

CEMETERY AND FUNERAL BUREAU

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July 1, 2010

All Participating Funeral Establishments
(See attached mailing list)

RE: Reply to Audit Response of Cemetery Funeral's Audit of the CMT issued March 16, 2010

To All Participating Funeral Establishments:

The Department of Consumer Affairs' Cemetery and Funeral Bureau is in receipt of the response to the Bureau's above-mentioned audit findings regarding the California Master Trust (CMT). In the Bureau's March 18, 2010 memo to all funeral establishments participating in the CMT, the Bureau directed each establishment to submit to the Bureau its resolution to the deficiencies noted in the Bureau's audit report. On March 19, 2010, the Bureau provided notice to the participating establishments that the Funeral Director's Service Corporation (FDSC) and Comerica Bank would be preparing a response to the audit by April 30, 2010, after which the Bureau would determine whether any amended findings would be required.

Copies of the Bureau's audit report and the response submitted by Comerica Bank and FDSC to the audit report are found on the enclosed CD. If you need a hard copy, please contact the Bureau at (916) 574-7870 / emailcfb@dca.ca.gov

Comerica Bank and FDSC raised a variety of legal arguments in their response to the audit findings. The Bureau considered these arguments but found them without merit. The Bureau expects all of its Corrective Actions to be implemented. The Bureau's reply to the auditee's response to the findings follows.

Finding 1: FDSC Is a De Facto Trustee in Violation of BPC Section 7736

Bureau's Reply: The response provided no basis for amending this finding.

With respect to the corrective actions required, FDSC and Comerica Bank "propose that they will cause to be removed from the CMT website and all future written materials" information that they believe could infer that the State of California authorized Comerica to serve as the trustee of CMT. If this means that Comerica and FDSC are immediately making efforts to remove any inferences that the State of California authorized Comerica to serve as the trustee of CMT or that the Department of Consumer Affairs reviews the CMT trust program annually, then this would correct the deficiency identified in Corrective Action No. 3 going forward.

With respect to the responses to Corrective Actions Nos. 1 and 2, FDSC and Comerica Bank request assistance from the Bureau to "ensure that the Amended Trust Agreement is satisfactory to the Bureau going forward." It is the Bureau's position that the Trust Agreement must reflect that the responsibility for managing and administering the CMT rests with a legally

valid Trustee (i.e., one that meets the requirements of Section 7736 of the Business and Professions Code). It is the Trustees' responsibility to draft an agreement that meets all legal requirements and ensures that trust powers are not improperly delegated to an entity not meeting the requirements of Section 7736. Based upon the response to the audit, it appears that Corrective Actions Nos. 1 and 2 have still not been implemented.

Finding 2: Payments Made in Violation of BPC Section 7735

Bureau's Reply: The response provided no basis for amending this finding.

With respect to the corrective actions required, FDSC and Comerica Bank "propose to agree to seek the Bureau's approval of any formal disparity resolution in the future" and seek advice and a letter of opinion from the Bureau or the Attorney General's office. The audit report explains the Bureau's opinion with respect to this finding and the factual and legal basis for finding the disparity resolution violated Section 7735. The Bureau's findings in this regard would be equally applicable to a similar disparity, should one occur "in the future." Based upon the response, however, it appears that none of the Corrective Actions have been implemented. The Corrective Actions must be implemented.

Finding 3: Trustees Failed to Return The Corpus To The Funeral Establishments Or Trustors as Required by BPC Section 7737

Bureau's Reply: The response provided no basis for amending this finding.

With respect to corrective action No. 1, FDSC and Comerica Bank request an opinion from the Bureau about "how to resolve the obvious and unresolved conflict that exists between GAAP and Business & Professions Code §7737..." However, Comerica Bank and FDSC do not identify what this "obvious conflict" is. Regardless, Comerica Bank and FDSC were provided with a written opinion explaining their responsibilities to return the corpus of the CMT on July 2, 2009. Their response does not include any resolution to stop and correct this past practice.

With respect to corrective action No. 2, the Trustees propose to return "to the trustors or their legal representatives their pro rata share of the \$23,807.09 difference in market to book value for these contracts." The Bureau agrees that refunds should be returned to these affected trustors or heirs. However, the Bureau has no way of verifying that this refund calculation is true and accurate because Comerica Bank and FDSC have failed to provide the documentation and raw data to support this refund calculation. In addition, Comerica Bank and FDSC have not explained how this practice will be corrected to ensure that this violation does not occur again going forward.

The Bureau also asserts that similar remuneration needs to be made for the other findings requiring remuneration including for Findings Nos. 2, 4 and 5 of the Audit Report. Further, this response does not specifically address the provision of records requested by the Bureau in accordance with Title 16 CCR section 1267.

As a result, these corrective actions have not been implemented.

Finding 4: Trust Paid Unauthorized "Participation Distributions" To Funeral Establishments in Violation of BPC Section 7735

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, Comerica Bank and FDSC propose to "develop and require a form to be completed by each funeral establishment.... which will list the funeral establishment's actual administrative costs, with backup documentation, related to its costs of administration." This is not an acceptable corrective action because funeral establishments are not responsible for administering trust operations that are the Trustee's obligation to perform. As a result, these corrective actions have not been implemented.

Finding 5: Trust Paid Unauthorized Fees to FDSC in Violation of BPC Section 7735

Bureau's Reply: The response provided no basis for amending this finding. However, the Bureau is revising its original estimate of the amount of monies retained by FDSC, on pages 3 and 26 of the Audit, based upon further internal review. The original estimates of the outstanding balance retained by FDSC, the remaining balance that was received for non-trust costs, and amounts paid to contractees performing administrative services were \$3,104,474, \$8,798,114, and \$7,373,957, respectively. The new balances are hereby revised to state \$2,030,418, \$7,724,058, and \$8,448,013, respectively.

In response to the Corrective Actions requested, Comerica Bank and FDSC have proposed and agreed to file a form the Trustee is already required by law to accurately complete, and then file it with the Bureau (see form requirement in Title 16 CCR § 1269). The most recent report for CMT was filed at the same time as this response was provided to the Bureau on April 29, 2010. However, that report failed to "break down their administrative fees" in accordance with the form as required per Title 16 CCR Section 1269 and as promised in this response. Comerica Bank and FDSC refused to acknowledge any other deficiencies in their proposed resolution and in response to this finding.

As a result, these corrective actions have not been implemented.

Finding 6: Funds not Returned to Trustor After the Funeral Establishment Not Able To Perform Contracted Funeral Services in Violation of Title 16 CCR Section 1274

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, Comerica Bank and FDSC have stated that they are "willing to review their contracts to determine if funeral establishments who had originally engaged the trustors for the preneed services are still licensed and able to perform

the service." To facilitate this, Comerica Bank and FDSC also request that the Bureau produce a list dating back to 2000 of the funeral establishments that are no longer licensed. In response the Bureau provides the following guidance:

The license status for each funeral establishment is on the Bureau's website at: [http://www2.dca.ca.gov/pls/wllpub/wllqryna\\$lcev2.startup?p_qte_code=FD&p_qte_pgm_code=4800](http://www2.dca.ca.gov/pls/wllpub/wllqryna$lcev2.startup?p_qte_code=FD&p_qte_pgm_code=4800).

As CMT has less than 350 participants,¹ it will be relatively easy for Comerica Bank or FDSC staff to identify the current status of its licensee-participants.

The Bureau is also providing a list of funeral establishments that were addressed in the audit report as not having the ability to perform the services contracted and those funeral establishments that recently notified the Bureau of their closing (see attached list).

If this means that Comerica Bank and FDSC thereafter identify all active contracts with a cancelled, inactive or revoked license and fully refund monies according to Title 16 CCR section 1274 or escheat the monies to the State Controllers' office as required by Code of Civil Procedure section 1517, then this would correct this type of deficiency for all such contracts on a going forward basis. However, similar actions need to be taken to identify active contracts that have been transferred without the trustor's authorization from a cancelled, inactive or revoked license to an active licensee. Comerica Bank and FDSC failed to address specifically their plans for complying with this finding prospectively, in terms of future practices. In other words, the Trustees failed to explain their plan to identify these types of contracts and to prevent inappropriate retention of these funds going forward.

As a result, these corrective actions have not been implemented.

Finding 7: Buying And Selling Funeral Services After Death or While a Death is Impending in Violation of BPC Sections 7694, 7697 and 7718

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, Comerica Bank and FDSC state they are "willing to work with the Bureau to implement a system to avoid any future misunderstandings regarding transfer of contracts." FDSC and Comerica Bank also request that the Bureau make available to them on a regular basis information regarding changes of ownership or changed funeral directors.

However, the Trustees' proposal fails to address the key corrective actions required by this finding. The Corrective Actions required the Trustees to cease their current practices, which

¹ The Trustees have the license numbers of participating funeral establishments. The funeral establishment's license number is used by the Trustees as a pre-fix to each contract number.

involved transferring preneed contracts from establishments unable to provide services due to the cancellation, revocation or inactive status of their licenses to active establishments without the written consent of the trustor and beneficiary, not to active establishments that have merely changed ownership or control.

As a result, these corrective actions have not been implemented.

Finding 8: Refunds to the Trustor Not Made Within 15 Days of Receipt of Written Request for Contract Revocation in Violation of Title 16 CCR Section 1264

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, the FDSC and Comerica Bank state that they disagree with this finding and will "agree to continue" their current practices. They further state that they are "willing to provide further examples of their compliance if so requested by the Bureau." These arguments lack merit and the Bureau disagrees with the characterization of past compliance efforts. The Trustees have therefore, refused to implement these corrective actions for this finding.

Finding 9: Failure To Maintain Preneed Trust Records in California in Violation of Title 16 CCR Section 1267

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, the FDSC and Comerica Bank state that they "have maintained all records required..." and will "continue said practice and maintain all records according to Code of Regulations §1267(a)-(j) and make those records available upon request." FDSC and Comerica Bank further allege that "Comerica Bank maintains a complete copy of the financial records at its office in Palo Alto, California. The auditor for the Bureau had a meeting with the representatives of Comerica wherein he was offered and given any record he requested." A meeting did occur in Palo Alto on December 21, 2007 between Bureau representatives and representatives of Comerica Bank. However, the auditor was not "offered and given any record he requested." Although some financial statements regarding the CMT were provided to the Bureau at the entrance conference for the audit on December 21, 2007, Comerica Bank did not make available for Bureau inspection the "complete financial records of all preneed contracts and arrangements" for the past seven years as requested. Section 1267 requires these records to be maintained and made available to the Bureau. At the December 21, 2007 entrance conference, the following records were not available:

1. Records of individual trustor or beneficiary ledger accounts, which set forth the amount of the contract, all payments received and all income prorated as required by Title 16, CCR 1267(b);
2. Records such as bank statements and reconciliations for checking accounts used to deposit payments received or disbursements made to

- the funeral establishments and/or funeral director, a trustor or investment and accounting for checks not yet presented and outstanding, bank deposits not shown on the bank statements as described in Title 16 CCR section 1267(e);
3. Cash receipts journals showing each payment received as required by Title 16, CCR section 1267(c);
 4. Cash disbursement journals showing each, disbursement to funeral establishments or trustors, and withdrawal for documented expenses as required by Title 16, CCR section 1267(d); and,
 5. A general ledger, posted monthly with respect to all accounts controlling the fiduciary relationship with the individual trustors as required by Title 16, CCR section 1267(f).

Instead, Comerica Bank provided the Bureau with a "transactional summary" document, which it purported provided sufficient detail to comply with the requirements of the regulation. However, that summary did not meet Section 1267's requirements and did not provide the detail requested by the Bureau and required by Section 1267. Further, the document did not cover January 1, 2000 through January 23, 2002 of the audit period.

To date, the Bureau has not received any evidence that all of the records required to be maintained per Title 16, CCR section 1267 are being maintained in California as required. As a result, these corrective actions have not been implemented.

Finding 10: Records Not Made Available For Inspection by The Bureau in Violation of Title 16 CCR Section 1267

Bureau's Reply: The response provided no basis for amending this finding.

In response to the Corrective Actions requested, the FDSC and Comerica Bank state that they "have maintained all records required..." and will "continue said practice and maintain all records according to Code of Regulations §1267(a)-(j) and make those records available upon request." FDSC and Comerica Bank further allege that "the Bureau has also visited the offices of Comerica to view the documents held by Comerica. Comerica handed over boxes of documents to the Bureau in that meeting." The Bureau held an entrance conference for the audit with representatives from Comerica Bank at its offices in Palo Alto, California on December 21, 2007. Although some financial statements regarding the CMT were provided, Comerica Bank did not make available to the bureau the "complete financial records of all preneed contracts and arrangements" for the past seven years as requested.

Section 1267 requires these records to be maintained and made available to the Bureau. At the December 21, 2007 entrance conference, the following records were not made available to the Bureau:

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1. Records of individual trustor or beneficiary ledger accounts, which set forth the amount of the contract, all payments received and all income prorated as required by Title 16, CCR 1267(b);
2. Records such as bank statements and reconciliations for checking accounts used to deposit payments received or disbursements made to the funeral establishments and/or funeral director, a trustor or investment and accounting for checks not yet presented and outstanding, bank deposits not shown on the bank statements as described in Title 16 CCR section 1267(e);
3. Cash receipts journals showing each payment received as required by Title 16, CCR section 1267(c);
4. Cash disbursement journals showing each disbursement to funeral establishments or trustors, and each withdrawal for documented expenses as required by Title 16, CCR section 1267(d); and,
5. A general ledger, posted monthly with respect to all accounts controlling the fiduciary relationship with the individual trustors as required by Title 16, CCR section 1267(f).

Instead, Comerica Bank provided the Bureau with a "transactional summary" document, which it purported provided sufficient detail to comply with the requirements of the regulation. However, that summary did not meet Section 1267's requirements and did not provide the detail requested by the Bureau and required by Section 1267. Further, the document did not cover January 1, 2000 through January 23, 2002 of the audit period.

Section 1267 requires this information to be made available for the Bureau's inspection. To date, the Bureau has not received any evidence that all of the records required to be maintained per Title 16, CCR section 1267 have been made available to the Bureau as required. As a result, these corrective actions have not been implemented.

As stated earlier, the Bureau expects all of its Corrective Actions to be implemented. The Bureau expects to receive a report from you, the licensees, explaining how you have implemented these corrective actions on or before **July 21, 2010**.

Sincerely,



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Supervising Auditor

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