

**IN THE CIRCUIT COURT FOR THE TWENTIETH JUDICIAL CIRCUIT,
ST. CLAIR COUNTY, ILLINOIS**

CHARLES G. KURRUS, III, P.C., d/b/a)
KURRUS FUNERAL HOMES,)

Plaintiff,)

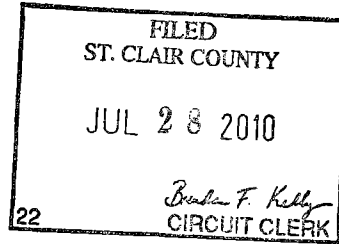
10-L-391

v.)

Jury Trial Demanded
On All Issues so Triable

MERRILL LYNCH, PIERCE, FENNER)
& SMITH, INC.; MERRILL LYNCH)
LIFE AGENCY; EDWARD L.)
SCHAIKER; PAUL W. FELSCH;)
MARK A. SUMMER; MERRILL)
LYNCH BANK & TRUST COMPANY)
FSB, MARK K. CULLEN; and)
SORLING, NORTHRUP, HANNA,)
CULLEN & COCHRAN, LTD,)

Defendants.)



COMPLAINT

Plaintiff Charles G. Kurrus, III, P.C., d/b/a Kurrus Funeral Homes (“Plaintiff” or “Kurrus”), brings its Complaint against Defendants Merrill Lynch, Pierce, Fenner & Smith, Inc. (“Merrill Lynch PFS”); Merrill Lynch Life Agency, Inc. (“ML Life Agency”); Edward L. Schainker (“Schainker”); Paul W. Felsch (“Felsch”); Mark A. Summer (“Summer”); Merrill Lynch Bank & Trust Company FSB (“MLTC”); Mark K. Cullen (“Cullen”); and Sorling, Northrup, Hanna, Cullen & Cochran, Ltd. (“the Sorling Firm”) (collectively “Defendants”).

Through its undersigned counsel, upon information and belief, Plaintiff states as follows:

INTRODUCTION

1. Plaintiff is an established, family-owned and -operated business. It has a proud tradition of providing funeral services to this community since 1883. It provides these services to customers and their families with respect, integrity, and compassion.

2. Among the services Plaintiff provides are pre-need contracts which enable the pre-selection and pre-payment of funeral services and merchandise. It is Plaintiff's experience that planning and paying for these arrangements in advance of their need is a loving gift that spares families the added stress of making many difficult decisions at an already difficult time.

3. Plaintiff reluctantly brings this action. It does so to recover the damages and losses it, and the trusts created by the pre-need contracts it has entered into with its customers, have sustained as a direct and proximate result of the Defendants' unconscionable conduct in designing, implementing, profiting from and fraudulently concealing the damage they caused to the Illinois Funeral Directors Association's ("IFDA") tax-exempt Pre-Need Trust (the "Tax-Exempt Trust," or "Pre-Need Trust").

4. As alleged in more detail below, these damages and losses were caused by the sale and concealment of more than 300 Variable Universal Life ("VUL") insurance policies to I.F.D.A. Services, Inc. ("IFDA Services"). IFDA Services, purporting to act as trustee for the Tax-Exempt Trust to which Plaintiff deposited the funds it received under pre-need contracts, purchased these policies in reliance on the advice, assistance, knowledge, and approval of all Defendants except Merrill Lynch Bank & Trust FSB ("MLTC"). Beginning on or before May 30, 2008, MLTC itself independently caused damage to the Tax-Exempt Trust by failing to protect the trust's assets and by refusing to account for its activities. Defendants' conduct in connection with the same is referred to herein as the "Life Insurance Enterprise."

5. As a result of the Life Insurance Enterprise, an enormous deficit exists in the Pre-need Trust. Thus, when a pre-need customer passes away, Plaintiff receives from the Tax-Exempt Trust a fraction of what it would have received, but for the Defendants' conduct, to pay for the funeral services Plaintiff is obligated to provide.

6. Plaintiff has kept faith with its pre-need contract purchasers, their families and the community it has served proudly for over a century by honoring each and every pre-need contract, despite the losses it has incurred by doing so. In the future, Plaintiff fully intends to honor each and every pre-need contract, again despite the losses of doing so. As a result, unless redressed by this Court, it is Plaintiff that has borne and will continue to bear the losses and damages the Defendants and the Life Insurance Enterprise have caused.

PARTIES

7. Plaintiff is an Illinois professional corporation which has its principal place of business in Belleville, St. Clair County, Illinois. Plaintiff is licensed under the Illinois Funeral or Burial Funds Act, 225 ILCS 45/1a *et seq.* ("the Burial Funds Act" or "the Act"). Pursuant to the Act, Plaintiff receives and has received payments from its customers pursuant to pre-need contracts Plaintiff has entered into to provide funeral services. Plaintiff is a member of IFDA and has deposited pre-need funds in the Tax-Exempt Pre-Need Trust. Consistent with the Burial Funds Act, the pre-need contracts state that, upon the death of the pre-need customer, the money to pay for that customer's funeral is to be transferred directly to Plaintiff to pay for the pre-need customer's funeral. (A sample of one of Plaintiff's pre-need contracts, with customer-identifying information redacted for privacy reasons, is attached as Exhibit A.).

8. Defendant Merrill Lynch PFS is a Delaware corporation that maintains its headquarters in New York, New York and has offices around the world, including in this

County. Merrill Lynch PFS is a U.S.-based broker-dealer in securities, a futures commission merchant, and is registered as an investment advisor with the Securities and Exchange Commission.

9. Defendant ML Life Agency is a Washington corporation headquartered in New Jersey and licensed to do business in Illinois. ML Life Agency maintains several offices in Illinois. ML Life Agency is a wholly-owned subsidiary of Merrill Lynch PFS that places and procures life insurance products and sells Merrill Lynch Life Insurance Company products pursuant to a general agency agreement. Upon information and belief, ML Life Agency is controlled by Merrill Lynch PFS and acts on behalf of Merrill Lynch PFS.

10. Defendant Edward L. Schainker was at all material times an employee or agent of both Merrill Lynch PFS and ML Life Agency and is the admitted architect of the Life Insurance Enterprise. Schainker is a resident of Illinois. In addition to other licenses and registrations he held at various times, Schainker was a licensed Illinois insurance producer from 1985 to May 18, 2009, when his license as an insurance producer was revoked by the Illinois Department of Insurance. Schainker was an advisor for the Tax-Exempt Trust beginning in 1983 and has acted with authority as an agent for Merrill Lynch PFS and for ML Life Agency in connection with the Life Insurance Enterprise.

11. Defendant Mark A. Summer was an employee or agent of Merrill Lynch PFS. Summer has been a licensed Illinois insurance producer since 2000. Summer, along with Schainker, was a co-salesperson for Merrill Lynch PFS on the IFDA and IFDA Services account. Upon information and belief, Summer acted with authority as an agent for Merrill Lynch PFS and/or ML Life Agency, and recommended and/or sold IFDA the life insurance policies at issue in this lawsuit. Summer is a resident of Taylorville, Christian County, Illinois.

12. Defendant Paul W. Felsch was an employee or agent of Merrill Lynch PFS and/or ML Life Agency. Felsch has been a licensed Illinois insurance producer since 1985. As a representative of Merrill Lynch PFS and/or ML Life Agency, Felsch advised Schainker and IFDA on various occasions, including at IFDA and IFDA Services Board of Directors meetings. Upon information and belief, Felsch acted with authority as an agent for Merrill Lynch PFS and/or ML Life Agency, and recommended and/or sold IFDA the life insurance policies at issue in this lawsuit. Felsch is a resident of St. Louis, St. Louis County, Missouri.

13. Defendant MLTC is a New Jersey corporation headquartered in New York, New York. MLTC acted as temporary trustee of the Pre-Need Trust, before officially assuming the role on or about October 23, 2008.

14. Defendants Merrill Lynch PFS, ML Life Agency, Schainker, Summer and Felsch are referred to herein as the “Merrill Lynch Defendants.”

15. Defendant Mark K. Cullen is an attorney licensed to practice law in the State of Illinois and resides in Illinois. Cullen is a principal of Defendant Sorling, Northrup, Hanna, Cullen & Cochran, Ltd., and in that capacity has been one of the attorneys advising IFDA, IFDA Services, and IFDA Services in its purported status as trustee for the Tax-Exempt Trust.

16. Defendant the Sorling Firm is an Illinois professional corporation which provides legal services to clients throughout this State. The Sorling Firm provided advice to IFDA, IFDA Services, and IFDA Services in its purported status as trustee for the Tax-Exempt Trust. Cullen and the Sorling Firm are referred to herein as the “Sorling Defendants.”

17. As alleged in more detail below, in furtherance of the Life Insurance Enterprise, the Defendants acting personally and through their agents, intentionally and improperly withdrew or used Tax-Exempt Trust funds for their benefit, or otherwise

intentionally violated the Burial Funds Act by participating in the Life Insurance Enterprise. Additionally, as alleged in more detail below, the Defendants fraudulently concealed their actions, their participation in the Life Insurance Enterprise, and the damages they caused Plaintiff.

JURISDICTION AND VENUE

18. This Court has personal jurisdiction over all the Defendants as they are either residents of this State, registered to do business in this State, transacted business in this State and/or committed tortious acts within this State.

19. Venue is appropriate in this County pursuant to 735 ILCS 5/2-101(1) and (2) because, *inter alia*, at least one defendant has an office in this County, and is therefore a resident of this County, and because some part of the transactions out of which this cause of action arose occurred in this County.

20. The causes of action alleged herein do not arise under the Constitution, laws, or treaties of the United States. Diversity does not exist under 28 U.S.C. §1332 because the Plaintiff and several defendants are Illinois residents and no party has been joined in this action without the intent to obtain a judgment against him or it.

STATEMENT OF FACTS

I. THE PRE-NEED CONTRACTS PLAINTIFF ENTERED INTO WITH ITS CUSTOMERS TO PRE-ARRANGE AND PRE-PAY FUNERAL EXPENSES

21. Like many funeral directors, Plaintiff assists its customers in pre-arranging and pre-paying for funeral arrangements. To assist in planning in advance for a customer's funeral arrangements, Plaintiff has entered into pre-need contracts under the Burial Funds Act, 225 ILCS 45/1a *et seq.*, to provide such services. Through these pre-need contracts, Plaintiff received

payments under pre-need contracts to be held in trust to pay for the funeral services and goods Plaintiff agreed to provide its pre-need customers.

22. The pre-need contracts at issue, which were drafted by IFDA Services and signed by Plaintiff and its pre-need customers, provide that deposited funds will be held in the Tax Exempt Trust until the customer's death. Acting as trustee of the Tax Exempt Trust, IFDA Services also held the funds Plaintiff deposited in trust - for the benefit of the Plaintiff and its customers - until the death of each pre-need customer. Pursuant to the Participating Member Firm ("PMF") Agreements executed by Plaintiff and IFDA Services, upon the death of a pre-need customer, the money for that customer's funeral is to be transferred directly to Plaintiff to pay for the pre-need customer's funeral and to provide for the merchandise and services as specified in the applicable pre-need contract.

II. THE IFDA PRE-NEED TAX-EXEMPT TRUST.

A. IFDA's first attempts to obtain a license to act as a trustee under the Act.

23. The Burial Funds Act establishes a regulatory structure that oversees funds generated by the pre-need sale of funeral merchandise and services. At all relevant times, the state official who purported to administer the Burial Funds Act was the Illinois State Comptroller.

24. In 1979, IFDA Services first sought to establish a pre-need trust to hold trust funds that funeral directors had received from their pre-need contract purchasers and requested that the State Comptroller approve its proposed entrustment plan.

25. The Comptroller originally rejected IFDA Services' request. After reviewing the documentation IFDA Services proposed for its entrustment plan, the Comptroller's counsel concluded that IFDA Services did not qualify for a license under the Act since it was not a seller of funeral and burial services. The letter from the Comptroller's counsel stated:

since the IFDA cannot qualify as a trustee (or a licensee) as defined in the Act, its only capacity can be as Depository of the Funds.

Of course, the IFDA does not qualify as a depository of the funds, as defined in Section (2) of the Act, since the IFDA is not a Bank, Savings and Loan nor a trust company.

26. On March 5, 1980 the Comptroller's counsel reversed this position and notified IFDA Services that then State Comptroller Roland Burris would find the IFDA Trust Plan acceptable, and would issue a license to IFDA Services to act as a trustee under the Burial Funds Act, if IFDA Services' proposed trust agreement were amended. Specifically, the Comptroller required that the trust agreement include a recital that IFDA Services "and the Funeral Home acknowledge and agree that they are subject to and are *duly licensed* in accordance with the 'Act,' and that until the services contracted for were delivered, "both the Trustee [IFDA Services] and the Funeral Home *continue to remain so licensed and shall fully comply with all the provisions of the said Act....*" (Emphasis added.)

27. In 1986, IFDA Services announced it would offer a tax-exempt option – the Pre-Need Tax-Exempt Trust – to allow pre-need contract purchasers to have income on the amounts they paid into trust grow on a tax-free basis. Rather than use the same counsel who represented IFDA Services in its earlier dealings with the Comptroller, on or about this time the Sorling Firm was retained. From approximately 1986 to 2009, the Sorling Firm represented IFDA, IFDA Services, and IFDA Services, in its role as trustee for the Tax-Exempt Trust itself in connection with the operation of the Trust. In 1987, the Sorling Firm contacted the State Comptroller to request approval to use pre-need trust funds to purchase life insurance policies. The Comptroller's counsel, however, declined to give that approval.

28. In a letter dated April 10, 1987, the Comptroller's counsel advised that, because prior opinions of the Attorney General regarding the entrustment of pre-need funds had been

very restrictive, and because “there are certain schools of thought that conclude that pre-need funds may not be used for such purpose,” the use of any trust funds to purchase insurance products must be subject to compliance “as per the opinion of the Attorney General.” While the Comptroller had requested that the Attorney General issue such an Official Opinion, none was ever issued.

29. Despite the absence of an official Attorney General Opinion, IFDA Services, purporting to act as and assuming the duties of a trustee, began using almost all of the funds that were deposited in the Tax-Exempt Trust to purchase insurance policies. Upon information and belief, the Sorling Firm advised IFDA Services, as trustee for the Tax-Exempt Trust, that such policies *could* be purchased with pre-need trust funds in compliance with the Burial Funds Act.

30. No notice was given to Plaintiff that counsel for the Comptroller had advised the Sorling Firm that any use of pre-need trust funds to purchase insurance products should be subject to compliance with an Official Opinion of the Illinois Attorney General. Nor was Plaintiff made aware that the overwhelming majority of funds deposited in the Tax-Exempt Trust, at least until 1997, were being used to purchase insurance policies.

31. Since the inception of the Pre-Need Trust, contracts IFDA provided to Plaintiff and other funeral homes “instructed [IFDA, as Trustee] to invest [each customer’s] account in a tax exempt fund,” and/or “authorized” IFDA Services to invest the customer’s account in a tax-exempt fund. *See e.g.* Funeral Trust Agreement, attached as Ex. A. Plaintiff did not know, and had no way of knowing, that this was not in fact being done for payments it sent to IFDA as Trustee to be deposited in the Pre-Need Trust.

III. KEY AMENDMENTS TO THE BURIAL FUNDS ACT EFFECTIVE JANUARY 1, 1994.

A. The Act was amended to permit the purchase of insurance policies so long as specific conditions were met.

32. As of January 1, 1994, the Burial Funds Act imposed restrictions on the investment decisions that any duly-authorized trustee under the Act must follow. It thus required that any trustee authorized to hold funds under the Act “shall, with respect to the investment of trust funds, exercise the judgment and care under the circumstances that persons of prudence, discretion and intelligence exercise in the management of their own affairs, *not in regard to speculation*, but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital.” (225 ILCS 45/4a(a) (emphasis added.)

33. While the 1994 amendment to the Burial Funds Act authorized a trustee to purchase life insurance with trust funds, it did so only if the trustee strictly complied with specific conditions. Section 2a(a) of the Act thus provided that “[i]f a *purchaser* selects the purchase of a life insurance policy or a tax deferred annuity contract to fund the pre-need contract, the application and collected premium shall be mailed within 30 days of the signing of the pre-need contract.” (225 ILCS 45/2a(a) (emphasis added.) Under the Act, a “purchaser” means the person who *originally* paid the money under or in connection with a pre-need contract.” 225 ILCS 45/1a (emphasis added).

34. The Act further specifically prohibited the purchase of insurance with trust funds for which the buyer or owner of the policy had no insurable interest. In particular, Section 2a(b) provided that:

No person whose only insurable interest in the insured is the receipt of proceeds from the policy or in naming who shall receive proceeds from the policy or in naming who shall receive the proceeds nor any trust acting on behalf of such person or seller or provider shall be named as owner or beneficiary of the policy or annuity.

225 ILCS 45/2a(b) (emphasis added).

35. In addition to these restrictions, Section 4a(d) of the Act imposed further restrictions on the use of trust funds to purchase insurance. Specifically, Section 4a(d) required that “[t]rust funds *shall not be invested by the trustee in life insurance policies* or tax-deferred annuities *unless*” the pre-need contract *purchaser* approves in writing and in advance the investment in life insurance policies or tax deferred annuities, (225 ILCS 4a(d)(2)), and the trustee informs the Comptroller that trust funds shall be removed from the trust to purchase life insurance before the investment is made. 225 ILCS 4a(d)(4) (emphasis added).

B. IFDA Services’ status as a licensed trustee under the Act was eliminated as Plaintiff’s statutory authority to change the trustee for funds it had submitted to trust was confirmed.

36. Also as of January 1, 1994, the Act was amended so that the State Comptroller only licensed “sellers” of funeral or burial services and not “trustees.” Since IFDA Services was not a seller of funeral or burial services, its status as a trustee under the Act was eliminated as of January 1, 1994.

37. Additionally, Section 2(g) of the Act was added to give sellers of funeral services the right to change the trustee holding funds deposited in trust. It provides that “upon notice to the Comptroller, the seller may change the Trustee of the fund.” 225 ILCS 45/2(g).

IV. HOW THE IFDA SERVICES PRE-NEED TAX-EXEMPT TRUST WORKED.

A. The Life Insurance Enterprise.

38. Aware that a safe, conservative, laddered, tax-exempt investment strategy would not generate the fees, commissions, and other income they desired to make from the Tax-Exempt Trust, Defendants Merrill Lynch PFS, ML Life Agency, and Schainker declined to recommend it. Instead, they planned an investment strategy that would maximize the money they personally could make with and from Pre-Need Trust funds. They did so intending to use Pre-Need Trust

funds improperly to obtain from the Tax-Exempt Trust a continuing source of significant revenue that would be difficult for others, including funeral directors who participated in the Tax Exempt Trust like the Plaintiff, to monitor and control.

39. Although the Merrill Lynch Defendants knew or should have known that an actuarial study to estimate the expected cash needs for the Tax-Exempt Need Trust was necessary, they did not obtain such a study before recommending the Life Insurance Enterprise. As a result, the Merrill Lynch Defendants knew or should have known that the investments in the Life Insurance Enterprise they recommended would have no correlation to any expected liquidity needs of the Tax-Exempt Trust.

40. Instead of safe, conservative, laddered and tax-exempt investments in tax-exempt funds, the Merrill Lynch Defendants advised IFDA Services to use the overwhelming majority of the funds in the Tax-Exempt Trust to purchase high commission, VUL “key man” insurance policies that the Merrill Lynch Defendants sold through ML Life Agency. In very large part, these VUL key man policies were issued by ML Life Insurance, then a Merrill Lynch affiliate. The Merrill Lynch Defendants sold, and IFDA Services, as Trustee for the Tax-Exempt Trust, purchased these policies from 1986 through at least 1997.

41. As of January 31, 2009, the Tax-Exempt Trust had paid at least \$88,272,900 in premiums for these policies.

42. To implement the Life Insurance Enterprise, the Merrill Lynch Defendants sought out various Officers and Directors of IFDA Services and other funeral directors associated with IFDA who were convinced, under false pretenses, to have “key man” life insurance policies issued on their lives. Proceeds from the policies would be payable on their deaths to IFDA

Services as Trustee of the Tax-Exempt Trust. Some of the insureds had as many as 6 key man policies written on their lives.

43. IFDA Services, Inc. was the owner of the policies the Merrill Lynch Defendants sold. Moreover, premiums paid for the policies were paid with funds from the Tax-Exempt Trust. In all, the Merrill Lynch Defendants sold IFDA Services, as Trustee of the Tax-Exempt Trust, over 300 policies from 7 different insurers on 131 individuals.

44. Most of the funeral directors who consented to allow insurance policies to be issued on their lives were unaware of the true nature of these investments or why the Merrill Lynch Defendants recommended them. These individuals were told that the policies were somehow intended to “endow” IFDA, that the life insurance policies were required to maintain the tax-exempt status of the Tax-Exempt Trust and/or that the nature and extent of the policies was related to the amounts that the insured funeral director had placed into the Tax-Exempt Trust.

45. Merrill Lynch PFS had the right and obligation to control Schainker and Summer and direct their actions, but did nothing to prevent the Life Insurance Enterprise from being implemented and carried out over the course of years, even though it knew about the scheme and knew or should have known that it was an unlawful and entirely inappropriate “investment plan” for the Pre-Need Trust. Similarly, as investment advisors, Schainker and Summer had the power to legally bind Merrill Lynch PFS with the decisions they made and the financial advice they provided with respect to the IFDA Pre-Need Trust.

46. Similarly, Merrill Lynch Life Agency had the right to control Schainker and Felsch as brokers or agents, but did nothing to prevent them from soliciting and coordinating purchase of the unlawful insurance policies for which an insurable interest never existed. As

insurance agents, Schainker and Felsch had the power to legally bind ML Life Agency with the decisions made and the policies solicited and purchased for the Pre-Need Trust.

B. The Nature of the VUL Life Insurance Policies the Merrill Lynch Defendants sold.

47. The VUL insurance policies that the Merrill Lynch Defendants sold to the Tax-Exempt Trust were very expensive policies that contained mutual fund investment subaccounts and/or unit investment trusts. These insurance policies were speculative bets on the lives of the insureds which varied in their rates of return based on investments in the subaccounts and/or unit investment trusts.

48. Many of these subaccounts and unit investment trusts in the insurance policies purchased with Tax-Exempt Trust funds were managed by or benefitted Merrill Lynch affiliates. For example, some of the insurance policies contained investment divisions which invested in designated mutual fund portfolios in the Merrill Lynch Series Fund, Inc., which in turn was managed by Merrill Lynch Asset Management, Inc. Other investment divisions invested in units of a designated investment trust in the Merrill Lynch Fund of U.S. Treasury Securities, for which Merrill Lynch PFS served as a sponsor.

49. Payment of the death benefit under any particular VUL key man policy depended on the mortality of the particular insured funeral director, and not on any needs of the Tax-Exempt Trust to fund anticipated funeral expenses of pre-need contract purchasers. Consequently, none of the “investments” in VUL policies bore any relationship to the foreseeable needs of the Tax-Exempt Trust. Moreover, the life insurance policies did not confer a fixed death benefit. Instead, they offered speculative pay-outs depending on the performance of the life insurance policies’ subaccounts or unit trusts if and when the insureds died.

50. The VUL key man policies also were not liquid – at least not without incurring significant tax liabilities. Any surrender of the policy before the death of the insured would subject any earnings in the subaccounts to taxation and destroy the supposed “tax-exempt” status of the “investment.” IFDA Services as Trustee could only hope to avoid paying taxes on the supposedly tax-exempt investments if the insured funeral director died “on time.”

51. Even then, the Tax-Exempt Trust could not avoid paying taxes for the large number of the policies that were classified as Modified Endowment Contracts (“MECs”) under the Internal Revenue Code. The Code treats an insurance policy as a MEC if the premiums paid on the policy exceed the amount that would be required to result in a paid-up policy before the end of a seven year period. Consequently, single-payment VUL policies purchased after June 21, 1988, when the Code was amended, were generally MECs.

52. MECs were not designed to maintain the tax-exempt status of the subaccount investments even if the insured funeral director were to pass. This is so because MECs are subject to excise taxes if the owner of the policy is a corporation or trust. Consequently, neither IFDA Services nor the Tax-Exempt Trust could ever hope to obtain any income from a MEC on a tax-free basis. Moreover, MECs are subject to income tax if the policies are surrendered, or if any of the funds are accessed, by loan or otherwise, before the death of the insured.

C. The VUL Policies Purchased on the Principals of Plaintiff.

53. At least three VUL Policies were purchased on the owners of the Plaintiff funeral home, Charles G. Kurrus, III (“Charles Kurrus”) and Dale Kurrus. Charles Kurrus was told by IFDA’s Executive Director Robert Ninker (“Ninker”) and Schainker that the insurance policy on his life was required to maintain the tax-exempt status of the IFDA Tax-Exempt Trust. Dale Kurrus was led to believe, also by Ninker and Schainker, that the amount of the insurance

policies issued on his life related to the amounts that Plaintiff had deposited in the Tax-Exempt Trust. Plaintiff now knows, but did not know and had no reason to know until recently, that neither of these statements was true. Neither Charles nor Dale Kurrus had any idea (and indeed Ninker, Schainker and the other defendants did not tell them) that the insurance policies constituted the overwhelming majority of the Pre-Need Trust's "investments."

54. In June 1994, both Ninker and Schainker came to Belleville, Illinois to have Charles Kurrus and Dale Kurrus sign insurance applications. Copies of the applications for Dale Kurrus, with personal information deleted, are attached as Exhibits B and C. Schainker purported to witness Dale Kurrus' signature on these applications on June 24, 1994, and certified that Dale Kurrus signed them in Springfield, Illinois. While the signature pages represent that Dale Kurrus signed the applications that day in Springfield, that statement is incorrect. Dale Kurrus did not learn of the false certification until recently, when the Illinois Secretary of State inquired about the insurance policies taken on his life as part of its investigation into Schainker's conduct.

55. None of the policy applications for Dale Kurrus that he signed specified the amounts of insurance subject to the policy. At the time, Dale Kurrus was told that approximately \$1,000,000 of insurance would be issued on his life.

56. Attached as Exhibit D is a purported request for an Amendment to the Phoenix insurance policy, dated December 1, 1994, that would increase the Target Face Amount to \$1,433,833. (See Exhibit D at ML-308-0023312.) Although the Amendment form required that Dale Kurrus fill in the place where, and the date on which, the form was signed, Dale Kurrus did not fill in either the date or the place that Exhibit D was allegedly signed by him. The statement

that this document was signed by Dale Kurrus in Springfield, Illinois on December 1, 1994, therefore, was and is false.

57. More importantly, Dale Kurrus did not sign Exhibit D. Schainker, however, purported to witness Dale Kurrus signing the document. Dale Kurrus also did not sign the document attached as Exhibit E, ML-209-0023311. In fact, the signatures for Dale Kurrus that appear on both of these documents were signed by someone other than Dale Kurrus. In other words, these documents were forged.

58. Rather than apply for a total of approximately \$2,000,000 in insurance coverage for Charles Kurrus and Dale Kurrus combined, Defendants applied for and issued more than \$10,000,000 in VUL coverage on their lives. Plaintiff was not told that this amount of insurance was taken out on the lives of its owners at the time.

D. The Defendants Knew or Should have Known that the VUL Insurance Policies Violated Illinois Insurable Interest Laws, the Burial Funds Act, the Illinois Consumer Fraud and Deceptive Practices Act and their duties to Plaintiff.

a. The Merrill Lynch Defendants.

59. The Merrill Lynch PFS & ML Life Agency knew or should have known that the investments in the VUL policies they recommended and sold violated Illinois insurable interest laws. When their agent, defendant Edward L. Schainker, sold each of these VUL policies, Schainker was aware that the Tax-Exempt Trust had no insurable interest in the policies. As a result, Schainker knew or should have known that these insurance policies were mere wagering bets on the lives of funeral directors. These “investments” were therefore against public policy, mere speculation and not investments made with regard to the permanent disposition of funds.

60. The Merrill Lynch Defendants, however, with Schainker at the helm, sold these policies because they were lucrative (to them) when they were sold and because they continued to generate income and fees (for them) throughout the life of the policy.

61. The other Merrill Lynch Defendants were also aware that IFDA Services as trustee had no insurable interest in the lives of the insureds for these policies. Despite this, they knew and approved of presentations that Schainker made to other state funeral directors' associations to start supposedly tax-exempt trusts of their own. Moreover, since Schainker was their agent, Schainker's knowledge of his scheme is imputed to both Merrill Lynch PFS and ML Life Agency.

62. The nature of the VUL policies and the Merrill Lynch Defendants' management of them allowed the Merrill Lynch Defendants to make commissions, fees and other income from the policies long after the VUL policies were sold. Merrill Lynch could and did advise and otherwise direct that moneys in the VUL policies' subaccounts be invested in funds that Merrill Lynch managed and/or unit trusts from which it received commissions, income or fees.

63. These commissions, fees and other income were substantial. They would not have been made if the pre-need trust funds had been invested, as they should have been, in laddered, tax-exempt instruments. Additionally, because of the illiquidity of the VUL policies, and because IFDA and IFDA Services relied upon the advice of the Merrill Lynch Defendants, the Life Insurance Enterprise essentially locked IFDA Services in, as Trustee for the Tax-Exempt Trust, as a Merrill Lynch client – so that the Merrill Lynch Defendants could continue to profit from the Tax-Exempt Trust and the thousands of statutory trusts commingled therein.

64. In particular, the VUL policies sold by the Merrill Lynch Defendants and the insurance companies that issued them paid policy fees, trailing commissions and fund fees which

diminished the Tax-Exempt Trust's value by more than 3% annually. Thus, to the extent that the insurance policies did not earn at least that much every year, the Tax-Exempt Trust actually lost money. Because they were wrapped inside the paper "earnings" of the insurance policies, these fees and the effect they had on the Tax-Exempt Trust were hidden. In fact, even after IFDA Services stopped purchasing VUL policies, premiums on the policies were paid with proceeds from new pre-need contract deposits, including instances when charges to individual policies required additional fees to keep the policies in force.

65. The Merrill Lynch Defendants, however, were acutely aware of the significant income they continued to derive from the VUL policies they had written, procured and sold long before, including the fees and income that were hidden from others. Defendants Schainker and Summer, for example, were "shocked" to learn in 2006 that their compensation did not include millions of dollars of premiums that were earned from policies that they had sold to IFDA Services as Trustee for the Tax-Exempt Trust years earlier. Specifically, in a November 14, 2006 e-mail, defendant Summer wrote:

As the 2006 FOG [Focus on Growth] campaign is drawing to a close, I wanted to take this opportunity to renew the discussion regarding our request to have the premiums from the variable universal life policies for the Illinois Funeral Directors Association (IFDA) the Alabama Funeral Directors Association and the Mississippi Funeral Directors Association (MFDA) be considered as "net new annuitized" business. From 12/01/05 through 09/01/06, the following is a summary of the total YTD (\$6,335,697 (with September, October and November premiums yet to be determined): IFDA \$2,559,537 ; IFDA \$2,524,264; MFDA \$1,251,896

We were understandably *shocked* to discover that again in 2006 we were not receiving any of the appropriate credit. Ed [Schainker] and I both work very hard for Merrill Lynch and strongly feel that this is unfair. The funeral directors associations are an integral part of our current business, *as well as our plans for future growth (and I might add significant revenue for Merrill.)*

(Emphasis added.)

66. Additionally, the very large amounts of Tax-Exempt Trust funds that were embedded in the policies' subaccounts and in unit trusts provided the Merrill Lynch Defendants and their affiliates with substantial sources of continuing income. Upon information and belief, as of November 2007, the subaccounts of the Tax-Exempt VUL portfolio had a value in excess of \$192 million; on that date, more than 36% of these investments, or more than \$70 million, were also in mutual funds that Merrill Lynch managed. As of August 2008, the portfolio had a value in excess of \$162, million and at least 38% of this amount, in excess of \$63 million, was invested in mutual funds that Merrill Lynch managed. The income, fees and commissions that the Merrill Lynch Defendants made from investment decisions regarding the mutual fund subaccounts and the unit trusts were also hidden from funeral directors like the Plaintiff.

67. The Merrill Lynch Defendants were aware that many of the VULs they sold were also MECs that destroyed the required tax-exempt nature of the trust.

68. As a result, the Merrill Lynch Defendants "intentionally and improperly ... use[d] trust funds" for their own benefit and otherwise intentionally violated the Burial Funds Act each and every time they obtained income from the Life Insurance Enterprise. *See* 225 ILCS 45/8. Additionally, the Merrill Lynch Defendants knew or should have known that each and every knowing violation of the Burial Funds Act also constituted a violation of the Illinois Consumer Fraud and Deceptive Practices Act (the "Deceptive Practices Act"). 815 ILCS 505/2Z.

69. The Merrill Lynch Defendants received trust funds when they knew that the transactions at issue were made as a result of a breach of trust on the part of IFDA Services, and in fact participated in that breach of trust.

70. As alleged in greater detail herein, the Merrill Lynch Defendants concealed the actual performance of the Tax-Exempt Trust from the Plaintiff and other IFDA members by,

inter alia, assisting in publishing “crediting rates” that falsely portrayed the Tax-Exempt Trust’s performance. The Merrill Lynch Defendants, through their agent Schainker, colluded with IFDA Services in fraudulently concealing the Life Insurance Enterprise and the damages it caused the Tax-Exempt Trust from Plaintiff and other IFDA members.

b. The Sorling Defendants.

71. The Sorling Defendants have refused to make full disclosure of their role in the Life Insurance Enterprise. Nonetheless, based on the limited documentation counsel for the Plaintiff has been able to obtain, the Sorling Defendants knew or should have known that the Life Insurance Enterprise violated Illinois law in several ways. First, as counsel for IFDA, IFDA Services, and IFDA Services as Trustee of the Tax-Exempt Trust, the Sorling Defendants knew or should have known that IFDA Services should never have used trust funds to purchase key man life insurance policies. Since the Sorling Firm was specifically advised by counsel for the Comptroller that any use of trust funds to purchase insurance products must await an Official Opinion by the Attorney General, and since no such Opinion was ever issued, the Sorling Defendants should have counseled IFDA Services not to buy any such investments with trust funds.

72. Second, the Sorling Defendants should have determined that none of the “key man” insureds qualified as a key man of a Tax-Exempt Trust and that the Trust, as a conglomeration of thousands of statutory trusts, could not have an insurable interest in the lives of funeral directors. Indeed, any trust that was created by the Burial Funds Act for the specific purpose of holding funds to pay for pre-need contracts simply could not have a “key man” as a matter of law.

73. Third, the Sorling Defendants were aware that most of the Tax-Exempt Trust’s funds were being “invested” in the VUL key man policies. Because the Sorling Defendants

knew that an overwhelming majority of the funds deposited from 1986 through 1997 in the Tax-Exempt Trust were used to purchase VUL key man insurance policies, they also were under a duty to investigate all aspects of the legality of these purported investments.

74. Any minimal investigation regarding any alleged insurable interest the Tax-Exempt Trust had in any of the key man policies, moreover, would have confirmed that the Trust, and the thousands of individual trusts commingled in the Tax-Exempt Trust, had no insurable interest in the policies. Indeed, since the Merrill Lynch Defendants knew this, the Sorling Defendants should also have known it.

75. The Sorling Defendants also knew or should have known that none of the insurance policies purchased after January 1, 1994 – including the VUL policies purchased on the life of Charles and Dale Kurrus – complied with the Burial Funds Act. While the Act was amended to allow the purchase of some insurance policies effective that date, Section 4a(d) clearly stated, and continues to state, that “[t]rust funds *shall not be invested by the trustee in life insurance policies* or tax-deferred annuities *unless*” several conditions are satisfied, including approval from the pre-need contract purchaser in writing in advance of the investment, (225 ILCS 4a(d)(2)), and prior notice from the trustee to the Comptroller that trust funds shall be removed from the trust to purchase life insurance before the investment is made. (225 ILCS 45/4a(d)(4), emphasis added.) None of these conditions occurred for any of the VUL policies.

76. Additionally, none of the policies purchased after January 1, 1994 complied with the Act since IFDA Services, as purported Trustee for the Tax-Exempt Trust, was the owner of the policies and the only interest it had in any of the insureds was the receipt of proceeds from the policies. These policies therefore violated section 2a(b) of the Act, which provides that “no person whose only insurable interest in the insured is the receipt of proceeds from the policy or

in naming who shall receive proceeds from the policy or in naming who shall receive the proceeds nor any trust acting on behalf of such person or seller or provider shall be named as owner or beneficiary of the policy or annuity.” 225 ILCS 45/2a(b).

77. As a result, all the policies issued after January 1, 1994 failed to comply with section Section 2a(b) of the Act., 225 ILCS 45/2a(b), and the Sorling Defendants knew or should have known this.

78. The Sorling Defendants also knew that IFDA Services had no authority under the Burial Funds Act to serve as a duly authorized trustee under the Act. Upon information and belief, the Sorling Firm knew of the changes to the Burial Funds Act on or before January 1, 1994 that eliminated IFDA Services’ ability to serve as duly licensed trustee under the Act and, at the least, should have advised the Plaintiff and the other IFDA members of this important fact.

79. The Sorling Defendants knew that IFDA Services’ legal ability to serve as trustee was important. The Sorling Firm recommended no later than 1996 that IFDA Services resign as trustee for both the Taxable and the Tax-Exempt Trusts *because IFDA Services had no authority to serve as trustee under the Burial Funds Act*. In particular, in a letter dated September 9, 1996 that summarized recommendations it had previously made to IFDA Services, the Sorling Firm stated that IFDA Services should:

Resign as Trustee. The Comptroller used to issue pre-need trustee licenses but, *as you know*, the Comptroller only issues licenses to providers. In order to eliminate any issue regarding the authority of the IFDA to serve as trustee, IFDA could resign as trustee and maintain a role as a “trust advisor.” Recall our concern that if the market value of the pre-need trust funds were to fall dramatically, that one or more pre-need customers could bring a class action alleging the IFDA was acting as trustee without proper authority and therefore would be liable for the loss in value of trust funds. The trust advisor would not have the same potential liability as the trustee of pre-need trust funds. Documents could be written in a way that would give the trust advisor much of the control currently enjoyed by the trustee, including the right to change the trustee from time to time. (Emphasis added.)

A copy of this letter is attached as Exhibit F.

80. Since IFDA Services did not resign as trustee as the Sorling Firm recommended, the Sorling Defendants have known that IFDA Services was, as the years rolled by, knowingly violating the Burial Funds Act each and every time that it took any action as trustee of the Tax-Exempt Trust. The Sorling Firm also knew or should have known that any fees IFDA Services charged the Tax-Exempt Trust for serving as a trustee violated the Burial Funds Act. Nonetheless, the Sorling Firm did not withdraw its representation of IFDA, IFDA Services, or IFDA Services as Trustee of the Tax-Exempt Trust, and likewise did not tell Plaintiff about this critical issue.

81. Since the Sorling Defendants knew or should have known that IFDA Services could not serve as a licensed trustee under the Act – an express condition of Comptroller Burris' approval of IFDA Services' entrustment plan – the Sorling Defendants should have known that their real clients were Plaintiff and the other IFDA members who received payments under pre-need contracts and submitted these trust funds to IFDA Services, and not IFDA Services as purported Trustee of the Tax-Exempt Trust.

82. The Sorling Defendants therefore knew or should have known that they could only fulfill their duties to their clients, Plaintiff and the other IFDA members who received payments under pre-need contracts and submitted these trust funds to IFDA Services, by making timely, accurate and complete disclosures of IFDA Services' lack of statutory authority to serve as trustee under the Burial Funds Act, the Life Insurance Enterprise and the damage it was causing the Tax-Exempt Trust, so that Plaintiff and other IFDA members could take appropriate action.

83. None of the Sorling Defendants advised Plaintiff that they had recommended that IFDA Services should resign as trustee. The Sorling Defendants made no disclosure despite the significant effect that this had on IFDA's legal ability to serve as trustee for the thousands of trusts and the trust funds IFDA Services had received from their pre-need contract purchasers under the Burial Funds Act. Rather than disclose these facts, IFDA Services, Cullen, the Sorling Firm and the Merrill Lynch Defendants continued to act as though IFDA Services had the authority to act as a trustee under the Act all along.

84. The Sorling Firm also knew or should have known that any knowing or intentional violation of the Burial Funds Act constituted a felony. 225 ILCS 45/8. Indeed, they recommended that IFDA Services resign because amendments to the Burial Funds Act made IFDA Services' continued violations of the Act knowing and intentional. What is worse, the Sorling Firm reviewed and approved of changes to IFDA Services' documents that continued to represent to Plaintiff that IFDA Services *could* serve as trustee, despite the changes in the Burial Funds Act that they concluded eliminated that status. The Sorling Firm also knew or should have known that IFDA, IFDA Services and the Merrill Lynch Defendants had intentionally and improperly used trust funds for their own benefits.

85. Despite their awareness that the Life Insurance Enterprise constituted civil and criminal violations of the Burial Funds Act., the Sorling Defendants took no action to advise Plaintiff of these facts, even though Plaintiff was entitled to receive payments under pre-need contracts under Section 1 of the Act. Moreover, the Sorling Firm knew or should have been aware that knowing violations of the Burial Funds Act also constitute violations of the Deceptive Practices Act and should have disclosed these violations to Plaintiff and other IFDA members as well. Instead, Cullen and the Sorling Firm repeatedly acted against the interests of their true

clients, even going so far as to refuse to provide pertinent information to certain IFDA member funeral homes concerned about the deficit in the Tax-Exempt Trust and seeking answers to their many questions unless they signed releases of liability.

86. Finally, upon information and belief, the Sorling Defendants submitted bills for legal services that they knew or should have known were directly or indirectly being paid for by monies that IFDA Services obtained while acting as Trustee, even though the Sorling Defendants knew that the Comptroller no longer had statutory authority to license trustees under the Burial Funds Act. The Sorling Defendants therefore intentionally and improperly used trust funds for their own benefit in violation of the Act.

V. THE LIFE INSURANCE ENTERPRISE BEGINS TO UNRAVEL.

A. The Situation When IFDA Services Stopped Purchasing VUL Policies.

87. As trustee, IFDA Services stopped purchasing VUL policies for the Tax-Exempt Trust in 1997. When it stopped purchasing these policies, most of the Tax-Exempt Trust's pre-need funds were invested in VUL policies.

88. Because the VUL policies were illiquid – the funeral director insureds were simply not dying - the Tax-Exempt Trust began to experience liquidity and deficit problems. Having little or no tax-exempt income from the investment of Pre-Need Trust funds in the VUL policies that it could access to honor pre-need obligations, the Tax-Exempt Trust instead began to use funds obtained from new pre-need contracts and trusts to pay for funeral and burial claims on earlier contracts. What should have been a conservatively run trust that commingled approximately 50,000 individual trusts became the equivalent of a ponzi scheme.

89. The liquidity and deficit problems of the Tax-Exempt Trust required the Defendants to obtain even more pre-need tax-exempt trust funds from new purchasers and the statutory trusts created by their contracts. These pre-need trust funds were often not invested to

earn interest to pay the funeral expenses of the purchasers who supplied the trust funds; instead, they were used to pay for funeral and burial expenses of earlier pre-need contracts.

90. Because the money Plaintiff deposited pursuant to pre-need contracts is to be paid directly to Plaintiff, and because Plaintiff has an interest in the trust *res*, Plaintiff is a beneficiary of the Pre-Need Trust. Any damage done to the Pre-Need Trust itself is therefore directly done to Plaintiff.

91. The Merrill Lynch Defendants continued their charade even as the life insurance policies started to “completely blow up.” For instance, the minutes from an April 2, 2008 meeting of the IFDA Board of Directors provide:

Ed Schainker and Paul Felsch addressed the Board. There are some policies that need to be exchanged and the death benefits reduced; same to same exchange. Phoenix policy exchanged into a Phoenix policy to lower costs. ***We would definitely have an insurable interest because we did when the policy was opened.*** Ed passed out a list of “A” candidates and “B” candidates. The A candidates are critical investments that we need to do something with or they will completely blow up. The B candidates aren't good investments either, but aren't as critical as the A list. Even though Merrill Lynch provided a list of 10 names on both the "A" and "B" lists, Merrill Lynch says IFDA should plan on converting every Phoenix and Hancock policy to their respective COLI product. The initial list of 10 names simply addresses those policies that require immediate attention. (Emphasis added.)

No disclosure was made to Plaintiff that any investments were about to “completely blow up.”

92. Recommending “exchanging” of policies, instead of liquidating them and disclosing the true situation to IFDA members, furthered Defendants’ fraudulent concealment of the Life Insurance Enterprise. Had the Merrill Lynch Defendants recommended in 2008 that these (and other) life insurance policies be liquidated then, IFDA Services would have been able to find a successor trustee free of conflicts of interest that could have served as a trustee under the Act and avoided further damage and losses to the Tax-Exempt Trust.

93. Rather than acknowledge the liquidity and deficit problems the Life Insurance Enterprise caused the Tax-Exempt Trust, the Defendants, each individually and acting in concert, fraudulently concealed the nature and extent of these problems from Plaintiff and other members of IFDA. IFDA, IFDA Services and the Merrill Lynch Defendants thus issued, or approved the issuance of, documents and reports that credited each pre-need contract purchaser's trust account as though the Tax-Exempt Trust, and thus each purchaser's trust account, had earned tax-exempt interest of 4% per annum all along. IFDA Services continued to pay funeral expenses on the basis of those credited rates instead of the rates the investments actually earned.

94. Upon information and belief, had the Merrill Lynch Defendants invested the Tax-Exempt Trust funds in safe, conservative and tax-exempt investments which complied with the Burial Funds Act, and had Merrill Lynch Defendants not subjected the Tax-Exempt Trust to the excessive commissions, fees and charges they and the Life Insurance Enterprise imposed upon the Tax-Exempt Trust, the Trust would not have had liquidity problems or a deficit. Instead, the income generated from investing funds obtained from Plaintiff's pre-need contract purchasers would have been sufficient to pay the credited rates that Plaintiff has already been paid and the balances of the Tax-Exempt Trust and individual trusts would be substantially higher than they are reported today.

95. Since Plaintiff had and has the statutory right to transfer the Pre-Need Trust funds it had submitted to IFDA Services to a successor trustee, keeping secret the liquidity and deficit problems the Tax-Exempt Trust suffered was critical. Had notice of the Tax-Exempt Trust's deficit or any question of IFDA Services' lack of legal status to serve as trustee been revealed in a clear and timely manner, the Defendants were concerned that Plaintiff and other funeral directors would demand to transfer the trust funds that they had deposited with IFDA Services to

new trustees. To avoid this, the Defendants led the Plaintiff and other IFDA members to believe that the Pre-Need Trust accounts actually were earning 4% each year on a tax-exempt basis.

96. Since the Tax-Exempt Trust was illiquid and running at a deficit, the Defendants knew or should have known that the Trust could not honor substantial trust transfers, especially at the false rates at which they had credited the individual trust accounts. Upon information and belief, the Defendants were concerned that, if it became known that the Tax-Exempt Trust could not honor transfer requests, such knowledge might cause a “run” on the trust when more funeral directors demanded to transfer funds they had committed to IFDA Services.

97. Schainker had always worn at least two hats: he was the IFDA financial advisor working for Merrill Lynch PFS, and was also the insurance broker working for ML Life Agency. With the search for a new trustee, Schainker put on yet another hat, working behind the scenes to convince MLTC to take over as trustee. One day he was answering questions on behalf of IFDA, and the next he was purporting to represent one of the many involved Merrill Lynch entities.

98. The liquidity and deficit problems in the Tax-Exempt Trust grew larger as the years went on. As early as 2001, the independent auditors of the Tax-Exempt Trust reported that the Trust had a deficit of more than \$10 million. No notice of the audit report was given to Plaintiff or other IFDA members. Instead, they were advised that the trust funds they had committed to IFDA Services had again earned 4%.

99. By May 2005, a compliance audit conducted by an accounting firm for the Illinois Office of the Comptroller (“IOC”) found that the Tax-Exempt Trust was underfunded and thus had a deficit of more than \$38 million. Again, no notice of this deficit was given to the Plaintiff

or other IFDA members. In 2006, the deficit had risen to more than \$41 million. By July 2008, it was in excess of \$54 million.

100. Rather than disclose the material facts regarding the deteriorating state of the Tax-Exempt Trust, with Merrill Lynch's assistance, the existing IFDA Board requested that the conclusions be kept secret. Purportedly relying on representations of the Merrill Lynch Defendants that the audit results were incomplete and inaccurate and on the advice of the Sorling Defendants, IFDA and IFDA Services asked that all audit related materials be protected from Freedom of Information Act requests. Upon information and belief, IFDA acted to keep these results secret, and conveyed the requests for secrecy to the IOC through the Sorling Defendants.

101. Despite this serious turn of events, and even though Defendants knew or should have known about the serious financial problems facing the Pre-Need Trust, on October 4, 2007, IFDA sent all of its members a letter informing them of the IOC's recent license revocation but promising that "there is no need for concern. All of the funds that Illinois funeral homes and their clients have placed into IFDA trust have been safely invested, and all of the money is accounted for." In fact, Defendants were recommending continued investment in the Pre-Need Trust through much of 2008.

VI. THE ILLINOIS DEPARTMENT OF INSURANCE BEGINS INVESTIGATING THE VUL INSURANCE POLICIES.

102. Sometime in 2006, the Illinois Department of Insurance (the "DOI") began investigating whether the VUL policies the Merrill Lynch Defendants sold complied with Illinois insurance laws. In October 2006, the general counsel for the DOI specifically requested that IFDA Services explain how it had an insurable interest in any of the purported key man policies. No notice of this investigation or of this specific request was given to Plaintiff.

103. By May 18, 2009, the DOI formally disclosed its conclusion that no insurable interest existed in the key man policies. On that date, the DOI issued an Order of Revocation which revoked Schainker's license as an Illinois insurance producer. In revoking his license, the DOI found that:

[Schainker] designed, recommended and sold his program to IFDA despite his awareness that the policies, from which he personally derived substantial income, did not comply with Illinois insurable interest laws and, further engaged in such conduct without regard to the potential negative impact on nearly 50,000 individuals and families throughout the State.

The variable universal life insurance policies sold to IFDA did not satisfy insurable interest requirements under Illinois law.

(A copy of the May 18, 2009 Order of Revocation is attached as Exhibit G.)

104. Schainker stipulated to an Order of Revocation rather than contest and submit to a hearing before the DOI.

VII. IFDA SERVICES' INABILITY TO SERVE AS TRUSTEE OF THE PRE-NEED TAX-EXEMPT TRUST IS FINALLY DISCLOSED.

105. Even before the regulators were knocking on IFDA's door, aware that IFDA Services could not serve as a Trustee of the Tax-Exempt Trust, and aware of the Trust's growing financial problems, the Defendants sought to obtain a new trustee and sought to have MLTC put in charge of the Tax-Exempt Trust.

106. Defendants' motive in seeking to have MLTC installed as trustee was obvious. MLTC would not only earn sizeable fees, it also would not investigate claims against the parties who damaged Plaintiff and the Tax-Exempt Trust, would not demand that Defendants provide just compensation to Plaintiff and other damaged IFDA members or restore the thousands of individual trusts commingled therein, and would not bring any actions for any such relief.

107. In September 2007, IFDA Services' inability to serve as Trustee under the Act was publicly disclosed. On September 17, 2007, the IOC formally informed IFDA Services that the license that had been issued to IFDA Services to serve as trustee under the Burial Act long ago was void *ab initio*. The IOC further advised that IFDA Services never had any legal capacity to serve as trustee for Pre-Need Trust funds under the Burial Funds Act. As a consequence, Plaintiff and other IFDA members were defrauded into depositing trust funds with IFDA Services even though the deposits were not technically made in accordance with Section 1 of the Burial Funds Act. Despite IFDA Service's lack of legal capacity to serve as a Trustee under the Act, the IOC established September 30, 2008 as "a reasonable deadline" for IFDA Services "transition to a lawful trust maintained in accordance with the IFBF Act." A copy of this notice is attached as Exhibit H.

108. On December 24, 2007, MLTC terminated – for the time being – discussions regarding becoming a successor trustee to IFDA Services. IFDA Services therefore needed to find a new successor trustee.

VIII. IFDA SERVICES NEGOTIATES WITH REGIONS BANK TO BECOME SUCCESSOR TRUSTEE.

109. In early 2008, Regions Bank ("Regions") tentatively agreed to become a successor trustee to IFDA Services, subject to the results of its due diligence investigation.

110. After conducting due diligence on the VUL policies, Regions concluded by April 2008 that it could not serve as a trustee unless the VUL policies were surrendered. Among other reasons, Regions concluded, without even considering whether IFDA Services had an insurable interest in them, that the ongoing costs of maintaining the VUL policies far exceeded any expected benefit from the policies. Indeed, upon information and belief, the cost to the Trust of maintaining these policies was 25 to 30 basis points per month of the amount in the policies.

These hidden costs of the insurance program – costs that were being paid to the Merrill Lynch Defendants and the insurers – were estimated to be between \$5.5 million and \$6.5 million per year. The Merrill Lynch Defendants opposed Regions’ plan to liquidate the policies. They had a clear economic interest in doing so, as the fees, commissions, premiums and other income they earned from the Life Insurance Enterprise would be eliminated if the policies were liquidated. Apparently still listening to the advice of the Merrill Lynch Defendants, and Schainker in particular, IFDA Services and the Sorling Defendants also opposed the liquidation of the policies. Accordingly, Regions declined to accept the trustee position.

IX. THE ILLINOIS DEPARTMENT OF FINANCIAL AND PROFESSIONAL REGULATION REJECTS IFDA SERVICES’ TRUST COMPANY APPLICATION, APPOINTS MLTC AS INTERIM TRUSTEE AND FORMALLY FREEZES THE TRUST ASSETS.

111. On May 30, 2008, the IDFPR issued an Order to Cease and Desist against IFDA Services finding, *inter alia*, that IFDA Services did not have a certificate of authority to conduct a trust business and thus violated the Illinois Corporate Fiduciary Act, 205 ILCS 620/2-4. The IDFPR likewise ordered IFDA Services to cease and desist from conducting a trust business, holding itself out to the public as a fiduciary, and accepting Pre-Need Trust funds as Trustee, among other things. The IDFPR found that IFDA Services did not meet the standards for receiving a certificate of authority under Illinois’ Corporate Fiduciary Act. Finally, the May 30, 2008 Order installed MLTC as an interim trustee for the Tax-Exempt Trust. A copy of this Order is attached as Exhibit I.

112. On June 25, 2008, IFDA held its annual meeting in Schaumburg, Illinois. At the annual meeting, the president of IFDA advised that an actuarial study was being prepared for the Tax-Exempt Trust. Upon information and belief, that study was paid for by Defendant ML Life Agency at the request of the Director of the DOI. No disclosure was made that ML Life Agency

paid for the study, nor has the study been publicly revealed. As a consequence, the Defendants have further acted to fraudulently conceal the nature and extent of the damage the Life Insurance Enterprise caused the Tax-Exempt Trust by concealing the results of this study.

113. Also at the annual meeting during, on the afternoon of June 25, 2008, some details concerning the VUL policies were disclosed to Plaintiff and the rest of the IFDA membership. The partial disclosure, however, was misleading and incomplete. No disclosure was made, for example, that IFDA Services had purchased MECs. Indeed, Schainker specifically represented to the IFDA membership at that meeting that none of the VUL policies were MECs.

114. On July 7, 2008, the IDFPR issued a Second Cease and Desist Order against IFDA Services. The Second Order prohibited IFDA Services from disbursing, expending, paying out any dividends, liquidating, loaning, refunding, or in any way alienating funds currently in its possession other than to pay burial or funeral claims. A copy of the second IDFPR Order is attached as Exhibit J.

115. Even after MLTC was given duties as an interim trustee, the Merrill Lynch Defendants continued to falsely deny that any of the VUL policies were modified endowment contracts.

116. On August 1, 2008, IFDA issued a memorandum to Pre-Need Trust participants, responding to requests for additional information as to how the Pre-Need Trust funds had been invested. This request for more information from participants further illustrates the utter lack of transparency that had been available to funeral home directors. This memorandum quotes Schainker:

IFDA Tax Advantaged Preneed Trust has historically been allocated conservatively with the majority of funds invested in the bond market, represented

through US Treasuries, government agencies, and corporate debt instruments. The current allocation as reflected in the attached report reflects approximately 65% of the total assets allocated to bonds and cash, and 35% to equities with both domestic and international exposure. The portfolio is managed for risk, with the volatility of the portfolio trading at approximately a 66% discount to the volatility of the S&P index. It should be noted that conservative or low risk portfolio allocation does not prevent negative performance.

Consistent with other misrepresentations, half-truths and concealments of material fact, Schainker's explanation omitted any mention of the existence of the life insurance policies, the impact they had on the liquidity of the Trust's funds, or how they factored into the Trust's available assets and deficits. Had Schainker and the Merrill Lynch Defendants not acted fraudulently to conceal their conduct and materially mislead Plaintiff, Plaintiff would have taken actions to protect the Pre-need Trust funds it had deposited earlier.

117. On November 3, 2008, the IDFPR issued a third Cease and Desist Order that again ordered that IFDA Services Cease and Desist from acting as a trustee with respect to the Tax-Exempt Trust. The November 3, 2008 Order specifically found that "IFDA [Services] continues to act as trustee of certain pre-need funeral trusts without authority" and that "the liquidity of IFDA trusts is severely impaired." Continuing its policy forbidding any disbursements other than to pay funeral or burial claims, the November 3, 2008 Order froze the Pre-Need Trust funds in the VUL policies. A copy of the IDFPR's third Order is attached as Exhibit K.

X. MLTC BECOMES PERMANENT TRUSTEE AND DISAVOWS OBLIGATIONS TO RESTORE LOSSES TO THE TRUST CAUSED BY ITS AFFILIATES.

118. On October 15, 2008, IFDA Services announced that MLTC would permanently assume the role of Trustee of the Tax-Exempt Trust, effective October 23, 2008. It did so not as a successor trustee, but pursuant to a separate trust agreement.

119. In connection with MLTC's assumption of the role of Trustee, Plaintiff was required to sign an agreement under which Plaintiff expressed its "desire[] to appoint MLTC as Trustee of the Trusts pursuant to Section 45/2(g) of the Act." (See MLTC Trustee Agreement, attached hereto as Exhibit L.)

120. As a condition of taking on the duties of Trustee, the agreement MLTC demanded Plaintiff and other funeral directors sign specifically excluded and disclaimed any obligation on its part to investigate or bring any actions against others, including its affiliates, who caused the Tax-Exempt Trust to sustain significant damages through the Life Insurance Enterprise. It also purported to waive the accounting requirements contained in the Illinois Trusts and Trustees Act, as amended, and corresponding provisions of other laws. Exhibit L, ¶ 25. As a result, the MLTC Trustee Agreement is against public policy.

121. Plaintiff did not have the ability to object to or negotiate the terms of this Agreement and only signed the document under duress. In particular, Plaintiff was informed that, if the Agreement was not signed under the precise terms that MLTC required, the IOC would revoke Plaintiff's license to operate as a Seller under the Burial Funds Act and thus would be put out of business. (See 10/24/2008 Letter from IOC to IFDA members, attached hereto as Exhibit M.)

122. As a consequence, and because the Trustee Agreement is against public policy, Plaintiff did not voluntarily agree to be bound by the terms of the Agreement and thus is not bound by its terms, including the terms under which MLTC purported to exonerate itself from any obligation to investigate the wrongdoing of any other parties, including its affiliates. Nor is Plaintiff bound by any provisions that would allow MLTC to release any parties, including insurance companies, from claims relating to the Life Insurance Enterprise.

123. Upon information and belief, the Merrill Lynch Defendants acted to place MLTC as an interim trustee and then as the permanent Trustee because they correctly believed that MLTC would not attempt to investigate, much less sue, its affiliates and all others who are responsible for the losses to the Tax-Exempt Trust. As it turned out, they were correct; MLTC has taken no action at all to recover damages to the Tax-Exempt Trust.

124. Moreover, MLTC, under the guise of becoming Trustee, assumed an integral role in the continued implementation of the Life Insurance Enterprise. It was fully aware of the millions of dollars per year that maintenance of the insurance policies was costing the Trust, yet it did not promptly eliminate those costs. Instead, MLTC continued to maintain the policies and rode the market to its bottom in the fall of 2008.

125. Upon information and belief, MLTC began the process of surrendering the VUL key man insurance policies in 2009 or the beginning of 2010. Upon information and belief, the process of surrendering the policies has now been substantially completed, with MLTC realizing considerably less for the beneficiaries of the Trust than it would have had it acted prudently, all the while preserving, for as long as possible, fees and commissions for the Merrill Lynch Defendants.

126. Additionally, upon surrendering the policies, MLTC has purported to release each of the insurers from any liability for issuing policies that violated Illinois law and were essential to effectuate the Life Insurance Enterprise. Because the policies were MECs, and because the owner of the policies was a corporation or trust, the supposedly Tax-Exempt Trust has paid or will be required to pay millions of dollars in income taxes and excise tax penalties from these surrenders.

127. On November 23, 2009, MLTC notified funeral directors in writing of its intent to resign as a trustee of the IFDA Pre-Need Trust, effective as soon as a new or successor trustee is designated. More specifically, the notice that MLTC sent to funeral directors on November 23 informed them that its resignation would become effective upon MLTC's receipt of written notice from the funeral director that a successor trustee had accepted the office of trustee for that funeral director's pre-need accounts. It further provided that, if, within 60 days of the notice, the funeral director did not select a successor trustee, MLTC reserved the right to petition the court to appoint a successor. While notifying Plaintiff and other funeral directors of its resignation, upon information and belief, MLTC made no attempt to similarly notify the 50,000 individual pre-need consumers across the state of Illinois. Recently, IFDA Services announced that Fiduciary Associates has agreed to become a successor trustee to those accounts remaining in the IFDA Pre-Need Trust.

128. Neither MLTC's purported role as Trustee, nor the role of any successor trustee, prevents Plaintiff and other IFDA members from asserting claims for the trust funds they submitted to IFDA Services.

XI. THE LOSSES TO THE TAX-EXEMPT TRUST AND SUBSEQUENT TRUSTS.

129. The losses the Tax-Exempt Trust has suffered, and thus the damages the individual trusts and trust accounts have sustained, are staggering. A preliminary review of (1) the actual cash flows the Tax-Exempt Trust received from pre-need purchasers who chose the tax-exempt option, (2) all the administrative expenses actually charged to the Tax-Exempt Trust, including the fees paid to IFDA Services and any fees paid to Plaintiff and other IFDA members; (3) the published rates paid over time for tax-exempt money market funds, intermediate notes and long term bonds, and (4) the actual payments of funeral and burial claims, reveals the magnitude of these damages. As of September 2009, based on information made available, the

value of the Tax-Exempt Trust was approximately \$135,000,000. Had the Defendants followed a safe, conservative, laddered, compliant investment strategy of investing in tax-exempt investments, upon information and belief the Tax-Exempt Trust would then have had a value of approximately \$280,000,000. Plaintiff would not have incurred, and would not continue to incur, the damages as outlined herein.

130. In other words, the damages to Plaintiff and the trusts commingled in the Tax-Exempt Trust that were directly and proximately caused by the intentional, illegal and unconscionable conduct of the Defendants and the Life Insurance Enterprise is estimated to be in excess of \$145,000,000.

131. The Pre-Need Trust accounts that Plaintiff established for its customers have suffered hundreds of thousands of dollars in damages stemming from the deficit in the Pre-Need Trust as a direct and proximate result of Defendants' conduct, and this number will only continue to grow. Plaintiff has also incurred damages based on injuries to its goodwill and reputation, and lost business opportunities due to the stigma now associated with pre-need contracts due to Defendants' conduct.

CAUSES OF ACTION

COUNT I

UNFAIR AND DECEPTIVE PRACTICES AGAINST ALL DEFENDANTS

132. Plaintiff hereby re-alleges and incorporates by reference the allegations set forth in Paragraphs 1 through 131 as paragraph 132, as though set forth in full herein.

133. At all relevant times, the Illinois Consumer Fraud and Deceptive Business Practices Act, 815 ILCS 505/1 *et seq.* ("the ICFA") was in effect. Paragraph 505/2 of the Act provides:

Unfair methods of competition and unfair or deceptive acts or practices, including but not limited to the use or employment of any deception, fraud, false pretense, false promise, misrepresentation or the concealment, suppression or omission of any material fact, with intent that others rely upon the concealment, suppression or omission of such material fact, ... in the conduct of any trade or commerce are hereby declared unlawful whether any person has in fact been misled, deceived or damaged thereby.

134. The ICFA further provides as follows:

Any person who suffers actual damages as a result of a violation of this Act committed by any other person may bring an action against such person. The court, in its discretion may award actual economic damages or any other relief which the court deems proper.

815 ILCS 505/10(a).

135. The ICFA further defines a “person” to include a “corporation,” a “trust” and/or the “trustee or *cestui que trust* thereof.” 815 ILCS 505/1(c). Plaintiff, whether individually, as a beneficiary, and/or as a statutory trustee relating to its sales of pre-need contracts, is a “person” within the meaning of Section 1(c) of the ICFA.

136. Plaintiff has suffered actual damages within the meaning of Section 10a of the ICFA, 815 ILCS 505/10a(a).

137. Defendants, individually and as a group, had the statutory duty under the ICFA to refrain from unfair or deceptive acts or practices and the concealment, suppression or omission of material facts in promoting and engaging in the Life Insurance Enterprise. Defendants, individually and as a group, violated that duty in numerous ways, including but not limited to:

- (a) making false and misleading statements regarding the Tax-Exempt Trust;
- (b) failing to disclose that IFDA Services had purchased VUL insurance policies that were in violation of the Burial Funds Act;
- (c) failing to disclose that no actuarial studies were performed to determine the liquidity needs of the Tax-Exempt Trust;

- (d) failing to advise IFDA Services to invest funds deposited in the Tax-Exempt trust in compliance with the Burial Funds Act;
- (e) failing to disclose that the Tax-Exempt Trust was illiquid and suffering a deficit;
- (f) failing to disclose that IFDA Services, as Trustee of the Tax-Exempt Trust, had no insurable interest in any of the “key man” VUL policies;
- (g) failing to disclose that many of the VUL policies were MECs which would have adverse tax consequences and were inconsistent with the purportedly Tax-Exempt Trust;
- (h) failing to disclose that the Merrill Lynch Defendants obtained significant hidden premiums, commissions and fees through the Life Insurance Enterprise, years after the policies were issued;
- (i) failing to disclose that crediting rates did not correspond with the actual financial performance of the Tax-Exempt Trust and that the thousands of pre-need purchasers’ trusts that were commingled within the Trust were not accurately stated;
- (j) failing to disclose that the Defendants intentionally withdrew or used trust funds for their own personal benefit;
- (k) failing to disclose that VUL policies, or amendments thereto, were issued on the basis of forged signatures; and
- (l) concealing their conduct and their participation in the Life Insurance Enterprise

138. Additionally, MLTC had the statutory duty under the ICFA to refrain from unfair or deceptive acts or practices and the concealment, suppression or omission of material facts in

promoting and engaging in the Life Insurance Enterprise and violated that duty in numerous ways, including but not limited to:

- (a) failing to disclose that it was in the best interests of the Tax-Exempt Trust to liquidate immediately in order to reduce costs and stop damages to the Trust *res*;
- (b) failing to act in the best interests of the beneficiaries of the Trust;
- (c) failing to protect the beneficiaries' assets by purporting to release liability of third parties who dissipated Trust assets;
- (d) failing to disclose and taking affirmative steps to conceal the true financial condition of the Tax-Exempt Trust;
- (e) accepting the office of successor trustee when it knew or should have known that it was not a licensed foreign corporate fiduciary under Illinois law; and
- (f) failing to act ethically in light of the numerous conflicts of interest that disabled it from taking action against those who had inflicted and continued to inflict damages on the Tax-Exempt Trust.

139. As described herein, Defendants' violations of the ICFA and the Burial Funds Act, their material misstatements and omissions, and their unfair, unethical and unscrupulous conduct, occurred in a course of conduct involving trade or commerce and are unlawful. The Defendants engaged in wrongful conduct while at the same time obtaining, under false pretenses, significant sums of trust fund money from Plaintiff and its pre-need customers.

140. At all relevant times, Schainker, Summer and Felsch acted as the employees and/or agents of Merrill Lynch PFS and ML Life Agency. Merrill Lynch PFS and ML Life Agency are therefore liable for the actions of Schainker, Summer and Felsch.

