



STATE OF INDIANA

DEPARTMENT OF FINANCIAL INSTITUTIONS



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Interpretative Letter 001-14

September 3, 2014

RE: Investment Alternatives for Preneed Funeral Trusts

Dear []:

This letter responds to the request by your client, [], that the Department of Financial Institutions (the "Department") confirm Indiana law does not prohibit an arrangement whereby a bank enters into an agreement with a third-party investment advisor for the investment of funds deposited pursuant to a preneed funeral contract in investments other than bank deposits or insurance contracts. This is the conclusion you reached in your letter of July 1, 2014 to [] on this subject.

Summary of Department Conclusion:

We respectfully disagree with your conclusion. It is the view of the Department that the applicable statutes governing funeral trusts and sale of preneed funeral services and merchandise require the financial institution to maintain said funds in bank deposits or to fund the plan through an insurance contract.

Background:

As outlined in your letter, pursuant to a written escrow agreement, [] (the "Bank") currently serves as an Escrow Agent and has control over funds deposited in certain trust accounts established in connection with preneed funeral contracts. The preneed funeral contracts are each established pursuant to a written agreement between the individual account owners and the funeral homes of their choice.

The Bank and the funeral homes are also a party to a "Selection of Investment Adviser and Hold Harmless Agreement" (the "Agreement"). The Agreement provides for the selection of [] of [] as Investment Advisor for the management, administration, investment, reinvestment and disposition of the escrowed funds and covenants to hold the Bank harmless in consideration for it using [] as Investment Advisor.

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In an email dated March 3, 2014, a Department field examiner advised [] that the above described structure does not comply with the requirements of the Indiana Code. The field examiner further explains: "As I indicated to you, our primary concern is for the safety of the end user's funds so as to ensure their desired services. To that end, State Statutes are quite clear as to what constitutes a permissible investment, i.e. bank deposit or an insurance policy. IC 30-2-10-3 lists the requirements to ensure the validity of such a trust, including 'names as trustee an Indiana institution qualified under section 2 of this chapter, and requires that all funds be deposited in that institution.' Under the proposed arrangement, I understand it to be that [] maintains control over the assets."

In response to the Department's email, [] apparently requested your analysis of the various statutes and the contractual arrangements between the Bank, individual account owners and the investment adviser which resulted in your letter of July 1, 2014 to [], in which you conclude Indiana law does not prohibit the arrangement described in your letter.

As I said at the outset, we have been asked to confirm your conclusion. In the alternative we will explain the Department's position in this interpretative letter. As is common practice, when this letter is issued publicly, we will remove the names of all parties.

Discussion:

The sale of funeral services and merchandise in Indiana is governed by a patchwork of statutory provisions adopted during the period from 1978 to 1999. IC 30-2-9 *et seq.* governs preneed funeral plans and funeral trusts established before 1982. IC 30-2-10 *et seq.* governs funeral trusts formed after 1982. IC 30-2-13 *et seq.*, adopted in 1991, addresses preneed funeral services and merchandise. IC 30-4-3.5 *et seq.* is the Uniform Prudent Investors Act and is specifically applicable to each of the three acts previously described in this paragraph. IC 30-4-3.5-1(c)(1)-(3).

Principles of Statutory Interpretation:

We begin our analysis with a review the basic rules of statutory interpretation that Indiana law embraces:

- A statute is given its clear and plain meaning if unambiguous, but if ambiguous a court must try to ascertain the legislative intent, and the court's primary goal is to interpret the statute to effectuate that intent. *Basileh v. Alghusain*, 912 N.E.2d 814, 821 (Ind.2009); *City of Carmel v. Steele*, 865 N.E.2d 612, 618 (Ind.2007).
- The Indiana Supreme Court describes the "intent" inquiry as follows: "[t]he court will look to each and every part of the statute; to the circumstances under which it was enacted; to the old law upon the subject, if any; to other statutes upon the same subjects, or relative subjects, whether in force or repealed, to contemporaneous legislative history, and to the evils and mischiefs to be remedied." See *Ashlin Transp. Services, Inc. v. Indiana Unemployment Ins. Bd.*, 637 N.E.2d 162, 166-67 (Ind.Ct.App.1994) (summarizing Indiana Supreme Court cases).
- Because Indiana statutes have no explanatory committee reports, there is little legislative history to examine beyond amendments to the statute. See, e.g., *C.C. v. State*, 907

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N.E.2d 556, 558-59 (Ind.Ct.App.2009). - See more at: <http://caselaw.findlaw.com/us-7th-circuit/1508582.html#sthash.oV6T66W9.dpuf>

In addition to the presumption against retroactivity, Indiana case law recognizes many other familiar presumptions of statutory interpretation:

- e.g., if language is used in one section but omitted in another, the court presumes that the legislature acted intentionally in doing so, see *City of Crown Point v. Misty Woods Properties, LLC*, 864 N.E.2d 1069, 1076 (Ind.Ct.App.2007) (internal citations omitted);
- statutes in derogation of the common law are to be strictly construed, see *Stanley v. Walker*, 906 N.E.2d 852, 862 (Ind.2009) (Dickson, J., dissenting) (citing *Bartrom v. Adjustment Bureau, Inc.*, 618 N.E.2d 1, 10 (Ind.1993)); and
- an amendment to a statute creates the rebuttable presumption that the amendment was intended to change the law, see *Turner v. State*, 870 N.E.2d 1083, 1087 (Ind.Ct.App.2007).
- Lastly, when the legislature passes several statutes during the same session, those should be interpreted in harmony, to give effect to each. See, e.g., *Ware v. State*, 441 N.E.2d 20, 22-23 (Ind.Ct.App.1982) (internal citations omitted). - See more at: <http://caselaw.findlaw.com/us-7th-circuit/1508582.html#sthash.oV6T66W9.dpuf>

Statutory Analysis:

While it is true that the Uniform Prudent Investor Act is specifically applicable to the provisions relating to the establishment of funeral trusts and the sale of preneed funeral services and merchandise, compliance with the prudent investor act does not justify ignoring the plain language of the funeral trust acts or preneed funeral statutes. The rules of statutory construction dictate that each of the acts must be read giving their clear and plain meaning unless there are ambiguities. In the case of ambiguities, legislative intent is examined to resolve those ambiguities.

Each of the three acts in question use language that indicates trust funds are to be deposited in accounts in financial institutions. IC 30-2-9 *et seq.* deals with prepaid funeral plans and funeral trust funds established before 1982. IC 30-2-9-1(b) provides "it is unlawful to enter into any agreement or contract for a purpose described in subsection (a) unless the agreement or contract requires that all payments be made by the settlor to an account in a:

- (1) bank;
- (2) trust company;
- (3) savings association; or
- (4) credit union;

whose principal office is in Indiana."

IC 30-2-9-1.5(b) further provides that "[a] funeral trust established under this section must:

(6) be either a time deposit, or account, or certificate of deposit in a financial institution, in the names of the settlor and the beneficiary payable on death to the survivor, or name the designed financial institution as sole trustee."

In 1982 the General Assembly adopted IC 30-2-10 *et seq.* governing funeral trusts formed after June 30, 1982. IC 30-2-10-2 provides that "[i]t is unlawful to enter into any agreement or contract for a purpose described in section 1 of this chapter unless the agreement or contract requires that all payments be made by the settlor to an account in a:

- (1) bank;
- (2) trust company;
- (3) savings association; or
- (4) credit union;

with an office in Indiana.

IC 30-2-10-5 provides in part that "[t]he contract under which funds are accepted under this chapter must be in writing and contain, as a minimum, the following provisions:

(6) A provision for full payment of the contract amount by the settlor, a description of the manner in which the funds are to be deposited, and *a statement that the interest will accrue to the trust account and a further statement that the principal and interest earned shall inure to the beneficiary* to cover all the costs incident to the beneficiary's performance of the contract, any excess to be refunded to the estate of the settlor or to the heirs at law."

[Emphasis added.]

In 1991, IC 30-2-13 *et seq.* was adopted governing the sale of funeral services and merchandise in advance of the time they will be needed which is commonly known in the industry as "preneed" funeral plans. IC 30-2-10-12.5 acknowledges that contracts for preneed funeral services and merchandise can be funded in cash, either paid in a lump sum or in installments, or an insurance policy, either newly issued or previously issued, or a combination of these means of payment. These provisions specifically authorize that the funds or insurance policies be placed in either a trust account (IC 30-2-13-12.5(c)) or escrow account (IC 30-2-13-12.5(d)). In the case of a trust account, the account must:

- (1) Be irrevocable and require either of the following:
 - (A) The seller deposit the insurance policy used to fund the contract into the trust account. . . .
 - (B) The seller deposit the cash used to fund the contract into the trust account. . . .
- (2) Designate the seller as the beneficiary of the trust.
- (3) Designate a trustee qualified under this chapter and authorize the trustee to assess the charges authorized under section 18 of this chapter.
- (4) Require that *a separate account be maintained in the name of each purchaser.*
- (5) Require that *any interest, dividend, or accumulation in the account be reinvested and added to the principal.*
- (6) Permit the assets of the several, separate accounts to be commingled for investment purposes.

(7) Require that on receipt of the seller's proof of delivery of services or merchandise the trustee shall remit to the seller the full amount in trust applicable to the purchaser's contract and all of the accumulated interest.

(8) Permit the seller to retain the remaining amount if the amount in the trust account is greater than the seller's total current retail price of all services and merchandise subject to the contract at the time of delivery of all services or merchandise subject to the contract.

... [Emphasis added.]

IC 30-2-13-12.5(c).

The plain language in all three acts indicates that the funds to pay for the funeral services and merchandise are to be deposited in the trustee's trust account or the escrow agent's escrow account. The plain language of these acts does not support the trustee transferring the funds to a third party investment adviser for investment.

Legislative Intent:

However, even if the acts are ambiguous so as to call into question whether a trustee may invest the funeral funds with a third party investment adviser, then the rules of statutory construction dictate that the intent behind the legislation must be examined. Again, since Indiana statutes have no explanatory committee reports, there is little legislative history to assist in ferreting out the legislative intent. The Department, however, has been directly and indirectly involved in a number of situations in which consumers have been defrauded in various illegal or negligent transactions leading to the loss of millions of dollars of consumer funds intended to pay for funeral services and merchandise.

The most notable case involving an Indiana financial institution was Robert Nelms and Debora Johnson-Nelms, owners of Memory Gardens Management Corp., who were charged in 2008 with looting a \$22 million trust fund established largely on behalf of Indiana consumers to provide funds for funeral and other burial expenses. Later that year, the Indiana General Assembly adopted HEA 1026 which implemented sweeping changes to funeral trusts and the sale of preneed funeral services, including felony charges for the kinds of violations found in the Memory Gardens case. Although not affecting Indiana consumers directly, the same Indiana financial institution served as the trustee for the Forest Hill Cemetery Trust in Tennessee and the Summerfield Cemetery Trust in Michigan. Both were highly publicized due to the embezzlement of trust funds by the owner, Clayton Smart, in collusion with Smith Barney investment broker, Mark Singer. Both Mr. Smart and Mr. Singer were convicted in Tennessee and Michigan. Mr. Singer was also convicted in Indiana.

Indiana was hardly alone in dealing with fraudulent schemes in the funeral trust and preneed funeral services and merchandise field. In 2008, Wisconsin officials persuaded a judge in Dane County, Wisconsin, to place the Wisconsin Funeral Trust in receivership when a shortfall of more than \$21.5 million was discovered. In 2009 Merrill Lynch Life Agency, Inc. paid the Illinois Division of Insurance \$18 million to settle a state investigation into the firm's role in an imploded funeral trust. In 2013 prosecutors in St. Louis, Missouri won convictions and plea agreements against individuals involved in a network of companies that included National Prearranged Services for bilking customers out of as much as \$600 million.

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While many of these events occurred after the adoption of the funeral trust and preneed acts, it is logical to conclude that the legislature has long viewed this area as one in which consumer protection is essential. As is illustrated in the descriptions of these various cases, the funeral trust and preneed funeral services and merchandise have many of the elements that attract the disreputable and unscrupulous and can lead to devastating losses to consumers: large sums of money, long periods of time before the money may be used and losses discovered, unsophisticated consumers concerned that their families are not burdened with funeral costs, and little or light regulation of funeral trusts and preneed plans. All of these factors lead the Department to conclude that the legislative intent behind these acts is at least in part to protect Indiana consumers.

While it is true that the Uniform Prudent Investor Rule does apply to these acts, given that consumer protection is one of the principal factors behind these acts, it is reasonable to narrowly construe the language in these acts and to conclude that the prudent investor rule would result in the trustee maintaining the funds in the accounts that are described in the plain language of the acts. As a fiduciary, the trustee must look at the safety of the funds and the necessity that they be available when they are needed at the death of the person for whom the trust was established. Unlike a situation where maximum return on investment is necessary to produce adequate income for future events, the funeral services and merchandise are already defined and in many cases guaranteed. The risks associated with higher returns on investment are not justified in these circumstances where all that is needed is to provide a set amount to pay for specified services and merchandise. While earnings are a part of the overall plan they do not support substantial risk.

Conclusion:

It is the Department's view that the application of the Prudent Investor Rule leads to the same result as a strict reading of the plain language of the statutes. The plain language of the statutes states that the funds are to be deposited in accounts of that institution. Applying the Prudent Investor Rule, the funds should be placed in safe, insured depository accounts of the institution and not with a third party investment adviser in uninsured accounts such as mutual funds. In the alternative, these plans may be funded by insurance policies.

I trust this letter is responsive to your inquiry. If you have additional questions, please contact me at the phone or email listed above.

Sincerely,

/s/ Constance J. Gustafson

Constance J. Gustafson
General Counsel

cc: Dennis L. Bassett, Director
Thomas C. Fite, Deputy Director