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Funeral fund runs a deficit

Pre-need trust financed with life insurance policies

By BRUCE RUSHTON
STAFF WRITER

Published Monday, February 25, 2008

A trust fund designed to pay funeral expenses for nearly 50,000 participants is running a $40 million deficit and has been paying out more than it has been taking in.

The Illinois Funeral Directors Association, which administers the fund, says it is solvent. But, at the behest of state regulators, the IFDA has decided to put a third-party trustee in charge of the $300 million Preneed Trust.

The trust currently is being kept afloat with life insurance policies taken out on IFDA board members, funeral home directors and association members. According to the IFDA board of directors, the insurance policies are worth about $160 million, more than enough to balance the books. But people have to die before money goes in the bank, and the IFDA says it will stop using life insurance as an investment tool.

Joshua Slocum, executive director of the Funeral Consumers Alliance, a watchdog group based in Vermont, said he has never heard of a funeral trust fund financed with life insurance policies on industry insiders.

"This is a perilous business practice," said Slocum, who keeps tabs on funeral trust funds across the nation. "It sounds like something you'd hear in a bad mafia movie. You're taking a gamble that your guys are going to die soon enough."

A consultant to the funeral industry disagrees.

While using life insurance to fund a pre-need funeral trust isn't common, there's nothing wrong with it, said Daniel Isard, president of The Foresight Companies in Phoenix, Ariz.

"I don't think there's anything illegal," Isard said. "I don't think there's anything immoral about the practice. Certainly, on the surface, it sounds negative. We don't see it in a lot of other trusts because most other trusts are not that large."

Not all of the money paid out by the IFDA has gone for funerals. The association also has been paying guaranteed interest to funeral homes that collect money from pay-in-advance customers and deposit it in the fund.

"We have typically offered (interest) rates that may have been in excess of what our investment returns have been," said Charles Childs, the IFDA's past president. "There were some guarantees, correct. In the future, we might not be able to do guarantees like we have in the past."

Consumers aren't at risk, Childs said. "No death claims have ever gone unpaid," he said. "We don't anticipate anybody's money to be in jeopardy at this point in time."

But a memo distributed to funeral directors makes clear that the fund has problems.

In the Feb. 15 memo, the IFDA board acknowledged a $40 million deficit and said the fund will be in trouble if beneficiaries all die at once or if money is withdrawn before the trust can collect on the insurance policies that are shoring up the fund. The board also said that it cannot predict when the association will get its financial house in order.

In the memo, the board says financial troubles are "a complex issue."

“The simple answer is that we paid out more in benefits than we made in our investments,” the memo states.

Officials with the state comptroller’s office have been concerned since 2006, when the state hired an accounting firm to examine the fund’s structure. The firm, McGladrey & Pullen, identified several potential problems in addition to the guaranteed interest and use of life insurance to make ends meet:

***** In 2005, IFDA Services, the subsidiary of the IFDA that administers the fund, received at least $515,000 more in fees than allowed by state law, which caps the amount of fees at 25 percent of earnings. The excess amount may have been as high as $1.4 million, McGladrey & Pullen reported. The IFDA disputes that any excessive management fees were paid to IFDA Services.

***** The trust had no written policy stating what information should be in loan files, and two of five loan files examined by McGladrey & Pullen had no credit reports for borrowers. In one case, a borrower was a member of the IFDA board, the firm reported. Childs disagreed with the finding and said the association has had policies in place “for some time.”

***** The trust did not require death certificates before paying out claims, and at least one claim was paid without any record of a death certificate. Childs said the issue has been rectified and no funds are paid unless the trust is convinced that a death has occurred.

***** One loan file did not include any sign that the loan had been approved by the trust’s loan committee. In addition, at least five IFDA board members had obtained loans from the fund, and no credit report could be found for one board member who borrowed. Childs disputed the finding, saying that anyone who borrows money from the fund must submit a proper application.

“The comptroller’s office did issue a report that indicated we had some assets-and-liabilities issues,” Childs said. “They’ve also suggested that we were bit larger than they’re used to regulating.”

Since the report was issued, IFDA officials have met several times with officials from the comptroller’s office, which has decided it should not have licensed the fund nearly three decades ago, said Carol Knowles, spokeswoman for state comptroller Dan Hynes.

“There were some things we saw that raised concerns,” Knowles said. “One of them was a higher interest rate being paid out than what they were earning.”

The comptroller’s office in 2006 told the IFDA that the trust should be regulated by the Illinois Department of Financial and Professional Regulation. In September, the comptroller’s office voided the fund’s license after concluding the comptroller’s office isn’t the proper regulatory agency, Knowles said.

The IFDA applied for Financial and Professional Regulation oversight in November 2006. The application is pending. In its Feb. 15 memo, the IFDA board told funeral directors that Regions Morgan Keegan, a Memphis-based investment firm, will manage the fund.

“We certainly believe the agreement we’re entering into with a third-party trustee will satisfy the regulators and consumers and funeral homes that are participants in the trust,” Childs said. “None of us funeral directors have the time or the expertise to manage a trust of this magnitude.”

Bruce Rushton can be reached at 788-1542.

How pre-need funerals work

Pre-need funerals typically are purchased by people who don’t want their loved ones to do anything but mourn after they’re gone.

The price of a contract — and what it covers — varies. In general, buyers pay for goods and services such as memorial services, caskets and burial vaults that are guaranteed to be provided upon death, no matter how much costs have increased.

The money paid is invested until it is needed.

In Illinois, funeral homes can operate their own pre-need investment funds, or they can put pre-need money into the Preneed Trust, an investment pool operated by the Illinois Funeral Directors Association.

More than 600 funeral homes participate in the Preneed Trust, which administers funds paid in by more than 49,000 people. The trust, established in 1979, currently has assets totaling $300 million.

Source: Illinois Funeral Directors Association

— Bruce Rushton

Consumer alliance, funeral industry disagree about pre-paying expenses

Some experts say pre-need funerals are a bad deal for most consumers.

“Prepaying for your funeral is a terrible idea,” said Joshua Slocum, executive director of the Funeral Consumers Alliance, a non-profit group that acts as a watchdog on the funeral industry. “This is a national scandal.”

Only people who need to shelter money from Medicaid should consider pre-need contracts, Slocum said. AARP, which acts as an advocate for the elderly, agrees. The group recommends that consumers who want to plan their funerals should put some money aside in banks instead of giving it to funeral homes.

The funeral industry takes exception to those arguments.

“It makes sense to do it so children aren’t burdened,” said Daniel Isard, president of The Foresight Companies, a Phoenix-based consulting firm to funeral homes. “It doesn’t matter about the math. It matters about the peace of mind.”

But Isard and critics of pre-need funeral plans agree on at least one thing: Consumers need to make sure they know what they’re buying.

The industry is huge. Isard estimates $60 billion is being held in pre-need funeral or cemetery trusts in the United States, and about $10 billion is deposited in those trusts each year.

With the exception of New York, no state has adequate laws to protect purchasers of pre-need funerals, Slocum said. He criticized Illinois for not requiring that all moneys from consumers be deposited in trust. He also faults Illinois for not requiring full refunds if consumers change their minds.

“There’s all kinds of hinky stuff in Illinois law,” Slocum said.

Illinois law allows funeral homes to keep 5 percent of the money when someone signs a pre-need funeral contract. Beyond that, the law allows pre-need contract sellers to keep 15 percent of the price of burial vaults.

“No goods or services have changed hands,” Slocum said. “They’re basically paying themselves for nothing.”

Illinois doesn’t require full refunds if consumers on installment plans miss payments or if a purchaser doesn’t end up using services. By contrast, New York requires that all moneys received from consumers be put in trust, and full refunds are required, Slocum said.

AARP says that consumers should have any contracts reviewed by a lawyer before signing. That might be going overboard, Isard said.

“This is an industry that is, by and large, as ethical as they come,” Isard said.

Critics say funeral homes often lock in consumers so that they can’t get services from another provider if they move to another state. Isard agreed that consumers should ask whether they will be required to use a certain funeral home.

“Portability is a critical point,” Isard said. “Make sure that the terms and conditions are what you want.”

Rather than purchase pre-need funerals, AARP says consumers should set up bank accounts for funerals and give trustworthy friends or relatives — not funeral directors — access to the money upon death.

Other tips from the AARP and the Funeral Consumers Alliance include:

***** Inquire about refunds and cancellation penalties.

***** Ask how your money will be invested. If it will be used to buy an insurance policy, get the name of the insurance company. If the money is going into a trust account, ask what financial institution will be in charge of the trust.

***** Find out what happens if plans change. If you move to another state, can you get a refund? If the funeral home is sold, will the contract be honored? If the casket you want isn't available, what other arrangements will be made?

— Bruce Rushton

Reader Comments - 47 comments

***James* wrote at 2/25/2008 4:35:16 AM**

Sounds like,dang if you do and dang if you don't.I know some one who is going through this now,the casket that was paid for "is no longer made".So people should really look into this before they make the move in to this plan.

***Question* wrote at 2/25/2008 6:44:47 AM**

If forever reason this fund does become insolvent would that mean bodies would just sit and wait until it's fought out in court or someone finds other means to pay?

***Dan Rogers (78)* wrote at 2/25/2008 7:27:39 AM**

Dan Hynes has been in Office for 10 years and he is just now making this public? How much campaign has the IFDA given to Mr. Hynes in 10 years maybe that would explain why..I've been paying for 11 years and now my family is out of luck.. Just another democrat pay to play ploy at the expence of Illinois elderly..

***Barbara* wrote at 2/25/2008 7:30:21 AM**

My Mother had a pre-paid plan, for what it was worth. I was with her when she purchased it. When the day came to use it, I was told we had additional charges for use of viewing room, an urn, did I want her hair done (she was going to be cremated!) On and on. You can imagine what I told them.

***Family Guy* wrote at 2/25/2008 7:37:18 AM**

Why not just by life insurance your self?? & Take care of your loved ones your self.

***How come* wrote at 2/25/2008 7:44:24 AM**

major problems we talk about in this country involve two main entities called government and insurance?

***The concluding paragraph tells it all* wrote at 2/25/2008 8:28:53 AM**

“None of us funeral directors have the time or the expertise to manage a trust of this magnitude."

***Northwest Illinois* wrote at 2/25/2008 8:29:37 AM**

My parents both have pre-paid/pre-arranged funerals. When my mother passed away, the funeral home was very helpful and everything went fine, from shipping her back to Illinois, to the music played, to the actual service. Of course, my parents had covered every detail before they left the state. I am hopeful that things will go as well when my father passes. The funeral home we used has been in business for a very long time with a history of good service, so I am sure that makes a difference, too.

***Something Smells Rotten....* wrote at 2/25/2008 8:39:59 AM**

Loans to members....no evidence or paperwork??? And the excuse that they were not making as much on their money as they were paying out doesn't float either. Maybe a few thousand difference here and there but $40 million??? Come on people. Sounds like someone is doing some back door financing or scraping a little off the top. Gee, what a shock that would be huh? And our government is involved. You know, the guys who write more checks that they have money in the bank. Then they say "Huh, why lookie there, we are millions in debt." If it were complicated I might be able to sorta understand, but we are talking about basic math here folks.

***Area Funeral Director* wrote at 2/25/2008 8:44:45 AM**

Please know that not all funeral homes invest their pre-need money in IFDA. We use a life insurance product that is used specifically for pre-need funerals. The money is not in the hands of the funeral home until the death has occurred. Almost all funeral homes, including the ones who use IFDA for funding, are extremely trustworthy establishments who's main goal is to help families in their time of need.

***To Barbara:* wrote at 2/25/2008 8:47:38 AM**

A pre-arranged funeral covers only the items that you agreed upon when the contract was made. The funeral director should have made you aware of that fact, but if you chose not to include those items, but did wish to use them, you would have to pay for them. If I hire a contractor to remodel a bathroom, but then decide to also do my kitchen, I would expect to pay for that extra service.