

CNA FINANCIAL CORP
Form 10-Q
November 02, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2009

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission File Number 1-5823

CNA FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

36-6169860

(I.R.S. Employer
Identification No.)

**333 S. Wabash
Chicago, Illinois**

(Address of principal executive offices)

60604

(Zip Code)

(312) 822-5000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class
Common Stock, Par value \$2.50

Outstanding at October 29, 2009
269,026,759

**CNA Financial Corporation
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Periods ended September 30 (In millions, except per share data)	Three Months		Nine Months	
	2009	2008	2009	2008
Revenues				
Net earned premiums	\$ 1,707	\$ 1,799	\$ 5,035	\$ 5,386
Net investment income	660	439	1,755	1,449
Net realized investment losses, net of participating policyholders' interests:				
Other-than-temporary impairment losses	(232)	(584)	(1,330)	(840)
Portion of other-than-temporary impairment losses recognized in Other comprehensive income	84		173	
Net impairment losses recognized in earnings	(148)	(584)	(1,157)	(840)
Other net realized investment gains (losses)	48	(67)	228	27
Net realized investment losses, net of participating policyholders' interests	(100)	(651)	(929)	(813)
Other revenues	73	72	213	240
Total revenues	2,340	1,659	6,074	6,262
Claims, Benefits and Expenses				
Insurance claims and policyholders' benefits	1,283	1,519	3,919	4,380
Amortization of deferred acquisition costs	365	355	1,063	1,083
Other operating expenses	272	294	814	724
Interest	34	33	95	100
Total claims, benefits and expenses	1,954	2,201	5,891	6,287
Income (loss) from continuing operations before income tax	386	(542)	183	(25)
Income tax (expense) benefit	(108)	218	30	92
Income (loss) from continuing operations	278	(324)	213	67
Income (loss) from discontinued operations, net of income tax (expense) benefit of \$0, \$9, \$0 and \$9	(1)	9	(2)	10

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Net income (loss)	277	(315)	211	77
Net income attributable to noncontrolling interests	(14)	(16)	(38)	(40)
Net income (loss) attributable to CNAF	\$ 263	\$ (331)	\$ 173	\$ 37
Income (Loss) Attributable to CNAF Common Stockholders				
Income (loss) from continuing operations attributable to CNAF	\$ 264	\$ (340)	\$ 175	\$ 27
Less: Dividends on 2008 Senior Preferred	(31)		(94)	
Income (loss) from continuing operations attributable to CNAF common stockholders	233	(340)	81	27
Income (loss) from discontinued operations attributable to CNAF common stockholders	(1)	9	(2)	10
Income (loss) attributable to CNAF common stockholders	\$ 232	\$ (331)	\$ 79	\$ 37

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

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Periods ended September 30 (In millions, except per share data)	Three Months		Nine Months	
	2009	2008	2009	2008
Basic and Diluted Earnings (Loss) Per Share Attributable to CNAF Common Stockholders				
Income (loss) from continuing operations attributable to CNAF common stockholders	\$ 0.86	\$ (1.26)	\$ 0.30	\$ 0.10
Income (loss) from discontinued operations attributable to CNAF common stockholders		0.03	(0.01)	0.04
Basic and diluted earnings (loss) per share attributable to CNAF common stockholders	\$ 0.86	\$ (1.23)	\$ 0.29	\$ 0.14
Weighted Average Outstanding Common Stock and Common Stock Equivalents				
Basic	269.0	269.0	269.0	269.6
Diluted	269.2	269.1	269.1	269.6

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements
(Unaudited).

Table of Contents**CNA Financial Corporation (CNAF)
Condensed Consolidated Statements of Comprehensive Income (Unaudited)**

Periods ended September 30 (In millions)	Three Months		Nine Months	
	2009	2008	2009	2008
Net income (loss)	\$ 277	\$ (315)	\$ 211	\$ 77
Other comprehensive income (loss), net of tax				
Changes in:				
Net unrealized losses on investments with other-than-temporary impairments	(36)		(70)	
Net other unrealized gains (losses) on investments	1,906	(1,212)	3,815	(2,246)
Net unrealized gains (losses) on investments	1,870	(1,212)	3,745	(2,246)
Unrealized gains (losses) on discontinued operations and other	5	(3)	5	(3)
Foreign currency translation adjustment	39	(44)	110	(53)
Pension and postretirement benefits	1	(2)	4	(5)
Allocation to participating policyholders	(17)	10	(36)	24
Other comprehensive income (loss), net of tax	1,898	(1,251)	3,828	(2,283)
Comprehensive income (loss)	2,175	(1,566)	4,039	(2,206)
Net income attributable to noncontrolling interests	(14)	(16)	(38)	(40)
Other comprehensive (income) loss attributable to noncontrolling interests	(18)	9	(29)	17
Total comprehensive income (loss) attributable to CNAF	\$ 2,143	\$ (1,573)	\$ 3,972	\$ (2,229)

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements
(Unaudited).

Table of Contents**CNA Financial Corporation (CNAF)
Condensed Consolidated Balance Sheets (Unaudited)**

(In millions, except share data)	September 30, 2009	December 31, 2008
Assets		
Investments:		
Fixed maturity securities at fair value (amortized cost of \$34,880 and \$34,155)	\$ 34,718	\$ 28,887
Equity securities at fair value (cost of \$639 and \$1,016)	972	871
Limited partnership investments	1,890	1,683
Other invested assets	6	28
Short term investments	4,075	3,534
 Total investments	 41,661	 35,003
Cash	128	85
Reinsurance receivables (less allowance for uncollectible receivables of \$357 and \$366)	6,644	7,395
Insurance receivables (less allowance for doubtful accounts of \$211 and \$221)	1,720	1,818
Accrued investment income	429	356
Receivables for securities sold and collateral	235	402
Deferred acquisition costs	1,138	1,125
Prepaid reinsurance premiums	223	237
Federal income tax recoverable (includes \$428 and \$299 due from Loews Corporation)	434	294
Deferred income taxes	1,383	3,493
Property and equipment at cost (less accumulated depreciation of \$488 and \$641)	363	393
Goodwill and other intangible assets	141	141
Other assets	624	562
Separate account business	452	384
 Total assets	 \$ 55,575	 \$ 51,688
 Liabilities and Equity		
Liabilities:		
Insurance reserves:		
Claim and claim adjustment expenses	\$ 26,906	\$ 27,593
Unearned premiums	3,392	3,406
Future policy benefits	7,864	7,529
Policyholders funds	200	243
Collateral on loaned securities and derivatives	1	6
Payables for securities purchased	502	12
Participating policyholders funds	55	20
Long term debt	2,056	2,058
Reinsurance balances payable	339	316

Other liabilities	2,553	2,824
Separate account business	452	384
Total liabilities	44,320	44,391
Commitments and contingencies (Notes D, E, G, H, and J)		
Equity:		
Preferred stock (12,500,000 shares authorized)		
2008 Senior Preferred (no par value; \$100,000 stated value; 12,500 shares issued; held by Loews Corporation)		
	1,250	1,250
Common stock (\$2.50 par value; 500,000,000 shares authorized; 273,040,243 shares issued; and 269,026,759 and 269,024,408 shares outstanding)		
	683	683
Additional paid-in capital	2,176	2,174
Retained earnings	7,046	6,845
Accumulated other comprehensive loss	(247)	(3,924)
Treasury stock (4,013,484 and 4,015,835 shares), at cost	(109)	(109)
Notes receivable for the issuance of common stock	(30)	(42)
Total CNAF stockholders equity	10,769	6,877
Noncontrolling interests	486	420
Total equity	11,255	7,297
Total liabilities and equity	\$ 55,575	\$ 51,688

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements (Unaudited).

Table of Contents**CNA Financial Corporation (CNAF)
Condensed Consolidated Statements of Cash Flows (Unaudited)****Nine months ended September 30**

(In millions)

	2009	2008
Cash Flows from Operating Activities		
Net income	\$ 211	\$ 77
Adjustments to reconcile net income to net cash flows provided by operating activities:		
(Income) loss from discontinued operations	2	(10)
Loss on disposal of property and equipment	13	1
Deferred income tax provision	81	6
Trading portfolio activity	(621)	472
Net realized investment losses, net of participating policyholders' interests	929	813
Undistributed (earnings) losses of equity method investees	(151)	137
Net amortization of investment discount	(169)	(217)
Depreciation	63	56
Changes in:		
Receivables, net	849	712
Accrued investment income	(73)	(54)
Deferred acquisition costs	(13)	4
Prepaid reinsurance premiums	14	(6)
Federal income taxes recoverable	(140)	(276)
Insurance reserves	(488)	(238)
Reinsurance balances payable	23	(34)
Other assets	(66)	(6)
Other liabilities	(177)	(174)
Other, net	4	5
Total adjustments	80	1,191
Net cash flows provided by operating activities-continuing operations	\$ 291	\$ 1,268
Net cash flows used by operating activities-discontinued operations	\$ (16)	\$ (7)
Net cash flows provided by operating activities-total	\$ 275	\$ 1,261
Cash Flows from Investing Activities		
Purchases of fixed maturity securities	\$ (18,099)	\$ (39,989)
Proceeds from fixed maturity securities:		
Sales	15,507	36,545
Maturities, calls and redemptions	2,568	3,374
Purchases of equity securities	(262)	(170)
Proceeds from sales of equity securities	510	177
Change in short term investments	(460)	(165)
Change in collateral on loaned securities and derivatives	(5)	(57)

Change in other investments	101	(153)
Purchases of property and equipment	(46)	(90)
Other, net	2	3
Net cash flows used by investing activities-continuing operations	\$ (184)	\$ (525)
Net cash flows provided by investing activities-discontinued operations	\$ 16	\$ 17
Net cash flows used by investing activities-total	\$ (168)	\$ (508)

The accompanying Notes are an integral part of these Condensed Consolidated Financial Statements
(Unaudited).

Table of Contents**Nine months ended September 30**

(In millions)

Cash Flows from Financing Activities

	2009	2008
Dividends paid to common stockholders	\$	\$ (122)
Dividends paid to Loews Corporation for 2008 Senior Preferred	(94)	
Principal payments on debt		(150)
Return of investment contract account balances	(10)	(421)
Receipts on investment contract account balances	3	3
Stock options exercised	1	1
Purchase of treasury stock		(70)
Other, net	28	26

Other Terms of the Notes

The provisions of this section supersede and replace the definition of **Market Measure Business Day** set forth in product prospectus supplement EQUITY INDICES SUN-1.

Market Measure Business Day

A **Market Measure Business Day** means a day on which:

(A) the Eurex (or any successor) is open for trading; and

(B) the Index or any successor thereto is calculated and published.

Autocallable Market-Linked Step Up Notes	TS-8
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Autocallable Market-Linked Step Up Notes

Linked to the EURO STOXX 50® Index, due December 20, 2019

The Index

All disclosures contained in this term sheet regarding the Index, including, without limitation, its make-up, method of calculation, and changes in its components, have been derived from publicly available sources. The information reflects the policies of, and is subject to change by, STOXX Limited (STOXX or the Index sponsor). The Index sponsor, which owns the copyright and all other rights to the Index, has no obligation to continue to publish, and may discontinue publication of, the Index. The consequences of the Index sponsor discontinuing publication of the Index are discussed in the section entitled Description of the Notes Discontinuance of an Index beginning on page PS-22 of product prospectus supplement EQUITY INDICES SUN-1. None of us, the calculation agent, or MLPF&S accepts any responsibility for the calculation, maintenance or publication of the Index or any successor index.

General

The Index is a capitalization-weighted index of 50 European blue-chip stocks in 11 Eurozone countries. Publication of the Index began on February 26, 1998, based on an initial Index value of 1,000 at December 31, 1991. The level of the Index is disseminated on, and additional information about the Index is published on, the STOXX website. Information contained in the STOXX website is not incorporated by reference in, and should not be considered a part of, this term sheet.

As of October 31, 2016, the top ten industry sectors which comprise the Index represent the following weights in the Index: Banks (14.1%), Industrial Goods & Services (10.9%), Chemicals (9.0%), Personal & Household Goods (8.4%), Oil & Gas (6.9%), Technology (6.7%), Insurance (6.6%), Health Care (6.4%), Food & Beverage (5.8%) and Telecommunications (5.7%). As of October 31, 2016, the top seven countries which comprise the Index represent the following weights therein: France (36.2%), Germany (33.0%), Spain (10.6%), Netherlands (9.5%), Italy (4.6%), Belgium (3.9%), Ireland (1.2%), and Finland (1.2%).

Index Composition and Maintenance

For each of the 19 EURO STOXX regional supersector indices, the stocks are ranked in terms of free-float market capitalization. The largest stocks are added to the selection list until the coverage is close to, but still less than, 60% of the free-float market capitalization of the corresponding supersector index. If the next highest-ranked stock brings the coverage closer to 60% in absolute terms, then it is also added to the selection list. All current stocks in the Index are then added to the selection list. All of the stocks on the selection list are then ranked in terms of free-float market capitalization to produce the final index selection list. The largest 40 stocks on the selection list are selected; the remaining 10 stocks are selected from the largest remaining current stocks ranked between 41 and 60; if the number of stocks selected is still below 50, then the largest remaining stocks are selected until there are 50 stocks. In exceptional cases, STOXX's management board can add stocks to and remove them from the selection list.

The Index components are subject to a capped maximum index weight of 10%, which is applied on a quarterly basis.

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The composition of the Index is reviewed annually, based on the closing stock data on the last trading day in August. Changes in the composition of the Index are made to ensure that the Index includes the 50 market sector leaders from within the Index.

The Index is subject to a fast exit rule. The Index components are monitored for any changes based on the monthly selection list ranking. A stock is deleted from the Index if: (a) it ranks 75 or below on the monthly selection list and (b) it ranked 75 or below on the selection list of the previous month. The highest-ranked stock that is not an Index component will replace it. Changes will be implemented on the close of the fifth trading day of the month, and are effective the next trading day.

The Index is also subject to a fast entry rule. All stocks on the latest selection lists and initial public offering (IPO) stocks are reviewed for a fast-track addition on a quarterly basis. A stock is added, if (a) it qualifies for the latest STOXX blue-chip selection list generated end of February, May, August or November and (b) it ranks within the lower buffer (ranks 1-25) on this selection list.

The Index is also reviewed on an ongoing basis. Corporate actions (including initial public offerings, mergers and takeovers, spin-offs, delistings, and bankruptcy) that affect the Index composition are immediately reviewed. Any changes are announced, implemented, and effective in line with the type of corporate action and the magnitude of the effect.

Index Calculation

The Index is calculated with the Laspeyres formula, which measures the aggregate price changes in the component stocks against a fixed base quantity weight. The formula for calculating the Index value can be expressed as follows:

$$\text{Index} = \frac{\text{free float market capitalization of the Index at the time}}{\text{divisor of the Index at the time}}$$

The free float market capitalization of the Index is equal to the sum of the products of the closing price, number of shares, free float factor, and weighting cap factor for the component company as of the time that the Index is being calculated.

The Index is calculated using a divisor that helps to maintain the continuity of the Index's value so that corporate actions do not artificially increase or decrease the level of the Index. The divisor of the Index is adjusted to maintain the continuity of the Index's values across changes due to corporate actions, such as cash dividends, rights offerings, stock dividends from treasury shares, repurchases of shares and self-tender, and spin-offs.

Autocallable Market-Linked Step Up Notes

Linked to the EURO STOXX 50® Index, due December 20, 2019

The following graph shows the daily historical performance of the Index in the period from January 1, 2008 through December 29, 2016. We obtained this historical data from Bloomberg L.P. We have not independently verified the accuracy or completeness of the information obtained from Bloomberg L.P. On the pricing date, the closing level of the Index was 3,271.76.

Historical Performance of the Index

This historical data on the Index is not necessarily indicative of the future performance of the Index or what the value of the notes may be. Any historical upward or downward trend in the level of the Index during any period set forth above is not an indication that the level of the Index is more or less likely to increase or decrease at any time over the term of the notes.

Before investing in the notes, you should consult publicly available sources for the levels of the Index.

License Agreement

BNS has entered into a non-exclusive license agreement with STOXX, which grants BNS a license in exchange for a fee to use the Index in connection with the issuance of certain securities, including the notes.

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STOXX has no relationship to BNS, other than the licensing of the Index and its service marks for use in connection with the notes.

STOXX does not:

- sponsor, endorse, sell or promote the notes;
- recommend that any person invest in the notes or any other financial products;
- have any responsibility or liability for or make any decisions about the timing, amount or pricing of the notes;
- have any responsibility or liability for the administration, management or marketing of the notes; and
- consider the needs of the notes or the owners of the notes in determining, composing or calculating the Index or have any obligation to do so.

STOXX will not have any liability in connection with the notes. Specifically, STOXX does not make any warranty, express or implied, and STOXX disclaims any warranty about:

- the results to be obtained by the notes, the owner of the notes or any other person in connection with the use of the Index and the data included in the Index;
- the accuracy or completeness of the Index or its data;
- the merchantability and the fitness for a particular purpose or use of the Index or its data;
- any errors, omissions or interruptions in the Index or its data; and
- any lost profits or indirect, punitive, special or consequential damages or losses, even if STOXX knows that they might occur.

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The licensing relating to the use of the Index and trademark referred to above by BNS will be solely for the benefit of BNS, and not for any other third parties.

Autocallable Market-Linked Step Up Notes	TS-10
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Autocallable Market-Linked Step Up Notes

Linked to the EURO STOXX 50® Index, due December 20, 2019

Supplement to the Plan of Distribution

Under our distribution agreement with MLPF&S, MLPF&S will purchase the notes from us as principal at the public offering price indicated on the cover of this term sheet, less the indicated underwriting discount.

We will deliver the notes against payment therefor in New York, New York on a date that is greater than three business days following the pricing date. Under Rule 15c6-1 of the Securities Exchange Act of 1934, trades in the secondary market generally are required to settle in three business days, unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade the notes more than three business days prior to the original issue date will be required to specify alternative settlement arrangements to prevent a failed settlement.

The notes will not be listed on any securities exchange. In the original offering of the notes, the notes will be sold in minimum investment amounts of 100 units. If you place an order to purchase the notes, you are consenting to MLPF&S acting as a principal in effecting the transaction for your account.

MLPF&S may repurchase and resell the notes, with repurchases and resales being made at prices related to then-prevailing market prices or at negotiated prices, and these prices will include MLPF&S's trading commissions and mark-ups. MLPF&S may act as principal or agent in these market-making transactions; however, it is not obligated to engage in any such transactions. At MLPF&S's discretion, for a short, undetermined initial period after the issuance of the notes, MLPF&S may offer to buy the notes in the secondary market at a price that may exceed the initial estimated value of the notes. Any price offered by MLPF&S for the notes will be based on then-prevailing market conditions and other considerations, including the performance of the Index and the remaining term of the notes. However, none of us, MLPF&S, or any of our respective affiliates is obligated to purchase your notes at any price or at any time, and we cannot assure you that we, MLPF&S or any of our respective affiliates will purchase your notes at a price that equals or exceeds the initial estimated value of the notes.

The value of the notes shown on your account statement produced by MLPF&S will be based on MLPF&S's estimate of the value of the notes if MLPF&S or another of its affiliates were to make a market in the notes, which it is not obligated to do. That estimate will be based upon the price that MLPF&S may pay for the notes in light of then-prevailing market conditions, and other considerations, as mentioned above, and will include transaction costs. At certain times, this price may be higher than or lower than the initial estimated value of the notes.

The distribution of the Note Prospectus in connection with these offers or sales will be solely for the purpose of providing investors with the description of the terms of the notes that was made available to investors in connection with their initial offering. Secondary market investors should not, and will not be authorized to, rely on the Note Prospectus for information regarding BNS or for any purpose other than that described in the immediately preceding sentence.

Autocallable Market-Linked Step Up Notes	TS-11
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Autocallable Market-Linked Step Up Notes

Linked to the EURO STOXX 50® Index, due December 20, 2019

Structuring the Notes

The notes are our unsecured senior debt securities, the return on which is linked to the performance of the Index. As is the case for all of our debt securities, including our market-linked notes, the economic terms of the notes reflect our actual or perceived creditworthiness at the time of pricing. The internal funding rate we use in pricing the market-linked note is typically lower than the rate we would pay when we issue conventional fixed-rate debt securities of comparable maturity. This generally relatively lower internal funding rate, which is reflected in the economic terms of the notes, along with the fees and charges associated with market-linked notes, resulted in the initial estimated value of the notes on the pricing date being less than their public offering price.

Payments on the notes, including the amount you receive at maturity or upon an automatic call, will be calculated based on the performance of the Index and the \$10 per unit principal amount. In order to meet these payment obligations, at the time we issue the notes, we may choose to enter into certain hedging arrangements (which may include call options, put options or other derivatives) with MLPF&S or one of its affiliates. The terms of these hedging arrangements are determined by seeking bids from market participants, including MLPF&S and its affiliates, and take into account a number of factors, including our creditworthiness, interest rate movements, the volatility of the Index, the tenor of the notes and the tenor of the hedging arrangements. The economic terms of the notes and their initial estimated value depend in part on the terms of these hedging arrangements.

MLPF&S has advised us that the hedging arrangements will include a hedging related charge of approximately \$0.075 per unit, reflecting an estimated profit to be credited to MLPF&S from these transactions. Since hedging entails risk and may be influenced by unpredictable market forces, additional profits and losses from these hedging arrangements may be realized by MLPF&S or any third party hedge providers.

For further information, see [Risk Factors](#) [General Risks Relating to the Notes](#) beginning on page PS-7 and [Use of Proceeds and Hedging](#) on page PS-17 of product prospectus supplement EQUITY INDICES SUN-1.

Summary of Canadian Federal Income Tax Consequences

In the opinion of Osler, Hoskin & Harcourt LLP, Canadian tax counsel to BNS, the following is a summary of the principal Canadian federal income tax considerations generally applicable to a purchaser who acquires, as a beneficial owner, the notes, including entitlement to all payments thereunder, pursuant to this initial offering by BNS made in connection with the original issuance of the notes and who, at all relevant times, for purposes of the application of the Income Tax Act (Canada) and the Income Tax Regulations (collectively, the [Act](#)) is not, and is not deemed to be, resident in Canada, deals at arm's length with BNS and any transferee resident (or deemed to be resident) in Canada to whom the purchaser disposes of the notes, does not use or hold the notes in a business carried on in Canada, and is not a [specified non-resident shareholder](#) of BNS for purposes of the [Act](#) or a non-resident person not dealing at arm's length with a [specified shareholder](#) (as defined in subsection 18(5) of the [Act](#)) of BNS (a [Non-Resident Holder](#)). Special rules, which are not discussed in this summary, may apply to a non-Canadian holder that is an insurer carrying on an insurance business in Canada and elsewhere.

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This summary is based upon the current provisions of the Act and an understanding of the current administrative policies and assessing practices of the Canada Revenue Agency (the CRA) published in writing prior to the date hereof. This summary takes into account all specific proposals to amend the Act publicly announced by or on behalf of the Minister of Finance (Canada) prior to the date hereof (the Proposals) and assumes that all Proposals will be enacted in the form proposed. However, no assurances can be given that the Proposals will be enacted as proposed, or at all. This summary does not otherwise take into account any changes in law or administrative practices or assessing policies, whether by legislative, administrative or judicial action, nor does it take into account tax legislation or considerations of any province, territory or foreign jurisdiction, which may differ from those discussed herein.

This summary assumes that no interest paid on the notes will be in respect of a debt or other obligation to pay an amount to a person with whom BNS does not deal at arm's length, within the meaning of the Act.

This summary is of a general nature only and is not, and is not intended to be, legal or tax advice to any particular holder. This summary is not exhaustive of all Canadian federal income tax considerations. Accordingly, prospective purchasers should consult their own tax advisors with regard to their own particular circumstances.

Based in part on the published administrative position of the CRA, no portion of the interest paid or credited or deemed for purposes of the Act to be paid or credited on a note (including any amount paid at maturity in excess of the principal amount and interest deemed to be paid on the note in certain cases involving the assignment, deemed assignment or other transfer of a note to BNS or any other resident or deemed resident of Canada) to a Non-Resident Holder will be subject to Canadian non-resident withholding tax.

No other Canadian federal taxes on income or gains will be payable by a Non-Resident Holder on interest or principal, or on proceeds received by a Non-Resident Holder on the disposition of a note, including on a redemption, payment on maturity, repurchase or purchase for cancellation.

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Summary of U.S. Federal Income Tax Consequences

The following is a general description of certain U.S. federal tax considerations relating to the notes. Prospective purchasers of the notes should consult their tax advisors as to the consequences under the tax laws of the country of which they are residents for tax purposes and the tax laws of the U.S. of acquiring, holding and disposing of the notes and receiving payments under the notes. This summary is based upon the law as in effect on the date of this pricing supplement and is subject to any change in law that may take effect after such date.

This discussion applies to you only if you are the original investor in the notes and you hold your notes as capital assets for tax purposes. This section does not apply to you if you are a member of a class of holders subject to special rules, such as:

- a dealer in securities or currencies,
- a trader in securities that elects to use a mark-to-market method of accounting for your securities holdings,
- a financial institution or a bank,
- a regulated investment company or a real estate investment trust or a common trust fund,
- a life insurance company,
- a tax-exempt organization or an investor holding the notes in a tax-advantaged account (such as an Individual Retirement Account or Roth IRA),
- a person that owns notes as part of a straddle or a hedging or conversion transaction, or who has entered into a constructive sale with respect to a note for tax purposes, or
- a U.S. holder (as defined below) whose functional currency for tax purposes is not the U.S. dollar.

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This discussion is based on the Internal Revenue Code of 1986, as amended (the Code), its legislative history, existing and proposed regulations under the Code, published rulings and court decisions, all as currently in effect. These laws are subject to change, possibly on a retroactive basis.

This discussion, other than the section entitled Non-U.S. Holders below, is applicable to you only if you are a U.S. holder. You are a U.S. holder if you are a beneficial owner of a note and you are: (i) a citizen or resident of the U.S., (ii) a domestic corporation, (iii) an estate whose income is subject to U.S. federal income tax regardless of its source, or (iv) a trust if a U.S. court can exercise primary supervision over the trust's administration and one or more U.S. persons are authorized to control all substantial decisions of the trust.

If a partnership holds the notes, the U.S. federal income tax treatment of a partner will generally depend on the status of the partner and the tax treatment of the partnership. A partner in a partnership holding the notes should consult its tax advisor with regard to the U.S. federal income tax treatment of an investment in the notes.

No statutory, judicial or administrative authority directly discusses how the notes should be treated for U.S. federal income tax purposes. As a result, the U.S. federal income tax consequences of your investment in the notes are uncertain. Accordingly, we urge you to consult your tax advisor as to the tax consequences of your investment in the notes (and of having agreed to the required tax treatment of your notes described below) and as to the application of state, local or other tax laws to your investment in your notes and the possible effects of changes in federal or other tax laws.

We will not attempt to ascertain whether any entity the stock of which is included in the Index would be treated as a passive foreign investment company (a PFIC) within the meaning of the Code. If any such entity were so treated, certain adverse U.S. federal income tax consequences might apply to U.S. holders upon the taxable disposition (including cash settlement) of the notes. You should refer to information filed with the SEC or an equivalent governmental authority by such entities and consult your tax advisor regarding the possible consequences to you if such entity is or becomes a PFIC.

Pursuant to the terms of the notes, BNS and you agree, in the absence of a statutory, regulatory, administrative or judicial ruling to the contrary, to characterize your notes as a pre-paid derivative contract with respect to the reference asset. If your notes are so treated, you should generally recognize long-term capital gain or loss if you hold your notes for more than one year (and otherwise, short-term capital gain or loss) upon the sale, exchange, redemption, automatic call or maturity of your notes in an amount equal to the difference between the amount you receive at such time and the amount you paid for your notes. The deductibility of capital losses is subject to limitations.

However, it is possible that the Internal Revenue Service (IRS) could assert that your holding period in respect of your notes should end on the date on which the amount you are entitled to receive upon maturity or automatic call of your notes is determined, even though you will not receive any amounts from the issuer in respect of your notes prior to the maturity or automatic call of your notes. In such case, you may be treated as having a holding period in respect of your notes prior to the maturity or automatic call of your notes, and such holding period may be treated as less than one year even if you receive cash upon the maturity or automatic call of your notes at a time that is more than one year after the beginning of your holding period.

In the opinion of our counsel, Cadwalader, Wickersham & Taft LLP, it would be reasonable to treat your notes in the manner described above. However, because there is no authority that specifically addresses the tax treatment of the notes, it is possible that your notes could alternatively be treated for tax purposes as a single contingent payment debt instrument or pursuant to some other characterization, such that the timing and character of your income from the notes could differ materially from the treatment described above.

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Possible Change in Law. In 2007, the IRS released a notice that may affect the taxation of holders of the notes. According to the notice, the IRS and the U.S. Treasury Department are actively considering whether a holder of an instrument such as the notes should be required to accrue ordinary income on a current basis, and they are seeking taxpayer comments on the subject. It is not possible to determine what guidance they will ultimately issue, if any. It is possible, however, that under such guidance, holders of the notes will ultimately be required to accrue income currently and this could be applied on a retroactive basis. The IRS and the U.S. Treasury Department are also considering other relevant issues, including whether additional gain or loss from such instruments should be treated as ordinary or capital, whether foreign holders of such instruments should be subject to withholding tax on any deemed income accruals, and whether the special constructive ownership rules of Section 1260 of the Code should be applied to such instruments.

Medicare Tax on Net Investment Income. U.S. holders that are individuals or estates and certain trusts are subject to an additional 3.8% tax on all or a portion of their net investment income, or undistributed net investment income in the case of an estate or trust, which may include any income or gain with respect to the notes, to the extent of their net investment income or undistributed net investment income (as the case may be) that, when added to their other modified adjusted gross income, exceeds \$200,000 for an unmarried individual, \$250,000 for a married taxpayer filing a joint return (or a surviving spouse), \$125,000 for a married individual filing a separate return, or the dollar amount at which the highest tax bracket begins for an estate or trust (which, in 2016, is \$12,400). The 3.8% Medicare tax is determined in a different manner than the regular income tax. U.S. holders should consult their advisors with respect to the 3.8% Medicare tax.

Specified Foreign Financial Assets. U.S. holders may be subject to reporting obligations with respect to their notes if they do not hold their notes in an account maintained by a financial institution and the aggregate value of their notes and certain other specified foreign financial assets (applying certain attribution rules) exceeds \$50,000. Significant penalties can apply if a U.S. holder is required to disclose its notes and fails to do so.

Backup Withholding and Information Reporting. The proceeds received from a sale, exchange, redemption, automatic call or maturity of the notes will be subject to information reporting unless you are an exempt recipient and may also be subject to backup withholding at the rate specified in the Code if you fail to provide certain identifying information (such as an accurate taxpayer number, if you are a U.S. holder) or meet certain other conditions.

Amounts withheld under the backup withholding rules are not additional taxes and may be refunded or credited against your U.S. federal income tax liability, provided the required information is furnished to the IRS.

Non-U.S. Holders. This section applies only if you are a non-U.S. holder. For these purposes, you are a non-U.S. holder if you are the beneficial owner of the notes and are, for U.S. federal income tax purposes:

- a non-resident alien individual;
- a foreign corporation; or

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- an estate or trust that, in either case, is not subject to U.S. federal income tax on a net income basis on income or gain from the notes.

If you are a non-U.S. holder, you should generally not be subject to generally applicable information reporting and backup withholding requirements with respect to payments on your notes if you comply with certain certification and identification requirements as to your foreign status including providing us (and/or the applicable withholding agent) a properly executed and fully completed applicable IRS Form W-8. Gain from the sale, exchange or redemption of the notes, automatic call or settlement at maturity generally will not be subject to U.S. tax unless such gain is effectively connected with a trade or business conducted by you in the U.S. or unless you are a non-resident alien individual and are present in the U.S. for 183 days or more during the taxable year of such sale, exchange or settlement and certain other conditions are satisfied.

U.S. Federal Estate Tax Treatment of Non-U.S. Holders. A note may be subject to U.S. federal estate tax if an individual non-U.S. holder holds the note at the time of his or her death. The gross estate of a non-U.S. holder domiciled outside the U.S. includes only property situated in the U.S. Individual non-U.S. holders should consult their tax advisors regarding the U.S. federal estate tax consequences of holding the notes at death.

FATCA. The Foreign Account Tax Compliance Act (FATCA) was enacted on March 18, 2010, and imposes a 30% U.S. withholding tax on withholdable payments (i.e., certain U.S.-source payments, including interest (and original issue discount), dividends, other fixed or determinable annual or periodical gain, profits, and income, and on the gross proceeds from a disposition of property of a type which can produce U.S.-source interest or dividends) and passthru payments (i.e., certain payments attributable to withholdable payments) made to certain foreign financial institutions (and certain of their affiliates) unless the payee foreign financial institution agrees (or is required), among other things, to disclose the identity of any U.S. individual with an account at the institution (or the relevant affiliate) and to annually report certain information about such account. FATCA also requires withholding agents making withholdable payments to certain foreign entities that do not disclose the name, address, and taxpayer identification number of any substantial U.S. owners (or do not certify that they do not have any substantial U.S. owners) to withhold tax at a rate of 30%. Under certain circumstances, a holder may be eligible for refunds or credits of such taxes.

Pursuant to final and temporary Treasury regulations and other IRS guidance, the withholding and reporting requirements under FATCA will generally apply to certain withholdable payments made on or after July 1, 2014, certain gross proceeds on a sale or disposition occurring after December 31, 2018, and certain foreign passthru payments made after December 31, 2018 (or, if later, the date that final regulations defining the term foreign passthru payment are published). In addition, withholding tax under FATCA would not be imposed on withholdable payments solely because the relevant obligation is treated as giving rise to a dividend equivalent (pursuant to Section 871(m) and the regulations thereunder) where such obligation is executed on or before the date that is six months after the date

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on which obligations of its type are first treated as giving rise to dividend equivalents. If, however, withholding is required, we (or the applicable paying agent) will not be required to pay additional amounts with respect to the amounts so withheld. Foreign financial institutions and non-financial foreign entities located in jurisdictions that have an intergovernmental agreement with the U.S. governing FATCA may be subject to different rules.

Investors should consult their own advisors about the application of FATCA, in particular if they may be classified as financial institutions (or if they hold their notes through a non-U.S. entity) under the FATCA rules.

Both U.S. and non-U.S. holders should consult their tax advisors regarding the U.S. federal income tax consequences of an investment in the notes, as well as any tax consequences arising under the laws of any state, local or non-U.S. taxing jurisdiction (including that of the stocks included in the Index and BNS).

Validity of the Notes

In the opinion of Cadwalader, Wickersham & Taft LLP, as special counsel to the issuer, when the notes offered herein have been executed and issued by the issuer and authenticated by the trustee pursuant to the indenture and delivered, paid for and sold as contemplated herein, the notes will be valid and binding obligations of the issuer, enforceable against the issuer in accordance with their terms, subject to applicable bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium, receivership or other laws relating to or affecting creditors' rights generally, and to general principles of equity (regardless of whether enforcement is sought in a proceeding at law or in equity). This opinion is given as of the date hereof and is limited to the laws of the State of New York. Insofar as this opinion involves matters governed by Canadian law, Cadwalader, Wickersham & Taft LLP has assumed, without independent inquiry or investigation, the validity of the matters opined on by Osler, Hoskin & Harcourt LLP, Canadian legal counsel for the issuer, in its opinion expressed below. In addition, this opinion is subject to customary assumptions about the trustee's authorization, execution and delivery of the indenture and, with respect to the notes, authentication of the notes and the genuineness of signatures and certain factual matters, all as stated in the opinion of Cadwalader, Wickersham & Taft LLP dated February 11, 2016 filed with the SEC as an exhibit to a Current Report on Form 6-K on February 11, 2016.

In the opinion of Osler, Hoskin & Harcourt LLP, the issue and sale of the notes has been duly authorized by all necessary corporate action of BNS in conformity with the Indenture, and when the notes have been duly executed, authenticated and issued in accordance with the Indenture, the notes will be validly issued and, to the extent validity of the notes is a matter governed by the laws of the Province of Ontario or Québec, or the laws of Canada applicable therein, and will be valid obligations of BNS, subject to applicable bankruptcy, insolvency and other laws of general application affecting creditors' rights, equitable principles, and subject to limitations as to the currency in which judgments in Canada may be rendered, as prescribed by the Currency Act (Canada). This opinion is given as of the date hereof and is limited to the laws of the Province of Ontario and the federal laws of Canada applicable thereto. In addition, this opinion is subject to customary assumptions about the Trustee's authorization, execution and delivery of the Indenture and the genuineness of signatures and certain factual matters, all as stated in the letter of such counsel dated November 10, 2014, which has been filed as Exhibit 5.2 to BNS's Form F-3 filed with the SEC on November 10, 2014.

Where You Can Find More Information

We have filed a registration statement (including a product prospectus supplement, a prospectus supplement, and a prospectus) with the SEC for the offering to which this term sheet relates. Before you invest, you should read the Note Prospectus, including this term sheet, and the other documents that we have filed with the SEC, for more complete information about us and this offering. You may get these documents without cost by visiting EDGAR on the SEC website at www.sec.gov. Alternatively, we, any agent, or any dealer participating in this offering will arrange to send you these documents if you so request by calling MLPF&S toll-free at 1-800-294-1322.

Market-Linked Investments Classification

MLPF&S classifies certain market-linked investments (the Market-Linked Investments) into categories, each with different investment characteristics. The following description is meant solely for informational purposes and is not intended to represent any particular Enhanced Return Market-Linked Investment or guarantee any performance.

Enhanced Return Market-Linked Investments are short- to medium-term investments that offer you a way to enhance exposure to a particular market view without taking on a similarly enhanced level of market downside risk. They can be especially effective in a flat to moderately positive market (or, in the case of bearish investments, a flat to moderately negative market). In exchange for the potential to receive better-than market returns on the linked asset, you must generally accept market downside risk and capped upside potential. As these investments are not market downside protected, and do not assure full repayment of principal at maturity, you need to be prepared for the possibility that you may lose all or part of your investment.

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