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REPORT TO THE GOVERNOR OF MARYLAND RE:
CERTAIN ACTIVITIES OF INSURANCE COMMISSIONER
EDWARD J. HIRSH, JR. AND THE MARYLAND
INSURANCE GUARANTY ASSOCIATION, THE MARYLAND
INDEMNITY INSOLVENCY, AND THE AMERICAN
CENTENNIAL LIFE INSURANCE COMPANY INSOLVENCY

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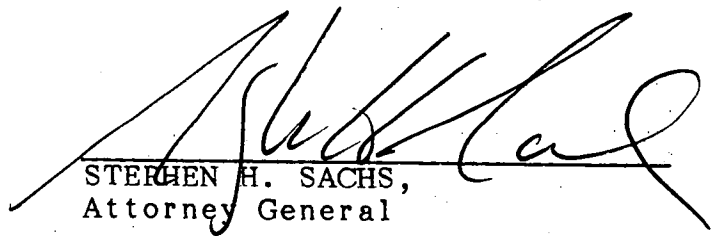
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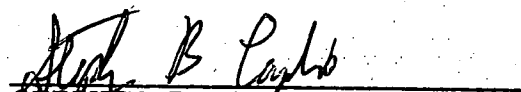
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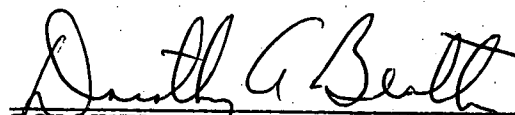
REPORT TO THE GOVERNOR OF MARYLAND
RE: CERTAIN ACTIVITIES OF INSURANCE COMMISSIONER
EDWARD J. BIRrane, JR. AND THE MARYLAND
INSURANCE GUARANTY ASSOCIATION, THE
MARYLAND INDEMNITY INSOLVENCY, AND THE
AMERICAN CENTENNIAL LIFE INSURANCE COMPANY INSOLVENCY

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June 3, 1982

SECTION I
INTRODUCTION
AND
EVALUATION¹

In August of 1981, a series of articles appeared in The Evening Sun alleging that State Insurance Commissioner Edward J. Birrane, Jr. had used his position as Receiver for certain defunct insurance companies, particularly Maryland Indemnity Company (hereafter "Maryland Indemnity"), American Centennial Life Insurance Company (hereafter "ACLIC"), and Southern Life Insurance Company (hereafter "Southern"), to award lucrative jobs of various kinds to friends and associates. The allegations also alluded to similar conduct in regard to the Maryland Insurance Guaranty Association (hereafter "MIGA") (App. I-1).²

After Governor Hughes requested advice from the Attorney General's Office regarding the matters raised about the insolvent

¹ This section of the report which contains evaluative comment may have a special status under the Maryland Public Information Act that Section II through IV may not have. Should any portion of the report be made public after July 1, 1982, consideration must be given to House Bill 1481, Chapter 431, Laws of Maryland, 1982.

² Documents appended to this report will be referred to as "App." followed by the section number, and sequence numbers, as they appear in the Appendix. A separate appendix, which contains the reports from our claims experts, is also provided. All other documents described in the report without designation are in our files and are available for review. One of those documents, a deposition of Mr. Preston Tull, is referenced as "Dep.".

insurance companies and MIGA, the Attorney General wrote to the Governor on September 14, 1981, suggesting that this office undertake an inquiry and outlining its scope. (App. I-2). Our inquiry has therefore focused upon the administration and operations of MIGA, the Maryland Indemnity insolvency³, the ACLIC insolvency, and the Southern insolvency.⁴ We have also reviewed the operations of the Life and Health Insurance Guaranty Association (hereafter "LHIGA").

This report contains the results of that inquiry. The focus of the report and of our inquiry itself has been on allegations of improper behavior. We took as our task examining and assessing claimed impropriety. We did not undertake to conduct a general survey of the operations of the Insurance Division or the entities discussed in this report. For that reason, we have not inquired into nor commented upon areas of satisfactory performance that might well have been apparent had our focus been different. We have, however, been extremely careful to comment on areas of satisfactory performance within the ambit of our inquiry.

³ Inadvertently referred to as "American Indemnity" in the September 14 letter.

⁴ As a result of document reviews and an interview with former Assistant Attorney General Alan P. Lipson, now a judge on the Maryland District Court, we quickly determined that no issues existed as to Southern resembling those which arose in the cases of MIGA, Maryland Indemnity and ACLIC. Therefore, we will not discuss Southern further in this report.

A crucial aspect of our findings is that they are incomplete. Although Commissioner Birrane was always cooperative and, we were told, urged others to cooperate with our inquiry, we were nevertheless seriously hobbled by the refusal of a number of witnesses to be interviewed. Several of the key witnesses did not even submit written statements, and the written statements supplied by those who refused to be interviewed, while supplying some information, were not subject to follow-up questioning and are no substitute for the in depth interviews we had requested both before and after receiving the written statements.

The significance of those interview refusals cannot be overstated. As will appear below, a number of these witnesses were key actors in episodes and transactions the propriety of which we question. Since we did not possess subpoena power or any other form of compulsory process, we were unable to learn the full truth about many crucial episodes. Our inquiry was thorough given the tools available to us. We emphasize, however, that it was not and could not have been an investigation into every possible avenue of suspicion, particularly in the absence of compulsory process for witnesses or documents.

Summary of Findings

Our findings in a nutshell are: that Commissioner Birrane failed to fulfill his duties to manage and regulate the affairs of MIGA and the Maryland Indemnity and ACLIC insolvencies; that both of the deputy receivers appointed by Commissioner Birrane failed to fulfill their duties to manage the insolvencies; and that a small core group of MIGA directors, each of whom had been appointed by Commissioner Birrane, failed to fulfill their duties to manage that guaranty association.

MIGA is a nonprofit association created by statute for the purpose of administering claims against certain insolvent insurers in Maryland. Maryland insurance companies fund MIGA by pro rata assessment. Insurance Commissioner Birrane has substantial statutory responsibilities for overseeing and regulating MIGA's operations. He appoints its board, may examine its affairs and must approve its plan of operation and its use of outside "servicing facilities" to handle claims. His broad responsibilities to examine and to regulate MIGA put at his disposal complete financial data on its operations and expenses and uniquely situate him to guide, and, in many ways, control, MIGA's activities and expenditures. He is the only public official with such authority.

Commissioner Birrane is also the statutory receiver for insolvent Maryland insurance companies, such as Maryland

Indemnity, a property, casualty and worker's compensation carrier, and ACLIC, an Atlanta based, Maryland chartered life and health insurer. His statutory duties as receiver include responsibility "for the proper administration of all assets coming into his possession or control".

We have found that MIGA, Maryland Indemnity, and ACLIC have made repeated payments of very substantial sums of money -- salaries, fees, commissions, etc. -- to a small, self-renewing clique of favored recipients who appear throughout the activities of the three entities. MIGA and the two insolvencies have been run without meaningful control over expenses, including travel and entertainment. Not infrequently, lucrative positions and service contracts have been awarded to the same persons or firms without any special reason justifying that selection and without any serious management canvass for other candidates or for less costly alternatives. And we are especially troubled by substantial evidence of management's blindness toward, or tolerance of, the propensity of some of its appointed employees or contractors to engage in "make work" schemes -- i.e., the performance of unnecessary tasks for the primary purpose of generating income -- often on a large scale.

Maryland Insurance Guaranty Association

Commissioner Birrane's new appointees to the MIGA board took charge in early 1979. Ralph S. Moore, a Birrane friend since the

late '60s, became its chairman. Administrative costs during the stewardship of the Birrane appointees have skyrocketed. Directors' travel and entertainment expenses for the two and one half year period January 1, 1979 to June 30, 1981 rose by 57.2% over the seven prior years of the Association's life.

Additional increased expenses resulted from Chairman Moore's insistence on the utilization of Free State Adjusters, Inc. as the primary "servicing facility" to handle claims. Free State was paid almost a quarter of a million dollars by MIGA from January 1, 1979 through June 30, 1981, the date through which financial information was generally available to us. Our claims expert reviewed Free State's work and found much of it was "unwarranted and reworked, resulting in overbilling". MIGA's former claims manager, Charles Mullaney, criticized Free State's billings as "outrageous" and "exorbitant". He found that Free State charged MIGA almost three times as much as did other available companies. Mullaney's protests about Free State ended with his abrupt and, he says, unwilling departure from MIGA, and his quick receipt of \$6,000 in "severance pay." Mr. Henry Prodoehl, Free State's president, refused our requests for interviews, as did Ramsey Gray, the former MIGA director who made arrangements for Mullaney's departure.

A MIGA board dominated by Birrane appointees retained Douglas Sharretts, a Baltimore lawyer, as MIGA's house counsel. Mr. Sharretts and Commissioner Birrane had shared law office

space for sixteen years. The new MIGA board also began to refer legal claims work to the Baltimore law firm of Simmons and Fields and to Baltimore lawyer Stanford Franklin, on a nearly exclusive basis. Robert Simmons and Russell Fields were friends of Chairman Moore, and Franklin was a long-time acquaintance of Commissioner Birrane and friend of Ralph Moore.

When MIGA's administrative assistant needed a secretary, MIGA directors short-circuited any search and hired Mr. Franklin's wife, Sylvia Franklin. Within weeks, the administrative assistant herself was discharged, and Sylvia Franklin became the \$20,000 per year administrative assistant. When MIGA moved its operations from downtown Baltimore to two separate locations in Towson, the rental agent for one of those locations, a previously residential apartment at Towson Towers, was Maryland Development and Investment Corporation (MDIC), of which Stanford Franklin is a Vice President and Director. MDIC provides a rent free law office to Mr. Franklin. MDIC was selected as the rental agent after Mr. Franklin steered Birrane-appointed director Hightower to MDIC. Mr. Franklin has refused our requests for an interview, as has former director Hightower, and MDIC's principal has refused to disclose its commission on the MIGA rental.

Maryland Indemnity Insolvency

Commissioner Birrane appointed Preston Tull, a friend of

Ralph Moore's who had been employed as claims supervisor at Maryland Automobile Insurance Fund (MAIF), to be his deputy receiver for Maryland Indemnity, a defunct property and casualty insurer. Mr. Tull now earns \$41,000 a year.

Mr. Tull has also been paid an additional \$58,000 for his alleged review and re-review of a group of Maryland Indemnity's worker's compensation files. Based on our expert's analysis of Mr. Tull's "review" and the lack of any coherent description of what the "review" consisted of or why it was done, we have concluded that his "review", if it occurred at all, was purposeless, severely inadequate and grossly overpriced. Commissioner Birrane, however, endorsed payment to Mr. Tull for the review, and no one else in authority genuinely questioned it. On the contrary, we recount below in great detail (pages 94-115) the extraordinary efforts of Commissioner Birrane to arrange for Mr. Tull's payment, including successfully drafting and lobbying for legislation the immediate purpose of which was to permit Mr. Tull to be paid, not by Maryland Indemnity of which Commissioner Birrane is Receiver, but by the ostensibly independent MIGA. According to Senator Harry McGuirk, the legislation's sponsor, Commissioner Birrane did not disclose this immediate purpose to him. Birrane-appointed MIGA Board members relied on Commissioner Birrane's letter approving Tull's work, and made the payment.

Commissioner Birrane ordered all of the Maryland Indemnity

worker's compensation files - closed as well as open files - sent to MIGA, which then authorized Free State to review each one, including the files Mr. Tull had just been paid for having repeatedly reviewed. That job, when only half completed, had already resulted in Free State's receipt of over \$40,000.00 from MIGA, an amount likely to double before the end of the assignment.

When Maryland Indemnity decided to sell its Baltimore City office building, Mr. Tull gave the listing agreement to MDIC, the Towson firm with Stanford Franklin connections that handled MIGA's long term lease. MDIC was paid a ten percent commission (\$24,000) on the sale of the building, three to five per cent higher than available alternatives. MDIC's higher commission cost the insolvency at least \$7,000, and perhaps as much as \$12,000, on the sale. The \$24,000 was paid to MDIC despite the fact that the purchase price was lower than the minimum sale price specified in the executed listing agreement. A different listing agreement was given to Maryland Indemnity counsel, and filed with the court.

Mr. Tull has been a substantial beneficiary of the travel and entertainment budget of Maryland Indemnity. From March 1979 through June of 1981, Mr. Tull has charged the insolvency over \$7,000 for his attendance at ten meetings of the National Association of Insurance Commissioners, and one meeting of the National Committee of Insurance Guaranty Funds. During the same

period the insolvency has spent approximately \$5,000 for Commissioner Birrane's expenses at the same meetings.

American Centennial Insolvency

Commissioner Birrane appointed his friend and former MIGA Board Chairman Ralph Moore to the job of deputy receiver of ACLIC, a life and health insurer, despite the fact that Mr. Moore's insurance experience was not in the life and health insurance field. Mr. Moore's salary is now \$41,000 a year.

ACLIC's accounting work is done by Andrew Caldwell and Associates, a five accountant firm which also does the accounting work for Maryland Indemnity and MIGA, and also Free State. It has been paid over \$300,000 by ACLIC to date for accounting services, and its services are continuing. The Caldwell firm's bills to ACLIC do not contain a breakdown of the services performed. Because of the lack of documentation to justify so large an expenditure, we have employed Coopers & Lybrand to evaluate the Caldwell billings. We will submit the Coopers & Lybrand evaluation when it is completed as a supplement to this Report.

ACLIC's Baltimore counsel is Stanford Franklin. He was chosen by Commissioner Birrane.

ACLIC's bookkeeper is Charles Witzen, who is also a book-

keeper for Maryland Indemnity and MIGA. His salary from all three entities is approximately \$40,000 a year. His wife, Shirley, is the ACLIC office manager at \$22,580 per year. His sister-in-law is also employed at ACLIC as a clerk.

When ACLIC offices were moved from Atlanta, Georgia to Towson, Maryland, a company styling itself "Office E-Z Move" was retained. According to Deputy Receiver Moore, "Office E-Z Move" was selected for the job because they were "just outstanding". "Office E-Z Move" is the trade name for Patricia Prodoehl, wife of the president of Free State. ACLIC outside adjusting work has been given to Free State.

ACLIC has reimbursed Mr. Moore over \$8,000 and Commissioner Birrane over \$10,000 in travel expenses, for their attendance at industry conventions.

We believe that the most important aspect of these findings is the pattern they reveal. While individual episodes are noteworthy, our most palpable, and unsettling, findings are (a) the pervasive extent to which a highly inbred group has benefitted financially from the affairs of these quasi-public entities, with little, if any, outside check or control on their behavior, and (b) the serious doubts that have been raised about the legitimacy of some of the expenditures made. These phenomena feed on each

other. The existence of old friends and acquaintances in a series of loosely related enterprises would be less remarkable if evidence of abuse did not exist. And it would be easier to credit the judgment of those authorizing and approving questionable billings if those authorities were not approving such billings for their friends and if the approving authorities were not themselves part of the small band of beneficiaries. Indeed, expenditures which would be accepted in a different climate as normal tend to take on, perhaps undeservedly, a more sinister cast in the atmosphere we have encountered here. The refusal of some witnesses to talk to us at all, of course, exacerbates the problem.

In making these findings we are mindful that we are not reporting on the activities of State agencies, and that many restrictions, such as competitive bidding requirements, that are applicable to such State agencies are inapplicable here. It must also be recognized, however, that those entrusted with the affairs of MIGA, whose funds are generated under compulsion of State law, and with the liquidation of the insolvencies, whose assets are in trust for the benefit of creditors, are handling the funds of others and can fairly be held to meet the normal fiduciary standards of honesty, diligence and prudence in the discharge of their duties.

B. Staff

In addition to members of this office, our inquiry team included Lawrence Melocik, a member of the Legislative Auditor's staff. Mr. Melocik's prior experience, reflected in his resume, included participation in audits of private insurance companies and the Maryland Insurance Division (App. I-3).

C. Methods

In the first four months, we reviewed literally thousands of pages of records and conducted numerous interviews, in person and via telephone. We also obtained the services of two retired insurance claims experts. Thereafter, we analyzed the facts we had assembled and prepared proposed findings of fact. Those proposed findings were provided to the Insurance Commissioner on March 19, 1982 and reviewed by representatives of each of the entities discussed herein. The Insurance Commissioner and those entities were invited to submit written comments on any factual assertion that we had made. We received written comments from each of the entities. On receipt of these written comments, we conducted additional interviews and analysis. We then met with the Insurance Commissioner and representatives of each of the entities to discuss their submissions, our additional information and the contents of this final report.

1. Documents

Generally, the types of records reviewed were:

- (a) Financial records and their documentation (salaries, rent, furnishings, travel, meals, etc.) at MIGA, Maryland Indemnity, and ACLIC;
- (b) Operations reports (plans of operations, status reports, daily correspondence and memoranda) at MIGA, Maryland Indemnity, ACLIC and LHIGA;
- (c) Legal opinions rendered by counsel to MIGA, Maryland Indemnity, and ACLIC;
- (d) Court records of Maryland Indemnity and ACLIC insolvencies;
- (e) Audit reports, both internal and by the Insurance Division, of MIGA, Maryland Indemnity, and ACLIC;
- (f) Adjusters' claim files for both MIGA and Maryland Indemnity;
- (g) Miscellaneous correspondence from the Maryland Insurance Division, Attorney General's Office, National Association of Insurance Commissioners, and National Committee on Insurance Guaranty Funds;
- (h) Relevant Maryland statutes.

2. Interviews

We conducted interviews of the following forty-eight named persons:⁵

⁵ Several persons agreed to interviews on the condition that their identities be kept confidential.

- (a) Virginia Barnes - Secretary/Director of Administration, Maryland Workmen's Compensation Commission
- (b) George Bereska - former LHIGA Board member
- (c) Edward J. Birrane, Jr. - Insurance Commissioner
- (d) Granville Bixler - MIGA Director
- (e) Richard Brooks - former Assistant Attorney General and former Deputy Insurance Commissioner
- (f) William Cahill, Esq. - Counsel for Maryland Indemnity
- (g) Andrew Caldwell - Financial Auditor for MIGA, Maryland Indemnity, and ACLIC
- (h) Evia Christian - Examiner, Maryland Insurance Division
- (i) Thomas Clarke - Claim Coordinator, American Mutual Insurance Companies
- (j) Hon. John Corbley - Secretary, Department of Licensing and Regulation
- (k) Frank Csar - Illinois Special Deputy for Liquidations
- (l) George Darley - former MIGA Claims Manager
- (m) Shirley Dugan - former MIGA Administrative Assistant
- (n) Patrick Foley - Vice President and General Counsel, American International Group
- (o) Sylvia Franklin - Administrative Assistant, MIGA
- (p) Jack Gandy - Claims Manager, Crawford & Co.
- (q) Robert Graham - former audit committee member for MIGA
- (r) Sidney Green - Chief, Life and Health Section, Maryland Insurance Division
- (s) Fred Hearn - Realtor
- (t) Fran Horner - former MIGA Administrative Assistant

- (u) Yancy Horner - former Chief Examiner, Insurance Division
- (v) Hon. Alan Lipson - former Assistant Attorney General, assigned to Insurance Division
- (w) Emmett MacCubbin - Chairman of LHIGA Board
- (x) Dennis Malone - Real estate agent W.C. Pinkard & Co.
- (y) Richard McCarty, Esq. - Assistant Counsel, American Insurance Association (and Executive Secretary, National Committee of Insurance Guaranty Funds)
- (z) Hon. Harry McGuirk - State Senator
- (aa) Albert Mezzanotte - Chairman, MIGA Board of Directors
- (bb) Ralph Moore - former MIGA Board Chairman; now Deputy Insurance Commissioner/Deputy Receiver, ACLIC
- (cc) Charles Mullaney - former MIGA Claims Manager (two personal interviews)
- (dd) Karen Murphy - former law clerk, Insurance Division, and former law clerk, Maryland Indemnity
- (ee) Richard Ober - former MIGA Board member
- (ff) Hon. James A. Perrott - Judge, Supreme Bench of Baltimore City
- (gg) Sharyn Rhodes - Former Maryland Indemnity Employee
- (hh) William Rogers - former MIGA Board Chairman
- (ii) Suzanne Sanyour - Records Clerk (subrogation), MIGA
- (jj) Douglas Schooley - independent claims adjuster, Schooley & Co.
- (kk) Carl Schultz - claims adjuster, General Accident Bureau
- (ll) Francine Semaya - Director of Licensing, American International Group
- (mm) Douglas Sharretts - Executive Officer, MIGA
- (nn) Patrick Smith - former Assistant Attorney General, assigned to Insurance Division

- (oo) Edward T. Steffy, Esq. - Counsel for LHIGA
- (pp) Donald Tesno - American Mutual Insurance Co.
- (qq) Doris Tippet - Secretary, Insurance Division
- (rr) Preston Tull - Deputy Insurance Commissioner/Deputy Receiver, Maryland Indemnity Co. (Deposition)
- (ss) H. May Van Wright - Realtor Maryland Development and Investment Corporation
- (tt) Stanley Vinton - former Rehabilitator ACLIC
- (uu) Charles Witzen - Bookkeeper, ACLIC, MIGA, and Maryland Indemnity
- (vv) Thomas Wooten - Claims Director, Equifax

Those who refused our requests for an interview are:

- (a) Deborah Corum - former Claims Coordinator, Insolvency Specialist, MIGA
- (b) Stanford Franklin - local counsel ACLIC; Vice President, Maryland Development and Investment Corporation; attorney receiving legal work from MIGA and Maryland Indemnity
- (c) Ramsey Gray - former MIGA Board member
- (d) James Hightower - former MIGA Board member
- (e) Henry Prodoehl - President, Free State Adjusters, Inc. (hereafter Free State)
- (f) Patricia Prodoehl - Office E-Z Move

Although each persisted in refusing our requests for interviews, Ms. Corum, Mr. Franklin, Mr. Gray and Mr. Hightower submitted written statements that discussed at least some of the topics that we would have asked about in a full interview. We have included those written statements in the Document appendix to this report and have referenced those statements in the body of the report noting both when those statements answered a

pertinent question, and when those statements left unresolved or unaddressed a point that we would have wanted to pursue.

3. Experts

Two retired claims experts, Mr. Clayton W. Hagen, and Mr. Frank Boyle were of assistance to our inquiry. Mr. Hagen, a property and claims manager for over 18 years with Royal Globe Insurance, reviewed several hundred claims files formerly processed for MIGA by various independent claims adjusters. Mr. Boyle, a worker's compensation claims manager for over 25 years with the General Accident Fire and Life Insurance Company, reviewed over one thousand worker's compensation claims files, primarily of the Maryland Indemnity insolvency. Their reports are referenced in the relevant sections of the report.

SECTION II
THE GUARANTY ASSOCIATIONS : MIGA AND LHIGA

A. Introduction

Edward J. Birrane, Jr. became Maryland's Insurance Commissioner on January 1, 1976 having been appointed to that position by the Secretary of Licensing and Regulation with the approval of Governor Marvin Mandel.¹ While the position originally carried no set term, a change in the law made the position an appointed one with a six year term. Commissioner Birrane was appointed by then Acting Governor Blair Lee to a full six year term effective July 25, 1977.² In June, 1978, Commissioner Birrane made three appointments to MIGA's eight member Board of Directors. Prior to then, he had made no new appointments to the Board but had instead reappointed members or representatives of the same insurers who had been appointed by his predecessor. In April, 1979, Commissioner Birrane made other new appointments to the eight man Board.

The principal issues addressed concerning MIGA arise in the period after January 1, 1979, a period in which Board appointees

¹ A chronology of the most significant dates in the events concerning MIGA that we recount here can be found at the end of Section II at page 83 of this report.

² The Birrane appointment was made during the period in which Blair Lee was Acting Governor by virtue of the June 4, 1977 letter by Governor Marvin Mandel in which he stepped aside as Governor.

of Commissioner Birrane -- Mr. Ralph Moore, Mr. Albert Mezzanotte, Mr. James Hightower and Mr. Ramsey Gray -- came to occupy the leadership positions on MIGA's Board of Directors.

After January of 1979,³ MIGA operations were characterized by dramatically increased administrative expenses (including director's expense and payments to servicing facilities), parochial hiring practices and diminished control over MIGA affairs by the full MIGA Board.⁴ During the same period, MIGA's plan of operation was changed to eliminate the annual audit that had evaluated the propriety of expenses.

Commissioner Birrane nonetheless insists that he has not paid close attention to MIGA affairs (describing MIGA as "out there somewhere"), an insistence subject to question in light of

³ The period under discussion will be January 1, 1979 to date. However, where financial data are discussed, the figures used will extend only through June 30, 1981 since complete financial data were not generally available after that date.

⁴ Both loss adjustment expenses and office expenses are administrative expenses and do not include any amounts paid to claimants.

Loss adjustment expenses are the costs associated with the investigation and disposition of loss adjustment claims. Loss adjustment claims are the claims made against the insurer (here the insolvent insurer) for personal injury and/or property loss by a victim, who may be either a policyholder (a first party claimant) or a person making claim against a policyholder (a third party claimant). The other category of claim paid by MIGA is the unearned premium claim, a claim made by a policyholder whose policy is cancelled by the insolvent insurer before its term had expired. Where such cancellation occurs, the policyholder is entitled to a refund of the unused portion of the premium. Office expenses include rent, salaries, utilities, supplies, director's expense (travel and entertainment), etc.

his statutory responsibilities and our findings about recent events at MIGA.⁵

B. The Maryland Indemnity Guaranty Association

1. The Operation and Regulation of MIGA

MIGA is Maryland's guaranty association for property and casualty insurers. LHIGA is its life and health guaranty insurance counterpart.⁶ Both associations were created by statute in 1971 for the primary purposes of protecting insurance policyholders and claimants in the event of insolvency of an insurer.

MIGA, created and governed by Article 48A, §§504-519, is a non-profit unincorporated legal entity whose members consist of certain property and casualty insurers authorized to transact the business of insurance in this State. As originally established, MIGA did not include companies writing worker's compensation insurance. However, effective July 1, 1981 the statute was

⁵ For example, Richard Brooks, former Deputy Insurance Commissioner, and Judge Alan Lipson, former counsel to the Insurance Division, both described the insolvencies (Maryland Indemnity and ACLIC) including the guaranty associations as areas that Commissioner Birrane had declared "off limits" to them.

⁶ LHIGA will not be discussed separately but will be discussed where appropriate throughout the report.

amended to expand MIGA's membership to include worker's compensation insurers.⁷

MIGA is funded by pro rata assessments against its member insurers. Each company recoups from its policyholders the amounts it pays to MIGA. A Board of Directors, appointed by the Insurance Commissioner, is responsible for the operation of MIGA. Each Board member remains a full time employee of his company and serves MIGA on a part time basis, without compensation.⁸ Board members may receive reimbursement for their expenses and the MIGA statute requires that the MIGA plan of operation set forth the amount and method for such reimbursement. The Board may hire staff or may contract for outside services. The use of an outside contractor or "servicing facility" to handle claims is specifically conditioned by statute on Insurance Commissioner approval. The Insurance Commissioner

⁷ Prior to this change in the law, beneficiaries of worker's compensation policies were protected in the event of the insolvency of an insurer by Article 101, §85-89 which provided that awards made by the Workmen's Compensation Commission were to be paid by the State Insurance Department out of funds collected by departmental assessment of Maryland insurers writing worker's compensation insurance. A more detailed examination of this change in the law is included in Section III of this report.

⁸ In most respects the MIGA statute is similar to those which establish property and casualty guaranty associations in other states. The National Committees of Insurance Guaranty Funds (NCIGF) and the National Association of Insurance Commissioners (NAIC) have developed a model statute and model plan of operation for each guaranty funds. Those models, with some variation, have been adopted in most states. MIGA diverges from the model act primarily in that its Board members are appointed by the State Insurance Commissioner and not by the insurance industry. According to Richard McCarty, former Executive Secretary of the NCIGF, the model act is designed to achieve industry control over the use of what is industry money, primarily through industry control of the appointment of Board members.

also has the power to revoke the designation of a servicing facility if he finds that claims are being handled unsatisfactorily.⁹

Other than the Insurance Commissioner, no other state official or body has the responsibility or the authority to regulate MIGA. The Commissioner's responsibility is broad. In addition to his power to approve and revoke the designation of servicing facilities, and his appointment of the MIGA Board of Directors, the Insurance Commissioner has the duty to examine and to regulate MIGA. MIGA must submit annual financial reports to the Commissioner in a form that he determines, and any changes to MIGA's plan of operation (the written statement of MIGA procedures) must be approved in writing by the Commissioner.

MIGA's plan of operation sets the terms of its Board members (up to six years) and states the duties of its Board: to review the plan annually; to review all contracts with servicing facilities; to review operating expenses and claim costs; and to review the need to assess for additional monies or the appropriateness of refunds to members. The plan also requires an annual audit and establishes MIGA's basic framework, calling for an

⁹ The Insurance Commissioner has suggested that his power to revoke a servicing facility can only be triggered by his receipt of a complaint. Article 48A, §510 does not require such a complaint. In an April 1978 letter to then MIGA Chairman, William Rogers, Commissioner Birrane threatened to revoke all MIGA servicing facilities under Article 48A, §510 (App. II-3). He did not reference receipt of any complaint and we have no evidence that any complaint had been made.

administrative assistant and an executive officer and dividing operations into four departments: Administration, Claims, Legal and Detection and Prevention of Insolvencies.

2. MIGA Before 1979

The first MIGA Board of Directors, and subsequent Boards until the 1978 appointments of Commissioner Birrane, consisted of high ranking executive officials of Maryland's property and casualty insurers. These members appear to have brought to the Board not only a knowledge of insurance but also managerial and administrative skills.

The first Board did almost no business until 1972 when the first insolvency, that of LaSalle National Insurance Company, occurred. Thereafter, in this early period the Professional Insurance Company, Interstate Insurance Company and Gateway Insurance Company went insolvent and the claims by Maryland residents against those insolvent companies were handled by MIGA. Most of the claims against those companies had been resolved by 1979. The other insolvency for which MIGA had handled claims prior to 1979, one whose MIGA claims work spans the two periods discussed in this report, is that of Maryland Indemnity.

The early MIGA Board, faced with relatively small insolvencies, chose to contract with member insurers for handling of

loss adjustment claims. We have located written contracts for most of the arrangements with these servicing facilities. Unearned premium claims were processed manually by MIGA's administrative assistants. The early Board was careful to obtain bids on goods and services to be purchased. Board minutes not only show Board action on such contracts but also reflect the reasons why the purchases were made.

With the coming of the Gateway insolvency, the Board was for the first time faced with a large volume of claims. To handle the growing volume of loss adjustment claims, the MIGA Board decided in late 1974 to hire a claims manager, Mr. George Darley. Rather than using an insurance company claims department as a servicing facility, Mr. Darley handled the loss adjustment claims. Where necessary, he was authorized by the Board to use an outside adjusting firm. The administrative assistant continued to process unearned premium claims. Where the work was more than MIGA's two person staff could handle, temporary staff was used. MIGA obtained the part-time services of off-duty employees of the Insurance Division (which was in the same building as MIGA) to meet this need.

When Maryland Indemnity became insolvent in December 1977, MIGA faced an even larger volume of claims.¹⁰ MIGA's Board met

¹⁰ MIGA claims payments totals have fluctuated depending on the number of insolvent companies, the number of Maryland claimants for those insolvent companies and the state of completion of claims work for a particular insolvency. MIGA made almost no claims payments during the period 1971 through 1974. Then during the period 1974 through 1976, Cont'd.

this increase by taking the following steps: hiring additional staff adjusters (those hired were former employees of Maryland Indemnity); hiring additional clerical help (temporary); authorizing the use of additional outside adjusting firms; giving the claims manager (Mr. Darley) greater authority to pay claims and to assign cases to counsel; and renting additional space across the street in the Maryland Indemnity Building in order to house the claims operation.

For years prior to 1979, MIGA operations were subject annually to audit by a three member Audit Committee comprised of representatives of the State's three largest property and casualty insurers. This audit consisted of a full financial audit, a review of operations and expenses, and a review of the insurance practices of MIGA.¹¹ In April, 1980 (the audit for calendar year 1979) the audit procedure was changed.

3. MIGA 1979 and After

In 1979, Ralph Moore, Albert J. Mezzanotte and James Hightower, three Board members who had been appointed by Commissioner Birrane in June of 1978, assumed three of the four leader-

the onset of several insolvencies, including the Gateway insolvency, brought a heavy volume of claims payments. In 1977, that volume declined. Beginning in late 1977, the Maryland Indemnity insolvency brought another period of increased claims activity.

¹¹ We reviewed audit reports from the Audit Committee for the calendar years from 1973 through 1978, except 1977 which we were told could not be located. The report for 1973 included the period in 1972 after MIGA began its operations. Typically, these audits were conducted in the first calendar quarter following the year being audited.

ship positions on the MIGA Board. The fourth leadership position was filled by Ramsey Gray, who was appointed by Commissioner Birrane in April, 1979, to fill the vacancy on the Board created by the expiration of the term of William Rogers, who had been MIGA's Board Chairman since December 1975. With Mr. Rogers' departure in April, 1979, Ralph Moore was elected Chairman of the MIGA Board and Mr. Hightower was elected Vice Chairman. Mr. Moore appointed Mr. Hightower, Mr. Mezzanotte and Mr. Gray to serve as the Executive Committee, with Mr. Hightower as its Chairman.¹²

¹² Mr. Ralph Moore, told us that he was introduced to Edward Birrane in the late 1960's by Patrick O'Doherty, now a senior partner in the firm of O'Doherty, Gallagher & Nead, and that he had since that introduction become a friend of the Commissioner. At the time of his appointment to the MIGA Board, Mr. Moore was claims manager for Cuna Mutual and had had 15 years of insurance claims experience. Mr. Moore left MIGA's Board in May, 1980 when he accepted the position as Deputy Receiver of ACLIC.

Mr. Albert Mezzanotte came to MIGA's Board with over 20 years of insurance claims experience with Kemper Insurance Company. At the time of his appointment to the Board, he was Kemper's Baltimore claims manager. Mr. Mezzanotte was reappointed in 1981 to a second three year term on MIGA's Board.

Mr. James Hightower, in response to our request for an interview, sent us a three page letter which stated inter alia that he saw "no need for an interview." In his letter he described himself as "a prominent member of Baltimore Claims Managers Counsel including the position of Chairman." Mr. Hightower was the Claims Manager of Bituminous Insurance Company when he was appointed to the MIGA Board. Mr. Hightower said in his statement that he was asked by Commissioner Birrane to submit a resume and be interviewed. Thereafter, he was appointed to the Board. Mr. Hightower indicated no particular friendship with Commissioner Birrane prior to the appointment. He did indicate that he has known Free State's President Henry Prodoehl for 20 years, that he has used the company and that he has high regard for their work. Mr. Hightower's letter is shown at App. II - 43.

Mr. Gray responded to our request for an interview with a written statement that did not include his background. He declined our further request for an interview. We were told by the other persons interviewed that Mr. Gray had insurance claims experience and that he had been with Prudential Insurance Company while he was on the MIGA Board. Mr. Gray recently left Prudential and at that time resigned his position on MIGA's Board of Directors. Mr. Gray's written statement is shown at App. II - 44.

The character of these Board appointments differed from those in MIGA's earlier years in that the appointees were claims managers of the member insurers rather than company executives. Commissioner Birrane explained to us his reasons for making these appointments. He said that since MIGA's primary business was to pay claims he had decided to change the orientation of MIGA's Board to reflect a greater emphasis on claims.¹³ He said that he was a friend of Ralph Moore, knew Mr. Moore to be an experienced claimsman, and had selected Mr. Moore on that basis.¹⁴ Mr. Moore, in turn, recommended Mr. Mezzanotte, Mr. Hightower and Mr. Gray.

The changes that occurred in MIGA's operations after 1978 were substantial. They can be summarized as follows:

1. After a search conducted by Ralph Moore, Charles Mullaney was hired as MIGA claims manager.
2. The staff adjusters who had been handling the Maryland Indemnity claims were fired and the remaining claims work was sent to outside adjusting companies. While originally a number of such adjusting companies were used, eventually Free State received the bulk of the work.

¹³ Commissioner Birrane did not make a corresponding change to the LHIGA Board where all directors hold executive positions with their companies. Mr. Frank Csar, Special Deputy to the Director of Insurance for the State of Illinois, told us in an interview arranged by Commissioner Birrane that he agrees that claims personnel such as claims managers and Vice-Presidents for claims should be appointed to the Boards of guaranty associations.

¹⁴ Mr. Moore told us he learned of the vacancy on the MIGA Board from his friend Preston Tull, the Deputy Receiver of Maryland Indemnity.

3. The names of Stanford H. Franklin and Simmons and Fields -- Stanford Franklin, Robert Simmons and Russell Fields were all friends of Ralph Moore -- were added to the roster of attorneys receiving MIGA legal work. After January 1, 1979, there were few new MIGA cases assigned to counsel; however, those that were assigned went to these newly added lawyers rather than the over a dozen firms which MIGA had used for the previous seven years.. The only exception appears to be the firm of O'Doherty, Gallagher and Nead which received MIGA legal work both before and after 1979.¹⁵
4. The MIGA offices were moved from the downtown location to Towson, at a 132% increase in monthly rental costs.
5. The size of MIGA's staff increased and with that increase MIGA's salary costs increased. The hiring of Douglas N. Sharretts, a long time associate of Commissioner Birrane, to the newly created position of house counsel at a starting salary of \$37,500 per year was the largest single item of increase in salary. The starting salary of claims manager Charles Mullaney was \$25,000 a substantial increase over the salary of the former MIGA claims manager George Darley.
6. MIGA's plan of operation was amended to remove the requirement of a yearly full-scale operational audit by an Audit Committee of insurance company representatives. As that amendment was implemented by the Board the new audit was a fragmented procedure which resulted in a financial review by a Maryland CPA who was to be an actuarial expert and a claims handling review by an insurance expert. This fragmented audit did not result in a full-scale operational review of MIGA.

During the period in which these changes were made, MIGA administrative expenses increased dramatically. From January 1, 1979 to June 30, 1981, MIGA paid out \$1,287,901 for loss

¹⁵ Stanford H. Franklin, who had known Ralph Moore since 1972, is the lawyer appointed by Commissioner Birrane as Maryland Counsel to ACLIC (See Section IV). Mr. Franklin currently shares an office in the Towson Towers with MDIC in addition to his firm's downtown office in the Equitable building. MIGA's administrative office, leased through MDIC, is also located in the Towson Towers. Mr. Franklin's written statement can be found at App. II-46.

adjustment claims.¹⁶ This was slightly higher than the similar total for MIGA's first seven years. However, loss adjustment expenses for the same January 1, 1979 to June 30, 1981 period were more than double loss adjustment expenses for that first seven year period.¹⁷

The following charts depict the jumps in MIGA expenditures.

¹⁶ Because the complete financial information was provided only through June 30, 1981, MIGA expenses after that date, including the \$58,000 payment which MIGA made in July 1981 to Preston Tull, Deputy Receiver of Maryland Indemnity, are not included in these figures. The payment to Mr. Tull is discussed in Section III of this report because it involves the Maryland Indemnity insolvency and his position as Deputy Receiver. Nor are payments to Free State for the Worker's Compensation file review which began after 7/1/81 reflected in these totals.

¹⁷ Loss adjustment claims payments for the 1971 through 1978 period totaled \$1,249,924. The figure for such payments 1979 through 6/30/81 was \$1,287,901 for an increase of 3%. Loss adjustment expenses however rose from \$265,000 (for the first seven years) to \$599,095 (after 1/1/79) representing an increase in those expenses of more than 125%.

The increase in office expenses was 77%, from a pre 1/1/79 total of \$385,165 to a total of \$682,746 after 1/1/79.

The addition of totals for MIGA's other form of payment activity — payment of unearned premium refunds — only makes the increase in total administrative costs more dramatic since MIGA refunded premiums totaling \$686,804 from 1971 through 1978 and refunded only \$189,597 after 1/1/79, for a drop of 72% in this claims payment activity.

When both types of payments to claimants are included (loss adjustment and unearned premium), the figures show a 24% drop in total claims payments from \$1,936,728 to \$1,477,498 but a 97% increase in MIGA's total administrative costs from \$650,380 before 1/1/79 to \$1,281,841 after.

Summary of Certain MIGA Expenditures

	<u>Claims Paid</u>		<u>Increase (Decrease)</u>
	<u>Period 1 (12/1/72- 12/31/78)</u>	<u>Period 2 (1/1/79- 6/30/81)</u>	
Loss Adjustment Claims Paid	\$1,249,924	\$1,287,901	\$ 37,977
Unearned Premium Refunds	<u>686,804</u>	<u>189,597</u>	(497,207)
Total Claims Paid	<u>\$1,936,728</u>	<u>\$1,477,498</u>	<u>(\$459,230)</u>

Total Administrative Expenses

	<u>Period 1</u>	<u>Period 2</u>	<u>Increase</u>
Loss Adjustment	\$265,215	\$ 599,095	\$333,880
Office	<u>385,165</u>	<u>682,746</u>	<u>297,581</u>
Total	<u>\$650,380</u>	<u>\$1,281,841</u>	<u>\$631,461</u>

Loss Adjustment Expenses

	<u>Period 1</u>	<u>Period 2</u>	<u>Increase (Decrease)</u>
Loss Adjustment Expense (LAE)	\$265,079	\$599,095	\$334,016
Miscellaneous	<u>136</u>	<u>-</u>	<u>(136)</u>
Total	<u>\$265,215</u>	<u>\$599,095</u>	<u>\$333,880</u>

Office Expenses

	<u>Period 1</u>	<u>Period 2</u>	<u>Monthly Average Period</u>		<u>Increase (Decrease)</u>
			<u>1</u>	<u>2</u>	
Rent	\$37,859	\$80,955	519	2,699	43,094
Salaries	226,856	388,767	3,108	12,959	161,911
Outside Serv.	44,034	59,121	603	1,971	15,087
Post. & Tele.	10,983	15,281	150	509	4,298
Off. Supplies	5,408	21,431	74	714	16,023
Printing	2,467	1,743	34	58	(724)
Directors Exp.	4,596	30,892	63	1,030	26,296
Audit Comm.	3,526	967	48	32	(2,559)
Legal Audit.	45,556	69,167	624	2,306	23,611
Insurance	<u>3,880</u>	<u>14,422</u>	<u>53</u>	<u>481</u>	<u>10,542</u>
Total	<u>\$385,165</u>	<u>\$682,746</u>	<u>5,276</u>	<u>22,758</u>	<u>297,581</u>

These summary figures demonstrate that the single, biggest item of increased expense is loss adjustment expense, which included approximately \$240,000 paid after 1/1/79 to outside adjusters. Of that \$240,000, one company - Free State Adjusters', Inc. - received \$202,853.¹⁸

These summary figures also demonstrate a substantial disparity between the level of claims payments and the loss adjustment expenses associated with such payments.

While MIGA financial figures examined on a year by year basis reveal some relationship between claims payments and administrative costs, the increase in the level of these administrative costs since January 1979 simply cannot be explained in terms of increased volume of claims activity. Since 1979 the cost figures have risen out of proportion to claims payments. Moreover, in 1980 when claims payments decreased, administrative costs did not decrease proportionately.¹⁹

¹⁸ The \$599,095 in loss adjustment expense after January 1, 1979 consists of \$346,815 in lawyers fees, \$240,631 in fees to outside adjusters and \$11,649 in miscellaneous expenses. The fees to outside adjusters include \$202,853 paid to Free State and \$37,778 paid to all other companies.

Lawyers' fees paid after January 1, 1979 include fees in cases assigned to lawyers both before and after that date. We have been told by former MIGA claims manager George Darley that a strict rotation system was used to assign MIGA cases to more than a dozen lawyers before 1979, and we have reviewed MIGA records which show such a rotation system. We have seen no records breaking down actual assignments in terms of a particular date.

¹⁹ We found for example that a dramatic drop (of 92%) in MIGA total claims payments from 1976 to 1977 from \$225,074 to \$17,112 was met with a nearly corresponding drop in loss adjustment expenses from \$58,653 to \$7,315 (a drop of 88%) yet MIGA showed an Cont'd.

The following are the actual cost figures for years 1978, 1979, and 1980:

	<u>All Claims Payments</u>		<u>Administrative Expense</u>	
1978	\$705,775]-20% increase]-31% decrease	253,576]-136% increase]-7% decrease
1979	847,224		599,571	
1980	581,340		559,845	

	<u>Loss Adj. Claims Payments</u>	<u>Breakdown of Administrative Expense Loss Adj.</u>	<u>Office</u>
1978	\$599,158	\$83,803	\$169,773
1979	840,651	304,701	294,870
1980	403,464	248,413	311,432

During our investigation, we have been repeatedly cautioned by Commissioner Birrane and others that care must be used in evaluating loss adjustment expenses, particularly adjusting costs, and that total dollar figures alone might not give an accurate picture. The number and complexity of claims, the method of adjustment and numerous other variables can, we were told, affect the cost and thereby skew the total costs. Because of these variables, and because the expense of outside adjusters, particularly Free State, has been so sizeable, we engaged the services of Mr. Clayton Hagen, an experienced claims manager, to assist us in reviewing loss adjustment expenses, particularly the charges of outside adjusting firms. His 38 years of experience in insurance claims work in Maryland and his review of over 500 MIGA claims files make his conclusions a dependable gauge for evaluating the loss adjustment charges.

increase in office expenses from \$55,609 to \$62,357 (a 12% increase).

Mr. Hagen found that the work performed by Free State "in many instances appears unwarranted and reworked, resulting in overbilling" and he concluded that "MIGA was overcharged [by Free State] for work (inadequate at times) performed." (Hagen Report at p. 79)

We have attached Mr. Hagen's full report in the Reports appendix to this report (referenced hereafter as "Hagen at p. "). While a review of that report is important to appreciate his conclusions fully, we will summarize briefly Mr. Hagen's review, in which he found serious irregularities in Free State's work, as follows:

Investigations in files where the claim had been made after the applicable statute of limitations had run. (See Hagen at p. 16-17)

Unnecessary investigation where no claim had even been made or where the claim had been denied by the insolvent insurer and no action had followed the denial. (See Hagen at p. 22-23, 25 and 28)

Unnecessary reinvestigation where the file had either been previously investigated by the insolvent insurer or the claim had been the subject of a binding arbitration award. (See Hagen at pp. 23-24 and 27)

Billings for reports that were never forwarded to MIGA. (See Hagen at p. 29)

Conflicts between attorney's bills showing telephone conferences and Free State bills showing personal meetings. (See Hagen at p. 9 and p. 10)

Excessive time spent by Free State on uncomplicated tasks (See Hagen at pp. 10-11, 15, and 30)

In our conversations, Mr. Hagen explained that he found little evidence in the claims files of MIGA directing or

controlling the activities of Free State.²⁰

Mr. Granville Bixler, a current MIGA Director and one of the Directors since 1971, told us that while claims costs would fluctuate in proportion to claims payments, his experience would lead him to say that the relationship would not be one of exact proportion because loss adjustment service costs are subject to inflationary pressures. Accepting that statement, the inflation rate does not account for the disparity.

MIGA's outside counsel, Mr. Thomas Gisriel, suggested that an explanation for the disparity between claims payments and administrative costs might be that costs incurred in a high volume year were actually paid out in a low volume year.

The finding of our expert, however, confirms the problems with loss adjustment expenses which are not attributable to volume of claims activity, inflation, or lag in end of year processing of payments. Moreover, MIGA counsel's suggestion misses the greater significance of the payment and cost totals. The jumps in MIGA expenditures should have been a red flag that effective control of expenditures might be lacking. The same

²⁰ In the written materials submitted by former MIGA Director Ramsey Gray, he included a transcript of a tape recorded meeting between Free State adjusters and then MIGA claims manager Charles Mullaney. A separate copy of that transcript was provided by Free State through its lawyer. That transcript shows that at the time Free State first began to do MIGA work, Mr. Mullaney provided a detailed description of the MIGA statute and how MIGA claims should be handled. There does not seem to have been effective follow up to that initial direction.

figures were available to MIGA yet no inquiry was undertaken by its Directors. During our interview, Mr. Bixler confirmed that the Board of Directors has not received figures broken down as we have done. He indicated that those totals, had they been brought to the Board's attention, would have been a basis for further Board inquiry. Mr. Bixler indicated that such matters are generally brought to the Board's attention by the Executive Committee, of which he is now a member. The figures in Mr. Hagen's review suggest that, at the very least, the MIGA expenditures may never have been carefully examined. These concerns are heightened by the more detailed examination of many MIGA expenditures, which follows.

4. Free State

a) The Rise of Free State

Prior to 1979, Free State had been paid by MIGA only \$90.00 in a single payment made in December, 1978. How it came to receive the lion's share of MIGA's adjusting work was a question we asked many of the people we interviewed.

The story seems to begin with the appointments in June 1978 of Messrs. Moore, Mezzanotte and Hightower to MIGA's Board. Soon after Messrs. Moore, Mezzanotte and Hightower joined MIGA's Board, they conducted a review of MIGA's claims operation. Following that review, they recommended to the Board that a new

claims administrator be hired. Ralph Moore was assigned the task of finding a suitable candidate. He recommended his friend Mr. Charles Mullaney, who was the District Claims Superintendent for American Mutual Insurance Companies. Mr. Mullaney was approved by the Board and became MIGA's claims manager on November 2, 1978.²¹ Mr. Mullaney was hired at a salary of \$25,000.

Mr. Mullaney told us that prior to his coming to MIGA Ralph Moore had introduced him to Mr. Henry Prodoehl, the President of Free State and encouraged him to use Free State adjusting services while he was still with American Mutual. He said that he was also told by Ralph Moore that "there is no way you can get the job at MIGA unless you pass muster with Henry." Thereafter, he did use Free State briefly at his company before coming to MIGA. Mr. Moore denies the conversation though Mr. Mullaney's account has been at least partially corroborated.²² Mr. Henry Prodoehl, President of Free State, has refused our repeated

²¹ MIGA Board Minutes indicate that Mr. Mullaney was the only candidate whose name Mr. Moore brought before the Board. Mr. Moore was asked at that time whether there were other candidates and his answer indicated that Mr. Mullaney was the only candidate that was available on loan from his company. Mr. Granville Bixler confirmed that it was his understanding that Mr. Mullaney was on loan from American Mutual and that American Mutual was paying Mr. Mullaney fringe benefits such as pension and insurance that were then unavailable to MIGA employees. Mr. Mullaney told us that he had not been "loaned" by his company, although his company did agree to rehire him if its claims department had a suitable opening at the time he left MIGA. His former supervisor Mr. Donald Tesno confirms Mr. Mullaney's statement. Moreover, Mr. Tesno told us that Mr. Mullaney was not paid pension or other benefits by the American Mutual Company, except that he was allowed to continue his life insurance coverage through the company for a short time. When Mr. Mullaney left MIGA in August 1980, he did not resume work for American Mutual.

²² We have confirmed with Mr. Tesno, Mr. Mullaney's former supervisor at American Mutual, that the company did make brief use of Free State at Mr. Mullaney's suggestion, beginning shortly before Mr. Mullaney left for the MIGA job. Mr. Tesno terminated that use of Free State several months later.

requests to be interviewed.

Soon after Mr. Mullaney came to MIGA, he began using Free State for MIGA work. He told us that Ralph Moore was responsible for this change. While Ralph Moore admitted that he had known Free State's Henry Prodoehl since 1977 and that he had used Free State's adjusting services and rented a car from that company while he was the claims manager of Cuna Mutual, he denied that he ordered Mr. Mullaney to use Free State. (Mr. Moore's choice of Free State for ACLIC business is discussed at Section IV.) Throughout this section and at other points in the report, we have recounted statements by witnesses such as Mr. Mullaney which are not wholly subject to corroboration. To the extent that a statement is corroborated we have so stated. Where another witness has issued a denial that, too, is stated.

On November 28, 1978, soon after joining MIGA, Mr. Mullaney met with then Chairman Rogers and Vice-Chairman Hightower to discuss claims handling. He indicated that he wanted to assign uninvestigated claims to independent adjusters and suggested the use of Crawford & Company (Crawford), Underwriters Adjusters Company (Underwriters), Free State and Johns Eastern Company (if that company decided to do the work). He further indicated that assignments would be based on territory and that periodic comparisons on pricing and quality would be made (App. II-1).

Mr. Mullaney explained to us that in discussing changes he

wanted to make at MIGA he had told Ralph Moore he wanted to use other outside adjusting companies. He specifically mentioned Johns Eastern Company (a company he had used for appraisals at American Mutual) to Moore as a supplement to Crawford, the company doing this work when he came to MIGA. Ralph Moore told him to add both Free State and Underwriters to the list. Mr. Mullaney did so. Mr. Mullaney said that he then sought a bid from each company. Johns Eastern declined to bid. He did obtain bids from the other three; however, only Free State submitted a written bid. We located the December 1, 1978 written bid of Free State which bid \$15.00 per hour, plus expenses (App. II-2)²³. The Free State bid did not make reference to any additional per hour surcharge for overhead or clerical work; however, the billings of Free State show that an additional per hour charge of between \$5 and \$6 has been made for each adjuster hour charged.

Mr. Mullaney described the bids he received from the three companies as "competitive" with one another and claims that he resolved to assign the work evenly to the three companies.²⁴ MIGA did not enter into a written contract with either Free State

²³ We checked with Crawford's manager Mr. Jack Gandy who told us that their rate in December 1978 was \$17 per hour. This was a flat rate plus expenses, i.e., the rate did not add any sums for overhead or secretarial services. Both were built into the adjusters rate. Free State charges a per hour rate for adjusters plus an additional per hour surcharge either for overhead or clerical expense. This additional charge was not reflected in Free State's written bid. Free State's most recent bills charge \$20 per hour plus a \$6 per hour surcharge. Current Crawford rates are \$25 per adjuster hour.

²⁴ Although Mr. Mullaney proceeded to assign adjusting work to the three adjusting companies — Free State, Crawford and Underwriters — he conducted an orientation session only for Free State's staff.

or any other adjusting firm it used. Although the Commissioner's approval was necessary in order to designate Free State as a servicing facility for MIGA claims handling, we were unable to determine that MIGA had obtained Commissioner Birrane's approval for the designation of Free State as outside adjuster. While MIGA's files contained a copy of a December 3, 1978 letter ostensibly sent to Commissioner Birrane for approval of four companies including Free State, Mr. Mullaney denied that he sent the letter to Commissioner Birrane, but said that he sent it to Ralph Moore at Mr. Moore's instruction (App. II-7). Mr. Mullaney told us that when he asked Mr. Moore why Mr. Moore wanted the letter, Mr. Moore told him that Commissioner Birrane would be displeased if anyone other than Free State were on the list. Mr. Mullaney's account of this incident is corroborated by the fact that Commissioner Birrane's files contain no copy of the letter. The Commissioner told us that he did not recall receiving such a letter.

During the period from December, 1978 through February, 1979, Mr. Mullaney assigned files to each of the three adjusting companies. Some of the assignments appear to have been for purposes of review and others for actual adjustment. MIGA records are not sufficiently detailed to permit a determination of the numbers assigned for actual adjustment to each company. In the period from February through May 1979, we found no record of any assignments being made. We confirmed that neither Crawford nor Underwriters received any assignments in this

period.²⁵ Claims assignments began again in mid-June 1979 when Mr. Mullaney began to assign the claims of the Reserve insolvency and several small insolvencies. The records show a change in the pattern of assignments. The pattern of assignments in this period showed a marked favoring of Free State over Underwriters, the other company used. Almost two thirds of all of the Reserve claims and all of the claims of the small insolvencies were assigned to Free State. This pattern apparently accounts for the fact that Free State was paid \$202,853 in loss adjustment expenses from January 1, 1979 to June 30, 1981 while during the same period all other adjusting companies combined were paid only \$37,778. Mr. Mullaney told us that he made the assignments in this fashion based on the directions he received from MIGA Chairman Ralph Moore.

In a May 25, 1979 letter to Mr. Hightower, Mr. Mullaney suggested that the MIGA claims operation be changed substantially. He recommended that its salaried adjusters (Mr. Darley, Mr. Smith and Mr. Brocato) be fired and that he, as claims manager, handle all remaining and future claims with the assistance of outside adjusters. He estimated that the use of this system would result in substantial savings to MIGA both in terms of office space and salary (App. II-4). Mr. Mullaney was permitted to implement his proposal by virtue of the Board's action at its

²⁵ Crawford's manager, Mr. Gandy told us that his company did not receive any assignments from MIGA after January 1979, except 13 small "dishonored draft" claims received in May, 1980.

May 31, 1979 meeting granting him "carte blanche authority for true fiscal policy". This was the same Board meeting at which Ralph Moore was elected MIGA's Chairman and at which the other Birrane appointees moved into MIGA's other leadership positions.

With the adoption of the Mullaney proposal, in June, 1979, Mr. Darley, Mr. Smith and Mr. Brocato, the staff adjusters, were fired.²⁶

Mr. Mullaney says that on June 21, 1979, he was told by Ralph Moore, by then Chairman Moore, to assign two thirds of all Reserve files to Free State and to assign to Free State old Maryland Indemnity files and any new Reserve files that might come in. Mr. Mullaney provided us with a note he wrote dated June 21, 1979 memorializing those instructions (App. II-5). Mr. Moore denies that this conversation occurred. However, the increase in the level of assignments to Free State after June 21, 1979 shows a pattern of assignment that substantially conforms to the instructions in Mr. Mullaney's handwritten note.²⁷

²⁶ While Mr. Mullaney said that the proposal to modify the claims operation was his idea, he also said that he was told by Ralph Moore to get rid of Mr. Darley because Mr. Darley had been complaining to him about the lawyers to whom MIGA cases were being assigned. Mr. Darley was unable to shed much light on this. He said that he and the two other staff adjusters were called by Mr. Mullaney into his office at 3:00 p.m. on a Friday afternoon and were told that they were fired and that was their last day. While Mr. Darley had complained about assigning closed or inactive files to outside adjusters and assignments of cases to counsel, he did not recall any mention being made of that at the time he was fired.

²⁷ In a January 16, 1980 letter to Ralph Moore complaining about Free State billings, Mr. Mullaney makes reference to the fact that he had earlier "severe problems" with the performances of Underwriters and Crawford (App. II-6). However, Mr. Mullaney told us that none of the problems with the other companies were sufficiently serious to warrant a Cont'd.

The billing totals and our examination of assignment records confirms that Free State received the bulk of the MIGA work in this period. Mr. Granville Bixler who was a Board member throughout this period and a Member of the Executive Committee (although an inactive one) from mid-1980 to mid-1981 stated that he knew Free State was one of the companies being used but did not know the extent of that use. Nor was he aware of the other outside services that Free State was engaged to perform in the period.

(b) The Controversy over Free State Billing

Claims Manager Charles Mullaney told us that beginning at least as early as January 1980, he began bringing billing problems on individual files handled by Free State to the attention of the MIGA Board Chairmen, first Mr. Ralph Moore and then Mr. Albert Mezzanotte. The documentation we have been provided by both MIGA and Mr. Mullaney supports his statement (App. II-6 to II-30). However, the witnesses we interviewed (and Mr. Gray through his written statement) give differing accounts of the circumstances surrounding Mr. Mullaney's complaints about Free State's bills.

dismissal. We contacted Mr. Jack Gandy of Crawford who told us that he, as the local manager of that company, had never been told of any such problems nor was he given any explanation of why his company had lost MIGA business. We received similar information from Mr. John O'Connell of Underwriters.

Of the 224 Reserve cases assigned to outside adjusters, Free State received almost 69%. Underwriters received assignments of Reserve cases, plus two Maryland Indemnity files, in the June-July 1979 period. Thereafter, that company received a few isolated assignments of Reserve files until November 1979, when it received the last MIGA work.

In recording the various accounts of the various witnesses, we must note that Mr. Mullaney's explanation of the basis of his concerns about the excessiveness of Free State billings has been largely corroborated, in our view, by the independent review by Mr. Hagen.

Mr. Mullaney said that he complained to Chairman Moore in early January 1980 about Free State billings.²⁸ By letter to Mr. Moore dated January 16, 1980, Mr. Mullaney characterized the Free State billings as "exorbitant" and suggested that Mr. Moore might wish to "reconsider the use of this facility" (App. II-6).

Following the January 16, 1980 letter, Mr. Mullaney says he continued to complain to Ralph Moore about Free State bills (App. II-11, II-12 and II-15).²⁹ Mr. Mullaney wrote to Henry Prodoehl, the President of Free State, and to Karl Prodoehl, its Branch Manager, complaining about Free State billings (App. II-8 to II-12) and had other contacts with Free State about billing (App.

²⁸ Mr. Mullaney furnished us a copy of a handwritten note bearing the date January 2, 1980 in support of that assertion (App. II - 13).

²⁹ In his written statement, former MIGA director Ramsey Gray suggests that Mr. Mullaney began making complaints about Free State only because the workload for the claims manager was dwindling and Mr. Mullaney was fearful for his job. Mr. Mullaney's first written complaint to Ralph Moore about Free State billings was in January 1980 at a time when the number of open files had decreased substantially since Mr. Mullaney's hiring. However, a large number of claims remained. Moreover, Mr. Mullaney's first documented complaint was a June 8, 1979 letter from Mr. Mullaney to Free State's Henry Prodoehl complaining about a \$418.50 bill in a file where Free State's work consisted of the taking of a single recorded statement. Other than Mr. Gray's statement to that effect, we have seen no evidence that Mr. Mullaney's job as claims manager was likely to end soon. In fact Mr. Sharretts, as Executive Director, continues to perform claims manager functions.

II-14 and II-15). Carbon copies of two of the letters to Henry and to Karl Prodoehl were sent to Ralph Moore: The one letter dated March 19, 1980 complained about a \$1,000 adjusting bill for a claim of \$337; the other dated April 8, 1980 characterized a Free State billing as "outrageous" (App II-11 and II-12). Mr. Moore took no action. Mr. Mullaney had discussed billing problems with Free State's Henry Prodoehl in April, 1980 and according to Mr. Mullaney's notes of that conversation, Mr. Prodoehl had suggested that Free State send interim bills. Mr. Mullaney had rejected that as a solution because the problem was the "outrageous" amounts of the bills (App. II-15).

When Mr. Moore left the MIGA chairmanship in May 1980 to become deputy receiver of ACLIC, Mr. Mullaney began taking his complaints to MIGA's new Board chairman, Albert Mezzanotte. The first such complaint according to Mr. Mullaney's note of May 28, 1980 concerned a bill for over \$1000 of which Mr. Mullaney could only justify \$367. Again according to Mr. Mullaney's notes, the conversation included a discussion about Mr. Mullaney's previous complaints to Ralph Moore concerning billing (App II-16).

In a May 29, 1980 letter, Mr. Mullaney complained to Mr. Henry Prodoehl about a bill (he sent a carbon of the complaint to Mr. Mezzanotte). Mr. Mullaney's notes show that he received a call from Mr. Prodoehl on June 4, 1980 in which Mr. Prodoehl claims to have spoken to Chairman Mezzanotte who had advised him that Mullaney would be given "carte blanche" authority to pay

Free State bills without reduction (App. II-17). By copy of Free State's June 4, 1980 letter to Mr. Mullaney, Mr. Mezzanotte received Free State's response to billing complaints on one file and a Free State offer to lower its billing on that file (App. II-18). By letter dated June 5, 1980, Mr. Mezzanotte accepted the offered reduction of the bill and requested that Free State begin sending interim bills (App. II-19).³⁰

On June 11, 1980, Henry Prodoehl answered a June 2, 1980 complaint of Mr. Mullaney's about six claims. (Again Mr. Mezzanotte was sent a carbon copy of Mr. Mullaney's complaint and Free State's response) (App. II-20 and II-21). In the Free State letter Mr. Prodoehl said that he understood that Mullaney would "proceed to place [the disputed bills] in line for payment." Mr. Mullaney's copy of the letter shows his handwritten note dated June 12, 1980 memorializing his conversation with Mr. Mezzanotte on that date in which Mr. Mezzanotte told him to wait and not pay the bills until after vacation (App. II-21). In an earlier note of a June 9, 1980 conversation, Mr. Mullaney wrote that Mr. Mezzanotte had told him to hold off on all billing complaints until after the June 12, 1980 Board meeting (App II-22). The Board minutes for that meeting reflect no discussion of or action on this problem. Mr. Mullaney says that he was not informed of any action. He did, however, continue with his complaints.³¹

³⁰ Although Mr. Mullaney told us that he did discuss with Mr. Mezzanotte the change to interim billing, he said that he did not tell Mr. Mezzanotte that he had rejected the same option only a month earlier when the suggestion had come from Mr. Prodoehl of Free State.

Cont'd.

On July 7, 1980, Mr. Mullaney forwarded 26 Free State disputed billings (totaling \$12,968) to Mr. Mezzanotte (App. II-22A). On July 9, Mr. Mezzanotte responded saying that he had met with Henry Prodoehl on July 7 and that the bills -- although they "may on the surface, have appeared on the high side" -- had been documented in that meeting. He then "suggested" that the bills be paid "without further delay" (App. II-23).

In two letters dated July 9 and 10, 1980, Mr. Mullaney sent twelve disputed additional bills (totaling \$3,690) to Mr. Mezzanotte (App. II-24 and II-25). These followed a July 8, 1980 conversation between Mr. Mullaney and Mr. Mezzanotte concerning the billings.

During this period Mr. Mullaney had his staff perform an adjusting expense study to compare the average per file billings of Free State and Crawford, and Underwriters. Based upon a review of 700 files, the comparison figures were these:

Free State	\$405.14 per file
Crawford	\$ 73.34 per file
Underwriters	\$139.20 per file

Mr. Mullaney prepared a letter dated July 14, 1980 to Mr.

³¹ Although the Board minutes themselves do not reflect discussion or action on this topic, an Exhibit to Mr. Gray's written statement includes what appears to be a June 16, 1980 written memorandum by Mr. Mullaney to the Board which references the June 12, 1980 Board meeting and which discusses and defends the costs associated with the handling of the Reserve Insurance Company claims. Mr. Mullaney did not raise in this memorandum his billing disputes with Free State (App. II-44).

Mezzanotte to advise him of the average rates (App. II-26). However, Mr. Mullaney said that he discussed his comparisons and the letter with Mr. Mezzanotte by phone and that Mr. Mezzanotte instructed him not to send the letter. He told us that he followed Mr. Mezzanotte's instruction.

After these complaints by Mr. Mullaney, the following occurred:

1. Mr. Mezzanotte met again with Henry Prodoehl of Free State.
2. Mr. Mezzanotte, in a letter dated July 18, 1980, criticized Mr. Mullaney's handling of the bill dispute, including a conversation with Free State's Henry Prodoehl that had caused Mr. Prodoehl "great consternation" and "considerable physical discomfort" and instructed him to handle these problems in the future without involving Mr. Mezzanotte. The letter went so far as to suggest that Mr. Mullaney might go elsewhere if he could not "shoulder his responsibilities" (App. II-27).³²
3. Mr. Mullaney suggested that the entire Free State billing problem be referred to MIGA's Board and that all files previously assigned to Free State be taken back (App. II-29). In the July 18, 1980 letter, Mr. Mezzanotte "recommended to" Mr. Mullaney that Mr. Sharretts, MIGA's house counsel, was to handle all future billing problems with Free State in light of the breach in Mr. Mullaney's relationship with Free State (App. II-28 and II-29).
4. Charles Mullaney involuntarily left MIGA.

Not surprisingly, Mr. Mullaney claims that there was a direct link between his challenge to Free State bills and his

³² Although Mr. Mezzanotte, in this letter and in our interviews with him, expressed displeasure with Mr. Mullaney's involving him in this matter, his letters up until this point in the controversy show no such annoyance and in fact state the contrary.

involuntary departure. Mr. Mullaney told us that when he returned to MIGA to clear out his desk on the Monday following his "resignation" he saw all of the disputed Free State bills in the "out" basket approved for payment in full.

It was former Director Ramsey Gray who presided over Mr. Mullaney's departure from MIGA.³³ Mr. Mullaney claims that he received warnings from Preston Tull, the deputy receiver of Maryland Indemnity, (see Section III) and from Ramsey Gray about the problems he was creating by his criticisms of Free State and that later (on the Tuesday before he left MIGA) he was told by Mr. Gray that he was to resign by that Friday because "he had called Henry Prodoehl a crook," and because he was "causing too many problems." Mr. Mullaney said that he denied saying such a thing and that he asked for a meeting with Mr. Prodoehl. He states that Mr. Gray told him that "Henry doesn't want any meetings." Mr. Mullaney stated that at one point in that Tuesday conversation Mr. Gray had indicated to him that he might stay if he called Henry Prodoehl and apologized; however, before he had done so Mr. Gray called him back and said it was too late, and that he was fired.

Mr. Mullaney told us that he threatened to take the matter to the MIGA Board but that Mr. Gray told him that if he did so he would receive no employment references and no severance pay. He

³³ Mr. Gray's description of Mr. Mullaney's leaving MIGA will be discussed infra.

agreed to resign and on August 15, 1980 received severance pay grossing \$6,000. There is no indication in the Board minutes that the Board members considered or approved this payment. Mr. Bixler said that he had not been asked to consider the issue of severance pay for Mr. Mullaney, though Bixler was at that time a member of the Executive Committee as well as the Board of Directors.

Mr. Ramsey Gray, in the written statement with respect to which we were not permitted to conduct an interview, has said that Mr. Mullaney's departure came after Mr. Mullaney had been told by Mr. Gray that the "Executive Committee had lost confidence in Mr. Mullaney's ability to effectively handle the MIGA claims department," and specifically that the Executive Committee was "very disturbed that he [Mullaney] had seen fit to involve [the Executive Committee] in trivial matters which were entirely within his express authority." Mr. Gray claims that he told Mr. Mullaney that the "Executive Committee had decided that his further services with MIGA were very much in doubt, at least on a full time basis."

Mr. Gray writes that Mr. Mullaney then inquired about severance pay and that he told Mr. Mullaney that it was their "intention to give him adequate severance pay and that we had, in fact, done so with other former MIGA employees."³⁴ According to

³⁴ We were not shown any written MIGA policy concerning severance pay. Mr. George Darley said that when he was fired with no advance notice he and the other two adjusters Cont'd.

Mr. Gray's written account, Mr. Mullaney called Mr. Gray the next day and "advised [him] that he had made a decision to resign." Mr. Gray immediately contacted MIGA's Administrative Assistant and told her to draw two checks payable to Mr. Mullaney. The first the balance of his weekly pay check, the other two months' severance pay. Mr. Gray hand-delivered the checks to Mr. Mullaney on the following day.

We asked Mr. Mezzanotte who was on the Executive Committee at the time about Mr. Mullaney's leaving; he did not tell us about Executive Committee action or decision on the matter. He said that he was out of town at the time. Mr. Bixler, the other member of the Executive Committee at the time of these actions, said that he was not consulted. We were told that there are no records of Executive Committee meetings for this time or for any time prior to September 1980. We can only conclude that while Mr. Gray said "the Executive Committee" acted, Mr. Gray did in fact act on his own.

We have discussed with Mr. Mezzanotte in two separate interviews the questions raised by Mr. Mullaney concerning Free State billing.³⁵ In the first interview Mr. Mezzanotte discussed Mr.

were given "a few days worth" of severance pay. Mr. Mezzanotte said that he had no part in the issue of the Mullaney severance pay but that he had paid severance pay to Mrs. Shirley Dugan when she left MIGA in 1979. He indicated Mrs. Dugan had been given severance pay equal to four weeks' salary. Mrs. Dugan, who told us she was asked to leave, confirmed that she was paid four weeks salary as severance pay. She was not aware that severance pay was a MIGA policy and in fact said that one of her secretaries had been terminated without any such payment.

³⁵ Mr. Mezzanotte did not tell us of any sinister reason why Mr. Mullaney might have given Cont'd.

Mullaney's complaints about excessive billings. In the second, Mr. Mezzanotte claimed that he was never asked to review the "excessiveness" of the work done but only the documentation of those bills. In both interviews, he told us that he told Mr. Mullaney to use whatever company he wanted to and to stop using Free State if he was dissatisfied. Mr. Gray, in his written statement that we were not able to question him about, also made the point about Mr. Mullaney's broad authority to handle the claims department.

We have reviewed the minutes of MIGA's May 31, 1979 meeting in which the Board passed Chairman Moore's motion to "give Mr. Mullaney carte blanche authority with true fiscal policy" and to advise Mr. Mullaney that the Board would "endorse...any act he undertakes in his professional judgment that affects the

discussed above, Mr. Mullaney said something to the effect that Free State was making so much money that he (Mullaney) ought to buy himself some letterhead and go into the business of adjusting MIGA claims. Mr. Mezzanotte's counsel said that this disturbed Mr. Mezzanotte, although he was not certain whether Mr. Mullaney was joking or not. Mr. Mezzanotte told Mr. Mullaney that he would pretend that it had not been said.

Mr. Mullaney, through his counsel, gave us a different account of this meeting. He said that he went to Mr. Mezzanotte's office to discuss problems with Free State billings and early in the conversation Mr. Mezzanotte asked the magnitude of the Free State billings. When he responded giving the large amount that Free State had been paid, Mr. Mullaney recalls that Mr. Mezzanotte made a joke about going into the adjusting business since it was so lucrative. Mr. Mullaney joined in the joke and said something that agreed with what Mr. Mezzanotte had said. Mr. Mullaney said they then went on with their meeting.

letter to Mr. Mullaney telling him that he was to have that authority to run the claims department (App. II-45).

As to the substance of Mr. Mullaney's complaints, Mr. Mullaney says they concerned Free State's excessive billing. Mr. Mullaney's letters both to Mr. Moore and Mr. Mezzanotte and his survey showing substantially higher average bills of Free State are strong evidence that Mr. Mullaney's concerns went to excessiveness and not merely the lack of proper documentation. We understand from Mr. MIGA's counsel, Mr. Gisriel, that it is Mr. Mezzanotte's position that he might have misunderstood the nature of the Mullaney complaints, because he did view the problem as concerning documentation.

As to his freedom to use whatever company he wanted, Mr. Mullaney said that he did not feel that he had authority to make assignments in light of Mr. Moore's express direction about the use of Free State. When Mr. Mezzanotte, who became Chairman in May of 1980, told him he was free to use whomever he chose, Mr. Mullaney told Mr. Mezzanotte about the Moore instruction. Mr. Mezzanotte told him he was free of any restriction that Mr. Moore may have placed upon him (App II-30). Mr. Mezzanotte confirmed this conversation. However, Mr. Mullaney told us that he had little new work to assign and that he did not believe he had the authority to reassign cases which had previously been assigned to Free State. Moreover, shortly afterwards, Mr. Mezzanotte told Mr. Mullaney "... I would recommend that you refrain from

discussing the propriety of the [Free State] billings and delegate future discussion to our Attorney of Record, Mr. Doug Sharretts." (App. II-27) As to Mr. Mullaney's general freedom to run the claims department, Mr. Mullaney told us that he felt that he had complete freedom in many areas. He said that he interpreted Mr. Moore's June 27, 1979 letter as giving him the necessary authority to fire the staff adjusters, but not the authority to disregard Mr. Moore's June 21, 1979 directive concerning assignments to Free State.

While Mr. Moore was Chairman, Mr. Mullaney told us that he felt he had virtually no freedom with regard to Free State. When Chairman Mezzanotte countermanded Mr. Moore's instruction about assignments, Mullaney felt he had been given authority to make assignments, though he had almost no cases to assign. Mr. Mullaney did not feel he had authority to withdraw cases from Free State. Nor were the cases withdrawn from Free State after Mr. Mullaney left MIGA. Even though Mr. Mezzanotte had indicated to Mr. Mullaney in his July 18, 1980 letter that Free State was going to return all files, that never occurred.

Since Mr. Mullaney's departure, Mr. Douglas Sharretts (under the title of Executive Director) has assumed the duties formerly performed by the claims manager. Mr. Sharretts, a long time criminal law practitioner, was hired as MIGA's house counsel in

mid-1979.³⁶ Mr. Sharretts has continued to use the services of Free State for all MIGA adjusting work. Mr. Sharretts has raised an occasional criticism about a Free State bill but he admits that he has pursued no adjustment of any billing that he considered to be a problem.

(c) Payments to Free State

In addition to the outside adjusting work done by Free State (for which it has been paid \$202,943) Free State was paid by MIGA from 1979 to 6/30/81 the following:³⁷

\$28,845 for calculating unearned premium, primarily for the Reserve insolvency³⁸

³⁶ Prior to coming to MIGA, Mr. Sharretts had for over sixteen years shared law offices with Commissioner Birrane, most recently on the 28th floor of 222 St. Paul Place.

³⁷ Free State also does the adjusting work for LHIGA. The company was selected by LHIGA's Board as the low bidder during a bid process in which both it and Crawford & Company participated. In Henry Prodoehl's written bid on behalf of Free State, he listed both Ralph Moore and Albert Mezzanotte as references as to the quality of Free State's work. LHIGA Director George Bereska contacted Mr. Moore, who by that time was Deputy Receiver of ACLIC. Mr. Moore gave Free State a favorable recommendation.

LHIGA has no written contract with Free State and billings show that Free State is billing in excess of the bid rate of \$18.00 per hour. Free State has been paid a total of \$79,811.60 by LHIGA from August, 1980 through October, 1981.

³⁸ Prior to 1979 the calculation of unearned premiums had been done manually by MIGA's administrative assistant. Later, Free State was hired to do the calculation. Free State then subcontracted the work to Applied Data Processing (ADP), a computer company. ADP did the computer work that calculated the premium refunds and prepared the refund checks. While we were able to obtain from MIGA the amount it paid to Free State, we were not permitted to interview Free State's representatives to find out what Free State paid ADP for the subcontract.

Mr. Bixler told us that the MIGA Board did discuss the use of computers for processing unearned premium claims as a cost saving measure and that the Board was provided with several names of computer companies who could do that work. He said that Cont'd.

\$ 2,007 for travel in connection with pickup of files
for Reserve insolvency

\$ 4,961 for file review³⁹

The total amount that has been paid to Free State by MIGA is \$238,756 as of June 30, 1981.

While we do not have complete financial data on payments to Free State since June 30, 1981, we do have partial information as follows:

\$42,103 through January, 1982 for partial review of worker's compensation files which were transferred at Commissioner Birrane's instruction from Maryland Indemnity when the MIGA statute was changed in July 1, 1981 to give MIGA responsibility for workers compensation claims.

\$ 1,016 for moving the worker's compensation files from Maryland Indemnity to Free State's offices.

Therefore, the total amount of payments from MIGA to Free State that we are able to document is \$281,875. All but \$90 of this total has been paid since January 1, 1979.

the Board was not told that Free State was the party to whom the contract was to go. In fact, he could not recall Free State's having been mentioned in the discussion.

³⁹ This file review was conducted at the time Charles Mullaney left as Claims Manager. Free State's representatives prepared written descriptions for Mr. Sharretts (who assumed the claims manager duties). MIGA records show that there were approximately 315 open files at this time. That number, however, includes files that Mr. Sharretts had been handling as house counsel and those assigned to outside counsel.

5. Claims Expense - Counsel

Prior to 1979, MIGA's Board, and later its Executive Committee, created a roster of attorneys to whom MIGA cases in litigation were assigned. That roster contained the names of a number of insurance defense firms.

After January, 1979, that roster was expanded but the assignments were no longer made to all of the attorneys on the roster. Mr. Mullaney told us that at around the same time he was instructed to assign work to Free State, he was also told by Ralph Moore to add the name of Stanford H. Franklin and the firm of Simmons and Fields, to the roster. Mr. Mullaney says that he knew both Mr. Robert Simmons and Mr. Russell Fields and knew both to be close friends of Mr. Moore. He added the names as requested and began immediately to assign all new cases to them.

We asked Ralph Moore how Mr. Franklin and the firm of Simmons and Fields were added to those receiving MIGA work. At one point in the interview he seemed to agree that he had suggested the addition; however, at a later point in the same interview, he said he did not know how those names came to be added.

We asked Mr. Douglas Sharretts, MIGA's Executive Director and the person now responsible for making the assignments, what the current arrangements are for assigning cases to counsel. He

furnished us a long roster of lawyers containing over a dozen names. However, on further questioning, Mr. Sharretts told us that he assigns all MIGA work to Stanford H. Franklin, Patrick O'Doherty, and the firm of Simmons and Fields. Mr. O'Doherty told us that to the best of his recollection he has never defended a MIGA case and that any assignments to his firm were more probably made to one of his partners.

6. Rental Costs

We have already noted that MIGA's office expenses rose substantially in the post January 1979 period. Rental cost was an office expense category of substantial increase. That increase was brought about by a relocation of MIGA's operations from two locations in downtown Baltimore to two locations in Towson in 1979.

Until the move, MIGA's administrative offices had always been in the One South Calvert Building, the same building where the State Insurance Division is located. The claims department operated from space rented in the Maryland Indemnity Building across the street from the MIGA administrative offices.⁴⁰

⁴⁰ The One South Calvert lease executed on 12/30/76 would have run through 12/30/79 and had an option to renew for a second three year period through 12/30/82. The rental for the approximately 900 square feet was \$410 per month and included all utilities, cleaning, etc. Had the option to renew been exercised, the rental would have risen to \$450 per month.

For approximately 800 square feet in the Maryland Indemnity Building, MIGA paid \$371.25. That amount, too, included electricity, etc. We located no written lease; however, the MIGA Board minutes for 7/24/79 have an entry indicating that MIGA had been Cont'd.

One reason given for the MIGA move to Towson was that space for the administrative office was inadequate. Director Granville Bixler told us the move was made because Towson would be more convenient for the Directors who attended periodic director's meetings.

Mr. Mullaney, who was claims manager at the time of the move, and Shirley Dugan, who was then MIGA's Administrative Assistant, told us that they were assigned the task of locating space large enough to house the administrative and claims operation together. They surveyed available office space, decided upon space large enough to house both the claims and administrative offices at 8508 Loch Raven Boulevard in Towson, and arranged the lease for that space.

However, before the lease for the Loch Raven Boulevard space was signed, Mullaney and Dugan were told to lease a smaller amount of the space at the Loch Raven location, enough to house only the claims operation, not the administrative office.⁴¹ A separate lease on a residential condominium at the Towson Towers, was arranged by then MIGA Director James Hightower, for the MIGA administrative office. Mr. Mullaney and Mrs. Dugan were not

offered "very favorable lease terms" for that location.

⁴¹ The space at 8505 Loch Raven Boulevard is rented under two separate three year leases. The first lease for 1135 square feet at \$710 per month was executed on August 20, 1979, the second for an additional 566 square feet across the hall for \$353.75 per month was executed on October 2, 1979. Both leases require MIGA to pay all utilities.

MIGA subleases the space under the second lease to ACLIC on a month to month basis for \$353.75 per month.

involved in the decision to house MIGA's operations at two separate locations nor were they involved in the selection of the office on the 12th floor of the Towson Towers. In fact, their original survey of available office space had included office space then being rented in the Towson Towers by the real estate firm of O'Connor & Flynn, the realtor who handled commercial leasing for the Towson Towers on all floors except the 12th and 13th floors (App II-31). The rental agent for the 12th floor condominium was MDIC.

Mr. Hightower, who told us he saw "no need for any interview", sent a written statement which described how he had selected the Towson Towers office. He wrote that while on the lookout for suitable office space he had a meeting with one of his company's attorneys, Stanford Franklin, at Mr. Franklin's Towson Towers office. Mr. Hightower inquired about available space in the same building and "Mr. Franklin suggested that [he] get in touch with Mrs. Van Wright [of MDIC]." In fact, Mrs. Van Wright and MDIC have offices in the same suite as Mr. Franklin.⁴² Although Mrs. Franklin was willing to give us some information on other matters, she refused to disclose her rental commission on the MIGA rental.

⁴² We must report that Mrs. Van Wright of MDIC has told us that although Mr. Franklin is both Director and Vice President of MDIC, he derives no financial benefit from the company. She did, however, tell us that Mr. Franklin receives from MDIC rent free use of office space in the Towson Towers suite occupied by MDIC. Mrs. Van Wright told us that this use was permitted because Mr. Franklin took over some of her late husband's clients whom he meets at the Towson Towers location.

MIGA rented the Towson Towers space through MDIC. The lease was signed by Messrs. Hightower and Moore. Mr. Moore told us that he had had no role in selecting the space and that he had not even seen it prior to his signing the lease.⁴³ Both Ralph Moore and Albert Mezzanotte told us that they were unaware of Stanford Franklin's connection with MDIC.

Several months later, Mrs. Sylvia Franklin, who had been recommended for MIGA employment by Mr. Hightower and who was hired in September 1979 (shortly thereafter she became the administrative assistant), recommended to Mr. Hightower that MIGA rent the remainder of the condominium suite, since the first lease had included only part of the total unit. That space was also leased through MDIC.

⁴³ The space at the Towson Towers is rented under two separate leases. The first executed on July 20, 1979 rented the first part of the residential apartment which has been converted into office space. We have been told that MIGA had been making use of the back portion of the apartment even before it had been formally leased. That part of the apartment was leased by lease dated January 31, 1980. The two leases on the Towson Towers office for a combined square footage of 1270 square feet (excluding the balcony) run concurrently through 1989. The combined rental remains \$1,100 per month until 1984, then it increases to \$1,350 per month for the remainder of the lease term.

We had originally been inclined to subtract from the gross square foot totals for the unit those portions that were not useable as office space, i.e., two full baths, a full kitchen, and the balcony. When MIGA's representatives protested, we contacted a Towson realtor who also rents office space in the Towson Towers to ascertain the practice. Since we were informed that it is customary in renting such units to include baths and kitchens but not a balcony, we have used the exterior dimensions of the unit as those dimensions are shown in the Baltimore County land records. Those dimensions support a square footage of 1270, that total is less than the 1494 (1391 plus balcony) that MIGA representatives gave us but is larger than that derived from the actual measurement of the unit by MIGA representatives (approximately 1230).

7. The Staff

MIGA'S Staff has grown since January 1, 1979.⁴⁴ However, if the use of temporary help in the pre-1979 period is considered, the increase, in terms of number of employees, has not been great. The salary figures after January, 1979 are considerably higher than in MIGA's first seven years. This increase can be explained by several factors:

The position of house counsel (later merged into the Executive Director position and occupied by Douglas N. Sharretts) now paying over \$40,000 per year, was only created and filled after 1979;

The salary and benefit packages of MIGA employees were substantially enlarged in this same period;

Additional secretarial help which had been hired on an as needed⁴⁵ temporary basis before 1979 was hired permanently after;

MIGA decided to create first a new full time position of claims coordinator and then one for detection and prevention of insolvencies. Doborah Corum held first the claims

⁴⁴ LHIGA, the guaranty association for life and health insolvencies, has no full time staff. LHIGA has a contract with the ACLIC Deputy Receiver Ralph Moore to receive certain services for which he is paid \$25 per hour. Although we were told that the agreement has been reduced to writing and that Mr. Moore submits monthly bills, we were not permitted access to that information. LHIGA invoked a confidentiality provision of its statute and Mr. Moore refused to consent to turn over any personal records on the arrangements of the amount of payments he has received to date.

LHIGA pays Ms. Marge Nolan, its administrative assistant, \$8 per hour to do bookkeeping and other administrative duties. Until recently, Ms. Nolan did this work, without charge.

⁴⁵ Prior to 1979, MIGA had obtained experienced temporary help during busy periods by hiring off duty employees of the Maryland Insurance Division. On September 28, 1978, Commissioner Birrane requested an opinion of the Maryland Board of Ethics on the appropriateness of this practice. (App. II-32) That Board concluded that employees should not work for both MIGA and the Insurance Division.

coordinator position then the detection and prevention slot. Miss Corum left MIGA in early 1981.

We found almost no MIGA hirings that came through neutral selection methods, i.e., newspaper advertisements, employment agencies, or job banks. Instead, most of the new staff members seem to have ties either to a MIGA Board member or a person already on MIGA's staff. That was certainly true of Charles Mullaney, who was a friend of Ralph Moore. It was also true of Deborah Corum, who was also a friend of Chairman Moore. Ms. Corum, who became MIGA's first claims coordinator and was later appointed to a newly created position in charge of detection and prevention of insolvencies, was a friend and former co-worker of Ralph Moore. Mr. Moore (then MIGA's Board Chairman) recommended her for the claims coordinator job, a job for which he wrote the job description and set the requirements. Ms. Corum was the only member of the Claims Department who reported directly to the Board Chairman (Mr. Moore) rather than to the Claims Manager.

Only when there was no involvement of the MIGA Board did we find use of a neutral solution method. Mrs. Shirley Dugan, MIGA's administrative assistant from April to October of 1979, advertised and interviewed before hiring a secretary. However, when it had become necessary for her to replace that secretary, the Board intervened and the procedure changed. Mrs. Dugan received a phone call from Sylvia Franklin expressing interest in the job. That call came on the same day Mrs. Dugan had discussed the need to fire her secretary with Directors Moore and

Hightower. Mrs. Dugan was later advised that Mrs. Franklin was her new secretary, though Mrs. Dugan had not interviewed Mrs. Franklin. Mrs. Franklin began work as Mrs. Dugan's per year secretary in September, 1979. Three weeks later, Mrs. Dugan was terminated by Director Albert Mezzanotte, and Mrs. Dugan was replaced in her \$20,000 per year administrative assistant job by Sylvia Franklin.

Mrs. Dugan liked her job, was not aware of any substantial inability of her work and told us she was forced to leave despite the fact that her husband was unemployed. Mr. Mezzanotte told us that Mrs. Dugan "left", but did not tell us that he had asked her to do so. He told us that Mrs. Franklin then moved naturally into the job of administrative assistant. (Mrs. Franklin resigned from MIGA on May 24, 1982.)

Mr. Douglas Sharretts was selected first in June 1979 as MIGA's house counsel and later, when Mr. Mullaney left, as MIGA's Executive Director. To our knowledge, Mr. Sharretts is the only MIGA staff member who was a close friend of Commissioner Birrane. The two had maintained an office sharing arrangement for approximately 16 years, an arrangement that we were told ended when Mr. Sharretts came to MIGA.

Mr. Mezzanotte told us that the assignment to search for house counsel was given to Mr. Ramsey Gray (immediately upon his joining the Board), and that Mr. Gray presented the Board with

only Mr. Sharretts name for consideration saying that many had been considered but that their names were confidential. The Board accepted Mr. Gray's candidate. We do not know who else he considered for the position (starting salary \$37,500). We were furnished copies of two letters in which lawyers declined the position because of its uncertain tenure (App. II-33 and II-34). One of the letters was sent by Russell Fields of the firm of Simmons and Fields, mentioned earlier.

Prior to his appointment as house counsel, Mr. Sharretts had been a staff attorney with the Public Defender's office and a private practitioner. Mr. Sharretts' practice was primarily criminal defense work. MIGA's counssel told us that Sharretts had represented Liberty Mutual and Aetna insurance companies when he was an associate at the firm of Semmes, Bowen & Semmes, and had also handled some tort cases in his private practice. When we interviewed Mr. Sharretts, however, he was unable to l any insurance work after his 1936 law school graduation, and we note that his time at Semmes, Bowen & Semmes occurred over 40 years ago. We do know, however, that he had done some subrogation work for the Maryland Indemnity after it went insolvent.

Mr. Sharretts told us that he learned of the MIGA job opening at a regular luncheon group that he attends. The members, he told us, include Commissioner Birrane, Preston Tull, and Bob Simmons (of Simmons and Fields). Since Mr. Sharretts was interested in the MIGA position, he prepared a resume and sent it

to all Board members. Mr. Sharretts says that the only Board member he knew at that time was Mr. William Marquess, a 1979 Birrane appointee to the Board. He was interviewed for the position by Mr. Marquess and Ramsey Gray. The MIGA Board minutes show that the Board was advised by Mr. Gray at its May 31, 1979 meeting that he had one viable candidate (we assume it was Mr. Sharretts). He was instructed to continue his search. No further Board action on Mr. Sharrett's selection is reflected in the minutes. However, the June 28, 1979 minutes do show that Mr. Sharretts had been hired by that time. In those minutes the Board is shown to have unanimously voted that no job description would be needed for Mr. Sharretts' position.⁴⁶

Whatever the circumstances of the Sharretts' hiring, we do not find evidence that the MIGA Board decision to utilize house counsel was a poor business decision and, in fact, we have been furnished evidence showing that the decision has resulted in cost savings to the association. We found no evidence that Mr. Sharretts' performance in the work he has done for MIGA as an attorney has failed to meet acceptable standards.

8. Other Outside Services

We will comment briefly on the selection of Mr. Charles Witzen, MIGA's bookkeeper, and Mr. Andrew Caldwell, of Andrew

⁴⁶ Prior to joining MIGA, Mr. Sharretts had terminated his office sharing arrangement with Commissioner Birrane and sold his law library to MIGA for \$3,500 (App. II-35).

Caldwell and Associates, the auditor who has conducted MIGA's audits for the years 1979 and 1980. Both of these men are discussed here primarily because they appear again in both the Maryland Indemnity and ACLIC insolvencies -- again as bookkeeper and auditor.⁴⁷

Mr. Charles Witzen became MIGA's part-time bookkeeper in 1979 at a rate of \$20 per hour for a 15 hour week. As the former assistant treasurer of Maryland Indemnity, he appears to have the necessary qualifications for the job. Mr. Witzen is also a part-time consultant to the Maryland Indemnity insolvency (since February 1979) and part-time bookkeeper for the ACLIC insolvency (since July 1980).

Mr. Andrew Caldwell had been asked by MIGA Chairman Ralph Moore to conduct the MIGA audit even before MIGA's Board voted in April 1980 to change the audit provision of the plan of operation to delete the requirement that a committee of insurers representatives do the audit. The plan, as amended, requires that the auditor be an actuarial expert and a Maryland certified public accountant. We asked both Mr. Mezzanotte and Mr. Moore what the reason was for the change. Mr. Mezzanotte said that he did not know; Mr. Moore said the change came because the Board wanted a local auditor who could spend more time on the audit.

⁴⁷ Of the entities we have discussed in this report, only LHIGA does not use Mr. Witzen and Mr. Caldwell for these services.

Since there are many "local" auditing firms, the reason for the selection of Mr. Caldwell's from among them was our next inquiry. Mr. Mezzanotte said that Mr. Moore selected Mr. Caldwell. Mr. Moore gave no reason for the selection but said he was happy with the choice. The reason for Mr. Caldwell's selection has never been explained to us. There was no bid process or canvass and we are not aware that any other firms were considered. While Mr. Caldwell is a Maryland certified public accountant, he does not satisfy the plan requirement that an "actuarial expert" be hired. Moreover, he had no particular property or casualty insurance auditor's experience prior to receiving the MIGA job, although he is now doing the accounting/auditing work for both the Maryland Indemnity and ACLIC insolvencies. He had done accounting work for Free State on a regular basis since 1977, and he continues that employment.

Mr. Caldwell says that he did not approach MIGA for the job. Rather he received a telephone call at his home in March 1980 from MIGA Chairman Ralph Moore. Mr. Moore offered him the job and he immediately accepted it.

9. Director's Expenses

The 572% increase in director's expense that occurred from 1/1/79 to 6/30/81 over the previous seven year period is almost entirely due to the level of reimbursement to directors for travel and entertainment expenses.

Prior to 1979, under the chairmanship of Mr. William Rogers, directors did not travel out of state at MIGA expense, nor were any entertainment expenses paid. Mr. Rogers explained to us that such things were, in his view, inappropriate charges to make to the Association to be passed on to the member insurers.⁴⁸ Subsequent MIGA chairmen as well as several MIGA Board members defended reimbursement for attendance at National Association of Insurance Commissioners (NAIC) and National Committees of Insurance Guaranty Funds (NCIGF) meetings because of the need for those who attend to learn more about handling insolvencies. We are not in a position to question the MIGA Board's decision to attend these meetings. We have interviewed (or received written statements from) a number of MIGA Directors and former Directors who served on the Board after April, 1979. Each of them has told us that such trips benefit the Association.⁴⁹

Regardless of the possible benefits of such attendance, the actual travel and entertainment expenses associated with such trips and entertainment expenses in general raise serious ques-

⁴⁸ On the contrary, LHIGA's Board has taken the position that its directors do not attend these meetings at association expense. In LHIGA's eleven year history, only a single travel expense (other than to LHIGA Board meetings) has been paid. In 1980, LHIGA Chairman Emmett MacCubbin attended a Florida NAIC meeting at the request of Commissioner Birrane for the purpose of discussing the ACLIC insolvency with the Tennessee Insurance Commissioner. Mr. MacCubbin went to Florida on one day and returned to Baltimore the next. His reimbursement of \$376.95 included no "entertainment expense." LHIGA's entire director's expense for 1980 totaled \$689.30 and for 1981 was \$240.70.

⁴⁹ While it had been suggested that the travel to such conventions was tied to increased claims payment activity, the dates of the trips do not support that contention. Few occur in 1979, MIGA's heaviest year of activity. Yet there is a decided upturn in such travel in 1980 and 1981 when claims payments are declining.

tions about the lack of control over such expenses. MIGA's plan of operation was not amended when the MIGA travel policy changed to specify the amount and method of reimbursement as it statutorily required. MIGA's Executive Committee minutes for October 15, 1980 state that prior approval for all meetings, conferences and seminars must be obtained from the Chairman and Vice Chairman. No criteria are stated for approving a request. Nor is there any apparent control over the expenses incurred at such meetings.⁵⁰

For example, in May, 1981 Director Ramsey Gray attended a NAIC Zone V meeting in San Antonio, Texas.⁵¹ He stayed a total of four days for which he was reimbursed a total of \$2,038.36. Included in that reimbursement were Mr. Gray's charges for \$945.50 in "entertainment expense". No person at MIGA received a breakdown of these expenses showing how the money was spent or a list of who was entertained. All that Mr. Gray provided were four stub type receipts on which the following amounts had been written in: \$336; \$274.50; \$251; and \$84. This "entertainment" expense was reimbursed, in addition to Mr. Gray's plane ticket,

⁵⁰ MIGA's records show that Miss Corum attended 4 NAIC and 1 NCIGF meetings in the 12 month period beginning April 1980. Director Gray attended 3 NCIGF and 2 NAIC meetings from February, 1980 through May, 1981. Mr. Mezzanotte also attended 3 NAIC and 2 NCIGF meetings in the period from December, 1979 to March, 1981. Ralph Moore from June 1979 until his appointment as Deputy Receiver for ACLIC in May 1980, attended two NAIC meetings and one NCIGF meeting. Another MIGA Director to attend one of these conferences was Mr. Hightower, who attended the single NAIC conference in Los Angeles.

⁵¹ In addition to the annual meetings of the NAIC, MIGA representatives have attended regional or zone meetings of that organization. Zone V included several Southwestern states. Maryland was in Zone II.

hotel, and \$55 per day meal allowance (App. II-36).

Nor was this Mr. Gray's only reimbursement for "entertainment" expenses while at one of these conventions. His reimbursements for his September, 1980 trip to the San Diego NAIC Zone VI meeting included \$662 in entertainment expenses (App. II-36).

We would have welcomed the opportunity to question Mr. Gray in detail about these expenditures and the others for which he was reimbursed by MIGA. He refused to be interviewed; therefore, we are left with his written statement about travel and entertainment which says as follows:

"I can only say that I was extremely active, principally because I was Vice Chairman of the Board and Chairman of the Executive Committee and that I incurred expenses commensurate with the expenses generally incurred by insurance executives throughout the country."

Mr. Gray also noted that his expenses are recoverable from the receiverships for which MIGA pays the claims and suggested that certain of his expenses have already been paid by the liquidator of the Reserve Insurance Company "without questioning the propriety of same." We have interviewed Frank Csar, the Illinois liquidator of the Reserve insolvency, and have reviewed MIGA's forms requesting reimbursement. MIGA has not yet requested nor has it received reimbursement for any travel expense. Mr. Csar indicated that his receivership makes reimbursement (including reimbursement for travel) so long as the

totals are within the average range billed by other insolvencies. While Mr. Gray also said that the various meetings that he attended concerned the Reserve insolvency, he did not explain so. Moreover, Mr. Csar, who is currently in charge of ten Illinois insolvencies including Reserve, told us that he does not attend NCIGF meetings nor NAIC meetings, except annual meetings and those for the Chicago Zone.

The only reference Mr. Gray made to his over \$2,000 in expenses including the \$945.50 undocumented "entertainment expense" for his San Antonio trip was as follows:

"When I was in San Antonio, attending an NAIC function on behalf of MIGA, I was the sole MIGA representative. It was, therefore, necessary for me to coordinate repeatedly with other attendees known to me, in order that I could keep fully conversant with the day-to-day decisions of the NAIC,, which directly affect all segments of the insurance industry (App. II-44).⁵²

Mr. Gray's comment clearly provides no explanation of his undocumented "entertainment" expense, and, even more importantly, Mr. Gray has not suggested that there was any MIGA review or oversight of his expenditures of MIGA money. Mr. Gray also failed to comment on his being reimbursed by MIGA for attending a March 1981 NCIGF meeting which NCIGF records do not show him as attending.

⁵² We note that Commissioner Birrane and ACLIC Deputy Commissioner Ralph Moore were also in attendance at this same convention and according to what they have told us, they too would have been interested in programs on insolvencies.

The principal expenses for MIGA travel were paid during 1979-1981 to the following:⁵³

Mr. Mezzanotte (12/79 - 6/81)	Total \$5,712.05
Mr. Gray (2/80 - 6/81)	Total \$6,625.98
Mr. Moore (6/79 - 5/80)	Total \$2,571.20 ⁵⁴
Miss Corum (4/80 - 6/81)	Total \$2,398.60 ⁵⁵
Mr. Hightower (one trip only)	Total \$1,259.85

Moreover, on several occasions MIGA trips to the NAIC and NCIGF conventions extended beyond the dates of the convention. NAIC annual meetings extend for five days, but the fifth day is not open to guaranty association representatives. NCIGF records show that its meetings are one day or two days in length, and the two day meetings are scheduled so that the first day's agenda does not begin until after noon and the closing day agenda closes by 4:40. In short, many of the extended convention stays seem

⁵³ A complete breakdown of the travel reimbursements for the individuals listed can be found in the Appendix. (App. II-37 to II-40A)

⁵⁴ Mr. Moore's travel to conventions for the period June 1979 to October 1981 for both MIGA and ACLIC totaled almost \$11,000.

⁵⁵ We were told by Mr. Moore that Miss Corum's travel was to aid her in the detection of insolvencies. Since Miss Corum was unwilling to be interviewed, we were unable to ask her how travel to six cities aided her in this effort. She did however provide a written statement in which she said she attended "sessions dealing with the history and causes of impairments. In that manner, [she] could be aware of potential insolvencies in other states, which might affect MIGA." (App. II-47) While MIGA declined to show us a copy of her final report (Miss Corum has recently left MIGA) because of its sensitive nature, its counsel told us that it contained 312 pages and listed 1470 companies. We are told that the report lists the following sources: Special Reports to the Insurance Commissioner, Official Reports to the Insurance Commissioner, the Best books, the National Underwriters and NAIC data basis and ISIS (The Early Warning System). All of these sources¹ are and were available to Miss Corum through the Maryland Insurance Commissioner's office. We were told of the use of no source that required travel outside of Baltimore.

questionable, but there was no effective oversight. Moreover, the MIGA Board doesn't seem to have considered whether it was truly necessary to have multiple MIGA representatives attend the same convention.

Instances where the stay of MIGA's representatives exceeded the convention agenda include Mr. Moore's five nights at the three day NAIC Zone III meeting in Lake Buena Vista, Florida (also attended by Miss Corum who also appears to have stayed five nights although she did not seek reimbursement for a hotel); Mr. Moore's three nights for a 9:30 to 4:00 NCIGF meeting held at O'Hare Airport in Chicago (also attended by Mr. Gray who also stayed three nights); Miss Corum's six night stay in San Diego California at a four day NAIC Zone VI meeting (also attended by Messrs. Gray and Mezzanotte who also stayed six nights); Mr. Gray's three night stay in Atlanta for a one and one-half day meeting which NCIGF records do not show he attended.⁵⁶ Mr. Mezzanotte also attended the Atlanta NCIGF meeting. The NCIGF confirms his attendance and he stated on his reimbursement request that he had lengthened his stay to four nights to permit him to meet with Mr. Henry Reid of Atlanta, the claimsman who had just completed a review of the MIGA claims procedures); Mr. Mezzanotte stayed seven nights at the Los Angeles annual meeting of the NAIC, which Mr. James Hightower also attended - - the

⁵⁶ Mr. Gray's reimbursement request said that he extended his trip by several days to meet with Commissioner Birrane, Ralph Moore and Stanford Franklin who were in Atlanta at the time. No purpose for such meeting was shown, nor was it explained why he could not have conducted any meetings in Baltimore.

convention, had four days of meetings open for MIGA attendance.⁵⁷

Entertainment expenses is another area where we discovered significant increased expense and little indication of control by MIGA's Board.⁵⁸ Requests by Directors for reimbursements were often paid without any explanation of any business purpose for the expenditure.

The principal recipients of entertainment expense reimbursements were Ralph Moore and Ramsey Gray. Complete breakdown on those reimbursements are attached to this report (App. II-36 to II-40).

Mr. Moore received entertainment reimbursements from MIGA⁵⁹ as follows:

1979	\$1,563.85
1980	\$ 961.62

⁵⁷ In his request for reimbursement, Mr. Mezzanotte indicated that he had extended his trip in order to qualify for an excursion fare. He indicated that the saving was \$260 and it appears that a saving in that amount may have been greater than the costs associated with two extra nights of lodging and expenses.

⁵⁸ Entertainment expenses for purposes of this discussion do not include charges made while traveling but include only entertainment in the Baltimore area.

⁵⁹ Mr. Moore began receiving reimbursements on April 20, 1979 and his last was May 14, 1980, when he left to become ACLIC Deputy Receiver. William Rogers, MIGA chairman until his term expired on April 15, 1979, told us that he had not permitted reimbursement of this type.

Mr. Gray received reimbursements as follows:

1979	\$ 247.15
1980	\$ 907.40
1981	\$1,104.03 ⁶⁰

Mr. Gray, in his written statement, explained his expenditures as follows:

When I hosted business dinners, I simply sought out a locale that was geographically convenient to the parties with whom I met. I incurred expenses in restaurants which offered a business ambiance conducive to the discussion of a myriad of topics concerning the Guaranty Association.

10. The Change in Audit Procedures

After having its first seven years of operations audited and examined by a three person Audit Committee made up of representatives of its largest member insurers, MIGA in 1980 changed its audit procedure for the review of MIGA's operation in 1979 and thereafter.

The final report by the Audit Committee, completed in March 1979, had several criticisms of MIGA's operation:

⁶⁰ Mr. Gray's reimbursements included \$392.50 for a dinner at the Tom Jones restaurant reimbursed to Mr. Gray which was attended by Mr. Gray and six others, including Ralph Moore, Deborah Corum, Sylvia and Stanford Franklin and Henry Reid of Atlanta Casualty, who would three weeks later conduct the claims review portion of MIGA's annual audit. No business purpose was stated on the request for reimbursement. (Check No. 1551 paid January 21, 1981 App. II-42).

1. The report criticized rehandling and duplicative handling of claims files which caused higher adjusting costs. The auditors suggested that the Board implement periodic review by claims personnel of member insurers.
2. The report expressed concern over expenses totaling \$10,690.50 and stated that the Board should review such payments to determine whether they were reasonable and proper expenditures for a guaranty association to make.

The Audit Committee also stated, in this its first report to criticize MIGA's operation to any large extent, that it would welcome the opportunity to take another independent look at MIGA's operations. Such an opportunity never came.

The amendment to MIGA's plan of operation changing its audit procedure was a fundamental one, altering not only the identity of the auditor but also the form the future audits would take. Previous audits by the Audit Committee had opened MIGA's entire operation to review by a group of auditors with property and casualty insurance expertise. The review had consisted both of a financial audit and an operational review, or audit of management functions. As can be seen from the description of the final report it submitted, the Audit Committee went beyond a mere review of the financial statements and examined the appropriateness of expenditures. Moreover, the Committee reviewed claims handling with an eye toward cost effectiveness.

The Audit Committee had conducted a financial audit, had reviewed the propriety of expenses, and had reviewed the claims

operation including the expenses associated with claims. What replaced it was a bifurcated process comprised of a financial review by a certified public accountant and a claims operation review by a senior claims official of a member company. Neither the financial audit nor the claims operation review under the new system examines the propriety of expenses.

The financial audit conducted under the new system differs from the prior system in that Mr. Andrew Caldwell, the man selected to do the financial audit, conducts his public audit in accordance with Generally Accepted Accounting Principles (GAAP). A GAAP audit may be of use to MIGA if the Board chooses to use the audit for purposes other than its own internal review, but we have seen no such use to date.

We asked Mr. Robert Graham, the head of the audit team for the Audit Committee and himself a Certified Public Accountant with experience in audit procedures with the guaranty associations of four states, why his audit had not been performed according to GAAP. He told us the Audit Committee had performed an "industry audit" rather than a GAAP audit because that was what MIGA had asked for. He added that the audit report was presented to the Board and was not used nor was he told that it was intended for use as a public audit. He told us that his Audit Committee could have and would have performed a GAAP public audit had MIGA requested it. Moreover, he told us that the Audit Committee could have performed a GAAP audit and continued to

review the propriety of expenses.

We asked Ralph Moore, MIGA's Chairman at the time of the April 1980 change, why the change was made.⁶¹ He suggested that MIGA wanted a Maryland auditor who could give more time to the work.⁶² He told us that he considered the new audits prepared by Mr. Caldwell to be "more thorough." However, Mr. Caldwell himself acknowledged that the scope of his review is more limited than the review conducted by the Audit Committee. Our own auditor, Mr. Melocik, has reviewed both the Audit Committee and Caldwell audits. He has informed us that although the financial report of Caldwell is the slightly longer of the two types, the difference is due to format, not scope and detail.

The second part of the review, the insurance claims review, might at first reading seem to complement the Caldwell financial audit in such a manner as to make the combination as complete a review as that made by the old Audit Committee. However, in actual operation, this review does not achieve that result. The individual called upon to review claims handling is insulated from the financial and cost data that had been available to the Audit Committee.

⁶¹ We also asked Mr. Mezzanotte about the change in audits. He told us that he did not know what the old audit procedure consisted of or who did it or what form it took. He did know that Mr. Caldwell's audit was limited to a financial review. Mr. Granville Bixler told us that he thought the Audit Committee had done an excellent job.

⁶² MIGA Board minutes suggest that Commissioner Birrane had suggested the requirement that the financial audit be performed by a Maryland auditor.

For the year 1979, the insurance review of MIGA was conducted by Mr. Thomas Clarke of the American Mutual Insurance Company.⁶³ Mr. Clarke's review lasted two to three days and consisted of interviews and review of claims department procedures and files. He was given no access to any financial records, expense records or any other cost figures on the MIGA claims operations or the operations as a whole. He told us that he viewed his role as limited to a review of claims handling procedures, i.e., staff functions; values placed on files for settlement; and amounts of reserves established. He did not undertake any evaluation of the cost effectiveness of the claims operation.⁶⁴

Mr. Clarke received his instructions on how to conduct the review in a meeting with Directors Moore and Gray prior to his review. Other than the limitations just stated, the only other instruction he received was that he was to review Mr. Sharretts' work as house counsel to determine whether MIGA was saving money by using house counsel. He spent a substantial part of his

⁶³ Mr. Clarke was recommended for the job by Mr. Charles Mullaney, then MIGA's claim manager. Until coming to MIGA, Mr. Mullaney had worked for American Mutual under Mr. Clarke.

⁶⁴ We questioned Mr. Clarke about several statements in his report that suggested access to financial records. For example, he stated that Mr. Sharretts' work as house counsel justified his salary; in another portion of the report he complimented Mrs. Franklin for purchasing office equipment at below retail cost. He explained that he had no access to the financial records on either of these points. The Sharretts' salary figure was orally supplied to him by Directors Moore and Gray. The information about the furniture purchases came to him in a conversation he recalls having with MIGA's outside auditor.

review time on that question, concluding that Mr. Sharretts' role in transferring cases and handling cases in the lower courts justified the employment of house counsel.

Mr. Clarke had not been directed to review loss adjustment expenses; however, he told us that he saw several bills from outside adjusters in some of the files. He said in his report "I find that Free State Adjusters, Inc. is expensive and yet they do supply a high quality work product."⁶⁵

For the review of 1980 claims handling, Henry C. Reid, a Senior Vice President of Atlanta Casualty (a company recently certified as an insurer in Maryland), was selected. Although shortly after the audit Mr. Reid became a member of MIGA's Board, he does not appear to have joined the Board until the completion of his audit. We did not interview Mr. Reid; we did review his report in which he describes his two day review as a "brief overview of general conditions found, specifically in the claims department."

⁶⁵ We asked Mr. Clarke why his conclusion seems to be different than that arrived at by our expert, Mr. Hagen. He told us that to try to compare the two reviews was like comparing "apples to oranges", because his review did not have as its purpose a review of the propriety of loss adjustment expenses and he merely was commenting on several bills he had seen in the course of a review of sampling of files, many of which did not even have bills in them for outside services.

C. MIGA Chronology

The following are the significant dates concerning MIGA.

- 7/1/71 The statute creating MIGA became effective.
- 9/30/71 MIGA's first plan of operations was approved by then Commissioner Thomas Hatem.
- 3/20/72 MIGA's Board learned of the first insurer insolvency (LaSalle National Insurance Company) over which it would have jurisdiction.
- 7/1/75 The statute was amended to remove the provision requiring the Insurance Commissioner to serve as MIGA Board chairman.
- 12/19/75 William Rogers became the MIGA Board Chairman.
- 1/1/76 Edward J. Birrane, Jr. became Insurance Commissioner serving at the pleasure of the Secretary of Licensing and Regulation.
- 7/25/77 Mr. Birrane was appointed to a full six year term as Insurance Commissioner.
- 12/16/77 The Maryland Indemnity Insurance Company, the largest company MIGA has had to deal with, went insolvent.
- 6/78 Mr. Birrane appointed Mr. Ralph Moore, Mr. Albert J. Mezzanotte, and Mr. James Hightower to the MIGA Board.
- 11/2/78 Charles Mullaney was hired as MIGA claims manager after a search conducted by Mr. Moore.
- 12/78 MIGA made its first use of Free State.
- 4/15/79 Mr. William Rogers' term on the MIGA Board of Directors expired.
- 4/31/79 Ralph Moore was elected Chairman of MIGA's Board; Albert Mezzanotte was elected Vice-Chairman and James Hightower was named to chair the Executive Committee that consisted of himself, Mr. Mezzanotte and Mr. Gray.

- 5/25/79 Mr. Mullaney suggested the use of outside adjusting firms rather than staff claims adjusters.
- 5/31/79 Mr. Mullaney's plan to change claims handling procedures was approved by MIGA's Board of Directors.
- 6/79 MIGA's staff claims adjusters were dismissed and the use of outside adjusters for most claims work is begun.
- 6/21/79 Claims manager Mullaney was told by Ralph Moore to increase assignments to Free State.
- 7/20/79 MIGA signed lease for Towson Towers space to house administrative operation.
- 8/20/79 MIGA signed lease for Loch Raven Boulevard office to house claims operation.
- 3/80 Mr. Andrew Caldwell was hired to do financial audit of MIGA.
- 4/80 MIGA's plan of operation was amended to abolish Audit Committee of member insurers and instead to use "actuarial expert" who is Maryland CPA.
- 5/80 Ralph Moore resigned as MIGA chairman to assume position at ACLIC. Mr. Mezzanotte became Board Chairman.
- 8/15/80 Claims manager Mullaney left after dispute over Free State billing.

SECTION III
MARYLAND INDEMNITY

A. OVERVIEW

Pursuant to Article 48A, Section 145(1) of the Maryland Code, Commissioner Birrane was appointed Receiver, in liquidation, for Maryland Indemnity, a property and casualty insurer, on December 16, 1977. One week later, Preston Tull was appointed Deputy Commissioner/Deputy Receiver of Maryland Indemnity to manage the day-to-day activities of the insolvency. Mr. Tull's limited insurance experience and background, his receipt of extra payment for alleged reviews of certain worker's compensation files of Maryland Indemnity, and his management of the insolvency, are all areas of concern identified by our inquiry.

Mr. Tull received an initial salary from Maryland Indemnity of \$15,000.00 per six months, and periodic raises since then have taken his present salary to \$41,000 per year. He also received the sum of \$58,455.00, in July of 1981, for his purported reviews of worker's compensation files of Maryland Indemnity, from December 1977 through June 1981, and similar reviews of Consolidated Mutual Insurance Company (hereafter "Consolidated") and Cosmopolitan Insurance Company worker's compensation files

(hereafter "Cosmopolitan").¹ We will explore the following questions concerning the propriety of the extra payment for worker's compensation file reviews: (a) how it came about that Commissioner Birrane and Mr. Tull concluded that the worker's compensation reviews were outside of Mr. Tull's contractual duties for the Maryland Indemnity receivership, and thus merited further compensation beyond his contractual rate of pay; (b) what work was performed by Mr. Tull when he did these "reviews", and what the value of that work was to Maryland Indemnity and ultimately to MIGA; and (c) how it came about that MIGA, the guaranty association discussed in Section II, above, paid Mr. Tull's bill in full, in July of 1981, for these reviews².

With regard to Mr. Tull's management of the insolvency itself, several expenditures and transactions will be addressed: (a) selection of counsel for claims defense and subrogation work; (b) selection of adjusters for claim reviews; (c) selection of real estate agent for sale of Maryland Indemnity building; and (d) use of insolvency funds for travel and entertainment. The need and value of the work performed by those selected, the methods used to select the particular firm or individual to do

¹ Mr. Tull received \$54,315.00 for "reviews" of Maryland Indemnity worker's compensation files, discussed in Section III B 3; he further received \$3,990.00 for "reviews" of Consolidated worker's compensation files, discussed in Section III B 8; finally, he received \$150.00 for Cosmopolitan worker's compensation file "reviews", which we do not believe merit separate discussion in this report.

² Section III B 7 explains the statutory change that transferred worker's compensation claims against insolvent companies from a separate Insurance Division account managed through the Maryland Indemnity insolvency to MIGA, effective July 1, 1981.

the work, and the lack of controls in regard to these expenditures are questions necessarily raised by the facts we discovered.

B. MARYLAND INDEMNITY WORKER'S COMPENSATION REVIEWS AND REMUNERATION

1. Preston Tull's appointment and salary

Prior to his December 23, 1977 appointment as Deputy Commissioner/Deputy Receiver for Maryland Indemnity, Preston Tull had worked for fourteen years at the Unsatisfied Claim and Judgment Fund (hereafter UCJF) which later became the Uninsured Motorist Fund of the Maryland Automobile Insurance Fund (hereafter MAIF), as a casualty claims supervisor. Mr. Tull's only other insurance employment noted on his resume for the Maryland Indemnity job, was a little over a year spent with John Roane, Inc. as an adjuster in training (App. III-1). Mr. Tull does not claim expertise in running an insurance company, nor any management experience beyond claims work (Dep. pp. 13-14).³

According to Commissioner Birrane, although he knew Mr. Tull by reputation when Mr. Tull worked at MAIF and UCJF, he first actually met Mr. Tull only a month prior to Mr. Tull's appointment as Special Deputy Commissioner and Deputy Receiver.

³ The reference, and the similar references throughout this section of the report, is to Mr. Tull's deposition conducted on December 1, 1981.

Mr. Tull and Ralph Moore had been friends for a number of years prior to Mr. Tull's appointment, according to Mr. Moore.⁴

Commissioner Birrane indicated that he passed along the Maryland Indemnity job opening by "word of mouth", but that he did not formally advertise the position. Mr. Tull stated that he learned about the job from Jack Gandy, claims manager at Crawford and Co., and applied for the job thereafter (Dep. pp. 18-19). Mr. Tull was the only serious candidate for the job, according to the Commissioner.

Mr. Tull's highest salary at MAIF amounted to approximately \$20,000 per year plus benefits which we have valued at \$4,000.⁵ His original contract as Deputy Receiver called for \$15,000 in

⁴ Frank Csar, the Illinois liquidator mentioned in Section II, has met Mr. Tull at NAIC meetings and "highly respects" Mr. Tull's ability.

⁵ Maryland Indemnity representatives have suggested that Mr. Tull's receivership salary, although greater than his previous State salary, was but a small increase, given the State benefits which Mr. Tull gave up when he left State employ for the receivership position. We have reviewed a memorandum from Maryland Department of Personnel Secretary Thornton, who suggests that pension contributions, health benefits, and employer's social security contribution, amount to 20% of a State employee's base salary, and leave days amount to another 20% of a State employee's salary. We recognize that Mr. Tull did not receive pension, health care, or employer's social security contributions from the receivership; however, our review of Maryland Indemnity records indicates that Mr. Tull's time was basically his own, and that he could in effect take whatever time off he desired as long as the receivership work got done. We therefore have added \$4,000 (20%) to Mr. Tull's approximate \$20,000 salary at MAIF, to arrive at a State salary and benefit package of \$24,000 prior to his Maryland Indemnity employment. Because his initial Maryland Indemnity contract called for a \$30,000 per annum salary, we conclude that Mr. Tull received a 25% increase in salary immediately upon entering his original contract with the receivership.

compensation for the first six months (App. III-3).⁶ The latest salary increase which Mr. Tull has received, effective July 1, 1980, resulting in a salary of a little over \$41,000 per annum, is based upon that contract's provision that Mr. Tull be paid the same salary as a Grade 21, Step 6 State employee, plus 20% in lieu of not receiving "any fringe benefits . . . to which State employees are entitled" (App. III-2, Article V, p. 2). That contract is for a three year term.

2. Preston Tull's contractual duties

Maryland law provides that the Insurance Commissioner be the Receiver, both in rehabilitation and liquidation, of insurance insolvencies occurring in this State. Article 48A, Section 132, Maryland Code. In accordance with that statutory responsibility, the Commissioner has the following authority:

"The Commissioner as domiciliary receiver shall be responsible for the proper administration of all assets coming into his possession or control." Article 48A, Section 145(4), Maryland Code.

"Upon taking possession of the assets of an insurer, the domiciliary receiver shall, subject to the direction of the court, immediately proceed to conduct the business of the insurer or to take such steps as are authorized by this subtitle for the purpose of

⁶ By petition of the receiver and order of July 17, 1978, Mr. Tull's salary became \$16,500 per six months, effective June 28, 1978. Effective December 28, 1978, the salary became \$17,325 per six months (Court Order of January 9, 1979). Effective June 28, 1979, at the behest of the receiver, the salary became \$18,200 per six months (Petition approved by Court Order of June 13, 1979).

rehabilitating, liquidating or conserving the affairs or assets of the insurer." Article 48A, Section 145(5), Maryland Code.

Each successive contract describes Mr. Tull's duties as Deputy Receiver as follows: "to provide assistance" to the Insurance Commissioner in connection with the Maryland Indemnity receivership (App. III-2, III-3, Article II, p. 1). Thus, Mr. Tull was to provide help for the Commissioner, who was responsible to administer all of Maryland Indemnity's assets and in fact to conduct all of Maryland Indemnity's business for the life of the liquidation. Consistent with the broad statutory authority of the Commissioner, and the very general nature of Mr. Tull's appointment, Mr. Tull concluded that his appointment by the Commissioner meant:

"Tull, you are my Deputy Receiver, and if it takes one hour, five thousand hours, all I ask is that you get the job done." (Dep. p. 94).

Because MIGA's jurisdiction included property and casualty claims but not worker's compensation claims, the latter claims had to be handled by the insolvency. Art. 48A, Sections 147-150 and 160, Maryland Code. The fact that MIGA was created to handle certain specific property and casualty claims does not detract from that responsibility in regard to claims not covered by MIGA, i.e. worker's compensation claims prior to July 1, 1981. (Frank Csar, the Illinois liquidator, stated that he, as liquidator, handles all "uncovered" claims within the insolvency.)

Accordingly, the "job" of Preston Tull as Deputy Receiver for Maryland Indemnity logically included handling Maryland Indemnity worker's compensation claims.

3. Preston Tull's review of Maryland Indemnity Worker's Compensation files.

In July of 1981 MIGA paid Preston Tull over \$54,000 for his reviews of certain Maryland Indemnity worker's compensation files. Mr. Tull's documentation suggests that these reviews were performed on a regular basis from December, 1977 through June of 1981.⁷ There is a serious question concerning Commissioner Birrane's and Preston Tull's determination that this work was beyond Mr. Tull's contractual duties. There are also serious questions about the nature of the "review" work itself, and the value of that work to Maryland Indemnity and MIGA.

(a) Were the reviews beyond Mr. Tull's contractual duties?

Despite Mr. Tull's broad contractual duties, as outlined in Section III B 2, and despite Mr. Tull's obvious understanding that his duty was to "get the job done" no matter what number of hours was involved, he and Commissioner Birrane concluded that Mr. Tull's management of the insolvency did not include the monitoring of the Maryland Indemnity worker's compensation files.

⁷ The documentation is described in Section III B 4.

At the time of insolvency Maryland Indemnity had approximately 10,000 worker's compensation claims, the vast majority of which were closed. Mr. Tull gave a rough estimate of 700 to 1500 "open" or "active files" (Dep. p. 47), which he later refined to a figure of 900. Of those 900 "open" files, only 35 claims were in active payment status during the insolvency, according to Maryland Indemnity representatives. While the exact basis for the conclusion by Commissioner Birrane that Mr. Tull would receive extra payment for worker's compensation file reviews is unclear, Mr. Tull described their decisional process this way:

"One of the things we [Tull and Commissioner Birrane] recognized early on was the fact that there was a problem in that Maryland Indemnity Workmen's Compensation claims was not covered by MIGA, therefore, he [Commissioner Birrane] needed someone to take care of these matters. He asked me if I would take care of the Maryland Indemnity WC claims, although under the existing statute . . . there was not any language whereby he could pay me for my duties performed on these cases. So I agreed with Mr. Birrane that I would take care of the Maryland Indemnity Workmen's Compensation claims. That is what I did." (Dep. p. 42).

Commissioner Birrane also stated that he did not consult receivership counsel William Cahill, the Attorney General's Office, or any other source of advice before he assumed that worker's compensation file reviews were outside the scope of Mr.

Tull's Deputy Receiver duties and contract, and thus deserving of extra compensation.⁸

The Commissioner also stated that because Mr. Tull would perform the reviews outside his normal working hours, he and Mr. Tull agreed that Mr. Tull would, if possible, receive extra payment for this work at the appropriate time. However, Mr. Tull told us that he had no set working hours for Maryland Indemnity and some of the time that he billed for reviews of worker's compensation files was time during his "normal working day" for the receivership (Dep. pp. 94-98).

Neither Commissioner Birrane nor Mr. Tull considered Mr. Tull's broad responsibilities to manage Maryland Indemnity's business to include the general supervision of these particular claims. Thus, in December 1977 Preston Tull began to perform reviews of worker's compensation claims of Maryland Indemnity, on their mutual understanding that he should be paid extra for this work, although the amount, source, and time of payment all remained undetermined.

⁸ Mr. Cahill's September 1980 opinion, regarding source of payment for worker's compensation claims expense, did not address the question of whether Mr. Tull's contractual duties fairly embraced the worker's compensation cases. It does not appear that Mr. Cahill was requested to determine that issue (App. III-29).

(b) Was the work performed by Mr. Tull both necessary and valuable?

We have been unable to determine the necessity and value of much of Mr. Tull's work, or to verify that the work was actually done.

Mr. Tull claims to have reviewed 500 open Maryland Indemnity worker's compensation files and 614 closed worker's compensation files between December 1977 and June 30, 1981.⁹ His own records demonstrate that, of these 500 open files, he reviewed 51 files five times, 275 files four times, 103 files three times, and 64 files twice.

We asked our worker's compensation expert Frank Boyle, who reviewed about two-thirds of the 326 files allegedly reviewed at least four times by Mr. Tull, to tell us whether these files by virtue of their contents justified more than a single review during the time of the insolvency. Mr. Boyle concluded that, of the 206 files he reviewed, only six deserved more than one review. In his judgment, over 95% of the time even a second review was unwarranted.

⁹ The 614 files which Mr. Tull's notes describe as "closed" were allegedly reviewed one time. Of these 614, 562 were reviewed between December 1977 and February 28, 1978, and 52 were reviewed in March of 1980.

Maryland Indemnity's representatives have advanced two reasons for Mr. Tull's reviews of Maryland Indemnity worker's compensation claims. First, in lieu of hiring an outside adjusting firm, Mr. Tull was to "review" and "adjust" the claims to "determine the validity" of same. Second, Mr. Tull was to "establish reserves" for these claims, in large part at the request of Maryland Indemnity auditors. Our inquiry disclosed, however, that no evidence exists of Mr. Tull's adjustment of any file, and that Mr. Tull did not establish any reserves.

The files themselves disclose that Mr. Tull's reviews of open files did not include any adjustment (claims investigation or evaluation) of the files. We asked worker's compensation claims expert Frank Boyle to evaluate Mr. Tull's "review" of open worker's compensation files. Mr. Boyle informed us that notations in a file are the recognized industry method for demonstrating that a claims file has in fact been reviewed for purposes of adjustment or setting reserves. With respect to Mr. Tull's work for Maryland Indemnity, Mr. Boyle found after a review of many files which Mr. Tull claims to have reviewed:

"My file review revealed only three files and these were Consolidated Mutual files in which there were minor contacts with Preston Tull. There was a Cosmopolitan Insurance Company file in which he wrote quite a few letters in 1980. Other than these there were absolutely no notes, reports, letters or any indication at all that he looked at or reviewed the file. I have, of course, checked his diary list of file numbers with my list of files I

reviewed and there are many, many which he and I have both listed and in which there is no evidence of a contact at all. I noted that a lot of Mr. Tull's work apparently was done in 1979 and is perhaps not now evident but certainly in the files which I looked at, there is nothing from him." (App. III-13).

Mr. Tull himself contradicted the Maryland Indemnity representative's suggestion that his reviews were for the purpose of establishing reserves:

Q. "Was one of the purposes you reviewed the file to establish some reserve on the files?"

A. No.

Q. Why not?

A. Well, I am working with a fund. I got a block of money here. I got a block of liability here." (Dep. p. 50).¹⁰

Mr. Tull went on to explain that, because he had taken a "swag" or "guess" at establishing an assessment of the Maryland worker's compensation insurers in May of 1978, to generate funds for the payment of worker's compensation claims, and because there had been no protest of that assessment, there was simply no need for Mr. Tull to establish a formal reserve until requested by Maryland Indemnity's auditors.

¹⁰ Mr. Tull's reference to "a fund" is a reference to the 1978 worker's compensation assessment levied by Commissioner Birrane, a fund of over \$1,000,000.00 out of which worker's compensation claims against Maryland Indemnity could be paid.

Maryland Indemnity's auditors in the Spring of 1979 requested that reserves be established. Despite the fact that Mr. Tull's review had been underway for well over a year when this request was made, Mr. Tull hired Charles Mullaney to establish these reserves.¹¹ Had Mr. Tull previously established reserves, Mr. Mullaney's engagement would have been unnecessary.

Beginning July 10, 1979, Mr. Mullaney set about to review some 664 open worker's compensation files of Maryland Indemnity and establish the necessary reserves. By September 19, 1979, Mr. Mullaney had finished his 27 page report, with 80 pages of backup notes, in which he not only set reserves but also made suggestions that certain files be closed, that other files be closely monitored, and that other administrative actions be taken. For all of this work Mr. Mullaney was paid a little over \$4,000, at the \$15.00 per hour rate. Mr. Mullaney's hiring, and his hourly rate of \$15.00 were expressly approved by Commissioner Birrane (App. III-11 and 12).¹²

Our expert Frank Boyle also looked at the Maryland Indemnity files for evidence of Mr. Mullaney's review. Mr. Boyle

¹¹ Mr. Mullaney was the claims manager for MIGA at the time, see Section II. He did the worker's compensation claim review on his own time. Mr. Mullaney had experience in adjusting worker's compensation claims. Both of our claims experts, Mr. Hagen and Mr. Boyle, were of the strong opinion that worker's compensation claims work demands such a specialized background. Other than a brief exposure to worker's compensation claims as a learning adjuster with John Roane, Mr. Tull had no such background (Dep. pp. 13-14).

¹² Mr. Mullaney's rate of pay is significant compared to the \$30.00 per hour rate of pay that Mr. Tull established for himself at the time of his submission of his bills to MIGA in July of 1981, Section III B 5.

characterized the Mullaney review as "fairly accurate although his notes are extremely brief and sketchy" (App. III-13). While Mr. Boyle "in many instances" disagrees with Mr. Mullaney's specific recommendations, he found the review itself readily apparent. In fact, the review by Mr. Mullaney is the only detailed, documented review of the Maryland Indemnity active worker's compensation files which Mr. Boyle found.

As a result of Mr. Boyle's review we conclude that, while Mr. Mullaney's two month, \$4,000.00 review of 664 files is adequately documented to demonstrate the work that he performed, there is virtually no trace of Mr. Tull's repetitious three and one-half year, \$54,315.00 review of 500 open files to indicate any work performed by Mr. Tull in regard to reserves, adjustment, or any other claims activity.

We interviewed Sharyn Rhodes, a former employee of Maryland Indemnity, who worked for the insolvency from its onset until September 20, 1979. Among Ms. Rhodes' duties was overseeing payments to claimants with worker's compensation awards. She estimated that there were about twenty claims in payment status while she was working for the insolvency. Ms. Rhodes, who was aware of the location of the worker's compensation claims on the second floor of Maryland Indemnity, recalls assisting Mr. Mullaney during his review of the worker compensation claims, either pulling files or storing files away at his request. Other than Mr. Mullaney's review of these files, Ms. Rhodes, who worked

8:30 - 4:30 on weekdays, does not recall anyone reviewing these files. She was not requested by Mr. Tull to locate or put away worker's compensation files. She does not recall ever seeing Mr. Tull reviewing, pulling, or storing worker's compensation files. She does not recall that Mr. Tull ever mentioned a worker's compensation file review.

4. Preston Tull's documentation

Mr. Tull's documentation in support of his request for extra payment for his three year review consisted of nothing more than invoices and a handwritten list of case numbers said to have been reviewed during a given month. Even a superficial count of the files listed (on yearly desk calendars) yields at best 500 open files which Mr. Tull reviewed, less than the 664 open files reviewed by Charles Mullaney, and far less than the 900 open files of the insolvency as estimated by Mr. Tull himself. Yet, according to Ramsey Gray, the former MIGA Board Director who was involved in the decision to pay Mr. Tull, the "daily diary" "helped form the basis for the ultimate review of the billings", (App. III-28, p. 1).¹³

Our review of the documentation discloses that the same files were claimed to have been looked at by Mr. Tull on several different occasions. For example, the files he states he first

¹³ MIGA's "review" of Mr. Tull's bill for his worker's compensation duties is discussed in Section III B 7 of the report.

reviewed during the month of March 1978, he claims to have reviewed in October of 1978, August of 1979, and April of 1981; the files first reviewed in May of 1978, were looked at again in December 1978, October 1979, and August of 1980. No need to re-review any of these files is documented, or remotely apparent.

5. Preston Tull's rate of pay

Mr. Tull billed at a rate of \$30.00 per hour for the review he claimed to have performed. Mr. Tull applied this rate, which is double the rate for the reserve/review performed by Mr. Mullaney in 1979, to all of his work, which spanned more than three and one-half years from December 1977 to July 1, 1981. Mr. Tull told us that rate was determined after "I called around to people in the industry, the independents, talked with some attorneys who are friends of mine. I arrived at that figure considering all things being equal, it was a fair amount" (Dep. p. 89).

There was never any agreement between Mr. Tull and Commissioner Birrane concerning the rate of pay. That rate was established by Mr. Tull himself at the time Mr. Tull submitted his request for payment in June of 1981, shortly before MIGA paid the entire request. Neither Commissioner Birrane nor MIGA officials ever questioned this rate of pay, despite the fact that Mr. Tull's rate was double the rate approved by Commissioner Birrane for the more experienced Mr. Mullaney.

6. The effort to have MIGA pay the Maryland Indemnity Deputy Receiver.

Mr. Tull's work on the Maryland Indemnity worker's compensation files began in late 1977. He was not paid for that "review" in 1977, 1978 nor even in 1979, though Charles Mullaney was paid promptly for his work on the same files in mid-1979. Mr. Tull in fact was not paid until after July 1, 1981, the effective date of the amendment to the MIGA statute, sponsored by Commissioner Birrane and discussed in Section III B 7, which, MIGA officials concluded, permitted payment of the Tull claim.

Mr. Mullaney had been paid from a worker's compensation escrow fund, established in 1978 by a special assessment on worker's compensation insurers.¹⁴ Sidney Albert was also paid (\$22,297.19) from the same fund for his defense of Maryland Indemnity worker's compensation claims before the Commission in 1978 and 1979 (Mr. Albert was house counsel for Maryland Indemnity at the time of insolvency, and is now a workmen's compensation commissioner).

¹⁴ Maryland Indemnity counsel stresses that the genesis of the escrow fund was an objection from then MIGA counsel Allan Gamse to the payment of worker's compensation awards out of insolvency funds. Mr. Gamse pointed out that the worker's compensation statute, particularly then Article 101, Sections 85-89, provided for a separate escrow fund to pay of such claims, and that insolvency assets (as to which MIGA is a creditor) would be wasted, if used to pay claims, rather than the escrow fund.

Mr. Gamse's objections had nothing whatsoever to do with the propriety of Mr. Tull receiving extra payment for his worker's compensation reviews, the nature of those reviews, or the value of those reviews to the insolvency. In fact, Mr. Gamse's criticism merely extended to the need for an assessment pursuant to Article 101, Sections 85-89 to fund claims payments. Thus, Mr. Gamse's protest was not germane to the issue of Mr. Tull's extra payment, an expense payment rather than a claims payment.

Neither Commissioner Birrane nor Mr. Tull questioned the propriety of these payments being made from the escrow fund.¹⁵ Mr. Tull was not paid from this fund. Nevertheless, both he and Commissioner Birrane repeatedly, if indirectly, sought legal approval for Mr. Tull's payment from the fund, from the Attorney General's Office. Without mentioning any benefit to Mr. Tull, both Commissioner Birrane and Mr. Tull, in 1979 and 1980, requested advice in turn from Assistant Attorneys General Patrick Smith (App. III-14), Alan Lipson (Dep. pp. 112-113), and law clerk Karen Murphy (Dep. pp. 113-114), as to whether the provisions of Article 101, Sections 85-89 would justify payments for various aspects of claims defense (App. III-31). Each time the question was posed, the answer was "no", because the language of the statute limited the use of the fund to payment of "awards" to claimants, rather than "awards" and "claims defense".

A fourth request by Commissioner Birrane, this time to receivership counsel William Cahill, resulted in an opinion of September 22, 1980, which concluded:

¹⁵ We do not address the propriety of such payments. Rather, we point out the contrast between these payments readily made at the time the services were performed, and the fact that Mr. Tull was not paid in the same manner from this same fund. Maryland Indemnity representatives have suggested that the legal opinion of William Cahill justified these payments. We note that Mr. Cahill's opinion, which did state that legal and administrative expenses could be paid from the fund, was issued on September 22, 1980, long after the payments to Messrs. Albert and Mullaney (App. III-29).

"since there is a duty to defend the fund which has been entrusted to you by reason of the assessments, it follows that the Legislature intended for the fund to be responsible for the payment of expenses incurred in connection with such defense." (App. III-29).

Mr. Cahill told us that the Commissioner did not mention Mr. Tull when he asked for this opinion.

Even after the opinion of September 22, 1980, Mr. Tull did not seek payment from the escrow fund. He said that he "didn't feel I had all the grounds I needed to receive payment without someone second guessing us" (Dep. p. 120). Apparently, Commissioner Birrane shared that view because he thereafter drafted and secured sponsorship for legislation which would later constitute justification for Mr. Tull receiving payment - not from Maryland Indemnity or its receiver, Edward Birrane, but from MIGA (acting through two Birrane-appointed directors).

The failure of the Commissioner or Mr. Tull to indicate to any member of the Attorney General's staff or to Mr. Cahill that Mr. Tull's additional payments were the reason for their requests, may suggest that Commissioner Birrane and Mr. Tull had misgivings as to the propriety of payment to Mr. Tull in excess of Mr. Tull's annual salary. Moreover, Commissioner Birrane's protracted pursuit of legal approval for Mr. Tull's extra payment stands in marked contrast to the facility of payments to Mr.

Mullaney and Mr. Albert, authorized by both the Commissioner and Deputy Tull. Commissioner Birrane's and Mr. Tull's misgivings were apparently resolved only by the passage of Senate Bill 1124, effective July 1, 1981 which repealed Article 101, Sections 85-89 and amended Article 48A, Section 504(b) of the Code, to transfer worker's compensation claims from the insolvency to MIGA. The payment to Mr. Tull by MIGA followed soon after the statute's effective date.

7. Preston Tull's source of payment - July 1, 1981

It is now clear that a primary motive for passage of the 1981 amendment to the MIGA statute was to insure payment to Mr. Tull for his worker's compensation "reviews". Commissioner Birrane told us that he drafted Senate Bill 1124 in part to afford Mr. Tull a source of payment for his worker's compensation claims reviews, and in part to make Maryland's MIGA statute close to NCIGF's model statute. One sentence of that Bill, which was introduced by Senator Harry McGuirk¹⁶, was of great significance to Preston Tull:

"On July 1, 1981, all the assets and obligations of every type and description of the workmen's compensation insolvency fund at the close of business on June 30, 1981 shall be transferred to the Maryland Insurance

¹⁶ In an interview on March 15, 1982, Senator McGuirk informed us that he had no idea that the passage of Senate Bill 1124 would result in a payment of more than \$58,000.00 to Mr. Tull. In fact, had he been aware of such a result, he assured us that "questions would have been asked."

Guaranty Association and administered through the appropriate account under \$506 of this subtitle."¹⁷ (App. III-15, p. 3). (emphasis supplied)

According to Commissioner Birrane and Preston Tull, and according to the opinion rendered by Douglas Sharretts, for MIGA, the language "obligations of every type and description" included Mr. Tull's bill, first submitted on June 22, 1981 to Commissioner Birrane for worker's compensation reviews of Maryland Indemnity (as well as Consolidated Mutual) files.

On or about June 30, 1981 James Sandkuhler, an employee of Caldwell and Associates, entered the Tull bill as an "accrued expense" on Maryland Indemnity's worker's compensation escrow fund.¹⁸ Neither Maryland Indemnity bookkeeper Charles Witzen, nor its financial auditor Andrew Caldwell could tell us who authorized such an entry, but Mr. Caldwell insisted that the entry must have been "client created", i.e., ordered by Mr. Tull or one of Mr. Tull's employees. Mr. Tull claimed he was "not

¹⁷ Maryland Indemnity representatives state that the reason for the amendment of Section 504(b) was to clear up the existing "statutory confusion" in regard to payment of loss adjustment expenses of worker's compensation claims. The amendment to Section 504(b) did not define the word "obligation". Nor did the amendment state whether the previous worker's compensation escrow fund included loss and adjustment expense. In fact, the amendment to Section 504(b) nowhere mentions "loss adjustment expenses". Therefore, the amendment completely sidestepped the issue of whether the previous statute, or the MIGA statute as amended, would provide for payment of worker's compensation loss and adjustment expense incurred prior to July 1, 1981. Moreover, the amendment was entirely irrelevant to the value, necessity, or billing rate for Mr. Tull's "reviews", discussed supra. in Section III B 4.

¹⁸ Mr. Sandkuhler's entry is noted as "recapped from list prepared by client. Reviewed all bills."

aware that an entry was made" (Dep. p. 125). In short, the authority for making the Maryland Indemnity journal entry is disclaimed by all concerned.

The journal entries disclose a total of twelve "accrued expense" items payable by MIGA (App. III-32). Of the \$70,102.78 total, Mr. Tull's claim of \$58,455.00 constitutes 83.4%. If the reimbursement of the Receivership by MIGA for previous payments made to Mr. Cahill for his worker's compensation activities is discounted, Mr. Tull's claim is over 90% of the outstanding claims "owed" by MIGA as of July 1, 1981.

We asked Commissioner Birrane how, if the Tull bill was not considered an "obligation" of the escrow fund for the three and one-half years prior to July 1, 1981, the passage of Senate Bill 1124 made Tull's work an "obligation" that could suddenly be paid by MIGA. The Commissioner responded that perhaps he had drawn the statute "inartfully" but that the intent was to include such bills as Tull's under the term "obligation".¹⁹

The "review process" by both Commissioner Birrane and MIGA of Preston Tull's submissions, in support of his claim for \$58,455.00, raises further questions. Commissioner Birrane

¹⁹ Commissioner Birrane's comments to the Senate Economics Affairs Committee on the Bill, as reflected in the Committee's file notes, do not mention Tull, but do mention attorney's fees (App. III-33). Furthermore, Secretary John Corbley of the Department of Licensing and Regulation advised us that when Commissioner Birrane asked for his support on the Bill, only the similarity to the Model Act was stressed.

stated that his letter of June 30, 1981, to MIGA Chairman Mezzanotte wherein he states that "I am satisfied that the services for which billing is made were performed to my satisfaction" (App. III-10), was not meant to foreclose review by MIGA of all aspects of the Tull claim. However, MIGA Chairman Mezzanotte told us that he took the Commissioner's letter to mean that the work had in fact been satisfactorily performed. Furthermore, former MIGA Board Member Ramsey Gray characterizes the letter as indicating that the Commissioner "was satisfied that Mr. Tull had done the requisite work on the files" (App. III-28).

Mr. Tull's June, 1981 bills were sent to Commissioner Birrane, who forwarded them to MIGA. They did not include his file number lists on the desk calendars, but included only invoices stating hours and monetary amounts. At the request of Charles Witzen, bookkeeper for MIGA, Mr. Tull produced his desk calendars for MIGA's inspection. Although these calendars contained nothing more than a list of file numbers, (after February of 1978, Mr. Tull's documentation consists only of notations made on the last day of the month, with a list of files allegedly reviewed during that month), Mr. Gray stated that the diaries were helpful in MIGA's "ultimate review" of the billings (App. III-28). Mr. Gray states that he also undertook "a thorough review of all of the bills, running adding machine tapes to confirm the accuracy of the figures" (App. III-28, p. 2).

Mr. Douglas Sharretts, counsel for MIGA, at the request of Chairman Mezzanotte, issued an opinion that Mr. Tull's bill was an "obligation" of MIGA, pursuant to amended 504(b) which Mr. Sharretts interpreted to include loss adjustment expenses. In one part of his analysis, Mr. Sharretts agreed with the previous opinion of Mr. Cahill, that former Article 101, Sections 85-89 permitted payments of loss and adjustment expense. Mr. Sharretts' opinion does not address the issue of whether Mr. Tull's pre-existing contractual duties would have included the worker's compensation reviews, whether the reviews themselves contributed to the "defense" of any of Maryland Indemnity's worker's compensation claims, whether the rate of pay unilaterally established by Mr. Tull was the "obligation" of MIGA to accept, or any matter which might pass upon the propriety of this payment, other than the source of Mr. Tull's payment (Opinion of Mr. Sharretts at App. III-30, and Opinion of Mr. Cahill at App. III-29).²⁰

MIGA thus paid Mr. Tull the full amount requested on the basis of (1) Commissioner Birrane's letter; (2) Mr. Tull's desk calendar notations and invoices; (3) Mr. Sharretts' opinion; and (4) MIGA's adding machine tapes verifying Mr. Tull's computations. No one at MIGA raised a question as to Mr. Tull's unilaterally determined rate of pay (double the rate of pay for

²⁰ As discussed in Section II, Mr. Sharretts shared law office space with Commissioner Birrane for many years. Furthermore, prior to his MIGA employment, Mr. Sharretts expressed his interest, over lunch, in doing some Maryland Indemnity legal work (subrogation), at which point Mr. Tull hired him, according to Mr. Tull (Dep. pp. 83-84).

Mr. Mullaney, as approved by Commissioner Birrane in mid-1979), the value to Maryland Indemnity of his reviews, or whether the Deputy Receiver was entitled to any extra pay for his review of the worker's compensation files.

We asked Mr. Tull to produce documentary evidence of his disposition of the MIGA payment. Specifically, we requested that Mr. Tull provide copies of pertinent tax, bank and other financial records. Mr. Tull voluntarily produced those records. They indicated that in August of 1981 (Dep. p. 142) the MIGA payment was invested, put to personal use, and placed in the account of his newly-formed receivership consulting firm ("Preston Tull, Inc.").

8. Consolidated Mutual's worker compensation reviews

Consolidated Mutual, a New York company, had become insolvent in May of 1979. Although the insolvency was in the New York courts, ten worker's compensation claims of Maryland claimants had to be reviewed by Maryland authorities for establishment of a reserve and any follow-up work. Without any formal appointment or contract, Commissioner Birrane appears to have designated Mr. Tull as the "deputy receiver in liquidation" for Consolidated.

Mr. Tull claimed to have spent 133 hours over a two year period on Consolidated claim "reviews" of these ten files. He

generated no documentation or calendar notations of these reviews other than "three files . . . in which there were minor contacts", according to our expert Mr. Boyle (App. III-13). Billing MIGA at the rate of \$30.00 per hour for 133 hours between January 1979 and June 1981, Mr. Tull requested \$3,990.00, which was promptly paid by MIGA in July of 1981.²¹

As in the case of Maryland Indemnity, the only documented review of Consolidated Mutual worker's compensation files was performed by Charles Mullaney in March of 1979, at the behest of Mr. Tull and Commissioner Birrane (Dep. pp. 61-62). The purpose of the review was to establish reserves as a basis for Commissioner Birrane, via an assessment, funding payment of the ten claims (App. III-8).²² Mr. Mullaney, who accomplished the job in two days, billed for, and was paid, \$305.00 at a rate of \$15.00 per hour. His bill was approved for payment on July 3, 1979 by Commissioner Birrane (App. III-6, III-7).

9. Summary

Mr. Tull told us that the purpose for all his worker's compensation reviews was "to determine whatever might be owing or due or the status; whatever. What a normal person would do in

²¹ Once more, Mr. Tull's rate of pay was established by Mr. Tull himself.

²² The assessment was levied in June of 1979, as a result of which the Commissioner transferred \$175,000.00 from the Maryland Indemnity escrow fund to a separate Consolidated escrow fund (Dep. pp. 61-62).

the claims field." (Dep. p. 41). His almost complete lack of notations or other work product suggests at best that there simply was not much to do in order to accomplish these purposes, whatever they were. For this "work", Commissioner Birrane acted time and again to facilitate Mr. Tull's receipt of extra compensation, ultimately in the amount of \$58,455.00.

C. INSOLVENCY MANAGEMENT

1. Introduction

In the following subsections, we will focus on the selection of individuals and firms to perform adjusting services (Free State), legal services (Douglas Sharretts, Stanford Franklin), real estate brokerage (MDIC), and other work for the insolvency. We will also examine various questionable items of expense such as travel and entertainment, charged to the receivership. Many of these firms and persons, who benefit financially from Mr. Tull's management of the insolvency, have also received work and been paid by MIGA (Section II) and ACLIC (Section IV).

2. Independent Adjuster Services (Free State)

Mr. Tull and MIGA assigned three jobs to outside adjusters from work growing out of the Maryland Indemnity insolvency; in all three instances Free State was selected. Mr. Tull first

assigned the relatively minor task of five "activity checks", to determine the actual physical condition of particular worker's compensation recipients, to Free State. Then, he had Free State review all of the insolvency's property and casualty files for potential subrogation reimbursement.²³ Finally, MIGA, partly upon the recommendation of Mr. Tull, authorized Free State's review of the approximately 10,000 open and closed Maryland Indemnity worker's compensation files (App. III-27, p. 1).²⁴

(a) Activity Checks

The "activity checks" appear to be a recommendation of Mr. Mullaney's worker's compensation review (Section III B 3) that Mr. Tull acted upon (Dep. p. 79). Mr. Tull authorized Free State to perform the activity checks because "I have known them, and seen their work product, and knew they did a good job, and at a reasonable cost" (Dep. p. 80, App. III-17).

For the five "checks", Free State charged a total of \$594.00, or \$118.80 per "check". At the suggestion of our expert Frank Boyle, we contacted Mr. Thomas Wooten, Claims Director for

²³ Subrogation is the process by which an insurance company, which pays its own insured for a particular loss, obtains reimbursement for those payments out of the proceeds which the insured later collects from the person who caused the loss or that person's insurer.

²⁴ The 10,000 files included all of the 664 open, active files previously reviewed by Mr. Mullaney, at a cost of \$4,000.00. The 664 files which Mr. Mullaney reviewed, included, in turn, all of the 500 open files repeatedly "reviewed" by Mr. Tull, at a cost of \$54,315.00.

Equifax (a claims investigation firm), who stated that, prior to August, 1981, its charge for each "check" was \$43.00, and that today its charge is \$50.00, less than one-half the Free State rate.

(b) Subrogation

The first time any of the entities discussed in this report utilized the services of Free State was in the Spring of 1978 when Preston Tull requested Free State to look at some Maryland Indemnity property and casualty files for possible subrogation recovery. The subrogation review consisted of Free State's looking at approximately 8,300 closed property and casualty files, for reimbursement potential. Free State was paid \$11,660.00 for this review. Free State employees (adjusters) performed the review.

Mr. Tull did not solicit any other adjuster firms for this work. Nor did Mr. Tull attempt to utilize the former in-house claims staff of Maryland Indemnity, some of whom were now employed by MIGA, and who were working on the second floor of the Maryland Indemnity building for this review (Dep. pp. 35-39). Our auto and casualty expert, Clayton Hagen, advises that the former Maryland Indemnity in-house adjusters were well qualified to perform this task. Maryland Indemnity representatives have

stated that Mr. Tull himself was capable of doing this job but believed that other duties took precedence.²⁵

(c) 10,000 file review

The most recent work on Maryland Indemnity files came to Free State from MIGA, after the effective date of Senate Bill 1124, which transferred all worker's compensation claims to MIGA. At that time Commissioner Birrane and Mr. Tull determined that all worker's compensation files of Maryland Indemnity, open and closed, should be sent to MIGA. According to Mr. Tull, the closed files were included at Commissioner Birrane's express instructions (Dep. pp. 100-101).²⁶ Commissioner Birrane stated that, with the passage of Senate Bill 1124, he felt it was necessary to get all of the worker's compensation files out of Maryland Indemnity.

²⁵ As noted in Section III B 2, Mr. Tull had no required hours. Furthermore, despite the fact that he elected to spend many hours on his review of worker's compensation files, duties which he claims were outside the scope of his contract, he was unable to find time for this claims review.

²⁶ This decision is in sharp contrast to normal MIGA procedure. Ordinarily a guaranty association receives only open files. For example, when Maryland Indemnity first became insolvent in 1978, Commissioner Birrane sent only open property and casualty files to MIGA. The closed property and casualty files, numbering over 50,000, are in the process of being reviewed, for cataloguing prior to destruction, by Maryland Indemnity staff member Doris Bender, who is paid the minimum wage for this work. MIGA's claim manager, Douglas Sharretts, told us that he recently requested from the receiver a few closed property and casualty files because correspondence, inquiries, or lawsuits pertaining to those files had come to his attention. By way of contrast, neither Mr. Sharretts nor any other MIGA official noted any recent activity in the worker's compensation files as justification for the Free State review.

MIGA paid Free State to move all these open and closed worker's compensation files to Free State offices and authorized Free State to conduct a review of all worker's compensation files "to see what was there", according to Douglas Sharretts.²⁷ Mr. Sharretts has no explanation of how this work, which as of January 1982 had already resulted in billings of \$42,403.30 for half the job, got to Free State, other than it "seemed to gravitate" there.²⁸

Mr. Ramsey Gray, who refused our interview request, stated in a written submission that MIGA decided to use Free State because: (1) "MIGA simply had no space to accomodate 26 filing cabinets full of files"; (2) "MIGA had no staff adjusters to handle that large volume"; (3) "Freestate had an expert (Mr. Mullan) who had a specialized background and training in handling Worker's Compensation files." The lack of space and lack of MIGA staff cited by Mr. Gray do not compel the selection of Free State to do the work. Insofar as Free State's expertise is concerned, we learned from Jack Gandy of Crawford and Co. that all adjuster

²⁷ Our worker's compensation expert Mr. Boyle learned that neither the Mullaney review nor any information from Mr. Tull was furnished Free State to assist their efforts (App. III-13, p. 5). Mr. Sharretts told us that the information was not furnished to MIGA.

²⁸ A letter from Mr. Ramsey Gray to MIGA Chairman Mezzanotte on June 24, 1981, stated that the joint recommendation of Messrs. Tull, Prodoehl, Sharretts and Gray was for Free State to "concentrate initially on the active files" (App. III-27). Because Mr. Gray and Mr. Prodoehl refused an interview, we do not know how or why the June 24 plan blossomed into the present review of closed files. Mr. Gray, in his written statement, did not address this point.

firms of any size have worker's compensation claims specialists; Crawford has four such employees.

Commissioner Birrane points out that it is the usual case for an insolvency to maintain one adjuster firm for all of its claims work. While that proposition may well be valid as a general rule, in the case of Free State there had already existed a history of complaints by Mr. Mullaney as to billing problems. Rather than explore and address Mr. Mullaney's concerns (as noted in Section II) MIGA has simply continued to give substantial jobs to Free State without solicitation of prices from other firms, and without consideration of the necessity for the work itself.

MIGA representatives, in the last two months, have had the opportunity to review the report of our expert, Frank Boyle, regarding the Maryland Indemnity worker's compensation reviews. Based upon Mr. Boyle's observation that Maryland Indemnity files were in disarray (App. III-13, p. 2), MIGA has now suggested that the review was therefore necessitated. This reason was not advanced by Messrs. Sharretts, Mezzanotte, Tull, or Moore during their interviews. Moreover, Mr. Boyle told us that sloppy files were no reason to conduct this review.

Former MIGA Director Ramsey Gray has submitted a written document in which he states that: "Freestate was requested simply to analyze every file so that a determination could be made as to which files could be closed and which files must remain open.

Only in that manner could a decision be made with respect to establishing reserves on that large number of cases." Mr. Gray goes on to conclude that MIGA's Executive Committee, as a result of the new reserves, could refund excess assessment monies to the member worker's compensation insurers. Mr. Gray, who refused our request for an interview, does not indicate that MIGA was made aware of Mr. Mullaney's 1979 reserve by Deputy Tull or Commissioner Birrane.

While Mr. Gray's written response (of April 26, 1982) emphasizes the need to set reserves as a reason for this review, we did not find any such rationale in MIGA documents, including Mr. Gray's own letter of June 24, 1981 describing the review (App. III-27). Moreover, given the very small number (35) of claims actually being paid during the four years of the insolvency, and given Maryland Indemnity's contention that Mr. Tull had made an informed "guess" at proper reserves in 1978, which had not been questioned by any member insurer, the \$80,000.00 expected to be paid to Free State for these new "reserves" remains a highly questionable expenditure.²⁹

We have not received a consistent or persuasive articulation of a reason for beginning the review of 10,000 files. Mr.

²⁹ Mr. Gray also states that, in order to insure correct reserves, employer forms had to be filed "to be certain that expenses were limited in accordance with the Statute of Limitations." Our expert, Mr. Boyle, responds that the statute of limitations is not a significant factor for claims that have been inactive from the claimant's side for four years or more.

Sharretts, at his interview on October 26, 1981, explained only why he felt the review should continue: (1) the review has disclosed that a small number of files contained employer forms which were never filed with the Workmen's Compensation Commission; this failure is a criminal misdemeanor calling for a maximum \$50.00 fine, under Article 101, Section 38(d); (2) and the failure to file such forms means that the applicable statute of limitations did not begin to run against the claimant, Article 101, Section 38(c).

Although MIGA asserts that the discovery of unfiled employer forms justifies the continuation of the Free State review, no MIGA official has claimed that the onset of the review was for the purpose of finding such forms. Furthermore, if the search for those forms is the justification for the review, our expert Frank Boyle states that the job could be ably performed by clerical personnel, rather than the more expensive claims adjusters whom Free State has assigned to the task (App. III-13, p. 5). Neither MIGA officials nor Mr. Henry Prodoehl has provided a rationale for the use of adjusters in this regard. We certainly do not fault MIGA for its attempt to comply with the statute; we do question the cost incurred, and the method of selection of a servicing facility, to do so.³⁰

³⁰ Actually, it is the employer who has criminal exposure for failing to file the employer's forms, according to Article 101, Section 38(d). Moreover, we have learned from Ms. Virginia Barnes, Secretary/Director of Administration, to the Workmen's Compensation Commission, that the failure to file the employer's forms routinely goes unprosecuted. As long as the claimant has filed his claim, he is fully able to prosecute his claim.

The "statute of limitations" problem, according to our expert Mr. Boyle, is insignificant because any substantial claim would have been raised by the claimant at an early date with the Commission, even if no employer form had been filed. Moreover, Mr. Boyle suggests that, if this rationale is the real reason for the review, it is very uneconomical both because of the limited benefit in light of the possible consequences and because Free State is using adjusters rather than claims clerks for work which Mr. Boyle describes as "merely consist(ing) of pulling out an employers report or an employees claim form and filing it with the Commission" (App. III-13, p. 5). (Because Mr. Prodoehl refused to be interviewed, we were unable to learn why more expensive adjusters' time, rather than clerical time, was used.)

Yet, as of this date the Free State review continues. Of the almost 5,000 files reviewed, we are told by MIGA counsel that unfiled employer reports have been discovered in 3% of the files reviewed.³¹ No question of the use of adjusters instead of clerks for this review, of the hourly rate, or of the cost effectiveness of this procedure has been raised by the.

³¹ Letter of January 28, 1982, from Thomas Gisriel to Stephen B. Caplis (App. III-19). A number of these forms have been found in files previously reviewed by Mr. Tull.

Commissioner or anyone at MIGA.³² Nor has the overriding "criminal" question been referred to any prosecuting or judicial agency for declaratory resolution, instead of the lengthy pursuit of the employer forms. Free State, based on its present billings and rate of completion, stands to be paid over \$80,000.00 for this review.

3. Worker's Compensation Defense

Mr. Sidney Albert, who had been house counsel for Maryland Indemnity worker's compensation claims prior to his appointment as a Workmen's Compensation Commissioner, earned over \$22,000.00 from the insolvency, much of those fees from work on cases which he handled prior to the insolvency. Mr. Boyle, our expert, found that Mr. Albert did "a very good job" on the files he worked.

Mr. Tull selected Stanford Franklin to succeed Sidney Albert as worker's compensation defense counsel for Maryland Indemnity,

³² Virginia Barnes, Secretary/Director of Administration of the Workmen's Compensation Commission, stated that she was visited on September 1, 1981 by Mr. Sharretts, who sought advice on the disposition of unfiled employer forms. (Prior to September 1, 1981, Ms. Barnes does not recall any specific communication from MIGA or anyone else, about these files. She believes that she may have been called by Mr. Sharretts, shortly before September 1, to set up the appointment). Ms. Barnes noticed that some of the files also contained unfiled claimant forms. She ultimately advised Mr. Sharretts to file whatever unfiled forms he possessed; she told us that, while she was greatly concerned about the unfiled claimant forms (for which she commended MIGA's discovery, but which MIGA has never used to justify its review), she was not nearly as concerned about the unfiled employer forms. In her 25 years with the Commission, it has been the routine practice of various employers not to file these forms, and the practice goes unprosecuted because complaining claimants ultimately force the form to be filed. Mrs. Barnes did state that, of the 135 employers' forms filed, she knew of no claimants who had contacted the Commission. In each of the 135 cases, the Commission had sent written notice to the claimant.

when Mr. Albert was appointed to the Workmen's Compensation Commission. Mr. Franklin's firm earned \$2963.00 in this capacity.³³

Mr. Franklin has been mentioned in Section II of this report in regard to his legal work for MIGA, MIGA's move to the Towson Towers, and his wife, Sylvia, former administrative assistant to MIGA. He is a long time acquaintance of Commissioner Birrane. Mr. Franklin presently serves as local counsel to ACLIC (Section IV), pursuant to his selection by Commissioner Birrane.

4. Subrogation - Property & Casualty Claims

Mr. Tull described his recommendation to Commissioner Birrane of Mr. Sharretts in 1978 as "an excellent selection" for subrogation legal work regarding property and casualty work (Dep. pp. 82-84). As noted earlier, Mr. Sharretts is a long-time friend and associate of Commissioner Birrane. Mr. Sharretts appears to have earned \$3,391.86 for subrogation work, part for a file review and part for contingent fees for monies recovered. While Mr. Sharretts had previous experience primarily in criminal law, Mr. Tull "based on my own experience in the field of claims

³³ Mr. Henry Rocklin, a partner in the Franklin firm, earned an additional \$550.00 pursuant to his selection for Consolidated Mutual worker's compensation defense work.

and subrogation over 20 some years" was well satisfied with Mr. Sharretts (Dep. p. 84).³⁴

Russell Fields and Robert Simmons were personal acquaintances of Ralph Moore, former MIGA Board Chairman and now Deputy Receiver for ACLIC.³⁵ Their firm earned \$1,673.91 for subrogation legal work performed. Other than Mr. Sharretts, and Simmons & Fields, the Maryland Indemnity records which we reviewed did not reflect any assignments of subrogation work.³⁶

5. Insolvency counsel

Weinberg and Green has billed, and received court approval, for over \$160,000.00 as a result of its representation of the receivership. We found that the firm's bills are detailed and itemized, both as to the nature of the work and the identity of the firm members performing the work. The firm bills quarterly; it does not receive payment until the court has approved the bill. All of the firm's bills are certified as "true and correct" by the Commissioner to the court. Besides several smaller lawsuits, the firm defended Commissioner Birrane as

³⁴ See, however, letter dated September 26, 1978 from Preston Tull to Douglas Sharretts, wherein Tull requests that Sharretts submit a status report on subrogation claims assigned six months earlier (App. III-18).

³⁵ As noted in Section II, Mr. Moore had Charles Mullaney add this firm, along with Stanford Franklin's firm, to MIGA's approved counsel list.

³⁶ Mr. Tull believes that Alan Rabineau, Esq. and "the Gomborov law firm" have had "a couple or very few" such files (Dep. p. 82). Both Mr. Rabineau and Mr. Gomborov had done defense work for Maryland Indemnity prior to its insolvency.

receiver and the receivership in a major piece of litigation, known as MIGA v. Birrane, involving several complex issues concerning MIGA's responsibility to pay certain claims, the status of reinsurers vis-a-vis the insolvency, and miscellaneous matters.

6. Real Estate Broker Services (MDIC)

In the Spring of 1979, after an unsuccessful attempt to lease the building the previous year, an attempt was made by Commissioner Birrane and Mr. Tull to auction the Maryland Indemnity Building, 10 S. Calvert Street. The auction produced several bids, but no final sale.³⁷ The receivership next determined to place the building with a broker. During the previous attempts to lease the building, the receivership had made contact with W.C. Pinkard & Co., specifically Mr. Dennis P. Malone as agent, and with Kornblatt & Associates.

When the insolvency determined to sell the building, Mr. Tull selected MDIC, the firm which provides free office space at the Towson Towers to Stanford Franklin, MDIC's commission was 10%. MDIC had not been involved in the prior lease attempts. Neither Pinkard nor Kornblatt was asked to submit a listing contract for the sale. Mr. Malone informed us that Pinkard's customary commission for a downtown central district commercial

³⁷ The high bidder submitted a contract which contained conditions which were not acceptable to the receivership.

property, such as the Maryland Indemnity building, was and is 6%.³⁸ We also contacted principals of Kornblatt & Associates, Parker-Frames, Kayne-Levin-Neilson-Bavar, and Manekin Corp., all major commercial brokerage firms for Baltimore City, who quoted us a range of 5-7% for the sale of such property in 1979.³⁹

Maryland Indemnity counsel have pointed out that Mr. Malone, on behalf of a prospective purchaser, submitted a contract to MDIC for a sale price of \$235,555.00 at a commission of 10% (App. III-34). Mr. Malone told us that when he attempted to submit a contract directly to Mr. Tull, he was referred to MDIC; his submission to MDIC necessarily quoted the 10% commission established by MDIC, as the listing agent, to be split evenly between MDIC and Pinkard. We note that the Malone contract did indeed call for a split commission, corroborating Mr. Malone. Furthermore, a May 18 handwritten memo by Mr. Tull confirms that Mr. Malone contacted Mr. Tull, who told Mr. Malone to submit his contract to MDIC (App. III-35).

MDIC and Mr. Tull executed the listing agreement on May 3, 1979. The contract of sale of the building was signed on June 1, 1979 (App. III-20). The buyer, Alan Rabineau, former defense

³⁸ The 6% rate was also confirmed by a principal of Pinkard.

³⁹ At the time of MDIC's selection, Mr. Malone wrote a letter to Commissioner Birrane criticizing the choice (App. III-18). Unaware of MDIC's 10% commission at that particular time, Mr. Malone's basic point was that a Baltimore City commercial brokerage firm was the logical choice to sell the Maryland Indemnity building, rather than a "relatively unknown" Towson firm, such as MDIC.

counsel to Maryland Indemnity (Dep. p. 82, App. III-23), was well known to both Commissioner Birrane and Mr. Tull, who were aware of his interest in the building from his previous sealed bid (the second highest) submitted at the auction. The building was sold within four weeks of the listing agreement, apparently without any advertising by MDIC despite a provision in the listing agreement requiring the realtor to spend "at least" \$1,000.00 advertising the property.⁴⁰

Moreover, it appears that the sales price obtained by the realtor was less than the price Commissioner Birrane or Preston Tull had considered - only four weeks earlier - to be the minimum acceptable price.

MDIC first drafted a listing agreement which, if executed, would have required it to procure a buyer at a purchase price of \$235,000.00, or such other price acceptable to the Receiver (App. III-22B). Commissioner Birrane considered the \$235,000.00 price too low, and directed that the \$235,000.00 figure be replaced with the sum of \$300,000.00. The Commissioner explained to us that, like selling a house, one always must start high. However, the \$300,000.00 figure typed in the new draft agreement was

⁴⁰ Mrs. Van Wright stated that, because her records for advertising are not broken down for individual properties, she could not state what MDIC spent for advertising the building. She said she recalls placing an advertisement in the Sunpapers for that sale, but said that the advertisement was not for sale at a stated price. Maryland Indemnity likewise has no records of MDIC's advertising of the building. Our check of Evening, Morning, and Sunday editions of the Sunpapers commercial property and business classified advertisements for the month of May, 1979 reveals no advertisement for the building's sale.

conspicuously modified by a provision, handwritten into the agreement, specifying a minimum \$250,000.00 sale price (App. III-22A). Therefore, the listing agreement, as executed on May 3, 1979, required that MDIC procure a buyer for at least \$250,000.00 before it could earn its 10% commission.

Still, just four weeks later, Commissioner Birrane or Preston Tull accepted a price below \$250,000.00, and receivership counsel - who was never told of the May 3, 1979 agreement which included the \$250,000.00 minimum - submitted a different contract, albeit also dated May 3, 1979, to the court (App. III-22C). The court approved the sale for \$240,000.00.

MDIC earned a \$24,000.00 commission on the sale of the building for \$240,000.00.⁴¹ Had Maryland Indemnity contracted with a major Baltimore brokerage, at a commission of 5-7%, as was customary for downtown Baltimore commercial brokerages, instead of with MDIC at a 10% commission, the receivership would have earned from \$7,200.00 to \$12,000.00 more on the sale to Mr. Rabineau.⁴² Had Commissioner Birrane or Preston Tull not quickly disregarded the \$250,000.00 minimum, the receivership may have

⁴¹ We do not address the adequacy of the sale price.

⁴² In a letter of May 14, 1979, explaining his selection of H. May Van Wright and MDIC, Mr. Tull states that he knew Ms. Van Wright through her former husband, the late David Ebersole (an attorney) and knew of Ms. Van Wright as "being a real estate broker who had an excellent record in her field", and as another reason, that he knew the firm to be "non political" (App. III-36). Although the letter implies some knowledge of the MDIC firm, both Commissioner Birrane and Mr. Tull stated that they were unaware that Stanford Franklin was a Vice President and Director of MDIC until our inquiry disclosed this fact.

earned at least an additional \$10,000.00 on the building's sale.

When asked about the two May 3rd listing agreements, and the presentation of only one of them to the Court, Commissioner Birrane stated that he had "no independent recollection"; nor could Commissioner Birrane inform us of the reason for the \$250,000.00 minimum, or the basis of the decision to abandon that minimum.

7. Audit and Bookkeeping

The firm of Andrew Caldwell & Associates was selected to perform audit services for the Maryland Indemnity insolvency in April of 1980, shortly before its selection by ACLIC as "special accountant", discussed in Section IV. In March of 1980, the firm had been selected by MIGA to perform its audit. Prior to Caldwell's selection, the firm of Main Hurdman (formerly Main Lafrentz) had performed the Maryland Indemnity audits since at least 1972, including the 1978 audit for the first year of insolvency.

Mr. Tull, in a letter to Commissioner Birrane of June 2, 1982, states that two "proposals" to perform the 1979 audit were "received"; one from Main Hurdman (the Maryland Indemnity auditor since at least 1972) and the second from Andrew Caldwell & Associates. As "the low bidder", Caldwell was awarded the work. Mr. Tull's letter does not indicate that a general canvass

of accounting firms was conducted; nor does the letter indicate how Caldwell came to be the only other firm, besides the previous auditor, to submit a "proposal" at all.

On May 7, 1980 the Circuit Court formally approved the Caldwell firm's contract with Maryland Indemnity to perform the 1979 audit at a cost not to exceed \$2,000.00. Similar contracts were approved on December 18, 1980 (1980 audit, not to exceed cost of \$2,200.00) and February 24, 1982 (1981 audit, at cost not to exceed \$3,000.00).

Mr. Charles Witzen, formerly an Assistant Treasurer at Maryland Indemnity at a salary of \$18,364.50 per year, resigned that position on February 9, 1979. On February 10, 1979, he was hired by the Maryland Indemnity receivership as a "consultant" on a part time basis at an annual salary of \$12,000.00. The petition of November 1979 asking approval for Mr. Witzen's appointment specifically cited his "long time familiarity of the affairs of Maryland Indemnity" and his "expertise in connection therewith." Mr. Witzen's reduction in salary appears commensurate with his part time status and Maryland Indemnity's decreased activity. We are nevertheless mindful that MIGA, ACLIC, and Maryland Indemnity, through separate agreements, now pay Mr. Witzen an aggregate annual salary of about \$40,000.

8. Travel and Entertainment

From March of 1979 through June of 1981, Mr. Tull has charged more than \$7,000.00 to the insolvency for his attendance at ten meetings of the NAIC and one meeting of the NCIGF. For the same period Commissioner Birrane has charged \$4,922.42 for travel to similar, or the same, meetings to Maryland Indemnity.⁴³ Often Commissioner Birrane and Mr. Tull attend the same meetings.⁴⁴ Normally, they will attend for the entire length of a given conference or convention.

Commissioner Birrane is quite adamant that his travel is necessary to keep abreast of liquidation and legislative developments, and to develop working relationships with Insurance Commissioners in other states. Commissioner Birrane is also adamant that our inclusion of airfare in travel expense totals is unfair.

Entertainment expenses other than travel charged by Mr. Tull amount to \$561.98 from December 1977 through June of 1981. This total includes charges for the entertainment of other individuals

⁴³ With the advent of the ACLIC insolvency (April, 1980) the Commissioner has been charging one-half of many of his travel expenses to Maryland Indemnity, one-half to ACLIC.

⁴⁴ Commissioner Birrane told us that he expressly directs Mr. Tull to attend these meetings.

(including Commissioner Birrane, Ralph Moore, and Stanford Franklin).

As a result of their statutory responsibility and authority, it is Commissioner Birrane and Mr. Tull who decide whether a particular trip is necessary or a particular expense justified. Effective, independent appraisals of their expenses do not appear to have been made.

Maryland Indemnity counsel has indicated that the Receivership followed the ACLIC travel policy, which was court-approved. We discuss the ACLIC travel policy in Section IV C 4(a) of the report. We observe here that the ACLIC travel policy was formulated in July of 1980 by Stanford Franklin, Ralph Moore and Commissioner Birrane, but was not submitted for Court approval until August of 1981, after the Evening Sun articles appeared. All of the Maryland Indemnity expenditures discussed here were incurred prior to August, 1981.

SECTION IV

AMERICAN CENTENNIAL LIFE INSURANCE COMPANY

A. Overview

In November of 1979, Commissioner Birrane¹, pursuant to Article 48, Section 132-164A, particularly Section 136, Maryland Code, applied to the Circuit Court for Baltimore City for appointment as Receiver directing rehabilitation efforts of ACLIC.² After a few months in the rehabilitation process, Commissioner Birrane, as Insurance Commissioner, successfully petitioned the Circuit Court on April 2, 1980 for termination of the rehabilitation, and appointment of the Commissioner as Liquidating Receiver for ACLIC in liquidation (App. IV-1).

Because of pending litigation in Georgia, discussed briefly in Sections IV B 2, and IV C 2, we did not have direct access to receivership records. At the instruction of John Taylor, Georgia counsel for ACLIC, the receivership supplied us with records after screening our requests. We were not permitted to examine

¹ As in the case of property and casualty insurance companies such as Maryland Indemnity, State law provides that the Insurance Commissioner shall also be the Receiver for life and health insurance insolvencies, with the same powers and duties described in Section IV B 2.

² Although ACLIC was and is a Maryland chartered company, engaged in the business of life and health insurance, its executive and operations offices and staff were located in Atlanta, Georgia at this time.

ACLIC records that, in ACLIC's view, disclosed material relevant to the Georgia litigation.

Our findings at ACLIC revealed: (1) selection of persons with limited, relevant experience in life and health insurance, such as Deputy Receiver Ralph Moore³ and auditor Andrew Caldwell & Associates; (2) substantially uncontrolled travel and entertainment expense; (3) questionable value of outside services utilized, such as Free State and its subsidiary, Office E-Z Move.

B. ACLIC APPOINTMENTS - STAFF AND CONTRACTUAL SERVICES⁴

1. Ralph Moore

On May 16, 1980, Commissioner Birrane successfully petitioned the Circuit Court for Baltimore City (Hon. Joseph H. Kaplan) for appointment of Mr. Ralph Moore as Special Deputy Insurance Commissioner to act for the Receiver in the ACLIC insolvency (App. IV-2). Prior to his selection of Mr. Moore, Commissioner Birrane had offered the position to Mr. Edward Gosling, a retired life insurance executive with Baltimore Life (Sun Life of Canada). Mr. Gosling, who had a life insurance

³ Ralph Moore was previously appointed to the MIGA Board by Commissioner Birrane, see Section II.

⁴ Throughout this section of the report, the court appointments discussed have resulted from action on a Petition filed by the Receiver, Edward J. Birrane, Jr. In each instance the Petition was unopposed and the Court granted the requested appointment without further proceedings.

accounting background, had been interviewed and recommended for the position by Sidney Green, Chief Actuary of the Insurance Division.⁵ Receivership records show that Mr. Gosling visited ACLIC's Atlanta offices from April 30 to May 2, 1980. According to Evia Christian, Mr. Gosling refused the job because of its projected duration.

Within a week of Mr. Gosling's decision, Mr. Sidney Green interviewed and recommended Mr. Dale Raubenstine, another person with life insurance accounting background, for the position. On May 9, 1980 Mr. Green submitted Mr. Raubenstine's resume to Commissioner Birrane and endorsed Mr. Raubenstine for the ACLIC position. Thereafter, Mr. Green attempted to arrange an interview between Commissioner Birrane and Mr. Raubenstine, but the interview "never materialized" because Commissioner Birrane told Mr. Green that he had "spoken to someone else [he] considered satisfactory for the position and who would be hired" (App. IV-13).

Commissioner Birrane's selection was Ralph Moore. Mr. Moore told us that only days prior to his May 16, 1980 appointment, he learned from Commissioner Birrane that he was having difficulty in finding a Deputy Commissioner/Receiver for ACLIC. At that

⁵ Mr. Gosling has been deceased since the Spring of 1981. We discussed his potential ACLIC employment with his widow Estella Gosling, as well as with Mr. Green and Mr. Evia Christian of the Insurance Division.

time, Mr. Moore told Commissioner Birrane he was interested in the position.⁶

Ralph Moore's insurance background prior to ACLIC was almost entirely in the property and casualty field.⁷ Mr. Moore's limited life and health insurance background raises questions about his selection for the ACLIC position which placed him in a position charged with day to day operation of a life and health insurer.⁸

⁶ Mr. Moore also told us that his interest in the job came "much to the surprise and pleasure" of the Commissioner, inasmuch as the job did not have a definite, permanent term.

⁷ ACLIC representatives have submitted evidence of several appointments or awards as indicative of Mr. Moore's qualifications for his post as Deputy receiver. Those are his membership in the Baltimore Claimsman's Association and his service as a director to that organization; his membership on the Claims Manager Council; his receipt of the Insurance Information Institute's Leadership Award and his selection to the advisory board of that group; and his selection to the MIGA Board. It was Mr. Moore's friend, Charles Mullaney, who nominated Mr. Moore for the Leadership Award. Secretary Corbley told us that receipt of the award automatically leads to membership on the Advisory Board. The institute is comprised of property and casualty insurance companies. Commissioner Birrane informed us that he would have appointed Ralph Moore even if he had not received these appointments or awards.

⁸ Mr. Moore's resume indicates that his only life and health experience was gained in his first post-college employment from 1965 to 1967 where he conducted "investigatory analysis of claims" including life, health and accident claims. Mr. Moore's MIGA experience from June 1978 to May 1980 would have given him background in how a guaranty association handles the claims of an insolvent property and casualty insurer. Frank Csar, the Illinois liquidator, in his interview, emphasized that Mr. Moore's two year MIGA experience and claims background made him more qualified than Mr. Csar himself, to run a life insurance insolvency. Mr. Csar, who has a law degree, has served as Chief Executive Officer of life and casualty insurance affiliates and had been Vice-President, General Counsel and Director of General Finance Company for some twenty years, felt that Mr. Moore's experience in liquidations (MIGA) made him peculiarly qualified to operate ACLIC.

Mr. Moore told us that his move from his previous employment at Commercial Union Insurance Companies to ACLIC was "a lateral one" in salary, but, notwithstanding the temporary nature of the ACLIC job, "for the betterment of myself, and my value to future employers". Mr. Moore's original contract was for a six month period at a salary of \$16,500 (App. IV-4). At the conclusion of the first six month contract, on November 27, 1980, Commissioner Birrane executed a five year contract providing Mr. Moore with compensation at the level of a state employee at Grade 21 Step 6, plus 20% (for lack of certain fringe benefits available to state employees), including any cost of living adjustments to be afforded State employees at that grade during the course of the contract. Since November 27, 1980, Mr. Moore's salary has been \$41,600.00 per annum (App. IV-3).

We learned from LHIGA officials that Mr. Moore is also paid by LHIGA, at the rate of \$25.00 per hour, for such services as co-signing checks. Mr. Moore has refused to tell us what amount of money he has been paid. LHIGA maintains that because their records are confidential by statute, they cannot give us that information. LHIGA did give us comparable payment information on Free State and its accountants without invoking the statute.

2. Andrew Caldwell & Associates

On May 20, 1980, the Caldwell firm (which had, since February 1977, done the accounting for Free State and which shortly before the ACLIC appointment had begun doing auditing work for both Maryland Indemnity (hired May 7, 1980), and MIGA (hired March 1980)), was appointed "Special Accountant" to ACLIC by the Circuit Court, pursuant to a petition filed by Commissioner Birrane.

Mr. Caldwell explained his appointment as follows. In late April of 1980, Mr. Caldwell attended an NAIC convention at Lake Buena Vista, Florida, as an outgrowth of his work for MIGA, which had employed his firm only a month earlier. While there, he happened to meet Commissioner Birrane, who mentioned his need for an ACLIC audit. They discussed the ACLIC job and apparently Mr. Caldwell was hired. Evia Christian, a member of the Insurance Division's staff of examiners then on duty at ACLIC's Atlanta offices, told us that several days after the NAIC convention, he was told that the Insurance Commissioner had hired the firm of Caldwell & Associates to do a CPA audit of ACLIC.

We attempted to learn the special reason that this firm had become the auditing choice of MIGA, Maryland Indemnity and ACLIC in the space of less than three months, but have had some difficulty doing so. The firm's selection for the ACLIC work,

for example, cannot be explained in terms of special life or health insurance accounting expertise. In fact, we know that Mr. Caldwell's four member firm did not have such expertise at the time Commissioner Birrane offered him the ACLIC job. Only after the firm was selected did Mr. Caldwell hire an auditor who possessed a life and health insurance background. We asked Mr. Caldwell about his firm's prior relevant experience and he told us only that he had gained a basic understanding of receiverships as Receiver for Delp Concrete Construction Company in 1975. We question whether Caldwell's selection by MIGA (in March, 1980) to do its financial audit, or the almost contemporaneous selection by Maryland Indemnity (on May 7, 1980) to do its auditing could have provided a basis for the firm's selection for the ACLIC work by Commissioner Birrane in April 1980.

Mr. Caldwell's firm has been paid approximately \$300,000 from May, 1980 through February 1982 for services to ACLIC. Those services are continuing. According to ACLIC representatives and Andrew Caldwell, the firm has prepared a 1979-1980 audit, is preparing subsequent year audits and has provided and continues to provide other support services to ACLIC.⁹

⁹ That audit and other services will be further discussed in IV C 2.

3. Free State (Office E-Z Move)

On June 2, 1980, the Circuit Court approved Commissioner Birrane's petition for permission to move ACLIC's current operations from Atlanta to Baltimore (the move actually was to 305 W. Chesapeake Ave., Towson, Md.).¹⁰ The petition was silent as to expenses related to the move (App. IV-10). In fact, Ralph Moore hired at a cost of over \$24,000 Office E-Z Move, an arm of Free State, to supervise and arrange the move and to perform certain move-related activities, including services to provide office supplies, equipment rentals and secretarial/clerical personnel. Office E-Z Move did not pack the property to be moved or perform the actual physical move. Those services were performed by United Van Lines.

Mr. Moore told us that Office E-Z Move was selected by him because "they are just outstanding" in the area of commercial moves. We learned that "Office E-Z Move" was in fact Patricia Prodoehl, wife of Free State President Henry Prodoehl (App. IV-21-23). Mr. and Mrs. Prodoehl repeatedly refused to be interviewed. They did, however, submit through ACLIC a "history" of Office E-Z Move. That "history" does not disclose the nature of services rendered or to whom the services were rendered (App.

¹⁰ We do not address the wisdom of moving ACLIC's operations to Maryland and in fact there is every indication that the decision to move can be justified. Rather, our concerns arise from the selection of Office E-Z Move, the value of its services, and the costs of its services.

IV-24). We checked the 1978, 1979, 1980 and 1981 Baltimore Metropolitan telephone directories, but found no listing for Free State as a commercial or office moving company and no listing at all for Office E-Z Move. We contacted C & P Telephone Company officials who advised us that the first listing for Office E-Z Move had been placed in the Baltimore telephone directory on December 17, 1981.

4. Stanford Franklin

On June 23, 1980, Commissioner Birrane authorized Stanford Franklin¹¹ to represent ACLIC as local counsel (App. IV-9), at the rate of \$70.00 per hour approved by the Court.

Mr. Franklin refused repeated requests for an interview. In a written statement, he explained his selection as ACLIC's local counsel by Commissioner Birrane, as follows:

"During the course of the conversation with Commissioner Birrane, he mentioned the appointment of Ralph Moore as Deputy Liquidator in charge of the American Centennial Receivership. I asked the Commissioner if the Receivership had appointed local counsel and was advised that only Atlanta Counsel had, at that time, been approved by the Court. I told the Commissioner that I would be interested in assisting him and he told me that he would be pleased to have my Firm represent the Receivership. Thereafter, the Commissioner

¹¹ Mr. Franklin, his wife Sylvia, and the real estate firm MDIC have all been discussed in Sections II and III of this report.

sought Court approval for my Firm to represent the Receivership and the Court ratified my appointment." (App. IV-28).

5. Other ACLIC Employees

Mr. Charles Witzen has been the bookkeeper for ACLIC since June 18, 1980 at a contractual rate of \$21.00 per hour, and has averaged 16 hours per week of ACLIC work. Besides this income, Mr. Witzen receives a flat fee of \$12,000 per annum from Maryland Indemnity, and a contractual rate of \$21.00 per hour, averaging 15 hours per week, from MIGA. Since his hiring by ACLIC, Mr. Witzen has earned approximately \$40,000 per annum for his services to the three entities.

Mr. Witzen's wife Shirley "runs the ACLIC office" at a contracted rate of pay of \$11.00 per hour for a 40 hour week, an annual income of \$22,580.00. She was hired on July 7, 1980. Her sister, Janet Nelson, has also been employed at ACLIC since September 15, 1980 in a clerical position.

Joseph Burns has been employed at ACLIC since September 2, 1980 in various capacities. The contracts of September 2, 1980 and December 2, 1980 between Mr. Burns and Deputy Moore describe Mr. Burns as a "claims coordinator" at an annual salary of \$18,000.00 (App. IV-15, 17). On April 1, 1981, after court approval of the petition by Commissioner Birrane, Mr. Burns' title became "Special Assistant Insurance Commissioner and

Assistant Deputy Receiver", with compensation at the level of a state employee at Grade 19, Step 2 plus 20% (for lack of certain fringe benefits available to state employees) for an annual income in excess of \$30,000.00 (App. IV-16).

Just prior to his ACLIC employment, in September of 1980, Mr. Burns was temporarily assigned as a legal assistant to the Insurance Division. During his State employment Mr. Burns was compensated at a Grade 12, Step 1 rate, approximately \$14,238.00 per annum plus fringe benefits.

C. EXPENSES¹²

1. Free State and Office E-Z Move

Free State's Office E-Z move has been paid over \$24,000 for services related to two moves of ACLIC operations from Georgia to Maryland. These services, with the exception of a spot file review, were billed under written contracts of June 24, 1980, July 24, 1980 and May 22, 1981 between ACLIC Deputy Receiver Ralph Moore and Mrs. Prodoehl (App. IV-21, IV-22 and IV-23). The services under the first two contracts relate to ACLIC's move of its current operations in July 1980. The

¹² As part of our review of the expenses discussed in this section, we have reviewed the file of ACLIC proceedings in the Circuit Court for Baltimore County. While in many cases the court has approved the requested engagements and appointments, at times even approving a rate of payment, the amounts discussed here were never presented to the Court for approval.

services under the third contract relate to the later move of ACLIC closed files made in February, 1981.

(a) The first move

For services related to the July, 1980 move, Free State charged and was paid the following amounts:

(1) Administrative services and expenses of Patricia Prodoehl for the move ¹³	\$4,321.77
(2) Office supplies and equipment rental, overhead, mileage	2,471.33
(3) Temporary secretarial help ¹⁴ at \$7.50 per hour per secretary	7,200.00

¹³ Mrs. Prodoehl's services, for which she charged \$25.00 per hour, are described as follows in the June 24, 1980 contract.

- "1. Arrange to inspect new office.
2. Order phone installation.
3. Arrange movers to meet with Mr. Moore in Atlanta.
4. Order stationary and cards as needed.
5. Consider needs for dictation equipment.
6. Measure and draw to scale the new office.
7. Inventory furniture in Atlanta.
8. Decide placement in Baltimore office.
9. Provide lunch and supplies for moving day.
10. Supervise packing of files in Atlanta.
11. Recommended purchase of additional equipment needed - purchase with approval.
12. Information on postage meters.
13. Buy office supplies as needed.
14. Supervise placement of furniture in Baltimore.
15. Supervise unpacking of files." (App. IV-21).

¹⁴ The temporary help consisted of Kathy Prodoehl and Gail Corum, whose sister Deborah was employed by MIGA (Section II). Gail Corum is now a Free State employee assigned full time to LHIGA "for claims processing".

(4) Administrative, organizational and supervisory services of Mrs Prodoehl at \$25.00 per hour ¹⁵	1,331.25
(5) "Spot review" of files ¹⁶	<u>776.00</u>
Total	<u>\$16,100.35</u>

Mr. Evia Christian is an Insurance Division Examiner who was part of the Division's rehabilitation and audit of ACLIC from December 1979 to May 1980.¹⁷ He recalls that as early as March, 1980 he was aware that a move of ACLIC's active operations to Maryland was likely to occur so that the Receivership could run more smoothly. Mr. Christian, in an affidavit supplied by ACLIC, indicated that "I did, generally, prepare the company for a move after the decision to move was made. I isolated and identified certain active files so that, when the time came, these files could be boxed up and moved to Maryland with some dispatch." Mr. Christian told us that he had organized and prepared the operations of the company for the move over the almost two months prior to his leaving ACLIC. He described the current, active files as ready to be placed in boxes (which he had already

¹⁵ Although no hourly rate for Mrs. Prodoehl's services is stated in the July 24, 1980 contract, ACLIC representatives told us that she billed and was paid at the \$25.00 per hour rate for her services in connection with the second contract.

¹⁶ That review was conducted by Henry Prodoehl and another Free State employee, and is not included in any of the three contracts.

¹⁷ There were two examinations of ACLIC by the Maryland Insurance Division, one during the rehabilitation period.

purchased) and to be moved.¹⁸ Both Mr. Christian and ACLIC representatives have impressed upon us the fact that ACLIC was an operating insurance company and that the move had to occur with "some dispatch". It was apparently to insure an expeditious move that Mr. Christian made his preparations.

ACLIC representatives have told us that the necessity for speed justified the selection of Mrs. Prodoehl to administer the move. They also indicated that the Atlanta services could not be handled by the ACLIC full time staff at that time, which consisted of Mr. Moore and Administrative Assistant Shirley Witzen. No explanation has been given as to why Mrs. Witzen, who insists that Mrs. Prodoehl's services were essential, could not have performed at least some of the Baltimore based tasks for the July 15 move such as inspecting the new office, ordering a phone, ordering stationery and cards, measuring and drawing the new office, deciding on placement of furniture and equipment, ordering equipment and supplies, obtaining postage meter information and supervising unpacking, the hiring and supervising of temporary secretarial/clerical help, purchasing office

¹⁸ The furniture which Mr. Christian thought should be part of the Baltimore ACLIC operation was subject to a legal dispute. Mr. Christian stated that he understood if that furniture were moved to Baltimore, it might later be declared the property of someone other than ACLIC.

supplies, and leasing equipment, in short the services provided by Office E-Z Move pursuant to the June 24, 1980 contract.¹⁹

(b) The Second move

In February of 1981, Mr. Small, of Caldwell & Associates, arranged the move of the old financial records of ACLIC from Atlanta to space at Loch Raven Boulevard, rented from the MIGA claims department. Free State charged as follows for services related to this second ACLIC move:

(a)	Administrative, organizational and supervisory services of Mrs. Prodoehl at \$25 per hour	\$4,500.00
(b)	Clerical help ²⁰	3,600.00
(c)	Office supplies	<u>36.26</u>
	Total ²¹	<u>\$8,136.26</u>

¹⁹ ACLIC representatives have now stated that they will submit in writing the rationale for their position that Mrs. Witzen could not perform these duties.

²⁰ That work was performed by Judith Prodoehl and Kimberly Ports for which Free State charged \$4.50 per hour.

²¹ Items (a) and (b) are included in the June 16, 1981 contract (App. IV-25).

Once again, we asked ACLIC representatives why Mrs. Witzen or other ACLIC staff could not have "administered, organized, or supervised" the cataloguing of ACLIC's closed files. Ralph Moore has responded, in a letter dated May 27, 1982 that "[I]t was virtually impossible to spare either of these individuals [Mrs. Witzen or Mrs. Nelson] anytime at all . . . for the purpose of supervising the young girls who were sorting the documents" at the Loch Raven "storage center".

With Mr. Moore's recent letter there was attached "SYNOPSIS OF BILL FROM OFFICE E-Z MOVE" which stated in part "[I]t must be remembered the temporary people employed at the minimum wage were in fact high school students, who had no idea whatsoever, the difference between general ledgers, inter-office memoranda, Board of Directors Minutes, etc.". However, ACLIC prepared documents supplied to us indicate payments to Free State for clerical help at \$4.50 per hour, rather than minimum wage, which raises the question of whether Office E-Z Move profitted beyond Mrs. Prodoehl's \$25.00 per hour charge.²²

(c) Static Reserve

In July of 1981, Commissioner Birrane and Ralph Moore authorized Free State to perform a "static reserve" of ACLIC life and health claims (App. IV-18). This reserve was not an

²² See App. IV-25, 3C.

actuarial reserve which would estimate future liabilities, but merely an inventory of present total liabilities. Free State charged, and received, \$10,600 for this review. The utility of this review is subject to serious question.

When we inquired as to the purpose of the "reserve", Commissioner Birrane stated that the reserve was to be sent to several interested purchasers of ACLIC business in order for them to have an approximation of ACLIC's claim liability status. In fact, according to ACLIC documents, the only company which received the "reserve study" was American International Group (hereafter "AIG"), a New York company.

We contacted Ms. Fran Semaya, Director of Licensing for AIG, the official to whom the "reserve" was sent (App. IV-19, IV-20). She stated that she had filed the reserve away in her office, without giving it to any AIG official connected with acquisition. In a recent letter to Commissioner Birrane, she elaborated that the reserve "was not warranted to pass on to my superiors at that time without an actuarial reserve." (App. IV-26). Both she and Vice President and General Counsel Patrick Foley of AIG averred that without an actuarial reserve, there was no reason for AIG to pursue the matter further.²³

²³ Mr. Frank Csar, the Illinois liquidator, told us that he issues only actuarial reserves on behalf of life insurance insolvencies under his jurisdiction.

The actuarial reserve performed by the Insurance Division in March of 1980 was never sent to AIG. This reserve was done by Sidney Green, Chief of the Life and Health Section of the Insurance Division for 22 years, a member of the American Academy of Actuaries and, in Mr. Foley's words, a "first-class" actuary. ACLIC representatives told us that in August 1981 Commissioner Birrane engaged a supplementary actuarial analysis to complement the static reserve.

2. Andrew Caldwell & Associates

The Caldwell firm, pursuant to Commissioner's Birrane's petition to the Circuit Court, was appointed "Special Accountant" for the ACLIC insolvency on May 20, 1980 (App. IV-12A). To date, the firm has billed and received from ACLIC over \$300,000.00 for various accounting services.

In February of 1981 Commissioner Birrane successfully petitioned for leave to have the Caldwell firm conduct an audit of ACLIC for the first year of the insolvency, April 2, 1980 through March 31, 1981.²⁴ On March 1, 1982, ACLIC filed an audit

²⁴ By order of August 31, 1981, the court required that audit to be completed on or before October 31, 1981. ACLIC petitioned for, and received, an extension of time to and including March 1, 1982 for the filing of the April 1980-March 31, 1981 audit (App. IV-12C). The audit is now due to be filed on June 1, 1982, and ACLIC representatives have stated that there will be no further extension of the filing time. In part because of the history of postponed filing dates for that audit, we will not delay this report until after the ACLIC audit is filed. As of the date of this report, the 1980-81 audit had not been filed.

with the Circuit Court, but for the year preceding insolvency, April 2, 1979-March 31, 1980. ACLIC's petition and the Court's initial filing order had all referred to an audit of the first year of the insolvency, but that audit was not filed. In fact, ACLIC's March 2, 1982 petition referred to the 1979-1980 audit in a context which may have suggested that the audit being filed had been ordered by the Circuit Court. (App. IV-12B). The earlier court orders pertained only to the April 1980-March 1981 audit, which will be filed on June 1, according to ACLIC representatives.

Mr. Caldwell has billed the receivership for approximately 6,000 hours of accountant work, at a rate of \$50.00 per hour. On April 23, 1982, Mr. Caldwell provided the following breakdown of his time in a written submission:

"3,000 - 3,600 hours of our time was spent on the March 31, 1980 audit, investigation of waste and mismanagement and reconstruction of the accounting records. Approximately 600 hours was spent on the March 31, 1981 audit and the remainder of the 6,000 hours was spent supporting the receiver and his attorneys."

ACLIC counsel has informed us that Mr. Caldwell has not submitted any itemized billings to the receivership for its review prior to payments to the firm. Other than the estimates provided in the recent Caldwell letter, neither Commissioner Birrane, receivership counsel, nor the court, has any precise idea of the amount of time spent on the tasks enumerated by the

firm. (Mr. Csar stated that, in his practice as Illinois liquidator, all accountant billings must be itemized and submitted to him for approval, and to the court for approval, before payments of those bills are made.)

Given the lack of specificity of Caldwell billings, and given the substantial monies expended by ACLIC for auditing services, we have engaged the firm of Coopers and Lybrand to review the work performed by the Caldwell firm for ACLIC and evaluate those billings. Over the opposition of ACLIC, represented by Stanford Franklin, we have obtained a court order making the Caldwell audit available to Coopers and Lybrand for their review.

3. Stanford Franklin

Mr. Franklin has been paid \$38,000 by ACLIC from the date of his appointment June 27, 1980, through October 1981. Since Mr. Franklin refused to be interviewed, we must base our description of his work on information gained from other sources. From ACLIC records, which do include billings from Mr. Franklin, it appears that he has reviewed ACLIC's lease at 305 W. Chesapeake Ave. in Towson; he has issued an opinion on ACLIC automobile and travel policy; he has filed periodic petitions with the court, none of which has entailed extended court proceedings; and finally, according to ACLIC's Georgia counsel John Taylor, Mr. Franklin

particularly then Secretary of Budget and Fiscal Planning Thomas W. Schmidt, as to whether Commissioner Birrane had to keep and submit records, regarding his use of the State vehicle. Secretary Corbley described for us the occasion in July of 1980 when Commissioner Birrane turned in his State car, and announced that he would no longer have to comply with the State's "unreasonable" requirements to document mileage and use now that he was no longer in need of a State car.

Commissioner Birrane's use of the Buick, though prominently mentioned in the Evening Sun articles, and while noteworthy, has limited significance. Commissioner Birrane told us that he has been temperate in his personal use of the vehicle, and, though there are no records to corroborate him, we will not question that statement.

The facts surrounding the Commissioner's possession of the Buick demonstrate that he was displeased with the travel restrictions that applied to his State vehicle. His friend and appointee Ralph Moore leased an automobile for a period that almost exactly coincided with the Commissioner's term of office, and Stanford Franklin then blessed Commissioner Birrane, rather than any full time ACLIC employee, as custodian of the Buick. Though on a relatively small scale, Commissioner Birrane nonetheless benefitted from the highly in-bred system he created.