LIFE & ANNUITY CASE STUDY

Lincoln Memorial Life Insurance Company ("Lincoln Memorial" or "the Company")

May 14, 2008: Status—Rehabilitation
September 22, 2008—Status: Liquidation

Root Causes of Insolvency

- Fraud—Policyholder funds were not placed in appropriate trust accounts in accordance with policy representation and state laws and regulations. Instead, funds were used in ways that created personal gains for the ultimate owners of Lincoln Memorial Life Insurance Company ("Lincoln Memorial" or "the Company") and a consortium of related entities. New business became the main source of funding for funerals that customers had paid for in advance. Ultimately, the trust accounts were significantly underfunded.

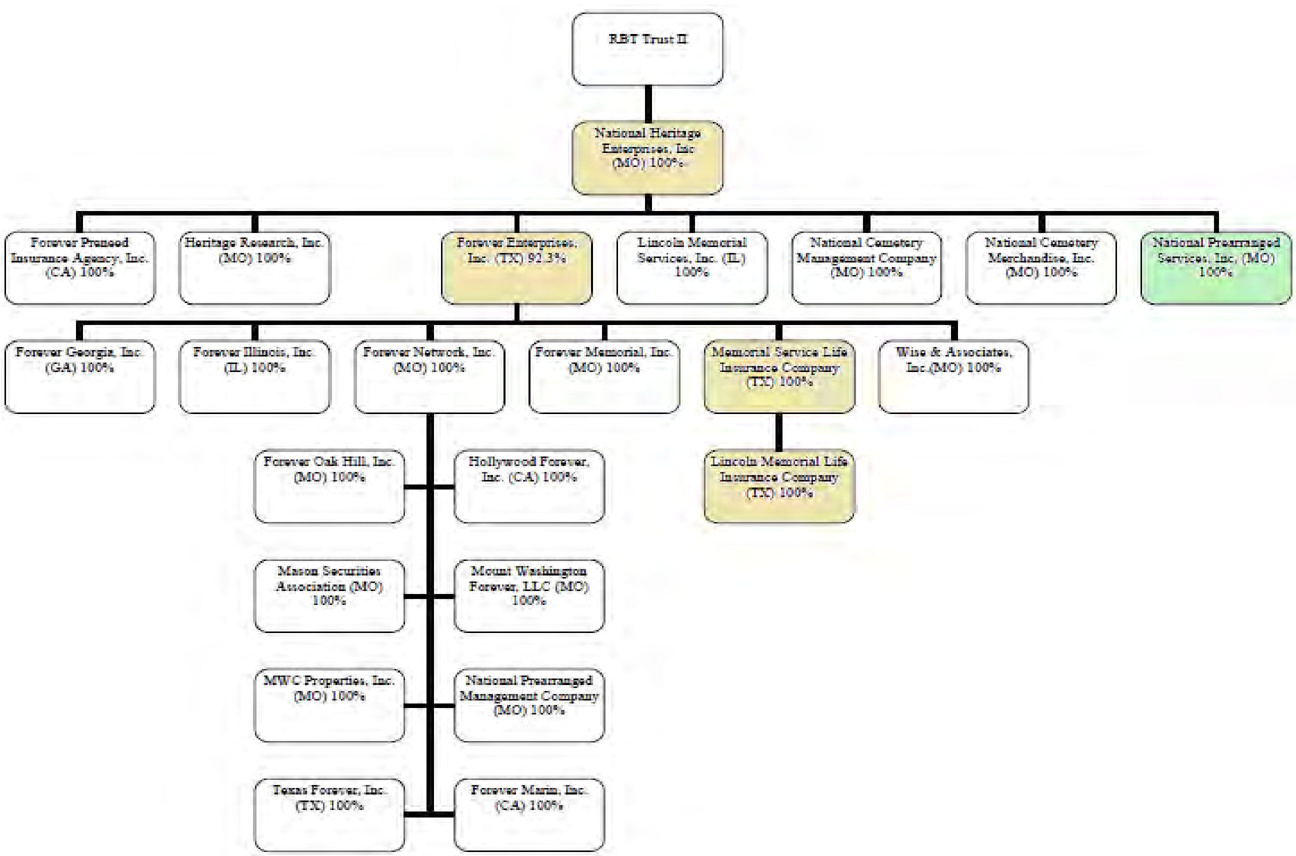
Section I—Background

Company Summary

Texas-domiciled Lincoln Memorial was licensed in 44 states as an accident, life, and health insurer. It was a wholly owned subsidiary of Memorial Service Life Insurance Company, which in turn is a wholly owned subsidiary of Forever Enterprises, Inc. (formally known as Lincoln Heritage Corporation). In 1998 Lincoln Memorial acquired World Services Life Insurance Company of America.

Lincoln Memorial offered ordinary life and individual annuity contracts that were designed to fund pre-need funeral services. Most of its policies were sold by National Prearranged Services, Inc. (NPS). NPS was an affiliated company that collected payment for the prearranged funeral contracts and remitted such amounts to the Company either directly or through assumed reinsurance.

Figure 1
LINCOLN MEMORIAL ORGANIZATIONAL CHART



Relative to all life insurers, based on direct written premium and annuity consideration as of year-end 2007, Lincoln Memorial's market share was very small (figure 2).

Figure 2

LINCOLN MEMORIAL MARKET SHARE

Total Filed - Total Life

2007 Rank	2006 Rank	Institution *	2007 State Direct Premiums & Annuity Considerations ($000)	2007 Market Share (%)
1	1	MetLife Inc. (SNL Life Group)	82,834,539	13.86
2	2	Prudential Financial Inc. (SNL Life Group)	42,347,519	7.09
3	3	Voya Financial Inc. (SNL Life Group)	38,049,175	6.37
4	5	Hartford Financial Services (SNL Life Group)	32,387,977	5.42
5	6	AEGON (SNL Life Group)	30,517,175	5.11
6	4	John Hancock (SNL Life Group)	29,783,898	4.98
7	9	Principal Financial Group Inc. (SNL Life Group)	22,696,476	3.80
8	7	American International Group (SNL Life Group)	21,948,870	3.67
9	8	New York Life Insurance Group (SNL Life Group)	21,874,343	3.66
10	10	Lincoln Financial Group (SNL Life Group)	21,531,912	3.60
125	**118**	**Lincoln Memorial Life Ins Co.**	**86,403**	**0.01**
		Total Life Premiums in Market	**597,643,217**	

* Market share information is presented on an "as-is" (pro-forma) basis based upon current filing sector and group composition.

Despite being domiciled in Texas, Lincoln Memorial's largest state was Missouri, based on 2007 direct premium, followed by Ohio and Iowa. The Company wrote in a total of 24 states in 2007 (figure 3).

Figure 3

LINCOLN MEMORIAL STATE MIX

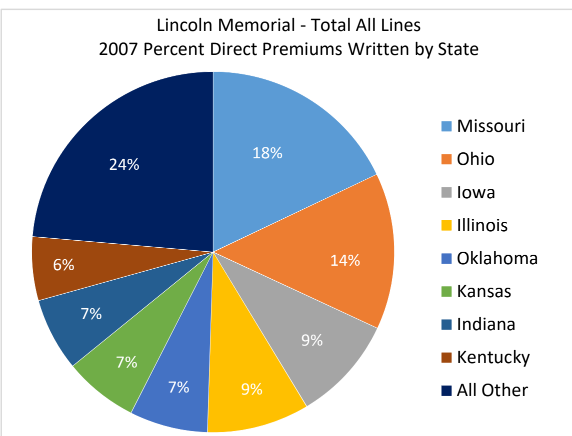
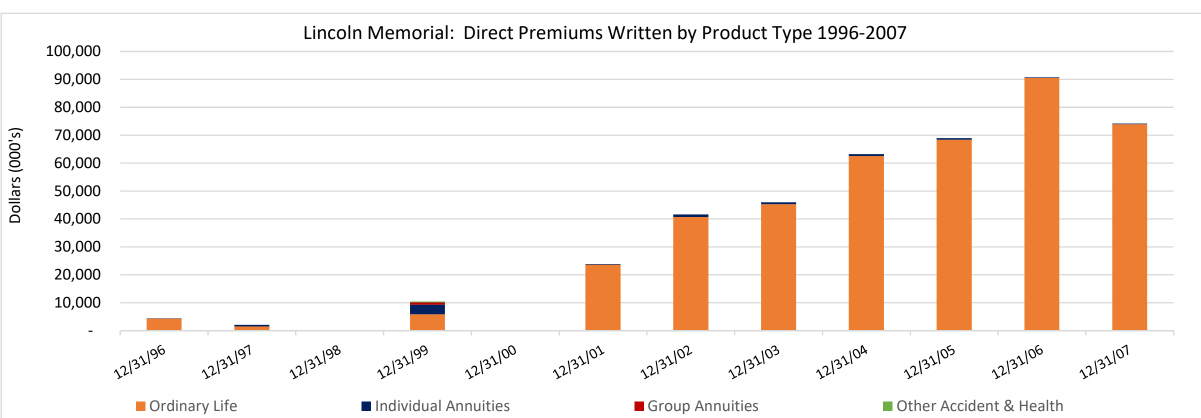


Figure 4

LINCOLN MEMORIAL HISTORICAL WRITTEN PREMIUM



A majority of the Company's business was ordinary life (99 percent), and premiums began to increase substantially, with double-digit growth rates beginning in 2001 through 2006 (figure 4).

Figure 5

LINCOLN HISTORICAL CAPITAL AND SURPLUS

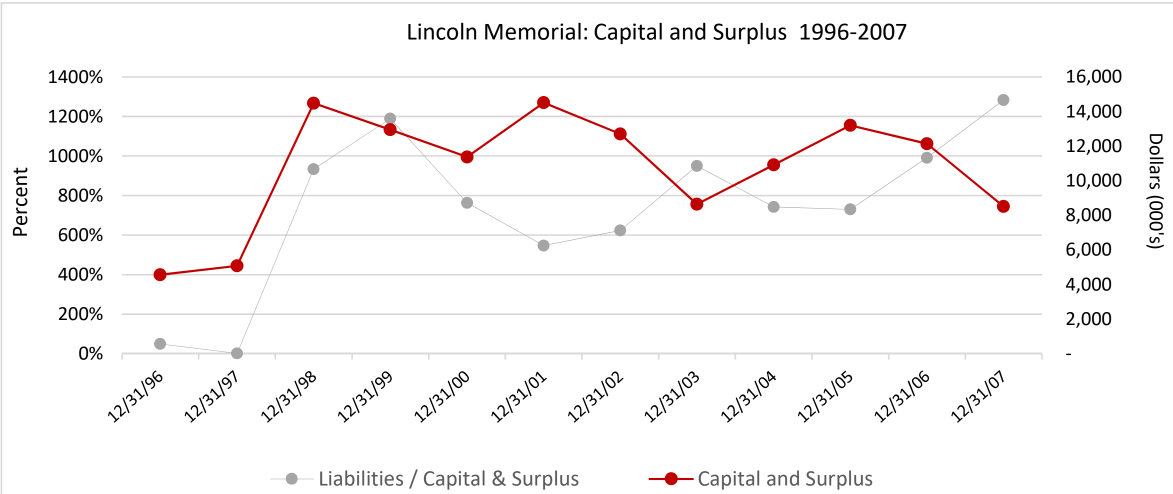


Figure 6

LINCOLN MEMORIAL HISTORICAL RESERVE LEVERAGE AND INVESTMENT MIX

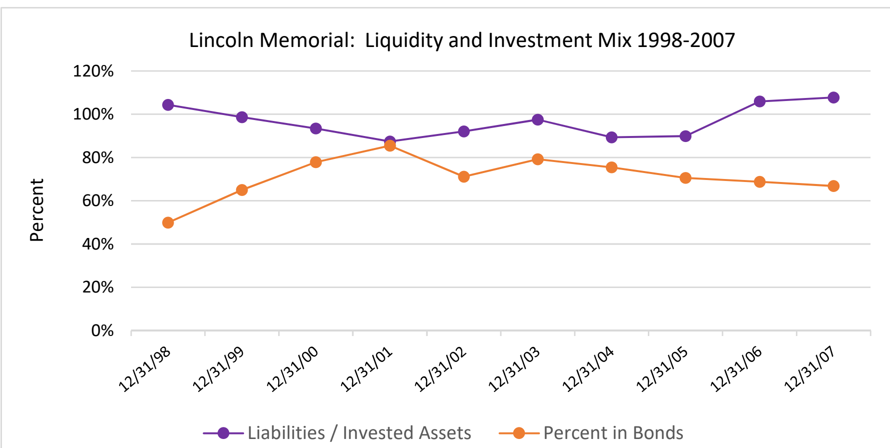
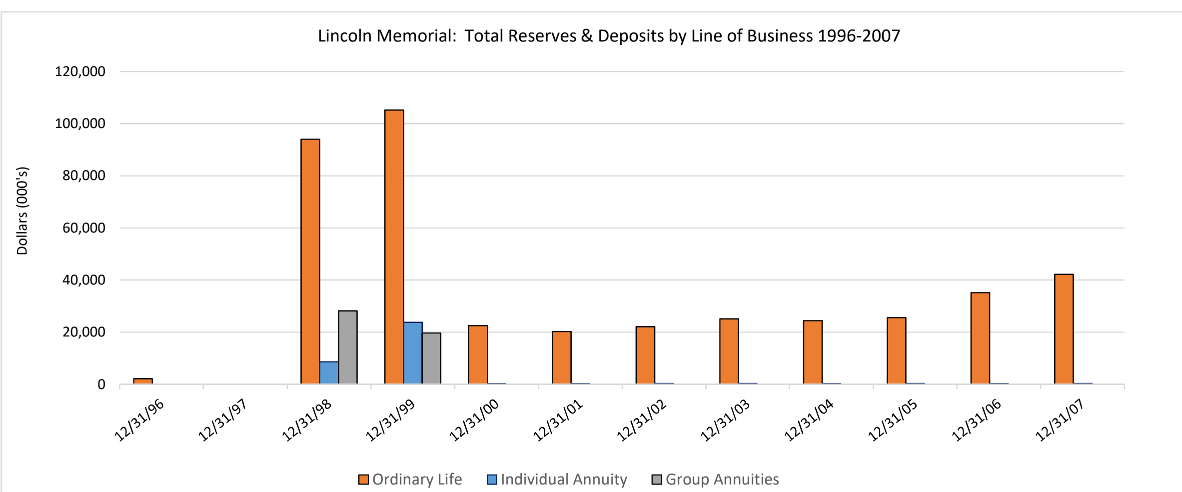


Figure 7

LINCOLN MEMORIAL HISTORICAL RESERVES AND DEPOSITS



Lincoln Memorial's capital and surplus had some volatility from 1998 to 2007, though a marked trend upward or downward was not apparent. Liabilities as a percentage of capital and surplus trended upward after 2001, which is consistent with the time period during which premiums grew (figure 5). Likewise, liabilities to invested assets trended upward gradually. The percentage invested in bonds trended downward during the 2001 to 2007 period (figure 6).

Please note that the decrease in reserves in 2000 relates to several significant life reinsurance transactions.

Lincoln Memorial's RBC ratio was relatively stable for the period 1999 through 2005, at which time it decreased substantially in each of the following two years (figure 8).

Figure 8

LINCOLN MEMORIAL HISTORICAL RISK-BASED CAPITAL RATIO

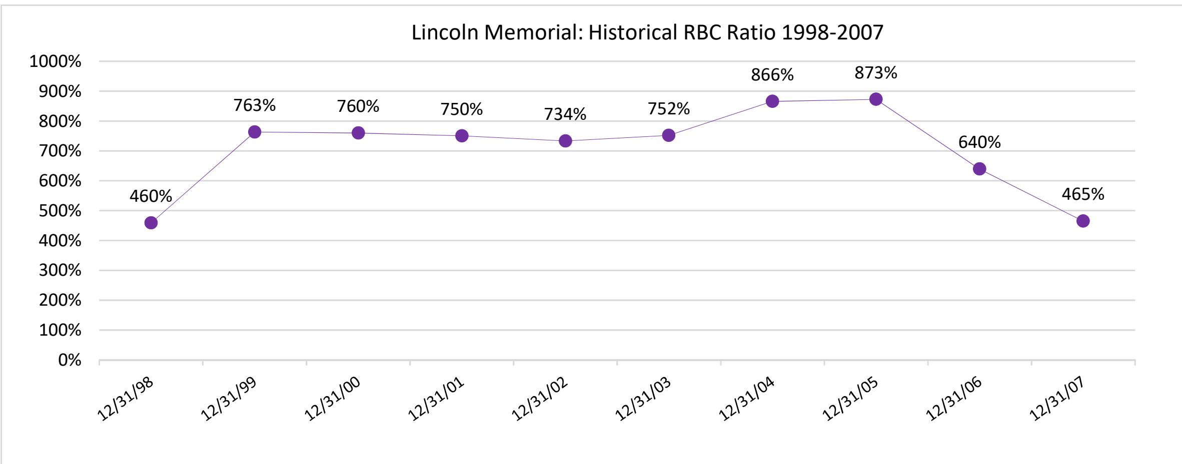
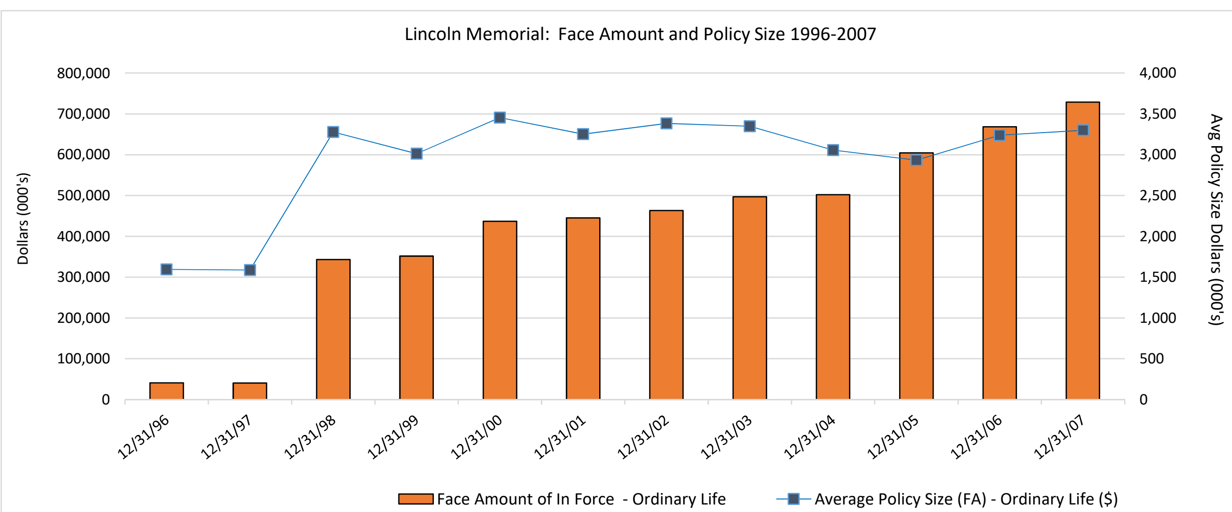


Figure 9

LINCOLN MEMORIAL HISTORICAL POLICIES IN FORCE



Lincoln Memorial's average policy size on ordinary life was relatively stable for the period 1998 through 2007, while the face amount of in-force policies increased year to year, consistent with the growth in business described above.

While not necessarily apparent from the financial data, Lincoln Memorial was involved in large-scale fraud.

Fraud Allegation

A complaint against Lincoln Memorial, along with numerous individuals and related organizations, was filed on August 7, 2009:

http://www.lincolnmemoriallife.com/documents/08-07-09%20Complaint.pdf

The allegations in the complaint include:

In perpetrating, assisting in, or negligently failing to detect the scheme to defraud the funeral homes and their customers, Defendants violated the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961 et seq., violated the Lanham Act, 15 U.S.C. §§ 1051 et seq., committed fraud, breached their fiduciary duties, violated numerous state consumer protection acts, committed fraudulent transfers, breached obligations to repay funds, and/or were unjustly enriched by more than half a billion dollars.

- From the early 1990s to 2008, NPS sold prearranged funeral contracts in states including Missouri, Illinois, and Ohio. Customers typically paid a single sum of money up-front for the contract. Insurance companies affiliated with the NPS (Cassity Consortium, described further below) issued life insurance policies related to the contracts.

- Plaintiffs are bringing this lawsuit to recover losses in excess of $600 million caused by the RICO Defendants' (as defined later in this Complaint) scheme to defraud hundreds of funeral homes and consumers across the nation into selling and purchasing pre-need funeral contracts marketed by St. Louis-based National Prearranged Services, Inc. ("NPS"), and purportedly backed by life insurance policies issued by two affiliated entities: Texas-based companies Lincoln Memorial Life Insurance Company ("Lincoln") and Memorial Service Life Insurance Company ("Memorial")

- NPS, Lincoln, and Memorial are part of a larger consortium of related entities that are all ultimately owned by a family trust of the St. Louis-based Cassity family, whose members are Defendants Doug, Rhonda, Brent, and Tyler Cassity. The majority of entities within this consortium are involved in some aspect of the funeral industry. This group of Cassity-controlled and -related entities is collectively referred to in this Complaint as the "Cassity Consortium."

- The Cassity family operated and ultimately owned NPS (which was formed in 1979), created Memorial in 1986, and acquired Lincoln as part of the Cassity Consortium in 1998. The acquisition of Lincoln and creation of Memorial were critical to perpetrating the scheme to defraud the funeral homes because the vast majority of pre-need funeral contracts sold by NPS were claimed to be backed by whole-life insurance policies issued by Lincoln or Memorial. The NPS/Lincoln/Memorial enterprise provided the RICO Defendants with a seemingly legitimate cover under which they could siphon off the pre-need funds entrusted to NPS by funeral homes and their customers all over the country.

- Defendant Doug Cassity is a disbarred Missouri lawyer who in 1982 was sentenced to two years in federal prison as a result of a felony fraud conviction. Defendant Doug Cassity used fraudulent letters of credit in order to obtain loans or lines of credit to acquire property and assets, and falsified an income tax return. As a result of his conviction, Doug Cassity was and is permanently banned from having any involvement in the insurance industry. Despite and contrary to this bar, Doug Cassity actively engaged in the management of all entities within the Cassity Consortium, including but not limited to NPS, Lincoln, and Memorial.

- The RICO Defendants intentionally misled funeral homes and consumers around the country into believing pre-need funds entrusted to NPS would be safeguarded in a trust and/or backed by whole-life insurance policies so that the funds would be readily available when a pre-need beneficiary died and the funeral home's death claim came due. Rather than safeguarding the pre-need funds they accumulated, the RICO Defendants systematically: (1) siphoned money away from NPS, Lincoln, and Memorial; (2) looted NPS's pre-need trusts; (3) used the funds from the pre-need funeral contract sales to enrich other entities within the Cassity Consortium as well as individual Defendants; and (4) depleted the cash value of whole-life insurance policies by repeatedly taking policy loans, converting the policies to "reduced paid up" ("RPU") status, mass surrendering the whole-life policies, and frequently replacing these policies with term life insurance policies that are of no cash value and that may be cancelled if premiums are not paid.

- The RICO Defendants concealed and knowingly failed to disclose these practices from the funeral homes and consumers, despite the RICO Defendants' knowledge that these practices would have been material to the funeral homes' decisions regarding whether to sell NPS pre-need contracts and consumers' decisions regarding whether to purchase NPS pre-need contracts.

- To further their schemes, the RICO Defendants hired Defendants Wulf and Wulf Bates (the "Investment Advisor Defendants") to act as purported "independent" investment advisors for the various NPS trusts holding the proceeds of the pre-need funeral contracts. Defendants Wulf and Wulf Bates subsequently appointed and authorized the president of both NPS and Lincoln (Defendant Sutton) to act as an "investment agent" for the pre-need trust funds, thus allowing the RICO Defendants to manipulate the trust assets directly.

- Defendants Wulf and Wulf Bates not only actively participated in the RICO Defendants' various schemes to loot NPS, Lincoln, and Memorial, but directed the investment of millions of dollars of NPS pre-need trust funds into Defendant Wulf's personal investment partnerships and Cassity family entities in which Wulf held a personal ownership interest.

- Defendant banks Bremen Bank, National City Bank (as the ultimate successor in interest to Allegiant Bank), Marshall & Ilsley, Southwest Bank, U.S. Bank (as the ultimate successor in interest to Mark Twain Bank), Bank of America, American Stock Transfer, and Comerica Bank and Trust (collectively, the "Trustee Defendants") served as trustees of the various NPS pre-need trusts and failed to supervise the NPS pre-need trusts' assets properly. The Trustee Defendants allowed the NPS pre-need trust assets to be pillaged through the purchase and mass surrender of life insurance policies from Lincoln, the transfer of cash to Cassity Consortium entities in exchange for promissory notes from those entities that the Cassity Consortium entities never intended to enforce, and numerous other acts detailed below.

- Defendants Scannell, Wittner, and Wittner's law firm, Wittner, Spewak & Maylack, P.C. (collectively, the "Attorney Defendants"), served as general counsel to the entities within the Cassity Consortium and were directly involved in and profited from the RICO Defendants' illegal schemes. Scannell and Wittner also committed legal malpractice by providing legal advice authorizing and assisting in the development and implementation of the techniques used to siphon money as described in this Complaint.

- The RICO Defendants siphoned away the pre-need funds through a variety of mechanisms, including:

    - Directing NPS, as the improper "owner" of the whole-life insurance policies issued by Lincoln, to take over $130 million of policy loans against the policies;
    - Directing NPS, as the improper assignee/beneficiary on the Lincoln whole-life insurance policies, to surrender thousands of policies so the RICO Defendants could confiscate millions of dollars of the cash surrender values;
    - Replacing the whole-life policies with term policies that required NPS to pay far less in monthly premiums to Lincoln, thus allowing the RICO Defendants to keep for themselves more of the funds received from the funeral home consumers;
    - Altering life insurance policy applications to allow the RICO Defendants to keep for themselves the bulk of the funds received from the funeral home consumers;
    - Taking tens of millions of dollars in cash out of the pre-need funeral trusts and replacing those funds with promissory notes, debentures, and general ledger entries that were never intended to be repaid;
    - Funneling the pre-need contract funds to other entities the RICO Defendants owned and controlled within the Cassity Consortium;
    - Paying commissions to themselves through NPS for insurance policies purchased from their own affiliated companies, Lincoln and Memorial; and
    - Reducing by millions of dollars reinsurance recoveries due to Lincoln and Memorial by wrongfully surrendering whole-life policies and issuing term policies in their place.

- The RICO Defendants used the ill-gotten funds for a variety of improper purposes, including personal enrichment. For example, NPS paid personal credit card and other expenses of some of the RICO Defendants, ranging from $150 to $3 million.
- The RICO Defendants looted NPS, Lincoln, and Memorial by engaging in sham transactions that included recording a note receivable without a promissory note in return.

The regulatory response to Lincoln Memorial's activities is described in the timeline below.

Timeline Summary

- **October 24, 2007**: Lincoln Memorial and Memorial Services (Memorial) were placed under an Order of Confidential Supervision by the Texas Department of Insurance.
- **March 17, 2008**: Texas Department of Insurance issued a No New Business Directive for Lincoln Memorial to cease writing new business in all states.
- **May 14, 2008:** Lincoln Memorial, Memorial, and NPS companies were placed on rehabilitation, as they were found to be in hazardous financial condition by the State of Texas at the request of the Insurance Commissioner.
- **September 22, 2008**: Lincoln Memorial, Memorial Services and National Prearranged Services companies were approved for liquidation.
- **August 7, 2009:** Complaint was brought against the Lincoln Memorial, Memorial Services and National Prearranged Services companies, their Executives, investment advisors, trustees, and other parties.
- **June 17, 2013:** The NPS Executives pleaded guilty in the $600 million Ponzi scheme.

Beginning in mid-2007, insurance regulators from various states began confidentially investigating the operations of NPS, Lincoln Memorial, and Memorial and uncovering the scheme to defraud. On October 24, 2007, Lincoln Memorial and Memorial were placed under an Order of Confidential Supervision by the Texas Department of Insurance. While under the Supervision Order (from the remainder of 2007 through mid-May 2008), the Defendants violated the order by taking improper actions without the knowledge and/or consent of the Texas Department of Insurance. They intentionally and fraudulently concealed these actions from the Supervisor and other regulators.

By early 2008, additional state regulators had also begun investigations. NPS, Lincoln Memorial, and Memorial were placed into receivership in Texas. Soon after, numerous states had revoked or suspended Lincoln's and NPS's right to do business in their states, and the FBI had begun an investigation into the illegal and fraudulent practices detailed in this Complaint.

Fraud Allegations—A Review of Financials

As shown below, the following observations regarding policy handling are consistent with the allegations noted in the case against Lincoln Memorial and other defendants.

- Significant increase in lapse in 2007
- Significant decrease in whole-life policies in 2007 and 2006
- Significant increase in term policies in 2007

Figure 11

LINCOLN MEMORIAL 2005 TO 2007 POLICY DATA ANALYSIS

Ordinary Life Surrenders

2007		Prior Year Comparison		2006		Prior Year Comparison		2005	
# of Policies	$ Amount	% Incr/(Decr) Policies	% Incr/(Decr) Policy Amount	# of Policies	$ Amount	% Incr/(Decr) Policies	% Incr/(Decr) Policy Amount	# of Policies	$ Amount
39,560	101,987,000	126.4%	178.9%	17,471	36,574,000	-11.7%	-32.4%	19,789	54,091,000

Ordinary Life Lapse

2007		Prior Year Comparison		2006		Prior Year Comparison		2005	
# of Policies	$ Amount	% Incr/(Decr) Policy Lapse	% Incr/(Decr) Policy Lapse Amount	# of Policies	$ Amount	% Incr/(Decr) Policy Lapse	% Incr/(Decr) Policy Lapse Amount	# of Policies	$ Amount
5,602	18,024,000	1332.7%	1367.8%	391	1,228,000	-5.3%	-28.2%	413	1,711,000

Whole Life Policies Issued During the Year

2007		Prior Year Comparison		2006		Prior Year Comparison		2005	
# of Policies	$ Amount	% Incr/(Decr) Policy Issues	% Incr/(Decr) Policy Issue Amount	# of Policies	$ Amount	% Incr/(Decr) Policy Issues	% Incr/(Decr) Policy Issue Amount	# of Policies	$ Amount
26,118	100,503,000	-14.2%	-20.2%	30,456	125,894,000	-46.3%	-36.3%	56,757	197,769,000

Term Policies Issued During The Year

2007		Prior Year Comparison		2006		Prior Year Comparison		2005	
# of Policies	$ Amount	% Incr/(Decr) Policy Issues	% Incr/(Decr) Policy Issue Amount	# of Policies	$ Amount	% Incr/(Decr) Policy Issues	% Incr/(Decr) Policy Issue Amount	# of Policies	$ Amount
67,605	178,436,000	1235.5%	3659.7%	5,062	4,746,000	-79.8%	-93.6%	25,096	74,367,000

Section II—Phase I Comparison

Based on the data available prior to insolvency, we summarized Lincoln Memorial's risk profile and compared it to the analysis performed in Phase I. The following charts include a percentile distribution from the insolvent and life industry samples as well as the risk thresholds ("TH") determined in Phase 1 and the Company data point. Low, medium, and high risk thresholds are denoted by the dotted line. The legend further indicates directional order.

Figure 12

LINCOLN MEMORIAL RISK PROFILE AND PHASE I COMPARISON

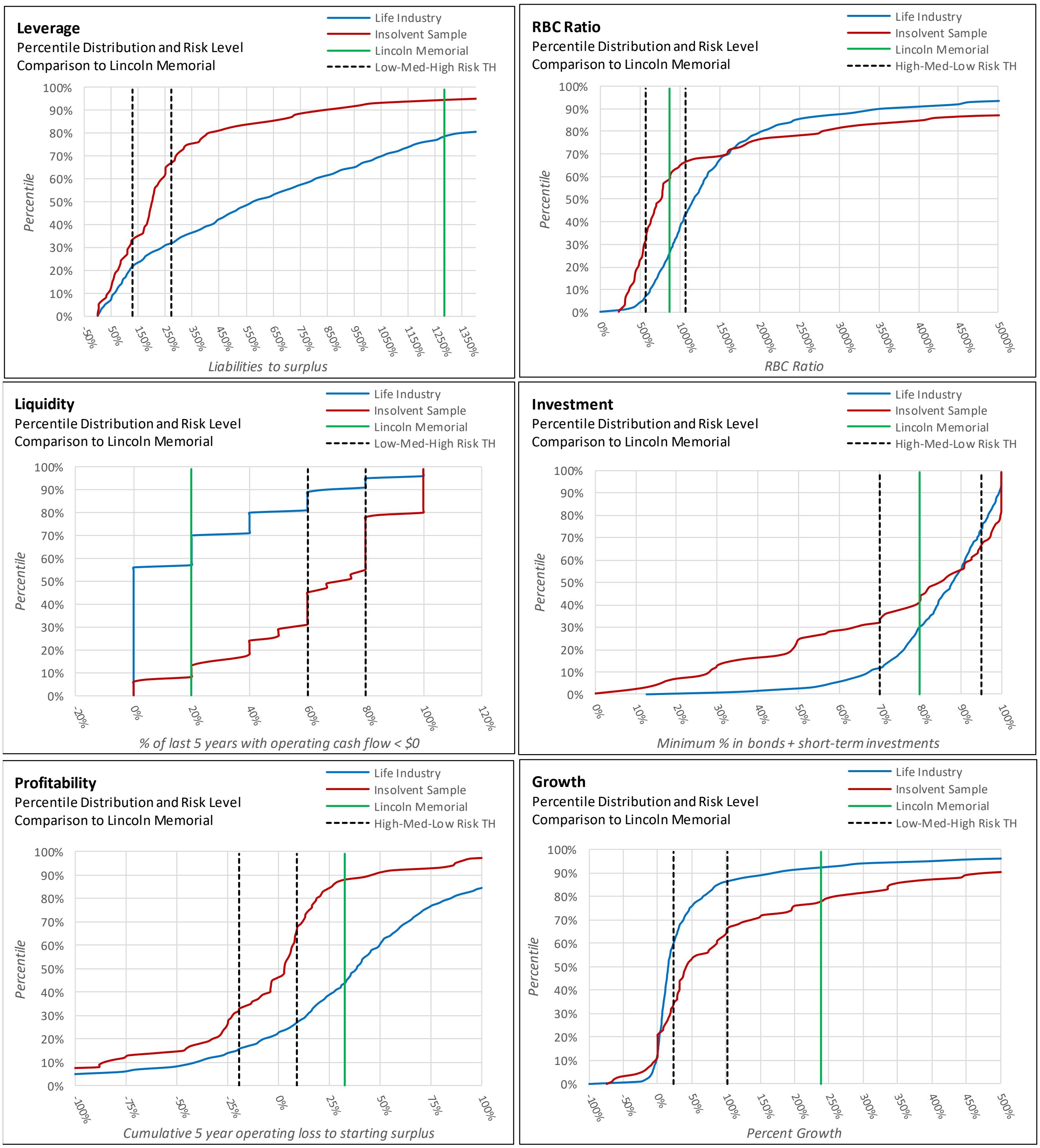
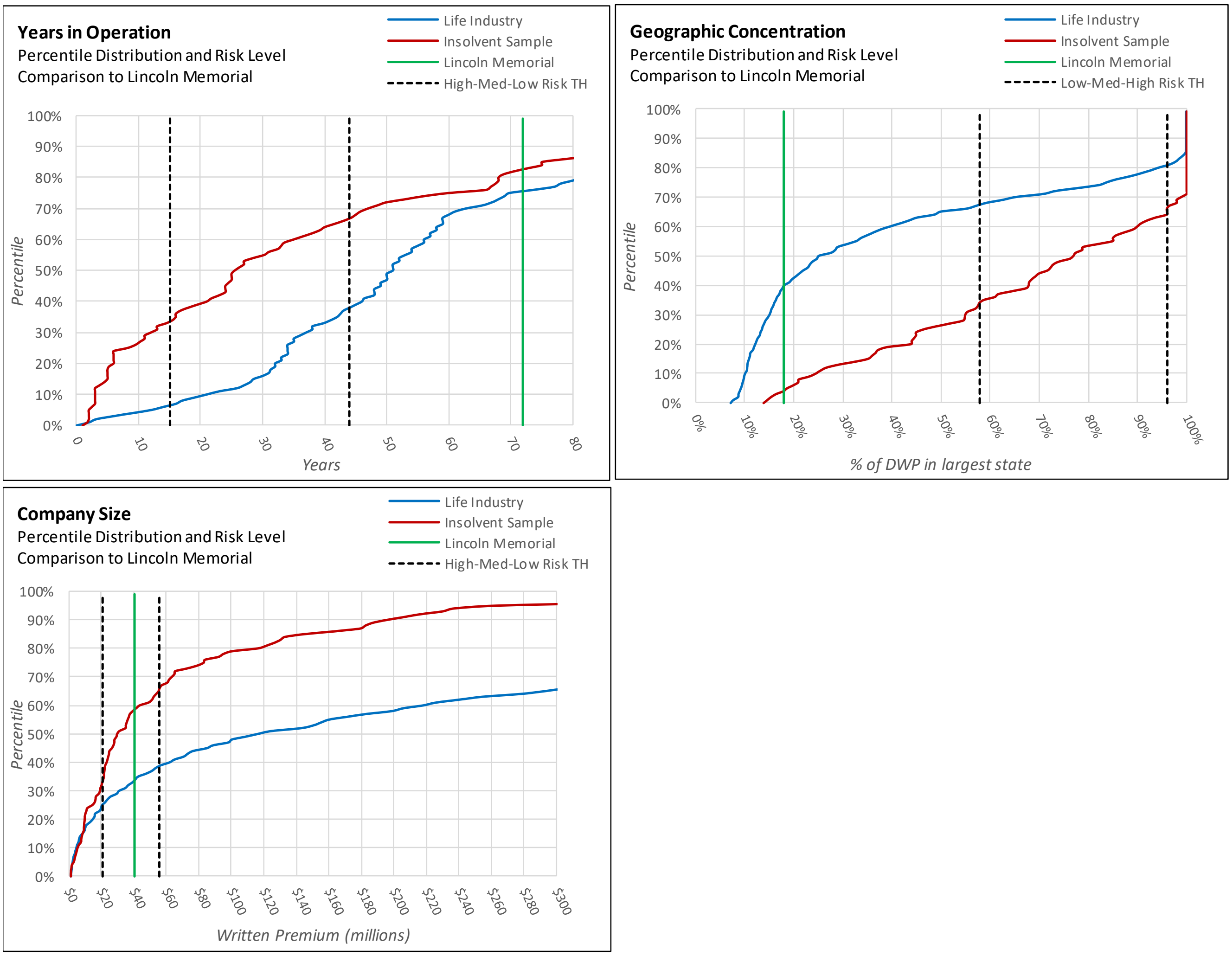


Figure 12 (cont.)



The following is a summary of observations related to figure 12:

- Overall, during Phase 1, the most indicative risk factors for the life & annuity cohort appeared to be premium growth, liquidity, investment, leverage, and RBC ratio.
- When compared to the insolvent sample and the industry sample (life & annuity cohort) in the charts above, Lincoln Memorial's highest notable risk factors were their premium growth and leverage.
- The Company also showed a medium percentile ranking in financial risk factors including investment and RBC ratio and a lower percentile ranking for profitability. This is consistent with the fact that the fraudulent activity did not impact the financials prior to being uncovered.
- Lincoln Memorial's number of years in operation is in the low-risk range. However, this notion is somewhat offset by the fact that the business mix for the pre-need contract picked up in the 1990s, long after the company's inception in 1936.
- Other demographic factors including years in operations and geographic concentration were in the low-risk category for Lincoln Memorial. Company size fell close to average.
- In this case, early indicators of insolvency risk would be more difficult to detect given the nature of the underlying issue of fraud.

Section III—Analysis of Key Findings

Some of the key observations from Lincoln Memorial's insolvency are as follows:

a) **Requirements on Corporate Governance**—Lincoln Memorial's ownership structure and related "consortium" may have lent itself to conflicts of interest. Stricter oversight of corporate governance may have had an impact on business decisions and thereby changed the course of the road to impairment. Some of the more recent corporate governance standards adopted by the NAIC, for example the annual corporate governance disclosure requirements and the enhancements associated with group supervision (Insurance Holding Company System Regulatory Act and Insurance Holding Company System Model Regulation with Reporting Forms and Instructions), may have helped with the identification of these issues.

b) **Assessment of Underlying Assets—**A review of the validity of underlying assets and confirmation as to their adherence to policy language appears to have been a significant issue in the case of Lincoln Memorial. In the practice of actuarial assessment, this area may often be overlooked, or, perhaps more commonly, disclosed as a reliance or limitation in cases in which the assets are believed to be valid. This points to the importance of actuaries, accountants, and investment specialists working in concert with one another in assessing the value of key assets and liabilities.

c) **Lapses—**The dramatic increase in lapse activity in 2007 was a potential indicator of unusual activity. There is no mention in the 2007 Statement of Actuarial Opinion of this activity. Currently, the only requirements for the Appointed Actuary regarding identification of unusual changes in the business in the current year (assuming those changes are not directly impacting reserve adequacy) are those required by Actuarial Standard of Practice No. 41, Actuarial Communications (ASOP41). ASOP41 requires a range of disclosures, including comment on any areas of risk or uncertainty or any subsequent events that might impact the analysis. In light of the actuary's understanding of the risk exposures of an organization, additional regulatory requirements that include commentary from the Appointed Actuary on general business trends could be a helpful addition to the surveillance process.