor market studies, variable medical reports and interpretations amongst international jurisdictions and remote claimant locations, to name a few. In addition, the change in DOL policy relative to War Hazard reimbursement of foreign nationals created additional adjustments. Although evaluations existed early in the life of the files and despite the foregoing issues, CNA's evaluative templates developed mid 2009 contained necessary information in the vast majority of cases that were well thought out and supportable based on the file information available at the time the evaluations were made. Examples of claim



files where the evaluations were either not supported or did not consider available information include claim numbers HWA00169 and HW029878.

## 6. Reserving

89% of the files reviewed met "Best Practices" industry standards in this category. Reserving losses where control over the medical treatment is limited can be both frustrating and difficult to project given the substantial dependence upon the treating physician's presumption. There is no doubt that the current claim staff has the technical ability to estimate and accurately set reserves as is evidenced by the favorable reserve adequacy percentages (see Exhibit 1 IL DBA A5). Despite the foregoing, CNA's established protocol notes that an initial reserve should be established within 48 hours of receipt of the loss, the reserve reflecting CNA's exposure should be reviewed and addressed within 30 days of receipt of the loss, and the reserves should be evaluated within 30 days as new facts and evidence develops.

The losses not meeting industry standards either did not contain documentation of the rationale supporting the established reserve, or the reserve appeared overly optimistic and was not reflective of the exposure. Examples of those files not meeting requirements are claims numbers HW550345 and HW030275.

Although the spreadsheet demonstrates which files AIM disagreed with CNA's evaluation, the net result amongst all files reviewed was less than \$100,000 and therefore not worthy of further discussion.

An additional issue that merits comment concerns the timeliness of large loss reserve adjustments. In addition to the findings presented in the SIGAR chart below, there appears to be an unreasonable, consistent delay in getting agreed large loss reserves into ACT. It is acknowledged that in the case of the SIGAR files many of the reserve adjustments at issue occurred in 2009 during the DBA reorganization. Despite the foregoing explanation, our review discovered losses where CNA acknowledged exposure, an appropriate reserve was recommended by the claim handler (which AIM agreed was appropriate) and often approved by management, yet the input into ACT was inexplicably delayed. This observation was brought to the attention of CNA management for their consideration and review. The files that

demonstrate this finding include HW029551, HW550394, HW029342, HW001271, HW026508, and HW026666.

#### 7. Litigation Management

95% of the files reviewed met "Best Practices" industry standards for litigation management. Due to the favorable benefit provisions in the DBA and the large number of foreign national claimants that are less litigious than US claimants, the number of litigated files was just under one third of the total reviewed. Of this group the majority was handled by staff counsel. There was good evidence that claim handlers had reviewed legal correspondence and discussed strategy with defense counsel. There were only four files that did not comply with CNA and/or industry standards. The files not meeting requirements are claims numbers HW550315, HW027766, HW550293, and HW033171.

#### 8. Medical Management

92% of the files reviewed met "Best Practices" industry standards for medical management. CNA established guidelines June 22, 2009 for international business including Defense Base Act claims. CNA developed a case management program to effectively service international business. The Process Statement defines a Case Manager as a professional who provides field and telephonic medical management to assess an injured Worker's healthcare needs, and facilitates maximum medical improvement (MMI)/full duty return-to-work (RTW). The primary focus areas of CNA Global case management are coordination of healthcare services and facilitating the selection of excellent providers. A further discussion of this program is provided in the document summary (Exhibit 1 IL DBA A18).

Given the foregoing, there were numerous examples demonstrating proactive medical management to ensure the injured worker secured the best medical care as quickly as possible. Unfortunately some of the medical problems exhibited in some of the files reviewed were a result of the poor quality of care in remote locations where access to competent medical care was limited or did not exist. Examples of

those losses where neither CNA nor their vendor complied with CNA's policies or industry standards are found in claim numbers HW001322 and HW550349.

#### 9. Documentation / Reporting

87% of the files reviewed met "Best Practices" industry standards in this category. Without question this category serves as the basis for many of the other categories. Although adjuster claim experience can substantially influence if not dictate a proposed course of action, evaluation, reserve, etc., documentation must exist to support and confirm the ultimate decision. For the most part the CNA claim handlers did a good job of following up to make sure that adequate support was submitted to justify the loss payment, reserve, and proposed plan of action. Examples of those files that did not contain the requisite support are claims numbers HW031490 and HW031995.

An additional factor that influenced the results in this category surrounded the file conversion from paper files to Claim Center notes, images and records. Although the AIM audit request included both paper and paperless files, in some of the files reviewed documentation of the older files was not available for review. Examples of this finding include claim numbers HW550293 and HW550020.

#### 10. Settlement/Negotiations

95% of the files reviewed "Best Practices" met industry standards in this category. Dashboard scorecards reviewed demonstrated activity for July 2011 and year-to-date 2011 advising the number of new losses reported, reopening, closings, conversions (from medical only to loss time), transfers and percentage turnover. For calendar year 2011 the DBA unit closed 72.9% when compared to the number of claims received. The CNA target is 95%.

Despite the foregoing result, it was impressive to find that negotiated settlements were for the most part near or under the stated reserves. As mentioned in the reserving section, the reserve adequacy percentages further demonstrate the success CNA has achieved over the last two years relative to the dollars paid at time of closure versus reserves carried at 18 months. A favorable observation was clear evidence of CNA's aggressive pursuit of Section 8(i) settlements as well as commutation of survivor benefit losses on death claims. The handful of cases where

a deficiency was noted was due to poor documentation to support the settlement paid. Examples of not meeting requirements are claim numbers HW550394 and HW029551.

#### 11.Recovery

98% of the files reviewed met "Best Practices" industry standards in this category. Only 3 files were deficient in this category due to inadequate or incomplete discussion of the third party resolution and recovery, if any. Clearly the claim handlers are aware of securing recovery and are looking for potential contribution resources. Examples of claims not meeting requirements are claim numbers HW029218 and HW550349.

Although there were past criticisms of delayed recognition and pursuit of War Hazard recovery, since the transition of this responsibility to the Recovery Group under Staff Counsel's supervision in 2009 as described above, procedures are in place that have resulted in significant improvement in this area.

#### 12.Fraud

Given the contract terms it is not surprising that the review team did not identify a file that was deficient in this category and therefore achieved a 100% compliance with "Best Practices" industry standards. All defense contractors are accepted policyholders and the benefit requirements are extremely liberal for the injured workers. With these parameters, there were only 3 files in the review sample that even had a potential fraud component; all of which were investigated and addressed per the terms of CNA's procedures and industry standards.

#### 13.Management & Supervisory Controls

92% of the files reviewed met "Best Practices" industry standards in this category. CNA has established certain guidelines for supervisory review of losses including a claim manager required reserve review at 9 months from the date of notice, write off of over payments, approval of panel counsel referral, and the establishment of life reserves. In addition, due to the high benefit structure under the DBA, files often exceed claim handler authority requiring additional review of not only the evaluation and reserves, but the preparation of Large Loss Notices, participation in round table discussions, litigation management and plans of action. It was encouraging to view,

and most notably post 2009, the significant involvement of front line management amongst the files reviewed. Examples of files where additional attention was required by management and/or the file demonstrated non-compliance to established guidelines include claim numbers HW026666 and HW001318.

#### 14. File Maintenance

Our review revealed that 91% of the files reviewed met "Best Practices" industry standards in this category. Given the number of individuals and organizations that have touched these files, the quality of file maintenance was quite good. Duplicate payments are addressed in this category as well as the notations and file images belonging to other losses. Although there was noted evidence of these findings in a handful of the files reviewed, the frequency was not significant. Examples of those files not meeting requirements are claims numbers HW550013, HW550293, and HW550020.

#### 15. Diary

Our review revealed that 95% of the files reviewed met "Best Practices" industry standards in this category. Diaries are being kept current and the files are seen regularly (within 30-60 days). Further, when requests are made for payment or information, the response time for processing the request is good. On a few noted instances, there were files wherein an extended time had passed with no current information or monitoring taking place. The examples of files not meeting requirements are claim numbers HWA00359 and HW026508.

#### 16. Claim Denial

In addition to the overall results, we reviewed two supplemental criteria to better measure specific aspects of the claims handling process: 1) AIM attempted to validate if the claim was denied and if AIM agreed with the denial; 2) was there a penalty assessed against and paid on the file, and the amount paid.

While the data reflects less than optimal results, the percentages are based on a small population of files. Of the 205 Loss Time cases reviewed only 37 involved denials of which AIM disagreed with CNA's decision on 9 claims. This result was driven by the 5 Sallyport denials and 1 SIGAR file discussed below.

<b>Area of Review</b>	<b>Loss Time Average Compliance Percentage</b>
Agree with denial of claim- yes.	76%
Disagree with denial of claim- no.	24%
Penalty Assessed against file.	1%

#### 17. Medical Only

48 medical only files were reviewed with the following results summarized in the chart below:

<b>Area of Review</b>	<b>Medical Only Compliance Percentage</b>
Timeliness	85%
Coverage	96%
Investigation	94%
Evaluation	90%
Medical Management	96%
Documentation / Reporting	96%
Contribution/Recovery	97%
Fraud	100%
Management & Supervisory Controls	92%
File Maintenance	100%
Diary	98%
<b>Overall Compliance Percentage</b>	<b>94%</b>

The main concerns in the only category with a result below 90% surrounded the failure to make prompt contact and timely follow up for medical support.

The chart below summarizes the claim denial results. There was only one medical only file where AIM disagreed with CNA's denial HWA00430. In this instance, the file documents failed to support the reasons for the denial.

Area of Review	Medical Only Compliance Percentage
Agree with denial of claim- yes.	98%
Disagree with denial of claim- no.	2%
Penalty Assessed against file.	0%

## **B. Sallyport**

### Underwriting Information

The four policies issued by CNA to Sallyport were reviewed (Exhibit 1 IL DBA C1). The annual policies inception 10/8/4 with the last expiring 10/8/2004. The annual premium is listed below:

- 2004-5: \$33,000
  - 2005-6: \$66,400
  - 2006-7: \$81,296
  - 2007-8: \$94,800
- Total: \$275,496

An inception to date loss run as of June 13, 2011 was provided showing 27 claims incurred to date with 12 claims closed and 15 claims open. The total incurred is \$2,306,958.14 (\$1,439,632 Reserve \$867,326.14 Paid). The total War Hazard recovery to date is \$783,920.

### Claim Information

Since all information relative to all remaining claimants existed in one file, claim # HW025059 was reviewed. The deceased worker on this loss was identified as Sabry Moyad. This is a War Hazard Claim. The claimant was one of 17 interpreters who were ordered off a bus and executed. Initial contact was timely made with the insured. 5 of the 17 claims are closed. The open companion files as of July 30, 2011 are:

HW025057 Zaid Ghassan Al-Saad  
HW025060 Mohammed AbdulAmer  
HW025061 Adrian Jaber  
HW025062 Ahmed Jaber  
HW025065 Raghdan Fadhil Mohammad  
HW025066 Sajjad Abdulrazaq  
HW025067 Ahmed Abdulqa Mahdi  
HW025069 Saddam Hassan Ushayal  
HW025070 Rafid Awad Hassan  
HW025071 Abdul Khudur Yakoob Khudair  
HW025072 Abdul Jabbar Qassim

Although this file references many of the companion files shown above, this individual file noted that CNA assigned MJM, the field investigator, on a timely basis. MJM's 2/1/07 first report was received on 2/5/07 (Exhibit 10). The file notes state the deceased's family would not allow investigators to meet with potential beneficiaries. Actually this didn't appear to be a significant issue since the deceased was single with no legal beneficiaries. He was survived by his mother, Fadhila Salman Shamkhi, who was not asserting dependency at that time. In addition, CNA was advised by the family that a bank account could not be established in the mother's name but only in a male's name.

A review of the investigators report notes that all pertinent information was obtained. It is unknown why funeral benefits were initially denied, though subsequently paid on an adequately timely basis. The Average Weekly Wage (AWW) was determined to be \$103.80 and \$463.44 was issued to Moyad's for funeral and burial expenses.



\$5,000 Special Fund payment was due 1 year from date of death. There was no evidence in the report regarding dependency.

There are long gaps in file (1/21/07-4/26/07, 5/1/07-7/20/07, and 7/20/07-10/31/07). There was a management review note which appeared to belong to a different file as it references "monitor medical treatment." The file was relatively silent, but for attempts at reimbursement from the DOL under the War Hazard clause for the \$5,000 Section 44 (c) death benefit paid to the Special Fund.

A new manager reviewed the file and reassigned the loss on 10/19/10. This included the other eight claimants that also filed demands with the assistance of counsel in December 2009 requesting parental dependent survivorship benefits.

Representing counsel secured affidavits from the deceased claimants' fathers stating dependency (without other supporting documents) as well as an \$80-90,000/parent demand. CNA rejected the demand.

The DOL requested the parties mediate the dispute, if possible. At mediation, the plaintiff's demand was reduced to \$47,000/parent. Parent's ages range from 59-72. CNA finally filed a Motion for Summary Judgment (MSJ) to dismiss the cases for untimely claim filing as the subsequent claims were filed at least several years past the DBA timeliness filing. CNA lost the MSJ motion on the basis of the Administrative Law Judge's deeming that the difficult circumstance of the war in Iraq justified "tolling" of the un-timely filing of DBA statute and that CNA had not objected to the legitimacy of their claim that were supported by only the affidavits already mentioned.

After the DOL 5/12/11 decision was received, the demand increased to \$500,000 for all claimants. CNA evaluated in the normal course of evaluating a DBA case based on the ages and life expectancy of the parents. The individual analyses of each parents claim are provided in the chart that follows on the next page:

Claim #	Claimant	Father	LE	Value	Mother	LE	Value
HW025059	Sabry	None	--	--	Yes	10 yr	\$11,394
HW025060	AbdulAmer	Yes	17	\$19,369.80	Yes	22 yr	\$25,066.80
HW025061	Jaber	None	--	--	Yes	27 yr	\$30,763.58
HW025062	Jaber	Yes	17	\$19,369.80	No	--	--
HW025065	Mohammad	None	--		Yes	24 yr	\$27,345.60
HW025066	Abdulrazaq	Yes	17	\$20,287.80	Yes	29 yr	\$34,608.00
HW025069	Ushayal	Yes	17	\$20,287.80	Yes	29 yr	\$34,608.00
HW025070	Hassan	Yes	16	\$18,230.40	Yes	18 yr	\$20,509.20
HW025071	Khudair	Yes	15	\$17,091.00	Yes	14 yr	\$15,951.60
			<b>Total</b>	<b>\$114,636.60</b>			<b>\$200,246.78</b>

The full value of the fathers' exposures for their claims was \$106,882 and on a commuted basis a value of approximately \$53,441; the mothers' were \$200,246.78 with a commuted value of approximately \$100,122. The combined total is \$153,563. Past benefits owed that are in arrears totaled \$4,800 for each of the 14 parents (7 sets). The total CNA value of all claims is therefore approximately \$220,763. Reserves were adjusted on each case by 5/17/11. Since payment is due 10 days from the date of the Order, CNA calculated the arrears benefits including COLA adjustments (section 10f) which totaled \$6,576.60 for each parent. CNA commenced paying benefits in accordance with DOL and DBA requirements.

CNA's handling of this case was for the most part good and their positions relative to eligibility and compensability were reasonable and in accordance with DOL and industry practice based on AIM's experience. The areas where AIM believes the file did not meet standards were for time lapses in diary review dates and evaluations that could be more clearly written.

The significant disputed issue in this case stemmed from the work of CNA's subcontracted on-site investigatory firm, MJM. CNA maintains, and AIM concurs, that the DOL needs to set forth better guidelines regarding the evidence and facts needed to determine parent beneficiary eligibility.

In AIM's discussions of this case with CNA management it is understandable that without more definitive DOL guidance as described above, if given the same fact pattern today, CNA's claim handling would likely not be different. Again, AIM agrees that the DOL needs to provide guidance relative to what constitutes adequate confirmation of parental benefit eligibility. For example, if an Iraqi family with the mother and father living in one dwelling with their adult children does this constitute parental dependency if one of their offspring is killed in conducting his or her work as a contracted U.S. employee and there are no financial records substantiating support?

In addition to the foregoing, file # HW025063 Ali Kadhim was provided. This claim was accepted as beneficiary documentation was provided demonstrating that the deceased was survived by a wife and a 5 year old child. The Department of Labor

approved the commutation order and a lump sum of \$164,400 was paid. Post payment it was determined the widow never received funeral benefits. The file was reopened and the funeral benefits were paid along with a 20% penalty (\$542.64). The file was then closed. WH reimbursement was approved 1/19/11. But for the failure to reissue the original payment, which AIM noted in file maintenance, AIM agreed with the handling of this case.

### **C. Office of the Special Inspector General for Afghanistan Reconstruction (SIGAR)**

#### **Original SIGAR Report**

A copy of the June 28, 2011 SIGAR report was provided for our review (Exhibit 12a). The report explained the audit parameters, a definition of the Defense Base Act as well as a historical review of the growth in claim volume from 309 in 2000 to 14,863 in 2009. In 2005, the United States Army Corps of Engineers (USACE) began awarding a series of contracts to CNA as the single DBA insurance provider. The United States Central Command Joint Theater Support Contracting Command (C-JTSCC) contracts were added to the USACE contract in 2008. As of March 2011 CNA has collected \$225M in premium. The premiums were based on labor costs for four labor categories: services, security, aviation and construction.

The report identified weaknesses in the USACE Defense Base Act Insurance Program. The SIGAR audit team objectives were to:

- determine the extent to which DBA premium rates were set at appropriate levels
- assess USACE and C-JTSCC's internal controls for ensuring that prime contractors and subcontractors obtain insurance in compliance with the DBA, and
- evaluate the process for billing and reimbursing contractors for their DBA costs

Specifically, the auditors alleged CNA's documentation was incomplete making it difficult for the auditors to accurately quantify accurate loss ratios; the loss ratios CNA used to compute annual premium quotes was inaccurate resulting in \$9.9M in overcharges; USACE and the C-JTSCC had poor internal controls to monitor

whether contractors were obtaining DBA insurance, and if so, whether the amount was sufficient, or whether the policies were renewed; CNA's process for billing and reimbursing contractors for DBA costs commingles funds in violation of US funding restrictions and limits USACE and C-JTSCC oversight over actual costs.

CNA's Comments on Draft SIGAR Audit Report No. SIGAR-033A (Exhibit 12b)

On July 14, 2011 CNA prepared a response to the criticisms made in the SIGAR report. CNA's response provided documentation to support the following:

- The negotiated premium rates were based on a 57.7% loss ratio calculation that was not only supported by credentialed actuaries who applied standard industry actuarial methodology, but was agreed to by USACE
- SIGAR's calculation of IBNR did not consider adverse loss development on known losses but only "Pure" IBNR. Further, the SIGAR report considered losses incurred in only the subsequent contract year rather than until the claims reached final settlement.
- SIGAR's assertion that CNA has overestimated reserves when compared against the final amount paid for closed claims is not credible since SIGAR did not review any closed claims. SIGAR did not provide support for their assertion and CNA's review demonstrated that the cases settled for close to the reserve amounts. Also, there was a change in Department of Labor policy that made insurers responsible for payment of foreign national war hazard claims.
- SIGAR's finding that CNA's individual case file data are inconsistent with losses reported to USACE is unsubstantiated.
- CNA does not include War Hazard claims in their calculation of the USACE loss ratio.

Large Loss Adjustments

The SIGAR auditors were critical of CNA's reserving process and intimated there was a conscious effort by CNA to delay reserve adjustments. To that end, AIM reviewed the files SIGAR selected and captured the Large Loss activity and corresponding reserve adjustments.

The results are shown below:

Claim Number	Date of Loss	Amount of Initial Reserve	LLR Approval Date	Amount of Reserve Adjustment	ACT Input Date
HW031264	3/10/10	\$ 68,293			03/10/10
			03/24/10	\$2,071,827	03/30/10
			11/18/10	\$ 305,674	12/09/10
HW026666	7/10/07	\$ 144,714			11/21/07
			undated	\$ 559,329	09/09/08
			12/09/09	\$1,218,833	03/01/10
			03/23/11	\$ 419,602	03/23/11
HW026508	2/25/07	\$ 13,000			10/17/07
			03/03/10	\$1,268,888	03/03/10
HW001318	4/30/06	\$ 60,928			06/04/06
			07/10/08	\$ 637,663	07/29/08
			12/02/09	\$ 513,023	01/28/10
HW027512	1/28/08	\$ 101,339			04/17/08
			02/24/09	\$3,794,056	03/04/09
			08/10/10	\$1,157,064	08/10/10
HW001271	4/05/06	\$ 27,178	04/24/06		04/24/06
			12/03/09	\$1,234,772	01/28/10

HW001496	10/19/06	\$486,412		10/31/06
			07/27/07	\$ 299,999 08/03/07
			12/04/09	\$1,061,017 02/10/10
			02/25/11	\$ 172,487 02/25/11

HW025806	2/25/2007	\$ 46,135		06/05/07
				\$ 33,096 08/07/07
			09/25/08	\$ 13,368 09/26/08
			10/28/08	\$ 155,797 10/28/08
				\$ 370 08/28/09
				\$ 10,000 09/04/09
			09/17/09	\$ 100,173 09/17/09
			12/08/09	\$1,441,416 02/10/10

HW025018	10/19/2006	\$ 15,000	11/27/06	11/28/06
			01/04/07	\$ 107,902 01/04/07
			05/09/07	\$ 115,902 05/09/07
				\$ 6,942 03/08/08
				\$ 3,001 09/23/09
			09/24/09	\$ 85,732 09/24/09
			07/28/10	\$1,597,301 07/28/10

HW030114	8/15/2009	\$ 20,000		08/20/09
			08/18/09	\$ 190,295 10/27/09
			3/24/10	\$1,067,194 03/24/10

HW001620	10/30/2006	\$13,000	11/10/06	
HW001620				11/06/06

Cont'd.

12/07/06	\$ 47,951	12/07/06
11/30/07	\$ 28,975	12/06/07
01/24/08	\$ 45,488	01/25/08
<i>No notes between 07/18/08 and</i>		
09/06/08	\$ 3,000	07/24/08
02/02/09	\$ 53,785	02/02/09
11/24/09	\$ 67,000	12/14/09
11/24/09	\$1,597,150	02/10/10
07/21/11	\$ 476,888	07/21/11

HW029342	4/20/2009	\$2		04/23/09
			04/27/09	\$ 92,431
			04/18/09	\$ 49,552
			12/04/09	\$1,222,022
				01/28/10

HW025433	3/8/2007	\$236,476		03/14/07
			08/17/07	\$ 30,000
			10/13/07?	\$ 93,512
			<i>Only see notes entry regarding LLR pending</i>	
			01/30/09	\$1,767,054
				\$1,367,599
				12/04/07
				02/03/10