

**SPECIAL INVESTIGATIVE REPORT:  
THE LOEWEN GROUP, INC.**

**SUNSET MEMORIAL PARK AND  
MORNINGSIDE MEMORIAL GARDENS**

**OCTOBER 2001**

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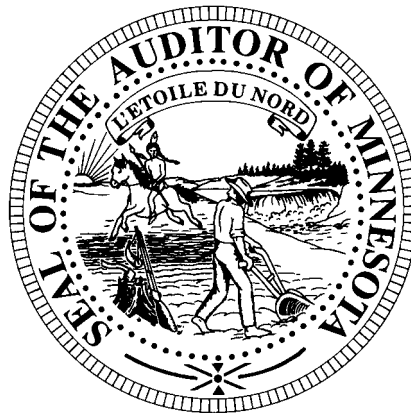
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### **I. INTRODUCTION**

The Office of the State Auditor (OSA) has completed an examination into statutory noncompliance by Sunset Memorial Park (Sunset) and Morningside Memorial Gardens (Morningside), two cemeteries both of which are holdings of The Loewen Group Inc. (Loewen), a Canadian corporation doing business in Minnesota and other states, Canada, and the United Kingdom. Loewen owns or operates approximately 1,000 funeral homes and 375 cemeteries. Approximately 90 percent of its total revenue is derived from U.S. operations.

This report is the conclusion of two years of investigation and analysis by the OSA. In June 1999, the OSA initiated an examination of Sunset based on information obtained from a consumer who alleged that payment for certain preneed goods were not properly trusted in accordance with Minnesota law, and that merchandise selected was not delivered as the cemetery represented. In addition, the OSA received information from both Hennepin and Anoka Counties for Sunset and Morningside, respectively, concerning preneed and permanent care and improvement trust fund reporting errors and inconsistencies. As part of this examination, the OSA reviewed information through year end December 1999.<sup>1</sup>

Although many of the records supporting both the preneed and PCI funds were obtained and reviewed to determine their accuracy, this examination did not include a formal audit of the financial activity of the cemetery accounts.<sup>2</sup>

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<sup>1</sup> NOTE REGARDING SCOPE: The OSA commenced its review of Morningside and Sunset in 1999. For over two years, the OSA has worked with Loewen to obtain complete trust fund data. Despite sending voluminous correspondence containing incomplete numbers, Loewen has yet to provide the OSA with final data. Therefore, in order to complete its review, the OSA relied upon data filed by Loewen with the Minnesota Department of Health and county auditors, as required by Minnesota law, as well as data supplied by Loewen's independent accountants. That data was essentially complete through 1999. Despite receiving post-1999 information regarding Loewen's data conversion process, to date, Loewen has failed to provide the final trust data for OSA analysis.

<sup>2</sup> The OSA reviewed the relevant Minnesota statutes governing preneed and permanent care and improvement trust accounts. It also examined consumer complaints and relevant county documents. The OSA determined that a broad examination was warranted for the purpose of evaluating overall compliance with both the consumer preneed and cemetery permanent care and improvement statutes.

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**A. Preneed Arrangements and Preneed Trust Funds**

Minnesota consumers have the option of selecting and prepaying for services and merchandise related to funeral and burial needs. These selections are otherwise known as preneed arrangement sales. Many consumers use this option as a means to pre-pay for their funerals and burials either for their own peace of mind or to avoid the extra emotional burden of making at-need purchases ordinarily borne by survivors.

Because of the significant amounts of consumer money involved in prepaying for funeral and burial expenses – an estimated \$73.5 million statewide<sup>3</sup> – Minnesota state law imposes an obligation on funeral and burial providers for the proper care and handling of consumer dollars. Whether for funeral or burial goods or services, once funds earmarked for preneed arrangements are received from the consumer, a relationship of implied trust is created, the oversight of which the Minnesota Legislature determined to be a matter of public interest.

The first Minnesota preneed law governing consumer funds was enacted in 1953. This statute<sup>4</sup> required that 100 percent of preneed sales proceeds paid by consumers be held in a trust account until the contract was either fulfilled by providing all services or merchandise selected, or the money was refunded to the consumer. Minnesota law required that the consumer's funds be deposited into a separate trust account in a federally insured financial institution within 30 days of receipt.<sup>5</sup> Further, at the time of death, any funds remaining in the trust and not used for the purposes designated by the consumer would revert to the decedent's estate. As amended, these provisions remain in law today.<sup>6</sup>

The matter of trust fund dividends was addressed in a 1967 amendment when the Legislature clarified the terms under which consumer assets were held in trust. A provision was added to Minn. Stat. § 149.11, requiring that all accruals of dividends on consumer trust funds must remain in the trust.<sup>7</sup> The 1967 amendment expanded

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<sup>3</sup> Minnesota Department of Health: Burial and Funeral Goods and Services Consumer Protection; January 2001.

<sup>4</sup> Minn. Stat. § 149.11-.14 (1953).

<sup>5</sup> Minn. Stat. § 149.12 (1953).

<sup>6</sup> See Minn. Stat. § 149A.97 (2000).

<sup>7</sup> 1967 Minn. Laws, ch. 32, § 1.

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the statute to apply to any contracts or transactions “with another person, partnership, association, or corporation . . . for or related to the disposition of his body.”<sup>8</sup> The Minnesota Attorney General’s Office has stated that this amendment brought cemeteries within the ambit of the preneed trust requirements.<sup>9</sup>

**B. Oversight Authority of the Office of the State Auditor**

Further amendments to the existing preneed trusting laws occurred in 1988 and addressed State Auditor oversight responsibility and sales reporting requirements.<sup>10</sup> The status of preneed trust funds were required to be reported on forms designed by the State Auditor. Licensed funeral establishments (i.e., mortuaries) reported their preneed activity to the Department of Health. Preneed sellers not requiring licensure reported to their respective county auditor. Both the Health Department and county auditors were to review the reports and were required to annually file a letter with the OSA indicating whether or not violations of the preneed trust requirements were found during their respective reviews.

The 1988 amendments also delegated to the OSA the oversight responsibility to act on any reported violations of the preneed trusting laws and make an independent determination of whether a violation is occurring or about to occur. If evidence of a violation is found, the OSA must conduct an audit and thereafter inform the appropriate agency of any findings of misconduct. The law was also amended to require that consumers be informed about the location of their trust account (e.g., name and address of financial institution) and that any changes be disclosed in writing.

As described above, the OSA is directed by law to examine any indication of violations of the laws governing the preneed and permanent care trust funds. Minnesota Statutes, Chapters 149A and 306, delegate broad oversight authority to the Office of the State Auditor regarding the financial activities of funeral providers and cemeteries. A key portion of this oversight authority specifically concerns the management of two types of trust funds maintained by funeral providers and/or cemeteries. The funds are: 1) preneed trust funds established on behalf of consumers who make contractual arrangements with funeral providers for the selection of funeral and burial services and merchandise in advance of need; and

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<sup>8</sup> *Id.*

<sup>9</sup> Office of the Attorney General, letter dated June 10, 1999.

<sup>10</sup> 1988 Minn. Laws, ch. 509, §§ 1, 2.

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2) permanent care and improvement funds, which are the resources set aside for the perpetual care and maintenance of cemeteries. The authority for the OSA to conduct oversight investigations of preneed arrangement trust funds is found at Minn. Stat. § 149A.97, subd. 8. The authority for the OSA to conduct oversight investigations of cemetery permanent care and improvement trust funds is found at Minn. Stat. § 306.97.

## **II. CHRONOLOGY OF EVENTS**

The OSA's review of certain Loewen-owned properties dates back to 1997. In August 1997, the OSA was contacted by a complainant representing the family of a recently-deceased individual. The complainant advised, and the OSA later verified, that a Mrs. Dahl, on December 17, 1994, purchased two full-size interment vaults from Sunset Memorial Park at a cost of \$1,500.00 each.<sup>11</sup> The \$3,000.00 purchase contract was signed by Mrs. Dahl and the entire amount paid in full to Sunset on December 17, 1994. Mr. Dahl died in December of 1994 and one of the full-size vaults was used in Mr. Dahl's interment at Sunset.

Mrs. Dahl died on August 15, 1997, and was cremated. A Sunset representative told the Dahl family that Mrs. Dahl's previously-purchased, full-size vault had been sunk in the ground prior to her death. The cemetery representative further stated that, since Mrs. Dahl had been cremated, it would be less expensive for the Dahl family to purchase and bury a small cremation vault (with an approximate cost of \$165), than to pay the cemetery the cost of uncovering, opening, and closing the already-buried, full-size vault. The Dahl family then contacted a funeral provider and purchased a cremation vault in which Mrs. Dahl was ultimately interred.

The family's funeral provider later discovered and advised the OSA that no full-size vault was ever sunk at Mrs. Dahl's burial plot by Sunset. Thus, the Dahls had paid Sunset \$1,500 for burial merchandise that was never provided by the cemetery. In addition, the family's funeral provider advised the OSA of concerns that the \$1,500 paid by Mrs. Dahl had never been placed in a preneed trust account as required by Minnesota law.

In investigating the complaint, the OSA first confirmed that Sunset had not sunk a full-size vault at Mrs. Dahl's burial plot. On August 22, 1997, representatives from the OSA, the Minnesota Department of Health, and the Dahl family examined Mrs. Dahl's burial plot. A

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<sup>11</sup> A vault is a receptacle that is sunk in the ground into which the casket is placed at time of burial.

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metal rod was sunk into the burial plot and surrounding ground, confirming that no full-size vault was buried at the site, only the small cremation vault.

Pursuant to Minn. Stat. § 149A.97 (Supp. 1997), the OSA subpoenaed Sunset in August of 1997 and requested that the cemetery provide financial records documenting the receipt, disbursement, and custody of consumer funds held by the cemetery. Financial records specifically relating to the sale of preneed merchandise and the handling of the cemetery's preneed trust account were requested. Following service of the subpoena, the OSA was contacted by a Minneapolis attorney representing Loewen. While certain financial documents responsive to the subpoena were provided in September 1997, Sunset provided no documents detailing deposits, transactions, or withdrawals from any preneed trust account despite repeated requests from the OSA. The OSA also confirmed that Sunset had never, prior to 1997, filed a preneed trust report with the Hennepin County Auditor's Office, as required by Minn. Stat. § 149.13, subd. 2.<sup>12</sup>

The limited financial records provided confirmed that Mrs. Dahl purchased and paid for two vaults at a total price of \$3,000. No portion of the \$3,000 sale was categorized as "trustable" or "%trust" on the sales journal. No other documents provided in response to the subpoena allowed the tracking of the \$3,000 paid by Mrs. Dahl after its deposit into Sunset's bank account.

In correspondence dated November 6, 1997, the OSA requested that Sunset provide all documents relating to the Dahl sales transaction. On November 17, 1997, the Loewen attorney contacted the OSA and verbally advised that Loewen had failed to establish and properly maintain the statutorily-required preneed trust account for Sunset, including the money for Mrs. Dahl. It was the position of Loewen's attorney that the requirement to maintain preneed trust accounts for Sunset's preneed consumers was triggered in 1994, when the cemetery began selling sealable vaults.<sup>13</sup>

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<sup>12</sup> Minnesota Statutes, § 149.13, subd. 2, was repealed in 1997. See 1997 Minn. Laws, ch. 215, § 47. Beginning in 1998, all providers of funeral goods and services, previously required to file statutory preneed trust fund reports with a county auditor, now file the reports with the Minnesota Department of Health. See Minn. Stat. § 149A.97, subd. 7 (Supp. 1997). However, Sunset had not complied with the statutory reporting requirements, as codified at Minn. Stat. § 149.13, subd. 2, prior to 1997.

<sup>13</sup> Sunset's attorney represented that, prior to 1994, all preneed merchandise purchased by consumers was immediately provided and interred by Sunset; thus, according to the attorney, Sunset had no legal requirement to establish or place money in a preneed trust.

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In November 1997, Loewen confirmed its preneed trust statutory violation and provided a 62-page preneed trust “catch-up” report that it had created, showing that the total dollar amount which should have been placed in trust by Sunset since 1994 was \$3,758,220.35. At the time, Loewen advised that no preneed trust documents were available for financial review given that no preneed trust accounts had ever been maintained by Sunset; thus, an audit of the preneed trust funds was not possible. Loewen also indicated its intention to immediately deposit over \$3.7 million of unfunded trust liability in a preneed trust account. This payment was subsequently made by Loewen.

With respect to Mrs. Dahl, Loewen confirmed that the second vault paid for by Mrs. Dahl was never purchased by Sunset or sunk at her burial plot. Thus, Mrs. Dahl paid \$1,500 for merchandise that was never provided and, following her death, Sunset misrepresented to the Dahl family that the vault had been purchased and sunk.

Based on these facts, as confirmed by Loewen’s legal counsel, the OSA found that several Minnesota laws may have been violated by Sunset. The OSA referred this matter to the Office of the Minnesota Attorney General for further review in December 1997. In 1998, the matter of Sunset’s underfunding of preneed trust accounts remained under review by the Minnesota Attorney General’s Office.

In 1999, a second complainant came to the OSA requesting assistance in reviewing another potential preneed trusting violation at Sunset. When investigating the consumer complaint in 1999, the OSA learned that in 1983, a wife and her husband selected on a preneed basis two burial vaults and granite companion memorial markers from Sunset. Money was paid in 1983 to Sunset by the couple for these preneed items. The husband died in March 1988. The wife died in May 1999. As of the date of her death, a burial vault had not been provided (i.e., interred) for the wife.<sup>14</sup>

On May 19, 1999, the OSA requested that Sunset provide an accounting of the wife’s preneed trust fund. All funds paid to Sunset by the wife were required, under Minnesota law, to be placed in trust for the goods and services that the couple had selected and paid, until that obligation was fulfilled. On May 26, 1999, Mr. Dan Nakagawa, Loewen’s Vice President for Regulatory Compliance, contacted the OSA to discuss the investigation. Mr. Nakagawa did not provide any detailed documents relating to the couple’s preneed trust account. Mr. Nakagawa stated that Loewen has been attempting to better understand

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<sup>14</sup> Subsequently, Sunset did provide a vault for the burial.

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Minnesota law since entering the cemetery business in Minnesota.<sup>15</sup> He advised that Loewen was installing an "HMIS computer system" at all its holdings across the nation. According to Loewen's senior corporate counsel, this computer system would allow prior records to be loaded and would provide a basis to determine the total outstanding, unfulfilled preneed account liabilities at Sunset, and other Loewen-owned cemeteries.

The OSA inquired as to any action Loewen had taken to address the preneed trusting violations noted by the OSA in its 1997 investigation of Sunset. Mr. Nakagawa stated this was the first he was aware of those prior problems at Sunset. The OSA was further advised that Loewen currently had approximately \$5.6 million of preneed trust funds on deposit in Minnesota for the benefit of Sunset consumers. Mr. Nakagawa believed that no trust fund withdrawals had been made since 1997 due to the fact that Loewen was aware of deficiencies in its trusting system and did not want to withdraw any trust funds, even after providing goods.

By letter dated May 28, 1999, the OSA advised Loewen of its serious concerns regarding Sunset's handling of preneed monies received prior to 1994 and the status of all funds that should have been placed in trust prior to and since that time. The OSA's letter discussed substantial discrepancies in information received to date from Loewen. The OSA noted that Loewen had represented it was not withdrawing any funds from Sunset's preneed trust account and had not made withdrawals since 1997. However, documents reviewed by the OSA indicated that Loewen had withdrawn over \$845,000 in 1998 for "servicing contracts." In addition, during the 1997 investigation, Loewen's attorney represented that Sunset had not maintained preneed trust accounts prior to 1997 because, prior to that time, all vaults sold were interred prior to need (thereby negating the need to place consumer's money into trust). However, the 1999 complainant's vault was purchased in 1983 and was not interred.

On June 1, 1999, Loewen filed for chapter 11 bankruptcy status in U.S. Bankruptcy Court.<sup>16</sup> The OSA was notified that any claim against Loewen that was or may be pending would not be resolved pending resolution of the bankruptcy petition.

On June 4, 1999, the OSA met with representatives of Loewen. Also present at the meeting were representatives from the Minnesota Department of Health and the Minnesota

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<sup>15</sup> Mr. Nakagawa advised the OSA that Loewen was the fourth owner of Sunset since the couple's money was first taken in 1983. Loewen acquired Sunset from the Osiris Holding Company in 1995; Osiris purchased Sunset from the Gibraltar Company; Gibraltar purchased Sunset from an individual owner.

<sup>16</sup> The bankruptcy proceedings are ongoing at the time of publishing this report.

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Attorney General's Office. At this meeting, Loewen representatives reiterated that Loewen was in the process of reconstructing and converting all trust documents for Sunset and Morningside into a database format. Loewen's representative, Mr. Nakagawa, advised that relevant trust records for both cemeteries had been stored in Philadelphia, but were currently in the process of being moved to Loewen headquarters in Vancouver, British Columbia. He further advised there were approximately 5,500 boxes of trust documents in transit at the time of the June 4, 1999 meeting. At this meeting, it was determined that Loewen would retain independent accountants to review the preneed and PCI trusts at both cemeteries. The OSA would work with Loewen and the independent accountants in reviewing the status of the trust accounts at both Sunset and Morningside. Loewen representatives indicated that Loewen would establish a timeline to follow in completing the record reconstruction, conversion, and audit process.

In a letter dated June 14, 1999, Loewen advised that the conversion of trust documents would take approximately four to six weeks. However, the conversion process was still underway in the spring of 2000; it was not until April 2000 that the OSA received data in a format that allowed OSA staff to begin their examination of the data. As of year-end 2000, Loewen continued to provide "updated" trust data, indicating that its conversion process was still ongoing. As of the date of this report, Loewen has failed to provide the OSA final trust liability reports for the period under review. In addition, the OSA's audit tests established that the preneed consumer database supplied by Loewen did not contain entries for all Sunset preneed consumers.<sup>17</sup> Loewen's inability to provide complete and accurate trust information for Sunset and Morningside both delayed and hindered the OSA's ability to conclude this report.

### **III. FINDINGS OF PRENEED ARRANGEMENT AND TRUST FUND VIOLATIONS**

#### **A. Failure to Adequately Fund Preneed Trust Accounts**

Minnesota's preneed arrangement statutes were established in 1953. Since its enactment, Minnesota law has required the trusting of 100 percent of funds paid by consumers for their selection of funeral and burial goods and services on a preneed basis. The law, in part, reads: "the total of all money paid by the terms of the transaction, contract, or series or combination of transactions or contracts shall be held in trust for the purpose for which it has been paid."<sup>18</sup>

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<sup>17</sup> See Section III.I of this report.

<sup>18</sup> Minn. Stat. § 149A.97, subd. 2 (1998).



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The OSA's review of the Sunset and Morningside preneed trust funds for the period ending December 31, 1999, attempted to reconcile the amounts held in trust and the amount of merchandise and service liability to assure that adequate funds existed in trust to pay at-need (at the time of death) for each of Loewen's customer's preneed selections.

**Loewen Analysis**

Loewen provided the OSA with its own summary analysis of its preneed trust fund assets, and merchandise and services liability in a letter dated February 3, 2000. The fiscal year 1999 balances provided by Loewen appear below in Table 1.<sup>19</sup>

**TABLE 1**  
**Loewen's Summary Analysis**  
**Comparison of Trust Assets to Liability for Unfulfilled Preneed Contracts**

	<u>SUNSET</u>	<u>MORNINGSIDE</u>
Trust Fund Assets (12/31/99)	\$ 6,682,892.61	\$ 4,050,571.72
Merchandise & Services Trust Fund Liability (12/20/99)	\$ 6,348,302.22	\$ 4,167,393.45
Surplus (Shortfall)	\$ 334,590.39	\$ (116,821.73)

In a December 20, 2000, letter to the OSA, Loewen provided additional preneed trust account summary figures for both Sunset and Morningside. Table 2 (below) shows both the book and market values of the trust accounts as summarized by Loewen. These figures are identical to those provided to the Department of Health for purposes of the annual statutory reporting requirements.

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<sup>19</sup> Loewen explained in its August 4, 2000, letter that the trust fund asset values represent partial *market values* per bank trust statements of the principal portion of the funds.

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**TABLE 2**  
**Loewen Trust Assets for Unfulfilled Preeed Contracts**

	<u>SUNSET</u>	<u>MORNINGSIDE</u>
Book Value (12/31/99)	\$ 6,964,984.44	\$ 4,193,275.96
Market Value (12/31/99)	\$ 7,019,120.99	\$ 4,157,068.77

**Loewen Trust Balance Reconciliation**

Loewen has not completed a final reconciliation between its list of preneed consumers and the trust assets identified above to determine the total amount of money that should have been in trust on December 31, 1999. In a May 27, 1999, letter to the OSA, Loewen represented that the Sunset preneed merchandise trust fund was "over funded," but that Loewen was faced with reconstructing preneed merchandise accounts created prior to its acquisition of Sunset. On August 4, 2000, in a letter to the OSA, Loewen acknowledged that the database trust fund liability values were different than the values previously reported by Loewen.<sup>20</sup> Further, interest earnings were never imputed to either the Sunset or Morningside trusts' asset values. (See Finding B below.)

In a letter dated September 11, 2000, the OSA again asked Loewen to reconcile the differences between the liability amounts provided in Loewen's February 3, 2000, summary reports and the liabilities calculated from Loewen's list of preneed consumers. Loewen responded in its December 20, 2000, letter to the OSA that the reconciliation process was ongoing, and that difficulties with the conversion to a new computer system had caused delays. The letter anticipated that the conversion would be completed before February 2001. Subsequent correspondence stated that the completion would be accomplished by the end of July 2001. As of the date of this report, the OSA has not received notification that the conversion is complete; however, Loewen has not provided the OSA with a final reconciliation for the period under review.

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<sup>20</sup> Loewen asserted that the liabilities were overstated, and ascribed the differences to :1) the summary report's exclusion of the portion of contracts that had been serviced by the cemeteries but that had not yet been withdrawn from the pre-acquisition contract accounts; and 2) additional cash receipts received after the summary was prepared but included in the database balances.

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**Underfunded Preneed Trust Accounts**

The baseline values used to compare the trust fund assets against the merchandise and services liabilities are, respectively, those taken from Loewen's February 3, 2000, summary report and the preneed customer data. These values for Sunset and Morningside appear below in Table 3.

**TABLE 3**  
**OSA Summary Analysis**  
**Comparison of Trust Assets to Liability for Unfulfilled Preneed Contracts**

	<u>SUNSET</u>	<u>MORNINGSIDE</u>
Trust Fund Asset Balance (12/31/99) Reported to MDH (FY99) <sup>21</sup>	\$ 6,682,892.61	\$ 4,050,571.72
Merchandise & Services Liability from Loewen's Database	\$ 6,897,184.60 <sup>22</sup>	\$ 4,551,852.64 <sup>23</sup>
Surplus (Shortfall)	(\$ 214,291.99)	(\$ 501,280.92)

Based solely on this data provided by Loewen, the OSA finds that Sunset cemetery's preneed trust fund is under-funded by \$214,291.99 as of December 31, 1999. The OSA further finds that Morningside cemetery's preneed trust fund is under-funded by \$501,280.92 as of December 31, 1999. The OSA recommends that Loewen make the necessary deposits to correct this underfunding.<sup>24</sup>

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<sup>21</sup> Loewen's August 4, 2000, letter to the OSA described these balances as *book values*.

<sup>22</sup> Contracts (5,757) through 12/31/99; payments received through 2/20/00.

<sup>23</sup> Contracts (3,255) through 12/31/99; payments received through 2/23/00.

<sup>24</sup> Loewen recently represented that the trust funds are overfunded based on a reconciliation of trust assets and merchandise liability as of May 31, 2001. The assets and liabilities for the period ending December 31, 1999, the scope of this report, have not been reconciled by Loewen.

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**B. Failure to Deposit Proceeds into Separate Trust Accounts/Failure to Account for and Credit Interest**

A series of communications between the OSA, the Minnesota Department of Health (MDH), and Loewen occurred during the course of this examination regarding Loewen's failure to properly segregate preneed consumer trust funds in accordance with Minnesota law. Initially, in a letter to the OSA dated May 24, 1999, a Loewen senior corporate attorney represented that before the law was amended in 1997, there was no obligation to provide for separate preneed trust funds for new accounts. However, statutes in existence since 1953 direct that trust fund deposits be carried in separate accounts in the name of the depositor as trustee for the individual consumer.<sup>25</sup> This requirement has applied to cemeteries since at least 1967.<sup>26</sup> Loewen further represented that the law did not create an obligation to review all of its existing preneed trust accounts and retroactively fund them into individual accounts because the law was not amended until 1997.<sup>27</sup>

A second letter to the OSA, dated May 27, 1999, from another senior Loewen attorney, acknowledged Loewen would review pre-acquisition accounts (before 1994) and determine the total value of its unfulfilled preneed accounts. This letter further acknowledged that Loewen had already undertaken to contract with a computer software vendor to enter all prior records into an electronic database to determine the total amount of unfulfilled preneed account liability. It was stated that the account reconstruction process would allocate to each individual account a proper amount of interest earnings based on the effective rate for each year's trust fund. From the language of this letter, it was implicit that Loewen understood its obligation to not only segregate its master trust into separate individual accounts, but also to retroactively allocate interest earnings to each account.

Subsequent to this letter, in September 1999, MDH officials met with representatives of Loewen. Established at that meeting were specific account segregation requirements.<sup>28</sup> In its June 20, 2000, correspondence to Loewen, MDH confirmed

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<sup>25</sup> Minn. Stat. § 149.12 (1953).

<sup>26</sup> According to representations made by the Minnesota Attorney General's Office.

<sup>27</sup> There was no indication that Loewen intended to review any of its pre-1997 accounts or take steps to separate them into individual trust funds.

<sup>28</sup> Loewen agreed to: 1) establish all new preneed accounts as separate accounts; 2) segregate June 1 to September 30, 1999, trust funds into separate individual accounts;

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that there had been little progress on the conversion of accounts. Loewen was informed by MDH that failure to comply with the conversion timetable it established would subject Sunset and Morningside to an enforcement action, including monetary penalties of up to \$10,000 for each unsegregated account.

The OSA inquired about the status of the conversion process in letters dated July 25 and September 11, 2000. The OSA acknowledged in September that some conversions had been completed, but noted that none of the preneed trust account data for Sunset or Morningside consumers provided to the OSA showed interest earnings credited to individual consumer accounts. The OSA requested that Loewen explain how it intended to credit consumer accounts with interest earnings and how the interest amounts would be determined, as it continued its process of converting the master trust to individual accounts. Also requested was up-to-date consumer account information that reflected the addition of interest, including the total amount of interest credited since the conversion process began.

Loewen's response, dated December 20, 2000, merely stated that the conversion process was ongoing. Reconciling the differences between trust fund liability amounts in its old versus its new, converted database were not materializing as it had hoped. Loewen acknowledged that the allocation of earnings income to individual accounts was delayed due to the slow pace of the database conversions.

Loewen further stated that its plan was to apply historic rates of return to the individualized accounts in order to calculate and credit the appropriate interest earnings to each account. The calculation of interest rates would be derived from the income shown on actual bank trust statements in addition to published indices that closely corresponded to the investment asset mix. It was Loewen's intent to obtain interest rates reaching back as far as the earliest date of any active, unfulfilled preneed contract. Once the interest rates were determined, Loewen made assurances that the new computer system would calculate the appropriate retroactive interest amount based on the contract date and payment history, and then allocate a credit payment to the individual accounts.

As a result of the above, the OSA determined that, contrary to statutory requirements, Loewen had not established individual consumer trust accounts at either Sunset or Morningside. Upon first inspection, the OSA found that Sunset had not established any consumer trust account. As described above, this finding was forwarded to the Office of the Attorney General in 1997. A subsequent inspection

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and 3) segregate all existing preneed funds (e.g., those created prior to June 1, 1999) into separate individual accounts.

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found a single, master preneed trust at Sunset and Morningside that commingled the deposits of all its preneed consumers. Minnesota law provides that preneed funds received from consumers must be placed in individual trust accounts.<sup>29</sup> The law reads, “[t]he money [required to be held in trust] must be carried in a separate account with the name of the depositor and the purchaser as trustees for the beneficiary.”

As a corollary to its failure to segregate consumer accounts, the OSA also found that Loewen failed to credit consumer accounts with the earnings income from the account’s principal balance. Minnesota law provides that the consumer is entitled to any interest earned on a preneed trust account.<sup>30</sup> The law reads, “[t]he funds held in trust, including principal and accrued interest, may be distributed prior to the death of the beneficiary upon demand by the purchaser to the extent that the trust is designated revocable. . . . the funds, including principal and accrued interest, may be distributed by either the depositor as trustee or the purchaser as trustee. . . .” Further, because there has been no application of interest income to the individual accounts, all the accounts have been denied the compounded earnings that they would have received on their appropriate historical balances.

As it has already acknowledged, Loewen must complete the process of segregating its master trust into individual consumer accounts. Loewen must also compute and allocate the appropriate amount of accrued earnings income to each of its active, unfulfilled preneed trust accounts. The crediting of interest must consider the historical earnings that would have been earned if the accounts had been properly segregated and accruing investment earnings throughout their existence.

The Minnesota Department of Health (MDH) has been, and is continuing to, monitor Loewen’s efforts to both segregate consumer accounts and credit them with the appropriate interest earnings. The MDH initially notified the OSA about Loewen’s failure to segregate consumer accounts at both Sunset and Morningside in a letter dated June 16, 1999. On June 27, 2000, Loewen agreed to a timetable under which all new and existing preneed accounts would be segregated. As of the date of this report, the OSA has not been notified that Loewen has completed its segregation process. Further, even as its segregation efforts reach conclusion, no assurances have been made that consumer accounts have been credited with the correct

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<sup>29</sup> Minn. Stat. § 149A.97, subd. 5 (1998).

<sup>30</sup> Minn. Stat. § 149A.97, subd. 6 (1998).

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interest earnings. It is important that MDH closely examine Loewen's progress to ensure that the lawful interest amounts are applied.

Absent historical data regarding individual consumer trust fund balances and the applicable interest rates, the OSA is unable to independently determine the financial magnitude of Sunset's and Morningside's failure to properly attribute interest earnings to individual consumer trust accounts.

This failure impacts over three decades of consumer trust accounts that still exist and have cumulative balances totaling millions of dollars and also those consumer trust accounts that have closed due to death. In short, it is reasonable to assume that Sunset's and Morningside's liability for uncredited interest may ultimately exceed several million dollars.

**C. Failure to Notify Consumers of Trust Account Information**

Minnesota law requires that specific information about a consumer's trust fund account be disclosed. All consumers of preneed trust agreements must be properly informed about the financial institution holding their trust fund payments. The disclosure provision states:

The location of the trust account, including the name and address of the institution in which the money is being held and any identifying account numbers, must be disclosed in writing to the beneficiary by the depositor as trustee at the time the money is deposited and when there are any subsequent changes to the location of the trust account.

Minn. Stat. §149A.97, subd. 5 (1998).

The OSA created a computer-generated random sample of consumers having active, unfulfilled preneed agreements using the consumer data files provided by Loewen. The OSA used the computer sample to select for examination specific preneed consumer files that were maintained on-site at both Sunset and Morningside. Documents found in these files included copies of original trust agreements, agreements for automatic bank withdrawal arrangements, memorial and marker installation purchase and work orders, sales data input and commission worksheets, certificates of delivery, and installment payment coupon book order forms. In addition to the cemetery's internal bookkeeping and account processing documents, these on-site files also appeared to include original or copied versions of all documents provided to the consumer with respect to his or her preneed trust agreement.

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It was evident from the OSA's review of the on-site preneed agreement files that Sunset and Morningside failed to comply with the above law in several respects. First, there was no separate document or other contract information provided to the consumer, which pertained to the establishment or existence of a preneed trust account. Using Sunset's form contracts as an example, there is no reference to a preneed trust in the document. Further, there is no itemization or listing in the contract document that indicates for the consumer whether payments for items or services are trusted. None of the preneed contracts reviewed itemize or indicate in any other manner the portion of consumer funds allocated to either the preneed merchandise trust fund or perpetual care trust fund. The OSA found that, as a consequence, Sunset's preneed consumers were not informed about what portion of their payments were trusted, whether their payments were allocated to a trust fund, or even the existence of a trust fund account.

The OSA also received a number of inquiries from individual preneed consumers requesting assistance in acquiring information about their preneed payments. These consumers were alike in that they each were unable to receive from Sunset preneed trust fund account information, such as a record of their payment history, trust fund balances, interest or earnings accruals, account numbers, and financial institution information about where their payments were deposited.

The OSA found that Sunset and Morningside failed to properly inform preneed consumers about the existence and location of their trust account(s) in violation of the law. In addition, the cemeteries did not take steps to provide the name, address, and identifying account numbers for the financial institution in which the consumer's trust deposits were held as required by law.

Loewen must immediately communicate to each of its preneed consumers the trust account financial institution information required by law and information about the balance and earnings deposited for each account. While the OSA understands that Loewen may not have finished segregating the master trusts into individual consumer trust accounts, completing that process should not impair its ability to notify active preneed consumers regarding information that by law should have already been provided.

**D. Failure to Properly Disburse Trust Funds**

Upon demand, preneed funds paid to funeral or burial providers by consumers and held in a revocable trust must be refunded. Minnesota law provides that prior to a beneficiary's death, consumers are entitled to a full refund of funds held in trust



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including any earnings, to the extent that the trust is designated revocable.<sup>31</sup> This right to a refund applies to any revocable preneed trust arrangement. The law states that “[t]he funds held in trust, including principal and accrued interest, may be distributed prior to the death of the beneficiary upon demand by the purchaser. . . .”<sup>32</sup>

The law further provides for the disbursement of preneed trust funds upon death. This provision reads as follows:

At the death of the beneficiary . . . the funds, including principal and accrued interest, may be distributed by either the depositor as trustee or the purchaser as trustee . . . . The funds shall be distributed in their entirety, with no fees to be retained by the trustees as administrative fees. The funds shall be distributed for the payment of the actual at-need value of the funeral goods and/or services selected with any excess funds distributed to the estate of the decedent.

Minn. Stat. 149A.97, subd. 6 (1998).

The OSA found that certain Sunset and Morningside consumers did not have their preneed funds disbursed in a manner consistent with state law. Further, the OSA found that individual consumers who had made requests for the cancellation of their revocable preneed trust agreements experienced delays and obstacles to the refunding of their deposits. The OSA recommends that Loewen disburse trust funds in compliance with Minnesota law in the future.

**E. Failure to Properly File Reports with Commissioner of Health**

Sellers of preneed arrangements in Minnesota must annually report their establishment’s consumer preneed trust transactions to the Minnesota Department of Health (MDH). The law states that, “[e]very funeral provider . . . that accepts [preneed trust] funds . . . must make a complete annual report to the [health department] commissioner.”<sup>33</sup> The law further requires that such reports contain the

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<sup>31</sup> Minn. Stat. § 149A.97, subd. 6 (1998).

<sup>32</sup> Minn. Stat. § 149A.97, subd. 6 (1998).

<sup>33</sup> Minn. Stat. § 149A.97, subd. 7 (1998). This reporting requirement produces preneed trust account data used by the MDH to annually review an establishment’s trust fund receipts including sales deposits, earned interest and other gains, and account disbursements for

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“identification and the state of each trust account, including all transactions involving principal and accrued interest, and must be filed by March 31 of the calendar year following the reporting year....”<sup>34</sup>

In a letter to the OSA dated June 16, 1999, the MDH stated that the annual preneed trust reports submitted by Sunset and Morningside for 1998 did not comply with statutory trust reporting requirements. The reports require trust fund account numbers and locations, individual beneficiary names, contract dates, itemized prices, beginning and end of year balances, total deposits, interest earnings, and withdrawals. The MDH also stated that the absence of detailed beneficiary information suggested the improper commingling of preneed trust fund assets between consumers. (The OSA found that both cemeteries improperly commingled trust fund assets between customer accounts. This violation is discussed in Finding B above.)

The OSA found that Sunset and Morningside failed to properly submit annual preneed trust fund reports in compliance with the statutory requirements. Both cemeteries failed to provide in their reports the required detailed trust information regarding individual customer accounts. Sunset failed to file the required reports every year prior to 1997. Also, on two occasions, Sunset failed to submit its report in a timely manner. The report for 1997 was submitted to the MDH in December 1998, over eight months late; the 1998 report was submitted over seven months late. The OSA recommends that Loewen timely file these reports in the future.

**F. Failure to Create and Maintain Preneed Consumer Records**

In Minnesota it is required by law that sellers of preneed arrangements create and maintain a detailed trust fund record of its preneed consumer transactions. The law reads, “[e]very funeral provider . . . that accepts funds [for preneed agreements] must create and maintain on its premises or other business location in Minnesota an accurate record of every trust fund . . .” Minn. Stat. § 149A.97, subd. 9 (1998). At a minimum, the record must contain these items:

- # Names of the purchaser, beneficiary, and depositor;
- # Date, location, identifying account numbers, and amount of funds deposited;
- # Subsequent changes to the location of the account, account number, or trustee;

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at-need purchase expenditures, refunds, and tax and fee expenses.

<sup>34</sup> *Id.*

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- # Date, amount, and payee of any distributions from the account; and
- # All supporting documentation, including a copy of the original trust agreement, and copies of any contracts for the purchase of preneed goods and services.

There is also a requirement in law that provides for the retention of preneed consumer trust fund records. The law requires that the records described above be maintained for three years following the release of trust funds. For at least seven years thereafter, the seller must either keep the records in storage or reduce them to an alternative storage medium (e.g., microfilm, CD).

Upon the commencement of the OSA's examination of Sunset and Morningside's preneed trust accounts, the OSA requested that Loewen provide copies of or access to all of its unfulfilled preneed customer account records. In addition, on May 21, 1999, the OSA requested preneed trust information with respect to a specific consumer whose 1983 payments for merchandise selections should have been placed in trust. The beneficiary died in May 1999 and Sunset was unable to provide the OSA with the appropriate trust records.

The OSA found that Loewen violated statutory record-keeping requirements with respect to Sunset and Morningside's preneed consumer trust fund accounts. At the time the OSA originally asked for the complete consumer account records, Loewen did not have them or otherwise make them available. The records sought did not exist on the premises of either cemetery or in any other Minnesota location. The production of the required records took over one year and delayed the progress of this examination. Over time, and with assistance from the OSA, the requested records were assembled and delivered. The OSA received the records in both electronic and paper formats. The records of the specific individual consumer whose case initiated the OSA's examination of Loewen were not located. To date, Loewen's ongoing record conversion efforts are still not complete and the OSA has yet to receive a complete and accurate record of all Sunset and Morningside preneed consumer trust fund accounts. The OSA recommends that Loewen take all necessary steps to ensure its preneed consumer records comply with Minnesota law.

**G. Failure to Provide Preneed Price Information**

Minnesota's preneed sales consumer protection law establishes clear disclosure requirements. The law states that,

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[i]n selling or offering to sell funeral goods or funeral services to the public, it is an unfair or deceptive act or practice for a funeral provider to fail to furnish accurate price information disclosing the cost to the purchaser for each of the specific funeral goods and funeral services used in connection with the disposition of dead human bodies to persons inquiring about the purchase of funerals.

Minn. Stat. § 149A.71, subd. 1 (1998).

The price disclosure law also specifically governs telephone inquiries. It reads,

Funeral providers must tell persons who ask by telephone about the funeral provider's offerings or prices any accurate information from the price lists . . . and any other readily available information that reasonably answers the questions asked.

Minn. Stat. § 149A.71, subd. 2(b) (1998).

As part of this compliance review, OSA staff made telephone inquiries to Sunset about its preneed merchandise and services offerings. When specifically requested by OSA staff, information about the prices of Sunset's burial merchandise was not provided. A failure to disclose pricing information upon request is a violation of Minnesota law.

The OSA recommends that Loewen familiarize its sales staff with Minnesota's disclosure laws applicable to preneed merchandise and services sales and make sure staff complies with these laws in the future.

## **H. Interest Charges on Preneed Agreement Selections**

The OSA found numerous instances of interest or finance charges on preneed merchandise selections. Most of the preneed contracts with interest charges were prepared by Morningside. Consumers were charged interest on their selections of preneed merchandise during the time they were making installment payments on their agreement. The interest charged to consumers was applied to the unpaid balance of the consumer's preneed merchandise selections.

The practice of charging interest on preneed merchandise is substantially different than on ordinary retail purchases. Retail purchases using ordinary credit terms usually allow the consumer to acquire the goods or utilize the services immediately.

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By contrast, in a preneed arrangement, there is no immediate possession of a consumer's funeral or burial selections; rather, the consumer merely identifies goods or services to be delivered later at the time of need. When there is no immediate possession of the good or utilization of the service, there is no rationale that supports the application of installment interest or finance charges. It is inappropriate that consumers were required to pay interest charges on undelivered merchandise or services.

It should be noted that the Minnesota Legislature recently banned the practice of applying interest or finance charges to preneed arrangements for funeral and cemetery goods and services.<sup>35</sup> The prohibition became effective on August 1, 2000.

The OSA recommends that Morningside and Sunset endeavor to identify their customers who have unfulfilled preneed agreements on which installment payments are currently being made and that assess interest fees or charges. All payments of interest should cease immediately and such consumers should be refunded their interest payments retroactive to at least August 1, 2000.

**I. Audit Tests**

The OSA performed four audit tests of the preneed consumer information for Sunset and Morningside supplied by Loewen in the form of a database to the OSA. Two of the tests were conducted to determine the completeness of the preneed consumer information. The other two tests were done to determine the accuracy of the consumer information supplied by Loewen.

**1. Completeness.**

The purpose of the two completeness tests was to determine whether the population of the Loewen preneed customer database supplied to the OSA was complete. The OSA checked completeness of the consumer database in two ways: (1) by randomly selecting callers to the OSA's consumer hotline and matching their information against the database information; and (2) by randomly selecting customer preneed agreement files from on-site visits to each cemetery and comparing them against the database information.

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<sup>35</sup> 2000 Minn. Laws ch. 438, § 34.

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**i. Sample of Telephone Hotline Calls.**

In 1999, the OSA established a telephone “hotline” to receive calls from persons with questions about funeral and cemetery practices in Minnesota. Many of the calls received from Minnesotans using this hotline concerned Sunset and Morningside cemeteries. The calls were recorded using a uniform data intake sheet. From a sample of 200 uniform data intake sheets, the OSA determined that 75 of these data intake sheets indicated the existence of preneed agreements at Sunset and 10 indicated the existence of preneed agreements at Morningside. The OSA then compared these 85 records to the preneed consumer database supplied by Loewen.

Of the 10 persons identified by the OSA for Morningside, all 10 were located on Loewen’s database. Therefore, based upon this sample comparison, the population of the preneed database appears complete for Morningside.

Of the 75 individuals identified by the OSA for Sunset, only 62 were located on the Loewen database. Therefore, the OSA was unable to determine that the population of the database for Sunset was complete.

**ii. Random Customer Check.**

In an effort to further determine whether the consumer database provided by Loewen to the OSA was complete, the OSA randomly selected customer preneed agreement files from each cemetery’s active preneed accounts during on-site visits to both Sunset and Morningside. Thirty customer files selected at Morningside and 40 files selected at Sunset were later compared to the Loewen consumer database to verify whether that database was complete.<sup>36</sup>

Of the 30 preneed customer files selected at Morningside, 29 were located on the Morningside preneed database. Therefore, based on this sample comparison, the population of the preneed consumer database for Morningside appears to be complete.

Of the 40 preneed customer files selected at Sunset, only 17 were located on Loewen’s preneed consumer database; 23 agreements from the sample could not be found on the database. Loewen subsequently represented that the 23 files in question were in fact inactive or without trust liability. The OSA verified that only 16 of those 23 files were inactive or without trust liability, leaving seven files

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<sup>36</sup> This search did not fully examine individual customer preneed arrangement files for discrepancies, inconsistencies, or erroneous information.

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unaccounted for on the preneed consumer database. Based on this information, the OSA is unable to determine that the preneed consumer database for Sunset is complete.

**2. Accuracy.**

In addition to completeness, the OSA performed two tests to determine the accuracy of the consumer database. The OSA checked accuracy in two ways: (1) by randomly selecting 75 preneed customers for Morningside and Sunset identified in the database and sending letters requesting verification of their preneed consumer information; and (2) randomly selecting unfulfilled contracts from the database and comparing them to the on-site files.

**i. Letter Sample Finding.**

Using a computer-generated random list, the OSA drew a sample of 75 customers for Sunset and 74 customers for Morningside from the preneed consumer database provided by Loewen. The OSA sent an initial letter to the 149 customers whose contracts were randomly selected. The letter listed all merchandise and services selected by the customer as the information appeared on the Loewen consumer's database. The letter asked the customer to verify whether the identified item(s) and price(s) correctly correspond to the item(s) selected at the time the preneed agreement was executed. Based upon customer verification responses received, customers generally agreed that items listed on the database appear to be accurate in description and price to those selected. However, it was interesting to note that some customers reported a real or perceived discrepancy or inconsistency between Loewen's database descriptions and the actual selections. For example, an agreement line item on the database marked as a "memorialization" selection shows a single price, but may include a bronze marker, granite slab, and urn.

During this review, other significant items noted by the OSA were as follows:

**# Customer addresses**

Mailing addresses provided to the OSA by Loewen for Sunset and Morningside preneed customers in many cases were not accurate. Twenty-five percent of the customers randomly selected for Sunset and 11% of the customers randomly selected for Morningside could not be reached using the contact information provided by Loewen.

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# Disputed amounts

In one case, the database itemization shows a price of \$1,110 and the consumer's price information stated \$1,600. In another case, the itemization shows \$905 and the consumer's price information stated \$1,230. In a third case, the itemization shows \$3,705 and the consumer stated the price was \$5,040. These cases show both that the consumer is paying an amount greater than the amount being trusted and that the consumer is not always aware that their entire payment does not go into trust. The OSA was unable to determine the purpose or nature of these discrepancies.

# Administrative fees

The consumer agreement did not always separately itemize a charge identified as "administrative fee" (usually \$75). However, the fee frequently appeared as a line on the database itemization. The purpose of the administrative fee was not apparent. More importantly, it appears that the consumer was not aware that: (1) an administrative fee was being charged for their preneed selection; and (2) that the proceeds deposited into their trust account for the payment of their selections was reduced by the amount of the fee.

**ii. Audit Sample Finding.**

The second test for accuracy performed by the OSA involved randomly selecting Morningside and Sunset unfulfilled preneed customer agreement data from Loewen's database to confirm that the same information appeared in the on-site paper files. An attempt was made to physically locate each of the sample customer files at the cemeteries.

A random sample of 61 preneed contracts was drawn from Loewen's database for Morningside. A random sample of 60 preneed contracts was drawn from Loewen's database for Sunset. An attempt was made to physically locate each of these sample customer files on site. Pursuant to Minnesota law, contracts for the purchase of preneed goods and services must be maintained on the sales premises or at another business location in Minnesota.

For Morningside, comparing the sample population selected from the database to the agreements found on site resulted in no significant discrepancies. For Sunset, the contract information for 20 of the 60 sample contracts selected from the database was found to be incomplete or missing during the on-site review. However, subsequent to the site visit, Loewen located and provided the OSA with



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preneed customer agreements for 19 of the 20 files not found during the on-site review. Ultimately, the comparison of the sample population selected from the database to the agreements found on site or provided by Loewen resulted in no significant discrepancies. The OSA notes its concern at the difficulty Sunset personnel experienced in locating a significant number of consumer files when a request for information was made.

During this specific test, other significant issues to note were as follows:

# Interest charges

Many of the preneed arrangements reviewed included installment interest or finance charges ranging from 4.75% to 12.5%. Because consumer payments are for "preneed" items, and there is no delivery of goods or services, there is no rationale supporting the application of installment interest or finance charges.<sup>37</sup>

# "PN Endow/Special Care"

Several of the consumer preneed files included in the database include an itemization for "PN ENDOW/SPECIAL CARE," with dollar amounts ranging from \$28.80 to \$144. The OSA could find no explanation in the agreements for these endowment or care fund charges. Although Minnesota law provides for a minimum permanent care fund deposit of 20% of the sale proceeds, there appears to be no authority for charging or collecting permanent care funds from the sale of preneed merchandise.

# Administrative fees

Several of the consumer database entries and preneed agreements included allocations of consumer funds for a purpose captioned as "ADMIN FEES." In each instance, the allocation is for \$75 and is included in the total amount charged the customer for a particular selection. For example, the purchase of a grave marker for \$1,090 may include the \$75 fee such that the amount actually allocated to the marker is \$1,015. In database entries and agreements where the "ADMIN FEE" is found, the funds received are not placed in the preneed merchandise trust fund.

It is unclear from the consumer agreements the purpose of the \$75 administrative fee. Absent a substantiating and legal purpose for such a charge, the administrative

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<sup>37</sup> Such charges are now explicitly prohibited by Minnesota law. See Minn. Stat. § 149A.97, subd. 4a (Supp. 2000).

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fee may constitute a violation of Minnesota law. Because Minnesota is a 100% trusting state, the receipt of all proceeds from a consumer must be deposited in a financial institution and upon disbursement, all funds, with no fees retained by the trustee as administrative fees, are distributed in their entirety.<sup>38</sup> Therefore, this administrative fee appears to violate the statute's intent, given that the fee appears to be a hidden charge paid by preneed consumers and ultimately retained by the cemetery.

The OSA recommends that the above charges be discontinued.

#### **IV. PERMANENT CARE AND IMPROVEMENT TRUST FUNDS**

##### **A. Introduction**

Permanent care and improvement (PCI) trust fund accounts are created to ensure that cemeteries are preserved and maintained in perpetuity. The entire principal portion of a PCI fund is preserved and in most cases must remain intact. Earnings income from a PCI fund may be only used for certain cemetery-related expenses.

Cemeteries are generally permitted by law to create a PCI fund. However, Minnesota law mandates that some cemeteries must establish PCI funds. All public cemeteries in or adjacent to a city with a population of over 50,000, must establish a PCI fund.<sup>39</sup> Minnesota law prescribes the amount and timing of deposits to the PCI fund: twenty percent of lot sale proceeds and ten percent of mausoleum burial space proceeds must be deposited into the PCI fund on a quarterly basis.<sup>40</sup> Net income from the PCI fund, which the trustee or board must provide to the cemetery at least semiannually, may only be used for the care, maintenance, and improvement of the cemetery and any of the roads leading to it.<sup>41</sup>

Minnesota laws enacted in 1971 required most cemeteries larger than ten acres to establish a PCI fund and file annual status reports on fund activity with the

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<sup>38</sup> Minn. Stat. § 149A.97, subd. 6.

<sup>39</sup> See Minn. Stat. § 306.76 (1998). These cemeteries are required to appoint a trust company or board to act as trustee of the PCI fund. See Minn. Stat. § 306.77 (1998).

<sup>40</sup> Minn. Stat. § 306.78 (1998).

<sup>41</sup> Minn. Stat. § 306.79 (1998).

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Department of Commerce.<sup>42</sup> In 1981, the law was amended to require that the annual reports be filed with the county auditor of the county in which the cemetery is located.<sup>43</sup> In 1998, the legislature made the OSA responsible for preparing the reporting forms on which cemeteries are required to report deposits and withdrawals of principal amounts and all receipts and disbursements.<sup>44</sup>

Also relevant to this examination are other laws governing reporting requirements for cemeteries and providing for the oversight role of county auditors and the State Auditor. Minnesota Statutes § 306.93, requires that cemeteries larger than 10 acres annually submit to the county auditor either an independently audited financial statement or certified letter prepared by a certified public accountant. The audit report or certified letter must review whether the amount in the PCI fund complies with the statutory PCI fund requirements applicable to the cemetery. Pursuant to Minn. Stat. § 306.95, county auditors must review the reports and notify the OSA of any statutory violations as well as file an annual letter disclosing whether or not any indications of statutory violations were detected upon review of the cemetery reports. Further, the law provides that the OSA must independently determine whether a statutory violation has occurred after such notification from the county auditor or upon reliable written inquiry by any person.<sup>45</sup>

**B. Background**

Minnesota Statutes § 306.761, requires that cemeteries larger than ten acres establish a PCI fund. Sunset and Morningside each exceed 10 acres in size. Cemeteries within or adjacent to cities with a population over 50,000 must establish a PCI fund.<sup>46</sup> Sunset is located within a city of over 50,000. Accordingly, both cemeteries are required to create and maintain PCI funds in compliance with Minnesota Statutes, chapter 306.

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<sup>42</sup> 1971 Minn. Laws ch. 894, § 1, see Minn. Stat. § 306.761 (1971).

<sup>43</sup> 1981 Minn. Laws ch. 139, § 1, see Minn. Stat. § 306.761 (Supp. 1981).

<sup>44</sup> 1988 Minn. Laws ch. 509, § 6, see Minn. Stat. § 306.761 (1988).

<sup>45</sup> Minn. Stat. § 306.97 (1998).

<sup>46</sup> Minn. Stat. § 306.76 (1998).

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The OSA obtained annual PCI fund reports submitted to Hennepin and Anoka counties for Sunset and Morningside, respectively. Sunset's reports covered the years from 1992 to 1999. Morningside's reports were for years 1996 to 1999. The OSA also received reports from Loewen's independent accountant. Using these Loewen reports, the OSA reviewed each cemetery's PCI fund activity and determined the following violations of law.

**C. Findings**

**1. Failure to File Certified Letters**

All cemeteries in Minnesota required to establish a PCI fund under Minn. Stat. § 306.761 are also required to annually file either an independently audited financial statement or a certified letter prepared by a certified public accountant, which reviews the PCI fund of the cemetery.<sup>47</sup> The letter or audited financial statement must review whether the amounts in the entity's PCI fund comply with the requirements of Minn. Stat. ch. 306. The independently audited financial statement or certified letter must be filed with the county auditor of the county in which the cemetery is located by March 31 if the cemetery operates on a calendar year basis and by 90 days after the end of the fiscal year if it operates on a fiscal year basis.<sup>48</sup>

According to records maintained by Hennepin County, prior to January 2001, Sunset's last timely filing of either a certified letter or independently audited financial statement with the county auditor was on December 27, 1990, for the fiscal year ending September 30, 1990. The OSA received a cumulative compliance report on February 18, 2000, dated January 30, 2000, which was prepared for Sunset by its independent accountant for fiscal years 1995 through 1998, and the nine months ending on September 30, 1999. The OSA received a second cumulative compliance report from Loewen on August 21, 2000, dated April 25, 2000, which was prepared for Sunset by its independent accountant for fiscal years 1991 through 1994. An audit report for the complete year ending December 31, 1999, was filed with the Hennepin County auditor on January 17, 2001.

The OSA found that Sunset failed to timely file the required annual certified letter or financial statement with the county auditor for each of the ten years from 1991 to 2000. Although the content of the two cumulative compliance reports prepared on Sunset's behalf by an independent accountant and sent to the OSA appears to

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<sup>47</sup> Minn. Stat. § 306.93 (1998).

<sup>48</sup> *Id.*

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satisfy the statutory requirement for review of its PCI fund, the delivery of the reports was not timely.<sup>49</sup> These reports each covered a period of approximately four years. Full compliance with Minnesota law requires that a financial statement or certified letter be filed annually and no later than March 31 with the Hennepin County auditor.

The OSA recommends that audited financial statements or certified letters that comply with Minn. Stat. § 306.93 be filed with the Hennepin County auditor.<sup>50</sup> Reports for years 2001 and after must be filed on an annual basis, no later than March 31, with the county auditor.

**2. Failure to Provide Notice of Trustee Change**

Sunset's 1995 PCI fund report to Hennepin County identified a \$42,265.93 principal withdrawal. The reason given by Loewen for the withdrawal was the complete transfer of PCI fund assets from North Shore Bank to Firststar Bank. Pursuant to Minn. Stat. § 306.761, subd. 4, a notice of a trustee change must be filed with the county auditor within 30 days after the change. In addition, pursuant to Minn. Stat. § 306.761, subd. 4, any change in the identifying account numbers or location of the fund must be reported to the county auditor within seven days of the change. Because the asset transfer to Firststar Bank constituted a change of the PCI fund trustee, Sunset was required to notify the Hennepin County auditor. Sunset failed to notify the county auditor about its change of PCI fund trustee pursuant to the requirements of Minn. Stat. § 306.761.

The OSA recommends that Loewen notify the Hennepin County auditor and provide the office with the required trustee information; it should also take the necessary steps to make timely notifications in the future.

**3. Improper 1999 PCI Fund Withdrawal**

Sunset's 1999 PCI report to Hennepin County showed a total withdrawal of earnings of \$581,822.55. The report noted that the withdrawal was comprised of \$7,881.69 in trustee fees and an "earnings distribution" of \$573,940.86. Total reported earnings for the 1999 period were \$80,798.60. In response to the OSA's inquiry

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<sup>49</sup> It should be noted that the OSA received these reports directly from Loewen. Loewen subsequently filed the reports of its independent accountant with the Hennepin County auditor on January 17, 2001, for each of the years from 1991 to 1999.

<sup>50</sup> A report for the 15 months ending December 31, 2000, dated June 19, 2001, was filed with Hennepin County on April 2, 2001.

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about the amount and purpose for the “earnings distribution,” Loewen stated that, “[o]ther than minor amounts, earnings were not distributed for the years 1992 to 1997 from the PCI fund.”

On May 10, 1999, Loewen instructed Firststar Bank to distribute all previously undistributed earnings income from the Sunset PCI account. These funds represented cumulative earnings income that the cemetery received but did not withdraw for the period from 1992 to 1998. Loewen’s instruction to the trustee stated that the purpose of the cumulative income distribution was to “reimburse the company for the money already expended for care and maintenance of the cemetery.” The independent accountant’s report for the years 1995 to 1999 confirmed Loewen’s rationale by stating that “[t]he cost of maintaining the cemetery was greater than the income distributions and the distributable net income annually and cumulatively for the period of examination.” However, the independent accountant’s report for the 1991-1994 period stated that “[c]emetery care and maintenance expenses related to each year’s income distributions were not available because during this period, Sunset was owned by someone other than the Loewen Group, Inc.”

It is evident that, through its combined 1998 and 1999 cumulative earnings distributions, Loewen sought to recoup the cost of Sunset’s cemetery expenditures made between 1992 and 1998 from previously undistributed PCI fund earnings income. The OSA finds that Sunset had no statutory basis for these prior-year earnings withdrawals from its PCI fund. According to Minn. Stat. § 306.79, a PCI fund trustee is obligated to provide to the cemetery at least semi-annually the entire net income of the PCI fund. Further, withdrawals or distributions of PCI fund earnings that occur in a particular year may only be spent on legitimate cemetery expenses incurred during that year. All distributed earnings income not expended for care, maintenance, and improvement after one year are required by law to be returned to the trustee and invested as part of the PCI fund principal. Earnings income not withdrawn to support current year expenditures may not be aggregated and subsequently withdrawn in a later year. Failure to make timely distributions of earnings income does not permit the cemetery to later instruct its trustee to make a “catch-up” cumulative earnings distribution. Therefore, Loewen may not withdraw accumulated but undistributed earnings income from its PCI fund to reimburse the company for Sunset cemetery costs already expended for any of its prior year cemetery care and maintenance expenses.

The OSA finds that Loewen must return to Sunset’s PCI fund principal balance all withdrawn funds, from either principal or earnings balances, used to support non-

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current year cemetery expenditures.<sup>51</sup> For the years 1991 to 1998, a minimum of \$493,142.26 (581,822.55 - [7,881.69 + 80,798.60]) of aggregated undistributed prior year income must be returned to the PCI fund. For 1999, any earnings not distributed to support statutory cemetery care and maintenance expenditures must be returned to the PCI fund.

With respect to future earnings withdrawals by Sunset, Loewen should develop internal controls to assure that withdrawals are made for purposes compliant with the statute. The OSA recommends that in its forthcoming PCI fund reports to Hennepin County, Loewen provide the county with an itemized list of its cemetery expenditures, including the amount of the expenditure and the purpose for which it was made.

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<sup>51</sup> Two observations must be made about Loewen's income distribution analysis. First, Loewen purports that its PCI fund trustee bank (Firststar Trust Co.) failed to make semiannual earnings distributions to Sunset as required by Minn. Stat. § 306.79. The result is that earnings income was not spent on cemetery care and improvements and the income reverted to the PCI fund principal balance. The fact that the cemetery did not receive PCI fund earnings income because it was never distributed is a management oversight. Notwithstanding its trust agreement with Firststar, Loewen should have withdrawn these funds on a timely basis. Loewen's repeated failure to assure that timely distributions of earnings income were facilitated by its trustee bank does not now entitle Loewen to reconstruct its accounts to calculate cumulative undistributed earnings and remove the funds from the PCI fund principal balance in a manner contrary to Minnesota law.

Second, Loewen rationalized its 1991 to 1994 prior year income distribution to reimburse itself for expenditures made by Sunset's previous owner. The OSA requested annual cemetery expenditure information, including the period between 1991 and 1994, to determine whether aggregate undistributed prior year earnings income was distributed in compliance with the statutory limitations. Loewen and its independent accountant represented that "during this period, Sunset was owned by someone other than The Loewen Group, Inc." By its admission, Loewen has no means by which to verify the amount or purpose of these expenditures. Because these funds were not timely withdrawn for cemetery expenditures, by law they reverted to the PCI principal balance. Now, several years later, Loewen and the independent accountant attempt to justify the withdrawal of these funds. There is no verifiable basis on which to support the taking of Sunset's prior year undistributed trust fund principal balance (recharacterized by Loewen as an earnings withdrawal) to reimburse Loewen for unknown and unquantified expenditures made by its predecessor owner.

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#### **4. Trustee Fees in Excess of Statutory Limits**

Minnesota state law establishes a maximum amount of compensation a financial institution may receive to serve as a cemetery PCI fund trustee. Trustee fee payments are limited to no more than five percent of the PCI fund's trust earnings.<sup>52</sup>

To determine whether Sunset and Morningside complied with the statutory trustee fee limit, the OSA reviewed the annual PCI fund reports filed with Hennepin and Anoka counties. Loewen annually reports earnings income to the counties on a calendar year basis. All earnings attributable to PCI fund investments are credited to the PCI fund balance immediately upon receipt and reported as income for that year. Trustee fees are reported to the counties as earnings withdrawals, or as part of a withdrawal amount for distribution of income and expenses. However, according to Loewen correspondence, trustee fees are not recognized as expenditures and included in reports to the county until they are paid. Therefore, the total trustee fees attributable to earnings income for a particular calendar year do not necessarily appear in that year's report. Loewen identified that there is a lag of a fiscal quarter or more between the time when earnings are attributable to the PCI trust and trustee fees are actually paid and appear on the report. Because of this timing discrepancy, the OSA could not determine calendar-year trustee fee amounts solely from the reports submitted by Loewen to Hennepin and Anoka counties and, therefore, also could not determine whether trustee fee amounts ultimately paid were within the five percent statutory cap.

In light of the difficulty in comparing PCI fund earnings income to trustee fee payments, the OSA relies on the reports of the independent accountant summarizing annual earnings income and trustee fee payments for the years 1991 to September 30, 1999.

Sunset: The independent accountant reported that for the years 1991 to 1994, total amounts paid to the trustee exceeded five percent of earnings income by \$6,421. Specific years in which overpayments occurred were not identified. For the years 1995 to 1998, it was reported that payment of fees in excess of five percent occurred in 1995 and 1998. In these two years, total amounts paid to the trustee exceeded five percent of earnings income by \$3,262.<sup>53</sup>

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<sup>52</sup> Minn. Stat. § 306.79 (1998).

<sup>53</sup> However, the independent audit reported that for the period 1995 to September 30, 1999, cumulative trustee fees paid were \$1,667 less than the five percent limit.



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Morningside: Loewen and the independent account reported that for the years 1996 to September 30, 1999, total amounts paid to the trustee exceeded five percent of earnings income by \$6,021.

Loewen acknowledges that overpayment of Sunset's trustee fees occurred in 1995 and 1998 by \$846 and \$2,416, respectively. Loewen acknowledges that Morningside's trustee fees exceeded five percent from 1996 to September 30, 1999 by a total of \$6,021. These payments represent funds that should not have been withdrawn from PCI fund earnings income because they exceeded the statutory five percent cap on trustee fees.

In conclusion, Sunset and Morningside violated Minnesota law by paying annual trustee fees in excess of five percent of gross trust earnings income. Accordingly, \$9,683 (\$6,421 for 1991-1994 + \$3,262 for 1995-1998) was paid in violation of law and should be returned to Sunset's PCI fund principal balance and \$6,021 (for 1996-1999) should be returned to Morningside's PCI fund principal balance.<sup>54</sup> The OSA further recommends that Loewen establish the internal controls necessary to limit its trustee fees to five percent of annual PCI fund earnings.

**5. Failure to Make Timely and Sufficient Deposits**

Minnesota law requires that cemeteries that have created PCI funds allocate to the fund a minimum of 20 percent of the proceeds from sales of cemetery lots (and 10 percent of the proceeds of sales of burial space in mausoleums).<sup>55</sup> The amounts collected from lot sales must be paid quarterly to the trustees of the fund. These amounts then become part of the cemetery's PCI fund.

Sunset, for the period between 1991 and 1999, and Morningside, for the period between 1996 and 1999, did not timely deposit the proceeds from sales of cemetery lots for permanent care into the PCI fund. Loewen acknowledged that proceeds from the sale of lots at both cemeteries designated for the PCI fund were remitted only after a contract was paid in full; payments on installment contracts for lot purchases were not remitted to the PCI trust until paid in full.

Proceeds from lot sales paid on an installment basis must be paid to the PCI fund when received, no less than quarterly, rather than when paid in full. Therefore, permanent care amounts received from the sale of graves were not timely deposited

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<sup>54</sup> Loewen was not the owner of Sunset when the 1991-1994 violations occurred.

<sup>55</sup> Minn. Stat. § 306.78 (1998).

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into the fund as required by Minn. Stat. § 306.78. Loewen's independent accountant recognized this violation and acknowledged that Loewen deposited \$173,014 into Sunset's PCI fund in the form of a "catch-up" deposit to remedy the violation. A similar deposit of \$35,459 was acknowledged by the independent accountant to remedy Morningside's violation.

The OSA's review of this issue finds that the cumulative "catch-up" deposits are inadequate. Loewen calculated a PCI liability shortage by identifying its unfulfilled contracts and multiplying total payments received by the appropriate percentage of PCI liability for that contract. Loewen did not consider earnings income on amounts that should have been deposited as cash was received. The total amount due to the PCI fund would have been greater if deposits from grave sales were made in a manner consistent with law, which requires ongoing PCI deposits from receipts of installment contract payments in addition to deposits from contracts paid in full. The failure to make installment contract deposits into the PCI fund at the time of receipt necessarily reduced the PCI fund balance that would otherwise have been available for investment earnings. Accordingly, but for the failure to make timely deposits, additional earnings income would have accrued.

The OSA cannot calculate whether Loewen's catch-up deposit amounts are accurate. Because Loewen was unable to provide the OSA with a year-to-year analysis of its trust deposit shortages, the OSA cannot calculate the amount of PCI deposits that should have been made on an ongoing basis rather than a catch-up deposit. However, it is clear that an additional deposit, equal to several thousand dollars, is required to remedy the lost interest earnings resulting from Loewen's failure to comply with Minnesota law.

The OSA recommends that Loewen review its calculation of annual trust deposit shortages in order to determine the appropriate amount to deposit. Accordingly, Loewen should deposit an additional amount into the Sunset and Morningside PCI fund principal balance sufficient to approximate the earnings that would have accrued had all PCI fund payments been made in accordance with Minnesota law. The OSA further recommends that Loewen comply with the law and deposit the proceeds from grave space sales upon receipt.

**6. Failure to Timely Report to County Auditor**

Minnesota law requires all cemeteries larger than 10 acres having a PCI fund to make an annual written financial report to the county auditor in which the cemetery

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is located.<sup>56</sup> This annual report covers the state of the cemetery's PCI fund, including all deposits and withdrawals of principal amounts and all receipts and disbursements. The report must be filed by March 31 for cemeteries that operate on a calendar year basis. The OSA reviewed Loewen's reports for 1991 to 1999 filed on behalf of Sunset cemetery.

Loewen acquired Sunset on March 17, 1995. For fiscal years 1995 through 1998, Loewen failed to file the mandatory report with the Hennepin County auditor by the deadline established in law. The 1995 and 1996 annual PCI reports were filed over six months late. The 1997 report was filed over eight months late.

The OSA recommends that Loewen comply with Minnesota law and take the necessary steps to ensure that future PCI reports are timely filed according to the statutory requirements.

## **7. Improper Withdrawal of Principal**

In cemeteries where a PCI fund is established, the fund's principal is inviolate. The law states that, "[t]he principal of a permanent care and improvement fund . . . must forever remain intact and invested by the trustees . . ." <sup>57</sup> The statute does permit limited principal withdrawals from the fund "to acquire additional land for cemetery purposes for the erection of a chapel, greenhouse, or other buildings . . . for the building or improvement of roads and avenues in the cemetery, or for both of those purposes." The net income of the PCI fund may only be used "for the care, maintenance, and improvement of the cemetery and the avenues leading to it."

The OSA reviewed the annual PCI fund reports for Morningside that Loewen filed with Anoka County. On three occasions, Morningside withdrew funds from its PCI fund principal balance in violation of Minn. Stat. § 306.79. The 1999 annual PCI fund summary filed by Loewen reported \$13,836.50 of principal funds withdrawn to pay state and federal taxes. Loewen reported principal fund withdrawals to pay administrative service fees to First Trust bank of \$2,331.40 in the 1997 annual summary and \$11,865.50 in the 1998 annual summary. These withdrawals violate the limited statutory purpose for the use of PCI funds.

The OSA recommends that the \$13,836.50, \$11,865.50 and \$2,331.40 improperly withdrawn from the Morningside PCI fund be returned in full to the principal balance.

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<sup>56</sup> Minn. Stat. § 306.761, subd. 2.

<sup>57</sup> Minn. Stat. § 306.79 (1998).

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The OSA further recommends that Loewen comply with the law and take the necessary steps to assure that future PCI withdrawals conform to the statutory requirements.

**8. Insufficient Funding of PCI Trust Funds**

The matter of the appropriate balance in the PCI funds of both Sunset and Morningside is the thread that runs throughout this review. It was the subject of multiple sets of correspondence between the OSA and Loewen as well as the focus of many discussions with company officials. To determine the appropriate trust fund balance, the OSA reviewed all of the information provided to it by Loewen that was relevant to the scope of this report, including annual PCI fund reports filed with Hennepin and Anoka counties for cemetery lot and mausoleum sales, trusting data, PCI fund trustee bank records, as well as the independent accountant's analysis. The OSA's analysis, the independent accountant's analysis, and Loewen's responses each indicate that the PCI funds at Sunset and Morningside were underfunded during the period of review. However, the amounts by which the funds were found to be deficient greatly differ among the three analyses.

Finding number IV.C.5, above, concludes that PCI fund deposits must be made when funds are received rather than when contracts are paid in full. Minnesota Statutes § 306.78 requires that cemeteries with PCI funds allocate to the fund a minimum of twenty percent of the proceeds from sales of cemetery lots and ten percent of the proceeds of sales of burial space in mausoleums. The amounts collected must be paid at least quarterly to the trustees of the fund.

In June 1999, the OSA determined that through year end 1998, the PCI funds at both Sunset and Morningside were underfunded by \$190,013.24 and \$78,717.18, respectively. In Loewen's independent accountant reports dated January 30, 2000, the accountants determined that through September 30, 1999, the PCI funds at both Sunset and Morningside were underfunded by \$173,014 and \$35,459, respectively.

After receiving the final 1999 annual reports submitted to the counties, the OSA calculated the PCI trust fund deficiency through year end 1999. The OSA determined that Sunset's PCI fund was underfunded by \$24,261 and Morningside's PCI fund was underfunded by \$40,133. These numbers reflect "catch up" deposits of \$173,014 and \$35,459 for Sunset and Morningside, respectively. These deposits were made pursuant to the independent accountant's September 30, 1999 report. Therefore, the OSA recommends that Loewen deposit \$24,261 into Sunset's PCI fund and \$40,133 into Morningside's PCI fund.

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Cumulative, so-called “catch-up” deposits like those made by Loewen for both Sunset and Morningside are not an acceptable means to supplement a PCI fund for amounts that should have been deposited in earlier years. The PCI funding process prescribed by law requires that deposits of sales proceeds be made at least quarterly. For each annual reporting period, the amount of deposit must be at least 20 percent of the proceeds from grave space sales and 10 percent of the proceeds of mausoleum space sales. The OSA acknowledges that Loewen made a significant catch-up deposit for Sunset in 1999 and for Morningside in 2000. While the deposits were made to remedy past errors, it is important to note that such deposits are not consistent with the statutory requirement. Further, because of the failure to make on-time deposits, the PCI funds were denied the interest income and compounded earnings that they would have accrued on their appropriate balances.

The OSA recommends that Loewen implement internal controls to prevent any further failure to deposit the mandatory minimum amount into the PCI funds.

**V. Conclusion.**

This concludes the OSA's present examination into statutory noncompliance by Sunset Memorial Park Cemetery and Morningside Memorial Gardens. As required by Minn. Stat. ch. 149A and ch. 306, this report will be provided to the Minnesota Department of Health, the Hennepin and Anoka County attorneys' offices, and the city attorney for the cities of Minneapolis and Coon Rapids for their review and consideration as to possible further action.

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# ADDENDUM

## A. Completeness of Preneed Consumer Database – Customer Population

### 1. Background

The purpose of this audit test was to determine whether the population of the Loewen preneed consumer database was complete.

In 1999, the OSA established a telephone “hotline” to receive calls from persons with questions about funeral and cemetery practices in Minnesota. Many of the calls received from Minnesotans using the hotline number concerned Sunset and Morningside cemeteries. Each of the calls was recorded using a uniform data intake sheet, which was maintained in an alphabetical file.

The “H to Z” portion of the complete hotline file was reviewed for caller comments about or references to Sunset. The entire “A to Z” file was reviewed for caller comments about Morningside. Intake sheets with such references were removed and copied. For example, for an intake sheet to be copied, there had to be explicit references to either a consumer’s belief that s/he actually has a preneed agreement, or some reference in the comments to specific goods or services that would likely be included in a preneed arrangement (e.g., marker, opening, vault, casket). Two-hundred call records were identified and copied. Based on the identified records, staff called each of the persons who called the hotline to verify whether the caller has a preneed arrangement with the cemetery. The verification process yielded 75 records indicating that a preneed agreement likely exists with Sunset. Similarly, ten records were identified as likely Morningside customers. The OSA then attempted to locate each of the customers with verified records on the Loewen preneed database.

### 2. Findings

#### a. Morningside

To the extent the OSA was able to determine, the population of the preneed consumer database was complete for Morningside. Of the 10 persons the OSA verified by phone as having a strong likelihood of a preneed arrangement with Morningside, nine were located on the Loewen database. The customer’s name for the record that was not located was forwarded to Morningside. Morningside staff subsequently provided additional information about the customer and it was located.

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**b. Sunset**

Of the 75 persons the OSA verified by phone as having a strong likelihood of a preneed arrangement with Sunset, 62 were located on the Loewen database. Thirteen consumer records were not found on the database. During its site visit to Sunset, the OSA conducted an on-premises search to locate the 13 preneed customer files. One file was found under the name of its purchaser, which reduced the search to 12 files. Installment contracts were located at Sunset for 10 of the 12 files and Sunset could find no contract information for one of its customers. Upon review, it is likely that the located agreements have no preneed liability. The agreements may have been exclusively for space, which carries no liability, or may have been fulfilled by the delivery of a vault or installation of a marker. The two “missing” customer files were obtained directly from the customer showing that the agreements were for non-trusted purchases. Therefore, the OSA was unable to determine that the population of the database for Sunset was complete.

**B. Completeness of Preneed Consumer Database – Random Customer Check**

**1. Matching Onsite Agreements Against Consumer Database**

During on-site visits to both Sunset and Morningside, the OSA randomly selected customer preneed agreement files from each cemetery’s active preneed accounts. The customer names from the 30 customer files selected at Morningside and 40 files selected at Sunset were later compared to the Loewen database to verify whether that database was complete. This search did not fully examine individual customer preneed arrangement files for discrepancies, inconsistencies, or erroneous information.

**2. Findings – Morningside**

Twenty-nine of the sample of 30 preneed customer files were located on Loewen’s Morningside preneed database. One agreement, number 7411, executed on January 11, 1986, was missing from the database. In addition to the purchase of two interment spaces, this preneed agreement was for the selection of two vaults and a bronze memorial. Subsequent to the OSA informing Morningside staff about the missing file, the cemetery provided the OSA with a copy of a database entry itemizing the customer’s specific selections, their prices, and the remaining account balance. No explanation was provided about the reason for the agreement to be missing from the database.



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### **3. Findings – Sunset**

Seventeen of the sample of 40 preneed customer files pulled from the vault in which active preneed contracts were stored were located by OSA staff on Loewen's Sunset preneed consumer database. Twenty-three agreements from the sample were not found on the database.

Loewen was provided with a list of the 23 agreements not found on the database and was asked to provide an explanation. Loewen's response was that "the upstairs vault at [Sunset] does not include the entire inventory of active preneed agreements. It contains those records, active and inactive, written from 1985 through current only. Those contracts written in 1984 and previous are found on the lower level and again there is no segregation of active and inactive preneed files"

A second letter from Loewen stated that, "[w]e have verified that the twenty-three (23) files in question are in fact inactive or are without trust liability." Documentation for twenty-two of the 23 files was faxed to the OSA on September 12. One agreement was subsequently located on the database. Upon examination, 16 of the 22 agreements selected from the vault were, in fact, inactive or without trust liability. These agreements have been fulfilled and should not appear on an active preneed database. Four of the agreements were solely for the purchase of cemetery space. Space has no preneed trusting liability. Because there were no other goods or services included in the agreement, it was not a preneed agreement that required trusting and therefore also should not have appeared on the database. The OSA questions why these agreements were located in the cemetery's vault containing active preneed agreements.

One agreement written in 1992 was for the purchase of space and a burial container (e.g., vault). Unless the container was installed, i.e., delivered, any agreement for burial containers has trusting liability and therefore should appear on the database. However, the response OSA received from Loewen was that "all vaults [purchased] between the years of 1985-1995 were installed prior to need at Sunset (which is no longer the practice) and therefore there would be no trust liability." If the contract was serviced and there is in fact no trusting liability, it is unclear why this agreement was located in the cemetery's vault containing active preneed agreements.

Based upon this information, the OSA was again unable to determine the completeness of the preneed consumer database for Sunset.

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**C. Accuracy of Preeed Consumer Database**

**1. Letter Sample**

Computer-generated random lists of customer preneed contracts were drawn from the populations of the preneed consumer databases for Morningside Memorial Gardens and Sunset Memorial Park provided to the OSA by Loewen. The total preneed consumer population for each cemetery is comprised of both pre- and post-acquisition customer contracts. In all, four databases of preneed consumers were provided: Morningside pre-acquisition, Morningside post-acquisition, Sunset pre-acquisition, and Sunset post-acquisition.

A sample of 75 preneed contracts was drawn from Loewen's database for Sunset and Morningside customers.<sup>1</sup> The actual sample size for Morningside was 74 because one of the files selected was not an actual consumer.<sup>2</sup> The OSA sent an initial letter to 149 customers whose contracts were randomly selected using mailing addresses provided by Loewen. The letter listed all items of merchandise and services selected by the customer as they appear on the Loewen database. The

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<sup>1</sup> Morningside: Total sample size of 74 customers (33 pre-acquisition and 41 post-acquisition); Responses received from 57 customers (19 pre-acquisition and 38 post-acquisition); Eight undeliverable letters (7 pre-acquisition and 1 post-acquisition).

Sunset: Total sample size of 75 customers (38 pre-acquisition and 37 post-acquisition); Responses received from 48 customers (16 pre-acquisition and 32 post-acquisition); Nineteen undeliverable letters (17 pre-acquisition and 2 post-acquisition).

<sup>2</sup> That file contained a fictional name used to represent the sale of a mausoleum light or grave candle. During a site visit, it was explained to the OSA by Morningside personnel that transactions for lights and candles, if sold separately from preneed agreements, were on an "over-the-counter" cash basis. These sales were not recorded under a customer's name. Rather, purchases were entered into the Morningside computer sales system under the fictitious name of Lou Candella (or multiple variations thereof). Lights and candles purchased in this manner appear on Loewen's preneed database, which shows that the sales proceeds were trusted, thereby implying that the merchandise was not delivered. However, Morningside personnel represented this merchandise was taken with the consumer at the time of payment. For example, the Morningside post-acquisition database has 32 entries for merchandise sales labeled "memory light-replace." Each of the entries show values listed in the column headings marked "total liability" and "amount in trust." According to the database, the total amount trusted for over-the-counter sales of memory lights and candles is \$4,655. Therefore, according to representations made by Morningside personnel, the Morningside preneed trust appears to be over-funded to the extent that these sales represent delivered merchandise.

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letter asked the customer to verify whether the identified item(s) and price(s) correctly correspond to the item(s) selected at the time the preneed agreement was made. A follow-up letter was sent to customers who did not reply, but not to those whose initial letters were returned by the US Postal Service as undeliverable. Based on customer verification responses received, customers generally agreed that items listed on the database appeared to be similar in description and price to those selected.

The OSA notes that some customers reported a real or perceived discrepancy or inconsistency between the Loewen database and his/her selection(s). Instances of discrepancy or inconsistency are described by topic below. In several responses, consumers noted that some items shown on the letter's itemized list, which was copied directly from the Loewen database, do not appear as separate items on their copy of the preneed agreement. Nevertheless, consumers noted that the total price of the items listed on the letter appeared to match the total amount of the agreement. A review of a small number of customer preneed agreements voluntarily provided to the OSA suggests that certain selections are grouped together and offered as a package. For example, an agreement's line item marked as a "memorialization" selection shows a single price, but may include a bronze marker, granite slab, and urn. The database itemization lists each component separately with its respective price.

**a. Letter Sample Findings - Sunset and Morningside**

**Overall accuracy** — Sunset and Morningside customers who were able to compare their preneed arrangement information against the data taken from Loewen's preneed database generally agreed that items listed on the database appear to be similar in description and price to those selected.

**Customer addresses** — Mailing addresses provided to the OSA by Loewen for Sunset and Morningside preneed customers in many cases were not accurate. A high percentage of the Sunset customer random sample (25 percent) could not be reached. Eleven percent of the Morningside sample could not be reached. Only three of the 27 customers who could not be located originated their customer agreements after the cemeteries were acquired by Loewen. Nevertheless, Loewen holds significant trust assets on behalf of both their pre- and post-acquisition preneed consumers and should endeavor to locate its customers with unfulfilled agreements.

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**Trusted selections** — In comparing their preneed agreement selections to the database information provided in the OSA letter, some customers identified discrepancies between prices shown on their agreement and the values listed on the letter. Across the entire sample, consumer agreements do not identify the specific selections for which payments are to be trusted, or what amount of the proceeds are to be deposited into their trust. For the selections and amounts shown on the consumer's preneed agreement, there should be an identification of the exact dollar amount that is to be held in trust whether it is paid in full at the time of the agreement or paid on an installment basis.

**b. Letter Sample Findings - Morningside**

**Cash sales** — Cash sales of over-the-counter merchandise do not appropriately belong on the preneed sales database. The Morningside preneed trust is overfunded to the extent that these sales represent delivered merchandise. See footnote 2 of this Addendum.

**Administrative fees** — The consumer preneed agreement does not separately itemize an administrative fee (usually \$75); however, the fee does appear as a line on the database itemization. The fee amount is incorporated into the price of a good on the agreement (e.g., casket or vault). Although it is part of the purchase price of the good on the consumer contract, the administrative fee payment is not trusted according to the database itemization.

The purpose of the administrative fee is not apparent. More importantly, it appears that the consumer is not aware that: 1) an administrative fee is being charged for their preneed selection(s); and, 2) that the proceeds deposited into their trust account for the payment of their selections is reduced by the amount of the fee.

**Disputed amounts** — In one case, for the selection of a grave opening, the database itemization shows a price of \$1,110 and the consumer's price is \$1,600. In another case, the itemization shows \$905 and the consumer's price is \$1,230. For the selection of a casket, one consumer noted that the itemization showed \$3,705 and the consumer believes the price is \$5,040. These random observations show both that the consumer is paying an amount greater than the amount being trusted and that the consumer is not always aware that their entire payment does not go into trust.

**Trusted funds withdrawn** — In one case, a consumer's selected preneed merchandise was delivered and corresponding funds were withdrawn from the trust.

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Accordingly, the customer should not appear on the database as having an active preneed account.

**Merchandise description** — In one case, the database itemization described a customer's merchandise selection as "Scroll under \$100." The customer noted that his price for the selection was \$800.

**c. Letter Sample Findings - Sunset**

**Disputed amounts** — In one case, for the selection of a grave opening, the database itemization shows a price of \$600 and the consumer's comment indicates that two openings were purchased at a total price of \$1,200.

**Trusted funds withdrawn** — In three cases, the customer's selected merchandise has been delivered and the preneed funds were withdrawn. These customers erroneously appear on the Loewen database as having active preneed accounts.

**Erroneous vault purchase information** — Erroneous information regarding the purchase of vaults was found as described below:

- # In one case, the database itemization shows three purchased vaults and an administration fee (all paid in full). No balance is shown in either the Amount in Trust or Withdrawn Amount columns. The customer noted that there are payments remaining on the preneed balance.
- # In one case, the database itemization shows the purchase of three vaults (all paid in full). No balance is shown in either the Amount in Trust or Withdrawn Amount columns. The customer noted that the person named on the database record has been deceased 21 years, yet this customer erroneously appears on database with active preneed account.
- # In two cases, the database itemization shows the purchase of two vaults (each paid in full). Preneed funds for one of the two vaults were withdrawn. The remaining amount in trust is for the second vault. The customer noted that his parents are deceased and that the burial merchandise was delivered. The customers erroneously appear on the database as having an active preneed account.

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- # In one case, the database itemization shows a double depth vault and interment fee. Preneed funds for both were withdrawn; however, the customer erroneously appears on the database as having an active account.

## **2. Audit Sample**

The OSA randomly selected Morningside and Sunset unfulfilled preneed consumer agreements from the Loewen database to examine the corresponding on-site files and compare them against Loewen preneed database information.

Computer-generated random lists of customer preneed agreements were drawn from the populations of the preneed consumer databases for Morningside and Sunset provided to the OSA by Loewen. The total preneed consumer population for each cemetery is comprised of all unfulfilled pre- and post-acquisition customer contracts.<sup>3</sup>

### **a. Morningside Background**

A random sample of 61 preneed agreements was drawn from Loewen's database for Morningside. An attempt was made to physically locate each of the sixty-one random sample customer files at the Morningside cemetery office in Coon Rapids. Pursuant to Minn. Stat. § 149A.97, subd. 9, contracts for the purchase of preneed goods and services must be maintained on the premises or at another business location in Minnesota.

During the OSA's onsite visit, Morningside staff directed OSA staff to examine its preneed agreement files, which were stored in the company's on-premise vault. Staff indicated that the vault was the storage site for all of the cemetery's fulfilled and unfulfilled preneed agreements. Customer contract information for each of the sixty-one randomly-selected agreements was located during the premises search.

### **b. Sunset Background**

A random sample of 60 preneed contracts was drawn from Loewen's databases for Sunset. An attempt was made to physically locate each of the sixty sample

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<sup>3</sup> The total number of contracts in the Morningside pre- and post-acquisition database provided to the OSA is 3,255. The total number of contracts in the Sunset pre- and post-acquisition database provided to the OSA is 5,757.

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customer files at the Sunset Cemetery office in Minneapolis. Pursuant to Minn. Stat. § 149A.97, subd. 9, contracts for the purchase of preneed goods and services must be maintained on the premises or at another business location in Minnesota.

During the OSA's onsite visit, Sunset staff directed OSA staff to examine its preneed agreement files, which were stored in the company's on-premise vault. Sunset staff indicated that the upstairs vault was the storage site for all of the cemetery's unfulfilled, active preneed agreements. However, complete contract information was not found during the premises search. Six customer files were not found on the premises. Fourteen files included only burial sheets or contract documentation for agreements that differed from the computer-generated sample agreement. (See the audit sample findings discussed below.)

**D. Audit Sample Findings**

**1. No Significant Discrepancies — Morningside**

Comparing the sample population database entries to the premises agreements, the OSA (e.g., customer contracts) found that the item selections listed on the database are consistent in description and price to those appearing on the premises files, with one exception. One customer agreement made during the pre-acquisition period listed a price for a memorial that was less than that listed on the database.

**2. Missing or Incomplete Files - Sunset**

Contract information for 20 of the 60 sample contracts selected from the database was found to be incomplete during the premises search. Of these 20, the OSA located fourteen files that included only burial sheets or contract documentation for agreements other than the computer-generated sample agreement. Six customer files were not found on the premises.

During the OSA's onsite visit, Sunset staff directed OSA staff to examine its preneed agreement files, which were stored in the company's on-premise vault. Sunset staff indicated that the upstairs vault was the storage site for all of the cemetery's unfulfilled, active preneed agreements. Following the site visit, contrary to information provided at the site, Loewen corporate staff informed the OSA that "[t]he upstairs vault at Sunset does not include the entire inventory of active preneed agreements. It contains those records, active and inactive, written from 1985 through current only. Those contracts written in 1984 and previous are found on the

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lower level....” The OSA was further informed that neither the upstairs nor lower level vaults segregate active and inactive preneed files.

Subsequent to the site visit, Loewen provided the OSA with preneed customer agreements for 19 of the 20 files not found during the onsite review. One customer agreement from 1996 was not located.

A comparison was made between the database entries and the consumer agreements found on site. A significant number of agreements were found onsite and on the database that appear to be inactive or fulfilled. According to the database, several of these agreements have no consumer funds remaining in trust. In some instances, it appears that the funds were withdrawn upon the delivery of the merchandise. The database notes total amounts withdrawn from the merchandise trust for every item selected in an agreement. In other instances there is no indication that consumer funds were placed in trust. This may be an indication that the merchandise was delivered either preneed or at-need. Several of the agreements reviewed show the selection of a vault without any payment into the trust and no notation of a withdrawal. Documentation in several files suggests that the agreements are either “closed” or that there is no further liability. Assuming that the contracts are fulfilled and the merchandise has been delivered, the OSA was unable to determine why these agreements appear on what Loewen describes as its Sunset unfulfilled preneed contract database.

### **3. Other Issues - Sunset and Morningside**

Although the review found no significant discrepancies in customer selections or price between the Loewen database and the consumer agreements, the OSA notes that a number of agreements in the sample include certain items that merit a separate discussion. The three elements that repeatedly occur throughout the sample concern: 1) the application of installment interest charges to preneed merchandise selections; 2) perpetual care income noted as “PN ENDOW/SPECIAL CARE;” and 3) administrative fees.

**Interest charges** — Preneed arrangements allow consumers to select and set aside payments for burial and cemetery merchandise (e.g., markers, vaults and caskets) prior to need. If the total purchase value of the selections is not paid in full at the time the arrangement is agreed upon, the seller may permit consumers to make periodic or installment payments toward their purchase. (The funds received by the seller are held in trust on behalf of the consumer until the death occurs, when the funds are used to make the actual purchases.)



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Certain agreements reviewed from the sample population of both Morningside and Sunset included installment interest or finance charges on selections of preneed merchandise. In these agreements, the observed interest rates ranged from 4.75 percent to 12.75 percent. These rates are applied to the unpaid balance of the consumer's preneed merchandise selections.

The principle of charging interest on preneed merchandise can be compared to that of a department store offering a line of credit to a consumer, which is available to permit the consumer to make payments over time for goods or services received. However, the practice of charging installment interest on preneed selections is substantially different than when used for a store purchase. For purchases using ordinary credit terms, the consumer is able to acquire the goods or utilize the services immediately (this is known as "delivery"). The cost of the credit is the consumer's charge for immediate possession when the consumer is unable to pay the full price on demand. By contrast, there is no immediate possession, i.e., delivery, of a consumer's preneed selections; the consumer merely identifies goods or services to be purchased and delivered at the time of need. When there is no delivery of the good or service, there is no rationale that supports the application of installment interest or finance charges. Consumer preneed agreements that charge individuals in this manner are inappropriate.

It should be noted that the Minnesota Legislature has banned the practice of applying interest or finance charges to preneed arrangements for funeral and cemetery goods and services. The prohibition became effective on August 1, 2000, and applies to all new agreements and those on which payments were still being made.

**PN endow/Special care** — Several of the preneed agreement database entries include allocations of funds for a purpose captioned as "PN ENDOW/SPECIAL CARE." For Morningside, such allocations are found in a significant number of agreements dated between 1969 and 1990 and no such allocations occur in the years between 1996 and 1999.<sup>4</sup> The allocations range in size from \$30 to \$140. For Sunset, such allocations are found in a significant number of agreements dated between 1960 and 1966, and between 1985 and 1988. The allocations range in size from \$28.80 to \$144.

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<sup>4</sup> The sample did not contain customer agreements from 1991 to 1995 because data for these years had not yet been provided by Loewen at the time the OSA conducted these audit tests.

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The Loewen database describes the allocation as “preneed endowment/special care” revenue. The consumer agreements that correspond to the database entries were examined to determine the purpose of the additional allocation. For consumers making only preneed merchandise purchases, the identified funds are posted to the perpetual care (i.e., permanent care or PCI) fund and not the preneed merchandise fund. In some agreements, the source of the funds is separately itemized as a “Care Fund Deposit.” At Sunset, in each agreement the source of the funds is separately itemized as “endowment care for memorials.” Other agreements show no itemization, but contain the funds within the purchase price of one of the customer’s merchandise selections. Where consumer agreements also include the purchase of cemetery space, these funds supplement the mandatory payments to the perpetual care fund. (By statute, at least twenty percent of cemetery lot sale proceeds must be deposited into a perpetual care trust.) In all instances, the identified funds supplement the cemetery’s PCI fund where the consumer purchases both space and merchandise as part of the preneed sales agreement.

As described, at Morningside, these additional permanent care fund revenues only appear in agreements that were created prior to 1996. At Sunset, these additional permanent care fund revenues only appear in agreements that were created prior to 1989. It appears that at Sunset, consumers were made aware of the additional charge for perpetual care. Language in the agreement describes the nature and purpose of the statutory 20 percent permanent care fee as well as the so-called endowment care for memorials. In certain Morningside files, it appears that consumers were not aware of the additional charge for perpetual care as it is not itemized on the agreement. Where it did appear on the agreement, it is not clear whether consumers were aware of the purpose for the charge. Further, in some cases contract terms describe the nature and purpose of the statutory 20 percent permanent care fee.

The OSA could find no explanation in the agreements of the so-called care fund deposit. The cemetery may supplement its permanent care revenues from grave space purchases. Minnesota law provides for a minimum permanent care fund deposit of 20 percent of the sale proceeds. However, there appears to be no authority for charging or collecting permanent care funds from the sales of preneed merchandise.

It should be noted that contract disclosure laws have been improved. The 2000 Minnesota Legislature modified the preneed sales laws to require that the seller disclose to the purchaser whether funds received are required to be placed in a

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trust. Further, the seller must disclose to the consumer the amount of money to be trusted.

**Administrative fees** — Several of the database entries and agreements included allocations of consumer funds for a purpose captioned as “ADMIN FEES.” Such allocations are found in a significant number of agreements dated between 1996 and 1999. In each case, the allocation is for \$75. Where it is applied, the fee is included in the total amount charged to the consumer for a particular selection. For example, the purchase of a grave marker for \$1,090 may include the \$75 fee, such that the amount actually allocated for the marker is \$1,015. At Sunset, such allocations are found in seven agreements dated between 1996 and 1999. In each case the amount is \$75. In one instance, the fee is itemized separately on the database, but on the customer’s agreement it is not itemized; rather, it is incorporated in the price charged to the consumer. The other six instances clearly show the \$75 fee on both the database entry and the consumer’s agreement.

In database entries and agreements where the ADMIN FEE is found, the funds received are not placed in the preneed merchandise trust fund. Unlike consumer funds that pay for the at-need purchase of good and services, the administrative fee funds are available to the cemetery immediately upon receipt. Sales tax charges appear to be treated in a similar manner; that is, initial payments received from the consumer are available to the cemetery immediately to cover applicable state taxes for goods prior to the cemetery’s actual “at-need” purchase and delivery of the goods.

It is unclear from the agreements the purpose of the \$75 administrative fee. At Morningside, it is evident from the agreements reviewed that this fee is not separately itemized on the agreement so that the purchaser is informed about the charge. As a consequence, the consumer is not informed that the entirety of their funds are not placed in a preneed merchandise trust fund. At Sunset, although the agreements clearly itemize the fee, this disclosure does not assure that consumers are informed whether their funds are placed in a preneed merchandise trust fund. None of the agreements reviewed at either facility itemize or identify in any other manner the portion of consumer funds allocated to either the perpetual care trust fund or the preneed merchandise trust fund.

The administrative fee charge may constitute a violation. Because Minnesota is a so-called “100 percent trusting” state, the receipt of all proceeds from preneed merchandise and services sales must be deposited in an appropriate financial institution. Upon the disbursement of trust funds, Minnesota law states that “[t]he

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funds shall be distributed in their entirety, with no fees to be retained by the trustees as administrative fees.”<sup>5</sup> Therefore, the administrative fee charge may be a violation of the statute’s intent, given that in some cases the fee appears to be charged without the consumer’s knowledge and is retained by the trustee.

It should be noted that the 2000 Minnesota Legislature modified the preneed sales disclosure laws to require that the seller disclose to the purchaser whether funds received are required to be placed in a trust. Further, the seller must disclose to the consumer the amount of money to be trusted. The disclosure requirements became effective on August 1, 2000. These provisions will clarify for the consumer whether there are funds received for charges or fees that are not deposited into the consumer’s preneed trust account.

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<sup>5</sup> Minn. Stat. § 149A.97, subd. 6 (1998).