

WISCONSIN DEPARTMENT OF  
FINANCIAL INSTITUTIONS,

Plaintiff,

vs.

Case No. 12-CX-44-A

WISCONSIN FUNERAL DIRECTORS  
ASSOCIATION, INC.

and

FIDUCIARY PARTNERS, INC., as Trustee  
for the WISCONSIN FUNERAL TRUST,

Defendants.

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MOTION BY THE RECEIVER FOR AN ORDER  
DIRECTING THE INVESTMENT OF THE TRUST'S ASSETS

PLEASE TAKE NOTICE that John M. Wirth, the duly-appointed receiver (the "Receiver") for Wisconsin Funeral Trust (the "Trust"), by his attorneys Mallery & Zimmerman, S.C. and Kravit, Hovel & Krawczyk, s.c., will bring the following motion before the Court, the Honorable Peter C. Anderson presiding, in his courtroom at 215 South Hamilton Street, Madison, Wisconsin at 10:00 a.m. on September 6, 2013, or soon after such date and time as counsel can be heard.

**YOU ARE NOT REQUIRED TO FILE ANY PAPERS OR APPEAR IF YOU DO NOT OBJECT TO THE MOTION. HOWEVER, IF YOU DISAGREE WITH THE MOTION, OR YOU WANT THE COURT TO HEAR AND CONSIDER YOUR VIEWS ON THE MOTION, THEN YOU MUST FILE A TIMELY WRITTEN OBJECTION WITH THE COURT OR APPEAR AT THE HEARING.**

The Receiver moves the Court, pursuant to Section 10(m) of the Court's Injunction and Order Appointing Receiver Over Wisconsin Funeral Trust dated October 24, 2012 (as amended, the "Appointment Order"), for direction and authorization to invest the Trust's assets. Although the Receiver is prepared to recommend and implement a specific investment strategy, the Receiver has agreed with certain other parties to (1) seek the Court's guidance as to the standards that govern the investment of the assets and then, after the Court has ruled on that issue, (2) seek approval of a specific investment strategy that fits within those Court-determined standards.

The Receiver maintains that, prior to the appointment of the Receiver, the Trust was governed by investment standards set forth in Wisconsin Statutes Section 445.125; however, as a result of the appointment of the Receiver, and the subsequent changes to the Trust, all as described below, the Receiver maintains that the Trust became, as of the appointment of the Receiver, a liquidating trust rather than a funeral trust governed by the standards set forth in Section 445.125. If so, the investment standards of Section 445.125 should not apply.

In support of this Motion, the Receiver states:

#### BACKGROUND

1. On September 14, 2012 (the "Filing Date"), plaintiff Wisconsin Department of Financial Institutions ("WDFI") filed a complaint against the Wisconsin Funeral Directors Association, Inc. (the "Association") and Fiduciary Partners, Inc. ("Fiduciary Partners"), as Trustee for the Trust, alleging violations of securities laws relating to the Trust.

2. On the Filing Date, WDFI also filed, pursuant to Wisconsin Statutes Section 551.603(2)(b)1, a motion for appointment of a receiver of all assets of the Association and the Trust.

3. On the Filing Date, the Court entered an order appointing the Receiver as interim receiver for the Association and the Trust.

4. On October 24, 2012, with the stipulation of Fiduciary Partners and the Association, the Court entered the Appointment Order.

5. The Receiver has issued subpoenas and is investigating how the Trust was managed and invested prior to the Receiver's appointment, and will in the future make decisions whether and when to make demands for restoration of funds, make claims and, if necessary, assert claims in litigation to recover money for the Trust from responsible parties.

#### ORGANIZATION OF THE TRUST AS A FUNERAL TRUST

6. The Trust was formed on March 29, 1999 pursuant to a Trust Agreement Establishing the Funeral Trust (the "Trust Agreement") dated as of that date executed by the Association, as grantor, and The Stephenson National Bank & Trust, as trustee. Upon information and belief, the Trust Agreement has been amended at least four times.

7. The Trust Agreement is by its terms "a common master trust account by which Funeral Homes may invest Preneed Contract funds received from Preneed Consumers and required to be trusted ... in accordance with the terms and conditions of Wisconsin Preneed Law...." (Trust Agreement, March 29, 1999, "Whereas" clause and ¶ 1.01.) It is a funeral trust for burial agreements funded by trusts, organized and existing pursuant to Wisconsin Statutes Section 445.125(1).

8. Since its initial organization, various parties specified in the Trust have changed. Pursuant to the Second Amendment to the Wisconsin Trust Agreement dated as of April 1, 2004 (the "Second Amendment") the original Trustee, The Stephenson National Bank & Trust, was replaced by Fiduciary Partners, as successor Trustee. At the same time, pursuant to the Second

Amendment, the original depository, First Business Bank of the Fox River Valley, was replaced with BMO Harris Bank f/k/a M&I Bank Wisconsin, N.A. The Association, over time, replaced the original Investment Advisor, Smith Barney Inc. Consulting Group, with Bluepoint Investment Counsel. The Receiver subsequently replaced Bluepoint Investment Counsel with Ziegler Lotsoff Capital Management, LLC. The Association replaced the original Servicing Agent, Charing Company Inc., with The Newport Group.

#### STATUS OF TRUST ASSETS AND LIABILITIES AND FAILED ECONOMICS OF THE TRUST

9. As of July 31, 2013, the assets of the Trust had a value of \$41,463,838.52,<sup>1</sup> and trust liabilities to beneficiaries totaled \$66,933,065.<sup>2</sup> The Receiver will be prepared to provide an update to those numbers at the hearing on this Motion.

10. The contracts entered into by the Trust's beneficiary funeral homes with depositors promise interest at a rate equal to 1% over the average of three-year Wisconsin certificates of deposit. That rate is currently 1.85% per year.

11. Because the contracts promise a fixed rate of return, liabilities to consumers (depositors) continue to grow regardless of whether the Trust's investments make or lose money. As created, the structure of the Trust posed a significant risk of insolvency from its onset. Such risk has become a reality. As a result of the market losses caused by the recent recession, the Trust's former Investment Advisors attempted to outperform the market through an irresponsibly aggressive investment mix. They failed. Miserably.

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<sup>1</sup> This amount includes \$4.05 million of private equities that cannot yet be liquidated. The balance of this amount is held in cash. This amount also excludes the value of claims the Trust has against third parties, including various claims that have been settled in principle but that have not yet been finalized. The Receiver estimates that the claims will add in excess of \$8 million.

<sup>2</sup> This estimate assumes claimants are entitled to claims for principal paid, plus interest accruing at 1% over the average rate for three-year certificates of deposit in Wisconsin from September 14, 2012 forward, but includes interest credited prior to that date despite the fact that the amount credited at times exceeded the contract rate. The Trustee reserves the right to challenge any amounts credited to the extent that amounts credited exceed 1% over the average rate for three-year certificates of deposit in Wisconsin. The specified liabilities also do not include unpaid trust or receivership expenses.

12. Regardless of any decisions made by the Receiver or this Court, the obligations of the Trust, without taking into consideration any withdrawals from the Trust, will continue to grow by about \$1.3 million per year.

13. Moreover, the Trust continues to incur administrative costs of approximately \$400,000 per year (without taking into consideration the cost of the Receiver and his attorneys, accountants and consultants). The Receiver has reduced administrative costs by approximately \$700,000, and may be able to reduce those costs further.

14. Therefore, in order for the Trust to break even, the Trust needs to generate nearly \$1.7 million in income (again, ignoring the extra costs resulting from this receivership, potential litigation and changes in the Trust resulting from withdrawals). Put another way, the Trust needs to currently earn at least 3.4% in order to not become more insolvent than it already is, without even considering receivership and litigation costs.

15. Without investing the Trust assets, the Trust will continue to accumulate losses that further jeopardize its beneficiaries. The Receiver estimates that losses in the next 12 months will be between \$1.5 million to \$1.7 million. These estimated losses do not take into account opportunity cost, inflation or the costs of these proceedings.

#### RESTRICTION ON INVESTMENTS

16. The Receiver is currently prevented from investing the Trust's assets. Section 10(m) of the Appointment Order provides that the Receiver is empowered to:

(m) Maintain current investments and assets until such time as the Receiver determines it is prudent to liquidate or sell or otherwise transfer such investments and assets, and maintain the proceeds from any such sale or liquidation in cash or its equivalent *until the Court enters an order approving its reinvestment.*

(emphasis added).

17. Now is the appropriate time to seek authority from the Court to invest the funds. Waiting longer will result in an increased deficit between the claims against the Trust and the assets in the Trust.

#### CHANGE IN THE NATURE OF THE TRUST

18. Initially, based on actions already taken in this receivership pursuant to the Appointment Order, the Trust fundamentally changed as follows:

(a) In light of the status of Trust assets and liabilities, and the failed economics of the Trust, and in order to avoid an unmanageable depletion of the Trust's assets, the Receiver froze the Trust except as provided in the Appointment Order, as amended.<sup>3</sup>

(b) The Trust stopped seeking or accepting new deposits.

(c) Various provisions of the Trust Agreement (e.g., Sections 6.01 through 6.03 and other provisions relating to the operations of the Trust) became inapplicable.

(d) The Association was divested of all responsibilities assigned to it in the Trust.

(e) Most of the duties and obligations ascribed to parties by the Trust Agreement have been assumed by the Receiver.

19. Equally significant, the Settlement Agreement with funeral homes recently approved by the Court has further fundamentally altered the Trust. Prior to that settlement, depositors were at risk of losing money and benefits. The Settlement Agreement assured depositors of receiving substantially all of the benefits they were originally promised, clarified the funeral homes' obligations to assure that depositors receive those benefits, and strengthened

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<sup>3</sup> In the Appointment Order, the Court authorized the Receiver to reimburse funeral homes (and in limited circumstances, others) for certain costs associated with depositors' funerals and further authorized the Receiver to pay costs associated with the receivership from the Trust.

the enforcement of those obligations. The risk has shifted from one essentially shared by depositors and funeral homes to one borne by funeral homes.

20. As of the date of this Motion, 94.3% of the dollars, and 93.7% of the burial contracts, deposited in the Trust are covered by a settlement between the Receiver and a funeral home. The deadline for accepting the settlement is September 30, 2013, and the Receiver is confident that all funeral homes will have settled by that date.

21. In effect, the Trust is no longer a going concern; rather, it exists solely to marshal and liquidate its assets for the benefit of the Trust's beneficiaries.

22. The Receiver maintains that, under Wisconsin law and the specific provisions of the Appointment Order, as amended, the Trust is now a liquidating trust rather than a funeral trust as described in Wisconsin Statutes Section 445.125(1)(b)1. Therefore, the Receiver maintains that the Court has broad equitable powers to direct the investment of the money in the Trust.

23. Moreover, under the statute under which the Receiver was appointed, Wisconsin Statutes Section 551.603(2), the Court has the broad authority to order such "relief as the court considers appropriate."

#### THE OBLIGATIONS OF THE TRUST ARE LONG-TERM

24. In order to understand the investment needs of the Trust, it is important to understand that the Trust is a long-term vehicle.

25. Last fall, the Receiver engaged the national actuarial firm of Milliman, Inc. to analyze the Trust and its depositors. Among other things, Milliman, Inc. analyzed the age and sex of the depositors, as well as the length of time their deposits had been in the Trust as well as the Trust's history of withdrawals, and compared that information to standard actuarial tables.



26. Milliman, Inc.'s preliminary report in late 2012 concludes that over 2,100 depositors are likely to be alive 10 years from the time of the report (about 20% of the depositors at the time of the Appointment Order), and over 500 depositors are likely to be alive 20 years from the time of the report (about 5% of the original depositors).

27. Milliman, Inc. is in the process of preparing a more detailed report that the Receiver will provide to the Court.

#### INVESTMENT OPTIONS

28. A myriad of options exist for investing the Trust's assets. This Motion focuses on three options: (a) what appears to be required for a burial trust under Wisconsin Statutes Section 445.125(1)(b)1. (certificates of deposit); (b) Treasury Bills, considering that, being backed by the full faith and credit of the United States, they are virtually as guaranteed as certificates of deposit; and (c) a diversified, conservative investment portfolio.

29. The Court would have an opportunity to approve the details of any investment option at a future hearing.

30. In any event, the Receiver would insist that any investment plan be safer than required under the Uniform Prudent Investors Act, Wisconsin Statutes Chapter 881 and, in particular, Section 881.01(3).

#### Wisconsin Statutes Section 445.125(1)(b)1.

31. If the Court determines that Section 445.125(1)(b)1. must be literally applied to this liquidating trust, then the Receiver is obligated to deposit (invest) all of the funds as follows<sup>4</sup>:

with a bank or trust company within the state whose deposits are insured by the federal deposit insurance corporation, deposited in a savings and

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<sup>4</sup> There is no case law that directly interprets this Statute.



loan association or savings bank within the state whose deposits are insured by the federal deposit insurance corporation, or invested in a credit union within the state whose savings are insured by the national board, as defined in s. 186.01 (3m), and shall be held in a separate account in the name of the depositor, in trust for the beneficiary until the trust fund is released ....

32. Based on the Appointment Order, the Receiver is of the opinion that the Receiver would need the Court's authorization to invest the money pursuant to Section 445.125.

33. Read literally, Section 445.125 *might* require the Receiver to break-up the master trust and put the funds in 10,827 separate, federally-insured accounts. The Receiver knows of no party who advocates for 10,827 separate, federally-insured accounts. Although that might have been the original legislative intent, the Receiver is left dealing with the fallout out of the numerous poor decisions that have made over the history of the Trust. Breaking up the master trust, and re-creating 10,827 separate accounts, would be incredibly expensive; would result in payouts to funeral homes considerably less than the 60% minimum payout currently projected; could very well be a breach of the Settlement Agreement with funeral homes; and would make administering the Settlement Agreement difficult, or perhaps impossible, thereby negating some or all of its benefits.

34. Therefore, regardless of how the Receiver invests the Trust's assets, the Receiver will not be in compliance with the requirements of Section 445.125.

35. It is, however, possible to maintain the master trust while investing its money in federally-insured accounts.<sup>5</sup> There are at least two programs offered by banks that would permit all of the funds, or substantially all of the funds, to be federally insured.

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<sup>5</sup> Under the current Federal Deposit Insured Corporation regulations, the Trust may be able to place \$1.25 million in a single federally-insured institution; however, the Receiver has yet to be able to find a financial institution that is willing to offer such a program. Therefore, the Receiver has analyzed other programs.

36. One such program would allow the Receiver to invest somewhere between \$10 million and \$15 million at large federally-insured commercial banks (the "Large Bank Program"). If the Court requires the money to be in federally-insured accounts, the balance of the money would be deposited through the CDARS program described below. A model established for the Large Bank Program shows an average maturity of 2.786 years with an effective yield to maturity of 0.886% (0.00886), or less than 1%. That yield would increase or decrease based on cash flow needs. If this fund were used for the majority of the long-term cash needs, the yield could be as high as 2-3%; however, it might be difficult to place \$10 million - \$15 million at longer-terms. There is a set-up or management cost to participate in the Large Bank Program, which the Receiver would negotiate if this route is required. The cost might equal or exceed the first year's interest.

37. The other program, known as CDARS (<http://www.cdars.com/>), is offered through a variety of regional and local banks. It has a much broader array of participants and can, therefore, accommodate all of the Trust's assets. However, it offers little in the way of long-term certificates, and therefore, offers a lower yield. Based on estimates provided to the Receiver, the yield would be considerably lower than the program described above, and may result in a yield somewhere around 0.3% (0.003). It also involves some financial institutions with much lower credit ratings and does not provide an option to exclude financially unstable institutions. All deposits would be insured by the FDIC. The CDARS program would have no direct cost; however, the initiating bank receives a spread.

38. Assuming the Trust invests approximately one-third of its assets in the Large Bank Program and two-thirds in the CDARS program, the Receiver expects that the effective

yield could be as high as 1%, but might be significantly lower if the Receiver is not able to place adequate dollars in long-term certificates.

39. Although the investment is "safe," it is fixed while the interest accruing on depositors' accounts is not. Therefore, to the extent interest rates rise over the next few years, as expected, the gap between income earned and obligations owed to depositors will continually and significantly increase.

40. The advantages and disadvantages of this kind of investment are as follows:

ADVANTAGES: Safe, federally-insured.

Lower investment cost.

DISADVANTAGES: Tremendous opportunity cost.

Interest rate risk – no ability to time reinvestment; expensive to take advantage of higher interest rates; interest earned does not correspond to the rising interest expense of the Trust.

Would result in an effective yield v. the obligations being incurred by the Trust of close to a negative \$750,000 in the first year alone (see below). If interest rates increase, the spread would be significantly greater.

#### Treasury Bills

41. Treasury Bills would be a very safe alternative to federally-insured accounts. Treasury Bills are backed by the full faith and credit of the United States government.

42. However, Treasury Bills do not comply with Section 445.125. If Treasury Bills are acceptable, the Receiver assumes that the Court can only reach this conclusion by determining that Section 445.125 does not govern the liquidating trust.

43. If the Receiver were to invest in Treasury Bills, the overall yield would be comparable or slightly better by a few tenths of a percentage point than the best case scenario for federally-insured accounts set forth above.

44. The advantages and disadvantages of Treasury Bills are similar to certificates of deposit except that Treasury Bills are easier to purchase in the durations desired and are significantly easier to cash out if cash flow is needed to due to unexpected deaths.

#### Conservative, Diversified Portfolio

45. Unlike the investment scheme utilized by the Trust's prior Investment Advisors and approved by its management, the Receiver believes that it is possible to craft a conservative, diversified portfolio heavily weighted towards fixed-income products.

46. The Receiver has consulted with investment professionals at a number of firms, including those at the Trust's current Investment Advisor (Ziegler Lotsoff Capital Management, LLC) and investment advisors at national and regional banks.

47. Any such approach, if structured appropriately, would include:

A. Monthly, quarterly and annual reporting of assets and liabilities in a clear and understandable manner to beneficiaries; and

B. Would require some reserves to buffer against market downturns. The reserves would be in the nature of some portion of the Trust's assets that, although invested, would not be available to pay claims until later so that there is at least partial protection against a market downturn.

48. A conservative, diversified portfolio, with a concentration in diversified, fixed-income products and a very limited investment in safe, publicly traded equities, would allow the Trust to take advantage of rising interest rates and would allow an increase in yields.

49. The details of such an investment portfolio would be considered at a future hearing; however, the Receiver believes that a portfolio properly invested, in today's market, would realize a yield of between 2.5% and 4.5%. The particular investments would be selected for their safety and stability.

50. A proper investment portfolio would narrow or eliminate the gap between the obligations on the burial contracts and the income received by the Trust, thereby helping to ensure that the Trust can in fact continue to pay 60%, or some higher amount, on funeral contracts. It is unlikely that there would be significant appreciation to eliminate the gap between the Trust's assets and liabilities; however, that gap should not be allowed to continue to spread.

51. If the gap continues to spread, and returns to funeral homes decrease, the viability of some funeral homes may be jeopardized. If funeral homes are forced out of business as a result of their own insolvency, depositors would be once again in jeopardy.

52. Various parties-in-interest may be skeptical, considering the history of the Trust. The Receiver maintains that the Trust's losses were not caused simply because the money was invested; rather, they were caused because the money was invested incredibly irresponsibly.

53. Most conservatively invested large dollar portfolios have rebounded. The Trust would not be in its current precarious position if the former Investment Advisors had not tried to make back market losses quickly or if they had been replaced by responsible or sophisticated management.

54. The Receiver believes that, although investing the assets in certificates of deposit or Treasury Bills would be better than the assets in cash, limiting the Trust to these inflexible, fixed-rate products would be imprudent and will cause additional damage. Interest rates are

bound to rise and, with a rise in interest, the spread between the Trust's income and the obligations incurred in connection with the burial contracts will significantly increase.

55. The Receiver was appointed under the equitable powers of this Court on petition pursuant to Wisconsin Statutes Section 551.57. The powers of a receiver are delineated in Wisconsin Statutes Section 813.23(2)(a)(1)-(6), which include requiring the receiver to "insure the conservation of such property" of the receivership, and "administer said property as an equity receivership." Without the restrictions of Section 445.125, the Receiver is a fiduciary, and therefore is responsible to manage the Trust and invest the *res* in accordance with the Uniform Prudent Investors Act, Wisconsin Statutes Chapter 881 and, in particular, Section 881.01(3).

56. Under this standard, the Receiver must exercise reasonable care, and "invest and manage assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the ... trust." The Receiver is to have "an overall investment strategy having risk and return objectives reasonably suited to the ... trust." Wis. Stat. § 881.01(3)(a)-(b).

57. If the Court allows the money to be invested in some manner other than federally-insured products, the Receiver intends to come back to Court promptly with a detailed investment policy, allowing the Court and parties-in-interest to question the Receiver and his advisors about the specifics of the policy, as well as the qualifications of the Investment Advisor and the Receiver's plans to make the investments transparent so that all parties know precisely what is happening.

#### RELIEF REQUESTED

58. For the foregoing reasons, the Receiver seeks an order that:

(a) Clarifies the standard of investment applicable to the Trust's assets, subject to further order of the Court approving a specific investment policy;

(b) Provides that the Trust is no longer a funeral trust governed by Wisconsin Statutes Section 445.125 but is, instead, a liquidating trust governed by the laws and equitable principles governing trusts generally under Wisconsin law;


(c) Changes the name of the Trust to WFT Liquidating Trust and authorizes the Receiver to make such change on the records of the Wisconsin Department of Financial Institutions;

(d) Clarifies that the Receiver, subject to the terms, conditions and limitations of the Appointment Order, is the Trustee of the WFT Liquidating Trust (subject to replacement at the conclusion of this case in a manner acceptable to the Court).

Dated as of August 30, 2013.

MALLERY & ZIMMERMAN, S.C.  
Suite 900  
731 North Jackson Street  
Milwaukee, Wisconsin 53202-4697  
telephone: 414-727-6276  
facsimile: 414-727-6306  
email: mmarx@mzmilw.com

MALLERY & ZIMMERMAN, S.C.  
Attorneys for John M. Wirth, Receiver

By:   
Michael A. Marx  
State Bar No. 1057107

CO-COUNSEL:

KRAVIT, HOVEL & KRAWCZYK s.c.  
825 North Jefferson – Fifth Floor  
Milwaukee, Wisconsin 53202  
telephone: 414-271-7200  
facsimile: 414-271-8135  
email: kravit@kravitlegal.com  
      cjk@kravitlegal.com  
      aha@kravitlegal.com

KRAVIT, HOVEL & KRAWCZYK, S.C.  
Attorneys for John M. Wirth, Receiver  
Stephen E. Kravit  
State Bar No. 1016306  
Christopher J. Krawczyk  
State Bar No. 1033982  
Aaron H. Aizenberg  
State Bar No. 1066340