DONALD W. ABSHIRE, ET AL.	19TH JUDICIAL DISTRICT COURT
-versus-	CIV. ACTION NO. 377713, DIV. "M"
THE STATE OF LOUISIANA, ET AL.	EAST BATON ROUGE PARISH, LOUISIANA

CONSOLIDATED WITH

ARTHUR A. LEWIS, ET AL.	19TH JUDICIAL DISTRICT COURT
-versus-	CIV. ACTION NO. 412265, DIV. "M"
THE STATE OF LOUISIANA, ET AL.	EAST BATON ROUGE PARISH, LOUISIANA

FILED: ______________________ ______________________ DEPUTY CLERK

PETITIONERS' SEVENTH AMENDED AND SUPPLEMENTAL PETITION

NOW INTO COURT, through undersigned counsel, come the Petitioners referenced in Paragraph 1 below, all being either persons of the full age of majority or entities authorized by law to maintain legal actions, and all being either policyholders, annuity holders, noteholders, equity owners, or holders of some other financial interest in, or affected by, Public Investors Life Insurance Company and/or Midwest Life Insurance Company and/or Public Investors, Inc., who respectfully represent as follows:

PARTIES AND JURISDICTION

1.

The Petitioners in this matter and their places of residence are listed in the previous Petitions and Exhibits attached thereto, all of which are incorporated herein by reference for all purposes. In general, the Petitioners are individuals and associations who are either policyholders, annuity holders, and/or note holders of Public Investors Life Insurance Company (hereinafter "PILICO"), Midwest Life Insurance Company ("Midwest"), and/or Public Investors, Incorporated ("PICO" or "PI"). Petitioners are residents of various parishes throughout the State of Louisiana.

2.

Made Defendants herein are:

a. The State of Louisiana, through the Department of Insurance of the State of Louisiana and the Department of Insurance of the State of Louisiana (hereinafter "DOI");

b. The Department of Insurance of the State of Louisiana ("DOI");

c. The State of Louisiana, through the Office of Financial Institutions of the State of Louisiana and Office of Financial Institutions of the State of Louisiana (hereinafter "OFI");

d. The Office of Financial Institutions("OFI").

3.

Jurisdiction and venue are proper in this Honorable Court, as established by Order of the Court of Appeal for the Third Circuit in <u>Abshire v. State through Department of Insurance</u>, 636 So.2d 627 (La.App. 3rd Cir.), <u>writ denied</u> (La. 1994).

4.

The DOI is an agency of the State of Louisiana which operates through the duly-elected Commissioner of Insurance. The DOI is charged with the duty and responsibility of overseeing and regulating activities relating to insurance companies doing business in this State, including licensing, examination, and other activities. It is the duty and responsibility of the DOI, in part, to enforce the insurance laws and regulations of the State impartially, honestly and expeditiously. To this end, the highest ethical, professional and work quality standards are to be exercised by the DOI in all formal and informal relationships with individuals, agencies and companies affected by the policies and actions of the DOI.

5.

The OFI is an agency of the State of Louisiana, which operates through the Director of the Office of Financial Institutions. It is charged with the duty and responsibility of overseeing and regulating activities relating to State-chartered financial institutions, including the Limited Function Financial Institution involved in this matter. The OFI has a duty and responsibility to participate in the development of new ideas, explore areas of potential expansion, and regulate providers of financial services within its jurisdiction in order to protect the public, enhance confidence in the financial institution system, and promote the expansion of commerce and industry and the economic stability of the State.

GENERAL FACTUAL BACKGROUND AND ALLEGATIONS APPLICABLE TO ALL COUNTS

6.

The plight of the Petitioners, and the pattern of deception, mismanagement, gross negligence, incompetence, fraud and other intentional misconduct which brought it about, arises out of an extremely complex set of facts. These facts involve literally dozens of affiliated companies, the creation and management of which confused the public and provided camouflage for elaborate corporate actions intentionally designed to steal and/or misuse money invested by unsuspecting citizens. The persons designing those transactions worked a massive deception upon the Petitioners, which will be described in detail hereinafter.

7.

The persons and entities which engaged in the fraudulent acts at issue worked hand-in-hand with the knowing involvement of Fred C. Dent, Douglas D. Green, Malcolm Ward, the State of Louisiana through the DOI, the State of Louisiana through the OFI, the DOI, and the OFI, among others, whose duty it was to prevent these very fraudulent activities.

8.

As laid out in detail below, the DOI and OFI <u>knowingly, intentionally, maliciously, wilfully, recklessly, and flagrantly subverted and violated the laws</u> of the State of Louisiana governing the regulation of insurance and financial institutions <u>for the express purpose of wrongfully depriving Petitioners of their property</u>. The DOI and OFI did not have the authority or discretion to violate and subvert the laws of the State of Louisiana as laid out below.

9.

All actions of the DOI and OFI at issue herein grievously harmed the Petitioners as a direct and proximate result. This fact has been admitted by the DOI, by and through the present Commissioner of Insurance, Jim Brown. This fact has also been admitted on behalf of the State, by and through Inspector General Bill Lynch, among others.

10.

Such a catastrophe could and should have been readily averted had the State timely carried out its statutory and regulatory duties toward these companies, their policyholders, annuitants, and note holders. As early as 1984, irregularities in the management of some of these companies were brought to the attention of the State Regulatory Defendants. By 1988, violations regarding investment limitations and affiliated transactions had become known to regulatory authorities nationwide, with examinations being conducted in Nebraska, Ohio, Kansas, and South Carolina. The State deliberately disregarded the plethora of information as to these violations, including the results of its own DOI Year End 1988 Examination Reports of PILICO and FF&C, which found both companies to be insolvent at that time. Figures reported in the Annual Reports of the various affiliated companies, available to the public and known to the State to be false, were never corrected, and those reports deliberately gave a false impression of financial stability to the public and to the private rating services which passed such information along to the public in their reports.

11.

Among those practices which the State Regulatory Defendants allowed to continue were illegal investments of company assets, which consisted in many cases of Petitioners' life savings. These investments not only included over-leveraging and pyramiding of illegal affiliated transactions, but also supported lavish lifestyles for the corporate officers and directors, including a corporate jet, boat house, expensive automobiles, and other luxuries. In addition, there was no reporting, as required by law, of the "employment" and "consulting" contracts of these individuals. In the end, the pyramid began to collapse under the weight of the ineptness, waste, extravagance, and illegality of these investments, and the State at last chose to step in, to orchestrate the demise of certain chosen companies, as best suited its interests, through the breach of its duties to the Petitioners and statutory violations.

12.

Put simply, the State and the State Regulatory Defendants orchestrated, permitted, encouraged, and supervised the illegal transfer of assets out of companies in which the Petitioners had an interest, or whose policies or annuities they held, and directly or indirectly into the only company covered by the LIGA Fund. The

State's primary motivation for this was simple, and in retrospect, it was plain: The State did not want a company covered by the LIGA Fund to fail. By 1989 the State Regulatory Defendants were acutely aware of the costs of the Champion debacle, both financially and politically, and sought to take <u>illegal</u> steps to prevent a similar impact on the LIGA Fund.

13.

As will be discussed further in the paragraphs below, if an insurance company covered by the LIGA Fund fails, the State loses tax revenues, but the individual citizens of the State who happen to be policy holders of that company are covered by the LIGA Fund, and suffer no financial loss. On the other hand, if an insurance company which is <u>not</u> covered by the LIGA Fund fails, the State does not bear the same loss, and the entire brunt of the loss must be borne by the citizens whose losses are not covered by the LIGA Fund. Here, the State used its monopoly power to regulate these companies for its own financial benefit, political motives and protection, and shifted the inevitable loss from itself to these Petitioners it was duty-bound to protect. The State deliberately preferred the general corporate coffers of the State of Louisiana to the financial interests and well-being of these individual citizens of the State. The State also used its unique monopoly powers to conceal and cover up the results of the intentional misconduct, gross incompetence, negligence, and/or corruption of the State Regulatory Defendants which led up to the point of crisis with the LIGA Fund. In order to achieve its goal, however, the State, by and through the DOI and OFI, had to (and did) commit gross and flagrant violations of statutes of the State of Louisiana.

14.

The State's direct financial interest in the LIGA Fund arises out of the fact that every insurance company admitted to do business in Louisiana must pay to the State an annual tax for the privilege of doing business here. This is referred to as the "premium tax," and is computed as a percentage of premiums written in the State. If the LIGA Fund is called upon to pay out claims to policyholders of a LIGA-covered insurance company due to the insolvency of that company, then the insurance companies which are members of LIGA are required to make cash payments to the Fund, in order to replenish the Fund and keep it at statutory levels. But when and if the companies are required to make payments into the LIGA Fund, the companies may claim a credit against the premium taxes otherwise due to the State of Louisiana. Thus a call on the LIGA Fund is an event of relatively little consequence to the member insurance companies, who are thereby able to obtain a dollar-for-dollar premium tax credit for the funds they must contribute to replenish the LIGA Fund. But a call on the LIGA Fund is an event of profound importance to the State of Lcuisiana, because every call on the Fund results in a reduction in the amount of premium tax which would otherwise be collected by the State. Thus, the State has a direct pecuniary motive to see to it that the Fund is not required to be tapped. In this case, the State protected itself, and assured itself of additional tax revenues, by making certain that if any of these companies failed, it would be the company not covered by the LIGA Fund. Here, the State Regulatory Defendants, whose primary obligation is to protect the policyholders and investors of Louisiana, deliberately and systematically sold out these Petitioners, who were least able to stand a financial loss--namely, those <u>not</u> covered by the LIGA Fund in the event of collapse of their insurance company.

<u>Structure of Corporate Insurance Entities Involved In This Matter</u>

15.

Public Investors, Inc. ("PICO") is a domestic insurance holding company with its principal place of business located in

Jefferson Parish, Louisiana. It has applied for relief under Chapter XI, converted to Chapter VII, of the U.S. Bankruptcy laws as of May 20, 1991, sub nom. In Re: Public Investors, Inc., No. 91-11228 "K", filed in the United States Bankruptcy Court for the Eastern District of Louisiana.

16.

Public Investors Life Insurance Company, Inc., ("PILICO") is a domestic life insurance corporation, whose principal place of business is located in Rapides Parish, Louisiana, and which is presently in liquidation in the 19th Judicial District Court, Parish of East Baton Rouge, as of May 15, 1991, sub nom. Douglas D. Green, As Commissioner of Insurance for the State of Louisiana v. Public Investors Life Insurance Company, No. 367, 197, Division "I".

17.

Midwest Life Insurance Company ("MIDWEST") is a domestic life insurance company, whose principal place of business is located in Jefferson Parish, Louisiana, and which is presently in liquidation in the 19th Judicial District Court, as of August 26, 1991, sub nom. John A. Dixon, Jr., as Commissioner of Insurance, Ad Hoc, for the State of Louisiana v. The Midwest Life Insurance Company, No. 368,127, Division "M". Prior to May 1, 1990, it was domiciled in Nebraska.

18.

Fidelity Fire and Casualty Insurance Company, Inc. ("FF&C"), is a domestic property and casualty insurance corporation, whose principal place of business is in Rapides Parish, Louisiana, and which is also in liquidation in the 19th Judicial District Court, Parish of East Baton Rouge, as of September 4, 1991, sub nom. to John A. Dixon, Jr., as Commissioner of Insurance ad hoc, for the State of Louisiana v. Fidelity Fire and Casualty Insurance Company, No. 370,097, Division "I". Unlike PICO, PILICO and MIDWEST, FF&C

principally wrote non-standard automobile physical damage and general automobile liability coverage. Also unlike PICO, PILICO, and MIDWEST, FF&C was required by law to pay assessments to the Louisiana Insurance Guaranty Association Fund, which provided coverage for the policyholders of FF&C in the event of insolvency.

19.

Insurance Premium Assistance Company ("IPAC"), whose principal place of business is in Jefferson Parish, Louisiana, is a domestic corporation which primarily financed the insurance premiums generated by the activities of FF&C. From December, 1988 to January, 1990, a period of slightly over one year, IPAC was licensed as a Limited Function Financial Institution ("LFFI") and was thus regulated by the Office of Financial Institutions, which granted both its LFFI license and its premium finance license. The LFFI license was not renewed in January of 1990.

20.

PICO, PILICO, FF&C, and IPAC are together part of a group of related subsidiaries and/or affiliated entities which were operated, controlled and/or managed under the umbrella of the Bomar Investment Corporation (BOMAR). BOMAR was a Louisiana holding company which purchased PICO (and its subsidiaries at that time, PILICO, FF&C, and IPAC, amongst others) on August 12, 1987. In 1986, prior to its purchase of PICO, BOMAR acquired Alliance Life Insurance (ALI), which was domiciled in Kansas. Later added to the constellation of BOMAR companies were MIDWEST in November of 1987 and Universal Guaranty Life (UGL) in November of 1988. On August 8, 1989, the name of Bomar Investment Corporation was changed to Riverside Holding Corporation (RHC). Both RHC and BOMAR (and thus PICO and its subsidiaries) were controlled by Mark Herman and Robert Bilbruck from approximately August 12, 1987 to December 8, 1989. Toward the latter part of 1989, UGL and ALI were sold to First Commonwealth Corporation, leaving RHC (formerly known as

BOMAR, and the owner of PICO and its subsidiaries), to be bought by Southshore Holding Corporation ("Southshore") on or about December 8, 1989. PRC Holding Company ("PRC") was chartered on January 26, 1990, by the owners of Southshore to hold PICO, PILICO, and certain other subsidiaries, but not to hold MIDWEST, FF&C, and IPAC. Both Southshore and PRC were controlled by B.F. Shamburger and Gary E. Jackson at all times relevant hereto.

21.

Other corporate interrelationships are detailed in the Paragraphs below, where appropriate.

Regulatory Structure Applicable to These Entities (Applicable to All Counts)

22.

At all times relevant to this action, all of the above-mentioned companies were, or should have been, regulated by the DOI and/or the OFI.

23.

The State Regulatory Defendants were aware of, supported, encouraged and participated in statutory violations by PICO, PILICO, IPAC, MIDWEST, and FF&C. In addition to information which was gleaned from the State Regulatory Defendants' own required reporting systems, their examinations of regulated companies, consumer complaints, and sources within the industry, said State Regulatory Defendants had as other sources of information the Examination Reports and information from the Departments of Insurance of various other states, including Kansas, Oregon, Ohio, Texas, Florida, and Nebraska, where affiliated companies were also operating, as well as Insurance Reporter Systems such as the National Association of Insurance Commissioners ("NAIC"), as well as their own intentional interaction with these companies.

24.

Due to the presence of members of the DOI, OFI, and their counsel, directors, and staff, at each other's meetings concerning these affiliated companies, knowledge of one State Regulatory Defendant with respect to these matters was known to each of the other State Regulatory Defendants, and these Defendants are solidarily liable to the Petitioners for the violations and damages described herein.

25.

As one example, representatives of OFI were present at the hearing of the DOI held on December 15, 1989, at which the purchase of Riverside by Southshore, and all attendant transactions, were approved by the DOI. Both the DOI and the OFI had been intimately involved in numerous meetings leading to this transaction, and they facilitated the transaction by deliberately circumventing the law, to permit it. This transaction is described in greater detail below.

26.

In addition to its general duty to protect the public interest, the State of Louisiana, through the DOI and its Commissioner, has a specific duty, and has specifically assumed a duty, to protect insurance company policyholders, depositors, annuitants, and note holders such as the Petitioners.

27.

This specific duty derives, among other places, from La. R.S. 22:1-695 (the "Insurance Code"), its comprehensive nature, its repeated references to the protection and best interests of the policyholders and the insurer's creditors, and the comprehensive and specific powers and duties delineated by it to the Commissioner to execute his statutory duty to examine, regulate, and supervise the affairs of insurance companies.

28.

Further evidence that the State of Louisiana assumed a specific duty to Petitioners may also be found in the Louisiana Department of Insurance Regulations, and in particular, Regulation 5 therein, which was directed to the Petitioners, among others, and which provides as follows:

> These are some of the protections and safeguards your Insurance Department offers to you:
>
> When You Purchase Insurance From Authorized Companies
>
> 1. Deposits must be made with the State for the protection of Louisiana policyholders.
>
> 2. Examinations of all authorized companies by the Department are made to determine if such companies are financially able to pay claims.

29.

The State, in the person of the DOI and OFI, assumed upon itself an even more specific and articulable duty to Petitioners herein. DOI and OFI took it upon themselves to manage and direct the affairs of the specific insurance companies involved herein. Once they did that, Regulation 31 imposed upon them several affirmative duties.

30.

Regulation 31:3(a)(1) imposed upon the DOI and OFI the duty to insure that "[t]ransactions with affiliates ... shall be fair and reasonable". The DOI and OFI intentionally, maliciously, wilfully, recklessly, and fraudulently violated this duty for the specific factual reasons articulated below.

31.

Regulation 31:3(b) imposed upon DOI and OFI the duty to insure diversification in the investment portfolios of these various companies, particularly PILICO and Midwest. Regulation 31:3 imposed upon them the duty to insure that any cash dividend did not exceed 15% of PILICO's surplus at its most recent fiscal year-end.

The DOI and OFI intentionally, maliciously, wilfully, recklessly, and fraudulently violated these duties, as articulated in the factual allegations below.

32.

In addition to the statutorily created duties assumed by the State, the State also owed the Petitioners a duty of honesty and loyalty. The DOI and OFI intentionally, maliciously, wilfully, recklessly, and fraudulently violated this duty, as articulated in the factual allegations below.

The Motivation of the State and the State Regulatory Defendants

33.

The failings by the State in these circumstances are of three types: (a) intentional, willful, outrageous, and malicious misconduct in the regulation and oversight of the companies at issue; (b) neglect, incompetence, and/or total failure to oversee the activities of companies intent on conducting a corporate "shell game" to steal and/or misuse money invested by unsuspecting citizens; and © advancing the State's own agenda, commencing in 1988, when it saw that at least some of the companies involved in this elaborate "shell game" were bound to fail, which would be politically embarrassing and financially detrimental to the State. At that point, the State's own agenda coalesced with the intentional and fraudulent agenda of the companies and those directing them. Thereafter, the State Regulatory Defendants became co-conspirators and engaged in intentional, reckless, willful and outrageous misconduct against the Petitioners. The DOI and the OFI did not have the discretion to engage in this type of behavior.

34.

Once the State and the State Regulatory Defendants realized that a catastrophic failure of these related companies was extremely likely, if not inevitable, the State Regulatory

Defendants began a concerted and deliberate effort to mold and shape the affairs of these companies, so that the companies which did fail would be the ones which caused the least amount of dollar loss to the State. Unfortunately, this meant that the loss would fall entirely upon the heads of these Petitioners, and others in their position. The State and its Regulatory Defendants made these efforts with full knowledge of the terrible cost of allowing the Petitioners to bear the full brunt of these financial failures. In order to pull off this scam, it was necessary for the DOI and OFI to breach their statutory duties as owed to the Petitioners and to intentionally breach and violate various State statutes.

OUTRAGEOUS, MALICIOUS, RECKLESS, WILLFUL, INTENTIONAL, FLAGRANT, AND FRAUDULENT MISCONDUCT BY THE STATE REGULATORY DEFENDANTS

35.

The elaborate and numerous transactions with respect to FF&C are at the core of the State Regulatory Defendants' failures with respect to the Petitioners, for FF&C is the company covered by the LIGA Fund, which they deliberately preferred and favored at the expense of these Petitioners. The State Regulatory Defendants' failures with respect to FF&C go back to at least April 5, 1988, when FF&C's Certificate of Authority was amended, admitting it to write casualty and property insurance (i.e., high-risk automobile insurance), despite approval of a rate structure by the rating commission which resulted in immediate "losses incurred" in the amount of 90% of premiums earned in 1988; 88% of premiums earned in 1989; and 91% of premiums earned in 1990. When taken together with "other underwriting expenses incurred" of 40.7% (1988), 26.8% (1989), and 30.8% (1990), FF&C was seen to be immediately and obviously insolvent, from the day it began issuing this sort of insurance, with DOI's blessing. It was, or should have been, clear that FF&C could never have been profitable as a carrier of this type.

36.

Despite this fact, DOI and OFI permitted FF&C to purchase $11.9 Million in "Certificates of Deposit" from IPAC, an affiliated premium finance company. The intricacies of this transaction are discussed in detail in the paragraphs below, but of present import is the fact that FF&C sold assets of excellent quality in order to purchase the CD's. In so doing, FF&C received the benefit of a $500,000 tax credit due to the treatment accorded its purchase of IPAC CD's as a Louisiana Qualified Investment. In truth, however, IPAC became insolvent within six months, and unable to honor the CD's, which would have proved a total loss to FF&C (as it was to PILICO), had FF&C not been specially "looked out for" by the State Regulatory Defendants. This "special treatment" was intentional, fraudulent, wanton and wilful conduct designed to steal money from the Petitioners, which design succeeded -- the Defendants herein did not have the discretion to engage in this behavior.

37.

FF&C's financial condition was so threatened that by early 1990 it was delinquent in the payment of its LIGA assessment by $423,196.00, which should have caused its license to be revoked by the State Regulatory authorities pursuant to La. R.S. 22:1384(2)(b). Instead, the State Regulatory Defendants permitted FF&C to merge with Bonneville Insurance Company, which at that time was also delinquent in its own LIGA assessments in the amount of $54,088, and should also have had its license revoked. All of this was permitted despite the need, on June 30, 1990, for a capital contribution of $4 million to FF&C. This capital was illegally transferred into FF&C out of MIDWEST, to the detriment of the Petitioners having an interest in MIDWEST.

38.

The State Regulatory Defendants further violated their duties by allowing the redomestication of MIDWEST into Louisiana, despite flagrant reported violations and an actual lawsuit filed by the Nebraska DOI, so that MIDWEST's legitimate assets could be used to shore up FF&C and to absorb FF&C's financial losses, after PILICO had finally been drained of all its assets.

39.

The substantial and valuable assets of PILICO and MIDWEST were both used to illegally maintain the financial viability of FF&C, and the repeated transfers provided opportunity for large sums of money belonging to these companies to illegally disappear. From the viewpoint of the State Regulatory Defendants, these transfers also provided the opportunity to protect the LIGA Fund. The State Regulatory Defendants permitted the unjustified transfer of funds from one of the companies into another, as if they were justifiably being transferred within the same company. Thus, the State Regulatory Defendants deliberately ignored proper corporate formalities, on which these Petitioners had relied in investing their funds, and also ignored the fair and reasonable affiliated transaction requirements of Regulation 31.

Specific Evidence Of The Scam Discovered During The Course Of This Litigation

40.

The above allegations of the Petitioners have been fully discovered over the course of the past several years by all parties to this litigation. Indeed, by Order of this Court, discovery is now closed. The Petitioners, based on the evidence discovered by them, have a Motion For Partial Summary Judgment As To Liability already on file with the Court which was taken under advisement. In order to demonstrate that the above intentional, malicious, flagrant, willful and outrageous misconduct actually was engaged in by the State Regulatory Defendants, the following allegations outlining the evidence discovered is put forth. Further, this evidence is attached hereto and incorporated herein by reference for all purposes.

41.

Current Commissioner of Insurance Jim Brown candidly described the plight of the Petitioners in his testimony to the Louisiana State Senate, as follows:

> Knowing they [i.e., DOI] were going to let this company drop, they removed all the good assets and put it into other companies that could then be drained off and let the shoe fall and let these people [i.e., Petitioners] left with nothing.
>
> * * * * * * * *
>
> ... there is a major lawsuit involving what the department [DOI] did and quite frankly I think it is a pretty good lawsuit. The exposure could be through damages much more than $25,000,000.

A copy of this testimony is attached hereto as Exhibit "B".

42.

Put simply, the DOI and OFI consciously and affirmatively preferred the financial interests of the State over those of the citizens they were pledged and duty-bound to protect. In order to achieve this result, it was necessary for the DOI and OFI to fraudulently, maliciously, recklessly, willfully, and flagrantly engage in misconduct and violate State statutes. In other words, the State targeted the Petitioners and used them as human financial shields against any further "hits" on the LIGA Fund. To say the least, the State has a duty not to use its own citizens in such a damaging and harmful manner.

43.

The State has admitted and conceded, by and through the Inspector General, that it had an affirmative duty "to protect the insured public from mismanagement, abuse and corruption ...", in which duty the Inspector General conceded that "The State [DOI] failed ..." See Exhibit "A", Report of the Louisiana Inspector General, at p. 4.

44.

The Summary Judgment Record, as filed by the Petitioners (and which is incorporated herein) is literally replete with breaches of this judicially-recognized breach of the duty of honest and loyalty. As to honesty: the instances of lying, concealment, and diversion of funds are virtually innumerable. In fact, the DOI Commissioner, Doug Green was convicted of multiple federal and state felonies, and is currently serving a term in the federal penitentiary, because of his conduct while in office during this Period.

45.

Contained below is a detailed outline of the financial transactions involved in this lawsuit:

A. On April 5, 1988, FF&C's Certificate of Authority was amended, allowing it to write casualty and property insurance despite approval of a rate structure which resulted in immediate insolvency for the company.

B. On November 22, 1988, Commissioner of the OFI, Fred Dent, waived a variety of mandatory statutory requirements and delays in order to permit IPAC to issue "certificates of deposit". Commissioner Dent's letter of that date to IPAC's counsel reflects his understanding that there were inter-company investment limit problems involved with these companies.

C. On April 24, 1989, the OFI approved Certificates of Deposit in the face amount of $40 million which had been "sold" by IPAC between December 28 and December 31, 1988, to its affiliates PILICO and FF&C. OFI bestowed its approval upon these transactions despite irregularities in the reporting of these Certificates of Deposit and despite IPAC's failure to file audited and unqualified financials by March 30, 1989, as required by law.

D. The OFI had issued IPAC's license as a Limited Function Financial Institution, expressly based upon the limitation that it would issue CD's upon the receipt of <u>cash or cash equivalents</u> from three specified affiliated companies. Yet, in May, 1989, OFI knew that at least $17 million of the $40 million in CD's had been illegally issued by IPAC in exchange for mere <u>journal entries</u> on the books of PILICO. OFI declined to issue a cease and desist order and also declined to revoke IPAC's license.

E. By June of 1989, OFI had knowledge that IPAC would be unable to honor these CD's if PILICO of FF&C were to surrender them and demand return of the cash and payment of the interest earned. These CD's expired in June, 1989, yet OFI permitted IPAC to <u>renew</u> the CD's even though they were issued in violation of Louisiana law.

F. By the time of this renewal, both the OFI and DOI also had notice of an evaluation for the National Association of Insurance Commissioners (hereinafter "NAIC") Securities Valuation Office, placing a value of "five cents on the dollar" on these CD's. Despite this knowledge, OFI still approved the rollover of these CD's on June 30th. OFI also allowed unlimited extensions of time for IPAC to fulfill its statutory obligation to file unqualified, audited financials, which it never in fact did.

G. These IPAC "CD's" figure prominently in the OFI's and DOI's plan to drain assets away from PILICO and to favor FF&C, at the expense of Petitioners. When these companies were being sold to the Southshore Group in December of 1989, the OFI and DOI were heavily involved in every facet of the transaction. The DOI actually appears as "Intervenor" in the transaction. Both the OFI and DOI allowed worthless IPAC CD's (then held by PILICO) to be exchanged for an unsecured and worthless "debenture" also issued by IPAC, in the face amount of $28.25 million.

H. <u>It was OFI Commissioner Dent who came up with the idea for these debentures, and suggested it to the Bomar/Southshore group</u>. While PILICO's "CD's" were exchanged for worthless IPAC "debentures", a wholly different treatment was accorded to FF&C's IPAC "CD's". These were exchanged for valuable assets. At this time, both OFI and DOI <u>knew to a certainty</u> that IPAC could not pay its "debenture", and knew also that the NAIC's Report, valuing the "CD's" at five cents on the dollar, had already been noted in the report of the DOI's own year-end 1988 examination of FF&C, filed on June 2, 1989. Yet the charade continued; the false and utterly worthless "debentures" were dreamed up as a "plug" figure which would <u>allow these companies to appear solvent</u>, so that the public, including Petitioners, would not know the truth of the situation.

I. As admitted by DOI's then-Chief Examiner, Malcom Ward, and then-Deputy Commissioner of DOI, Thomas Bentley, use of the term "CD" to describe the debt instruments issued by IPAC to PILICO was misleading in that these "CD's" were not insured by the federal government in any amount. <u>Despite this fact, the DOI and OFI allowed companies like PILICO to file financial statements reflecting assets using admittedly misleading terms such as "CD's" in order to allow these companies to entice the public to invest. The DOI and OFI also allowed the financials of PILICO to reflect as part of that company's assets "CD's" in the amount of $28 million, after those agencies had already received confirmation that those "CD's" were worth, at most, five cents on the dollar or a mere 5% of their face value</u>.

46.

As a result of the above intentional, malicious, willful, flagrant and fraudulent misconduct by the DOI and OFI, the policyholders and other instrument holders of these companies were misled. A false image was deliberately created in the public mind, and in the minds of the Petitioners, that these companies were among the strongest in the world, when in fact they were in an extremely precarious financial position.

47.

If accurate and non-fraudulent financial statements had been filed, the public, including Petitioners, would have known of the dangerous financial condition of these companies, and DOI and OFI would have been forced to take appropriate steps to stop the financial blood-letting of Petitioners and to recoup the assets rightfully belonging to PILICO and Midwest.

48.

It was, however, not in the State's own pecuniary interest to live up to its duty to protect the public, including most particularly Petitioners.

49.

Malcom Ward, the DOI's Chief Examiner testified that, in October of 1989, the top officials of the DOI, Doug Green, Commissioner, Tom Bentley, Deputy Commissioner, Ward himself, and others, acting together, determined that funds from the sale of stock owned by PICO in Universal Guaranty Life Insurance Company (UGLI) would be diverted to FF&C. The DOI actually structured and controlled the Southshore workout to make certain that FF&C got the benefit of the sale of the UGLI stock, even though FF&C was not entitled to these funds because FF&G did not own any of the UGLI stock. The DOI contrived an extremely complex transaction, the sole purpose of which was to divert these sales proceeds to FF&C. Once again, FF&C was favored over companies not covered by the LIGA

Fund. FF&C's IPAC CD's thereby got paid in full in cash, while PILICO received a worthless "debenture".

50.

Thus the DOI itself, in the person of its Chief Examiner, has admitted under oath that the DOI created a sham "agreement" for the sole purpose of unlawfully diverting the flow of funds or sales proceeds from the sale of the UGLI stock to FF&C. The DOI was not, however, acting alone. The agreement of the DOI and OFI, and most or all of those agencies' top executives, was derived with the understanding that the diversion of the UGLI proceeds to FF&C was for the purpose of curing FF&C's insolvency, avert its conservation or liquidation, and prevent the LIGA Fund from taking another "hit" as happened with Champion Insurance.

51.

It was understood and intended by the DOI and OFI that the policyholders, annuitants, and other instrument holders of PILICO and Midwest, <u>i.e</u>., Petitioners, would be left in an even more hazardous position since their monies were not guaranteed by the LIGA Fund or by the State of Louisiana in any other manner.

52.

Malcolm Ward admitted the fraudulent nature of this transaction and the breach of duty by OFI and DOI when he testified under oath as follows: "<u>In my opinion, the volume of CD's that PILICO was carrying on its annual statement far exceeded any reasonable guidelines as far as diversification of investments ...</u>". [emphasis added]

53.

Documents discovered in this matter also demonstrate the intentional, fraudulent, flagrant, malicious misconduct of the DOI and OFI:

A. **<u>December 28-31, 1988</u>:**

IPAC sold $11.9 million worth of CD's to FF&C, and $28.65 million in CD's to PILICO. <u>See</u> Exhibit "F".

B. March 9, 1989:

Fred Dent grants an extension of sixty (60) days for IPAC to file its statutorily-required audited financial statements. See Exhibit "E".

C. May 17, 1989:

Memorandum from Ann Lemenager (OFI auditor) to OFI Commissioner Dent reflecting OFI's visit to IPAC, noting that IPAC was not in compliance with OFI regulations. See Exhibit "M".

D. June 15, 1989:

Memorandum of meeting between OFI Commissioner Dent and various parties representing IPAC, including Mark Herman of Bomar, wherein OFI learned of severe problems that IPAC was having in other states. Commissioner Dent indicated that OFI felt obliged to take some strong action:

> "... this office [OFI] is going to issue some sort of affirmative action to prevent IPAC from continuing to exercise their license to issue CD's until the company has its business affairs in some order and we can see the financial condition of IPAC and its related companies."

Commissioner Dent also "emphasized the need for confidentiality about the matters because he has heard rumors that Mr. Herman and his related companies may have been targeted for an investigation." See Exhibit "N" (emphasis added).

E. June 30, 1989:

OFI agrees to "roll over" for six months, the $40 million face amount of IPAC CD's issued to FF&C and PILICO, despite IPAC's inability to honor them. See Exhibit "O" (emphasis added).

F. August 18, 1989:

Meeting between Commissioner Dent and others representing IPAC, to discuss the OFI examination as of June 30, 1989. Dent continues to threaten to issue a Cease and Desist Order. Mr. Dent "is concerned about public perception of LFFI [Limited Function Financial Institutions; i.e., IPAC] in light of the Champion/UFS situation". Mr. Dent was also "especially concerned about the issuance of CD's for other than cash", which clearly violated the IPAC charter issued by OFI. As mentioned above, in truth and in fact, some of the CD's had been issued by simply making journal entries among affiliates, and no cash had actually been given as consideration for those same CD's. See Exhibit "Q" (emphasis added).

G. August 24, 1989:

Fred Dent transmittal of the OFI examination report to IPAC, stating that:

> "The Report reveals that IPAC is in apparent violation of Louisiana statutes and the

> requirements of its license as a limited function financial institution. These violations are such that <u>this Office must take action</u>."

The Report. enumerates many egregious violations, and recommends that a Cease and Desist Order be issued requiring that IPAC provide monthly progress reports which contain current financial statements of itself and its affiliates; that IPAC be required to void and remove from its books all CD's which were not issued for the receipt of cash; and that IPAC should not issue any additional CD's, nor renew those currently on its books. <u>See</u> Exhibit "R". Unfortunately, OFI did not carry through with any of the mandatory requirements and did not take any corrective action at this or any other time.

H. **<u>September 29, 1989</u>:**

<u>William Smythe of the NAIC Securities Valuation Office writes to Larry Coleman of PILICO, indicating that IPAC's CD's have a value of only Five Cents on the dollar</u>. <u>See</u> Exhibit "H". The State Regulatory Defendants were aware of this situation at this same time.

I. **<u>October 19, 1989</u>:**

Memorandum from Dale Jacobs and Dale Babin (OFI auditors) to Commissioner Dent, outlining much of the above chronology and ending with a description of a conference between Dent, Hunter Wagner, and Jerry Willis, <u>et al</u>. on October 13, 1989, wherein "Mr. Dent asked Ann Lemenager to visit IPAC to see how much money it would take for them to become compliant with our laws." <u>See</u> Exhibit "F".

J. **<u>October 26, 1989</u>:**

Conference among OFI Commissioner Dent, Lynda Drake, Fred Tulley (representing DOI Commissioner Doug Green), Malcom Ward, <u>et al</u>. "to discuss the potential sale of Riverside, Inc. (Parent of IPAC)". The memorandum of the meeting notes that "this sale is important to the insurance commissioner's office because of the relationship between IPAC and two affiliate insurance companies: [FF&C] and [PILICO]." <u>See</u> Exhibit "S".

The memorandum (dated October 31, 1989/Exhibit "S") is extremely important for a variety of reasons. Among other things, the memorandum notes that:

- - IPAC is unable to pay its CD's, and they are worth only Five Per Cent (5%) of their face value.

- - These companies are insolvent, and "in all probability" will have to be closed.

- - The proposal for outside investors to buy these companies "<u>hinged on OFI's continuing to allow IPAC to operate as a limited function financial institution</u>. <u>They have to maintain the LFFI license</u> for the insurance commissioner to allow the CD's to be considered admitted assets on the insurance company's books".

- - "Therefore, <u>the insurance commissioner wanted OFI's support to prevent conservatorship</u> of the two companies."

- - "<u>If the license was dropped by OFI, the insurance commissioner would not be able to use these CD's</u> as admitted assets and the insurance companies would become insolvent ..."

K. **<u>October 31, 1989</u>:**

Dale Jacobs and Dale Babin visit IPAC's offices and determine (again) that IPAC does not have the ability to repay its CD's when they mature on December 30, 1989. <u>See</u> Exhibit "T".

L. **<u>November 3, 1989</u>:**

Letter from Commissioner Dent to Joel Herron, President of IPAC, indicating OFI's intent to issue a Cease and Desist Order to IPAC, based upon numerous violations. <u>See</u> Exhibit "U".

M. **<u>November 9, 1989</u>:**

Conference among Commissioner Dent, Dale Jacobs, Ann Lemenager, Hunter Wagner, Bob Shamburger, Joel Herron, <u>et al</u>. "to discuss prospective purchase plans for Riverside, Inc. and its effect on IPAC". <u>See</u> Exhibit "V".

Shamberger made it plain that OFI's endorsement of his plan was of critical importance: "Even with these changes, Mr. Shamberger felt that the Louisiana [DOI] would write up the CD's <u>if OFI could agree to accept</u> his proposed purchase plan." [emphasis added]

Mr. Dent then suggested that there might indeed be "alternative methods" whereby everyone could get what he wanted, involving writing off the IPAC CD's and injecting another asset into the company. <u>See</u> Exhibit "V" at p. A001285. "<u>It was agreed that all plans now hinge</u> on the [DOI]'s approval of <u>what assets could be substituted for the insurance company's CD's</u>."

Eleven days later, at the meeting between IPAC representatives and the OFI Commissioner and staff, Mr. Dent's suggestion of "alternative methods" to get rid of the CD's emerges, full blown, as the plan to replace the IPAC CD's with equally worthless IPAC "corporate debentures". <u>See</u> Exhibit "V", at p. A001265.

N. **<u>November 17, 1989</u>:**

This **very important memorandum**, from Dale Jacobs to Fred Dent, analyzes IPAC's proposal. <u>See</u> Exhibit "W". In a nutshell, Dale Jacobs understood, and so informed Fred Dent that the following would occur:

"Up to this point", the proposal was acceptable to Ms. Jacobs, "<u>since [as a result] FF&C will no longer be a threat to the guaranty fund</u>".

It was plain to Ms. Jacobs that the proposal "<u>is contingent on us [OFI] allowing IPAC to continue as a limited function financial institution</u>".

But Ms. Jacobs does not believe that this approach is realistic, for a variety of well-reasoned factors that she enumerates at page two of the memorandum. Indeed, the CD's are left "in potentially more risk of payment" with "[t]he insurance company still vulnerable to default, and OFI would still be vulnerable to criticism".

Ms. Jacobs states that "I personally do not know how the [DOI] could accept these assets as admitted assets under these circumstances." [emphasis added] She advises OFI to refuse IPAC's offer unless real, hard assets (and not phony "funny money") could be substituted.

Finally, Ms. Jacobs notes that if the OFI goes ahead with the long-threatened Cease and Desist Order (thereby fulfilling OFI's appropriate statutory role), "this could adversely affect the potential sales of the two insurance companies. It could potentially create the liquidation of the insurance companies -- attached with another hit to the [LIGA] fund." See Exhibit "W" at p. A001251 [emphasis added].

O. **November 20, 1989:**

Meeting between IPAC representatives and OFI representatives. See Exhibit "X". Mr. Griggers, President of PICO, notes that the most sensitive aspect of the situation is the $40 million in CD's issued to FF&C and PILICO. He notes that if OFI can agree, he should be able to consummate a transaction "that will generate sufficient funds to repay all of the CD's of the $11.7 million in CD's that IPAC owes [FF&C]." See Exhibit "X" at p. A001261. The CD-for-debenture swap is outlined. See Exhibit "X" at pp. A001265-1267. Griggers emphasizes to commissioner Dent that a Cease and Desist Order must be avoided because if it "got out" to the public that the companies were in trouble, it would make it difficult to keep enticing people to put money into these companies:

> "We believe, secondly, we would be caused sufficient damage if a consent order were issued or a C&D from the standpoint that if it became -- if it got out into the public there is a negative public perception sufficient enough to cause problems, well, first of all, with our business being conducted through [FF&C] and IPAC."

See Exhibit "X" at p. A001265.

Everyone at this meeting makes it clear that it is FF&C which is the OFI's major concern, and Griggers, et al. clearly feel their argument is enhanced by intoning the words "Fidelity Fire":

Mrs. Drake: "Just for my clarification, are you saying that ... all of the CD's will be made whole or the CD's to [FF&C] only?"

Mr. Griggers: "Okay. I probably didn't make that real clear. If the Commonwealth sale goes through ... out of that transaction, all of the CD's to [FF&C] will be paid off."

See Exhibit "X" at p. A001266 (Emphasis added).

P. **December 4, 1989:**

Memorandum from Dale Jacobs and Ann Lemenager to Lynda Drake, Deputy Commissioner of OFI. See Exhibit "Y". This memo notes again that "IPAC does not have the resources to liquidate its certificates of deposits as of the extended maturity date of December 31, 1989." Once again, looking out first for the favored child of the LIGA Fund, FF&C, the memorandum notes as follows:

> "If the proposed sale of the two affiliated insurance companies does take place, IPAC does appear to be capable of liquidating its [CD's] of $11,650,000 to [FF&C]. They will not, however, have the capacity to liquidate the remaining [CD's] of $28,650,000 to PILICO by December 31, 1989."

See Exhibit "Y" (emphasis added).

The memorandum notes only two legitimate alternatives, in the opinion of these two examiners: either issue a Cease & Desist Order immediately, or refuse to renew IPAC's license.

Q. **December 8, 1989**:

The "Renewal Plan" agreement between and among Southshore, IPAC, FF&C, and PILICO, with the DOI Commissioner entering as an intervenor. FF&C gets real estate and other consideration purportedly having a fair market value of $15.9 million in exchange for its IPAC CD's. PILICO gets IPAC "debentures" of $28.25 million in exchange for its IPAC CD's, (which were equally worthless). See Exhibit "L".[1]

R. **December 15, 1989**:

"Public Hearing" before John Fontenot, with Fred Tulley and Thomas Bentley representing the Insurance Commissioner; Ann Lemenager representing OFI; and various parties representing IPAC, etc. "Renewal Plan" approved. No minutes, no transcript, waiver of notice by all concerned. See Exhibit "Z".

S. **December 15, 1989**:
(same day as so-called "Public Hearing")

OFI orders IPAC to suspend its operations as a limited function financial institution. See Exhibit "AA". Note: this action occurs on the same day that OFI attended a "hearing" approving a "Renewal Plan" whereby worthless IPAC "debentures" would be exchanged for worthless IPAC CD's to PILICO. A "Cease and Desist Order" is issued by Commissioner Dent to IPAC, stating, inter alia, that IPAC had to liquidate its liabilities on the CD's issued to PILICO and FF&C by December 31, 1989 -- which Mr. Dent, et al. assisted IPAC in effectuating on the same day, December 15th, by means of the "Renewal Plan" debenture swap.

T. **December 15, 1989**:

OFI allows the sham transaction of the incorporation of a new premium finance company, Agency Premium Assistance Company (APAC) with enormous ramifications. APAC took over the business that had formerly been generated by IPAC with

[1] It is important to remember that this $28.25 million debenture was known by DOI and OFI to be included as an admitted asset on PILICO's financial statements and reports. See Exhibits "BB" and "CC". A security issued by an insolvent company (in this case IPAC) cannot lawfully be used as an admitted asset. La.R.S. 22:844; 22:844(C); 22:855.

apparently grave complications for persons other than Petitioners. See Exhibit "DD".

U. **December 20, 1989**:

Several things occur simultaneously:

- - Memorandum of Understanding is signed between OFI and IPAC. See Exhibit "EE".

- - Dale Jacobs, Ann Lemenager, and Pat Baker visited IPAC and verified that all CD's had been canceled and that a "debenture" of $28.25 million had been given to replace the PILICO CD's. See Exhibit "FF".

- - Emergency rule were filed in the Louisiana Register by the OFI, regarding a "Declaration of Emergency" as to limited function financial institutions. Although these rules had been referred to several times by memoranda from Dale Jacobs, they were not published in the Louisiana Register until December 20, 1989, five days after OFI approved the exchange of debentures for the CD's, without revoking the LFFI license of IPAC, and issuing a Cease and Desist Order only on the very day that it approved the exchange. The various conditions which the OFI permitted to exist with respect to IPAC were prohibited by the new "Emergency Rules".

54.

The foregoing documents -- produced in this litigation from the files of OFI and DOI -- establish, beyond any reasonable doubt, that OFI and DOI, working hand-in-glove, conceived and implemented a strategy during 1989 that was designed to bleed money and real assets out of PILICO and Midwest in exchange for worthless assets, including "debentures" issued by a company that DOI and OFI knew to be insolvent.

55.

The above-described factual allegations, testimony, and documents demonstrate, at a minimum, that the State Regulatory Defendants violated La.R.S. 22:844; 22:844(C); and 22:855, when they knowingly allowed "debentures", issued by an insolvent company, to appear as admitted assets on the books of PILICO and Midwest.

56.

The results of this cynical and illegal "strategy" were several: (1) PILICO and Midwest's chances of staying afloat were, at a bare minimum, greatly reduced, and it is not at all unfair to say that this "strategy" by the DOI and OFI actually caused PILICO and Midwest to fail; (2) When PILICO and Midwest did in fact fail, Petitioners were left "holding the bag" because the State had in effect stolen the assets that might have been used to pay them off and they were not covered by the LIGA Fund; (3) Policyholders of FF&C were covered by the LIGA Fund. Thus, when FF&C failed, because of all the real and valuable assets that the State had stolen away from PILICO and Midwest and put into FF&C, the amount that the LIGA Fund had to pay to policyholders of FF&C was greatly reduced if not eliminated, and thus, the State got what it wanted: It was spared another financial and political disaster, in the form of a "hit" to the LIGA Fund, so soon after the Champion Insurance debacle.

57.

The above allegations, testimony and documents create liability on the part of the State, and clearly establish the culpable involvement and negligence of DOI and OFI. The documents make it clear that, without the knowing assistance of the DOI and OFI, the insolvency of these affiliated entities would have been, of necessity, publicly acknowledged and publicly announced in 1988. The various transactions which siphoned money out of PILICO and Midwest, and into FF&C "to avoid another hit on the guaranty fund" could not possibly have taken place without the OFI's active complicity with the DOI and the private sector perpetrators.

58.

The actions by the OFI, in conjunction with the DOI, directly caused the loss of millions of dollars to Petitioners. As the DOI and OFI knew would happen, the Petitioners continued to be victimized by the future implications; i.e., that the bogus "CD's" of IPAC constituted some sort of real certificates of deposit, and were thus valuable assets on the books of PILICO and Midwest.

59.

The State Defendants had been aware of, and contributed to, the shaky financial condition of these entities on an ongoing basis, since at least 1986.

Factual Findings By The
<u>Louisiana Inspector General</u>

60.

On December 11, 1991, the State of Louisiana, by and through the office of the Inspector General, issued a detailed report on the matters at issue herein (hereinafter referred to as the "State Report"). The conclusions of the State Report constitute an admission of liability by the State.

61.

The State Report's findings make it clear that, "as a part of the December 15, 1989, agreement in which company assets were manipulated", FF&C (again, the "preferred child" of the LIGA Fund) was pumped full of cash which had been drained out of PILICO and Midwest:

> - - [FF&C] was assigned certain assets that wiped out the $11.9 million debt of IPAC, including various real estate.
>
> - - In the same December 15 agreement, Southshore agreed to make a capital contribution of $7 million to Fidelity.
>
> - - In addition to the $7 million belonging to [PILICO] which was diverted into FF&C in December, 1989, a substantial amount of cash from [Midwest] was also diverted into FF&C.
>
> - - The June 30, 1990, books of [Midwest] reflect that Midwest had provided a $4 million capital contribution to FF&C ...
>
> - - [A]n additional $1.3 million in loans and capital contributions to FF&C was also made from the funds of [Midwest].
>
> - - The need for these cash infusions extended beyond the mere operation of the insurance company at a loss.

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A".

62.

Also, in the summation section of the State Report, entitled, "WHERE DID THE MONEY GO?", it is stated that an additional $6.1 million was "donated funds (capital contributions)" to FF&C from Midwest. Id.

63.

Manifestly, at least $17 million of PILICO's and Midwest's cash, plus real estate and stock valued at over $15 million, are directly shown by the State Report to have been siphoned out of PILICO and Midwest and into FF&C, as a direct result of the December 15, 1989, machinations. These amounts do not take into consideration the more than $7 million not paid to PILICO as a result of Fred Dent's suggestion that Hibernia National Bank be paid instead. See Exhibit "OO".

64.

The State Report is unambiguous in its assessment of the December 15, 1989, agreement, which, as shown, was engineered mainly by Fred Dent and the OFI:

> THE AGREEMENT
>
> The key action in the takeover of [Riverside] and its affiliates by [Southshore] was approval by the [DOI] of a proposal detailing a series of transactions between the various companies. The series of documents was called the "Agreement".
>
> Although the stated purpose of the transactions was to enable Southshore more flexibility in moving funds to where they were needed at the moment, developments since then clearly demonstrate that the true objective was to give insolvent insurance companies in the Southshore group the appearance of being solvent in accordance with requirements of state insurance laws.

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A".

65.

The State Report also traces the flow of <u>Petitioners' funds</u> into FF&C, the state-preferred entity which would otherwise at that time have been a ward of the LIGA Fund. <u>See</u> State Report, Exhibit "A".

66.

The State Report also addresses the central importance of the OFI's assistance in keeping the IPAC Limited Function Financial Institution License alive -- so that the phony CD's could be left on the books, to be there to be exchanged for the equally phony IPAC "debentures":

> In November, 1989, IPAC was operating as a premium finance agency and as a Limited Function Financial Institution, <u>both licensed and regulated by the [OFI]</u> . The company was threatened with loss of its Limited Function Financial Institution license because of its inability to support the [CD's]. Such a license enabled the company to serve as a lender to its affiliates.
>
> To avoid loss of these licenses, Southshore engineered the complex series of paper transactions in the Agreement approved by the [DOI].

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A".

67.

It was not only <u>Southshore</u> that "engineered" the complicated series of paper transactions referred to by the State Report. The debenture swap was Mr. Dent's idea as Commissioner of OFI. As the State Report notes:

> ... the debenture was worthless and had it not been included as an asset of PILICO at that time [December, 1989], the company would have been insolvent.

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A".

68.

Actually, this is a somewhat imprecise use of language -- as is absolutely clear, the company was insolvent. A more precise description of the situation is that, had the "debenture" not been included as an asset of PILICO at that time, at the express direction and approval of both the DOI and OFI, PILICO would have appeared to be insolvent -- which would have been an accurate reflection of the truth. If the truth had come out, the DOI's and OFI's deliberate intentions to keep Petitioners "in the dark" would have been frustrated. Petitioners would have stopped paying their money, would have withdrawn the built-up value of their assets, and would not have lost the millions of dollars allowed to be drawn out of PILICO and Midwest and funneled uselessly into companies protected by the LIGA Fund.

69.

This State Report, a public document compiled by State Inspector General Bill Lynch, was prepared for and signed by Governor Buddy Roemer. The State Report constitutes the State of Louisiana's own official position on the facts at issue herein.

70.

The State Report constitutes an official admission of liability by the State of Louisiana.

71.

The attention of this Honorable Court is respectfully referred to the entire contents of the State Report (Exhibit "A"), but for convenience, certain of the State Report's conclusions and factual findings which constitute admissions of liability by the State are as follow:

> Objective of the State Report:
>
> The objective of the investigation is to bring to justice those persons both in the private sector and government sector responsible for perpetrating fraud upon the public and to recover any monies possible.

Findings of the State Report:

> Investigators have found a pattern of misrepresentation on official documents filed with the [DOI] which, in effect, enabled the insurance companies to continue in business as though they were in solvent condition.

State Report, Exhibit "A" at p. 2 (emphasis added).

> The State [DOI] failed in its duty to protect the insured public from mismanagement, abuse and corruption perpetrated by Southshore officials through a series of complex insider deals.
>
> Had the [DOI] not authorized continuation of the operations of PILICO, Midwest and Fidelity in December, 1989, policy holders and taxpayers would have been saved substantial sums of money which have been since lost through the diversion of premium income to other interests controlled by Southshore officials.

State Report, Exhibit "A" at p. 4 (emphasis added).

> The [DOI] permitted Southshore Holding Corp. to acquire Riverside Holding Corp. and its subsidiaries, approving an agreement that included a grossly inflated asset which was needed to give the companies the appearance of solvency.

State Report, Exhibit "A" at p. 41.

> The [DOI] failed to properly carry out this responsibility in evaluating assets claimed by the various insurance companies controlled by Southshore in their annual and quarterly reports.

State Report, Exhibit "A" at p. 44 (emphasis added).

72.

Inspector Lynch confirmed the substance of the State Report in sworn deposition testimony given in this action, as follows:

> Q: Did you find any evidence that the [DOI] sought to keep secret from the public what it believed to be the true financial condition of the companies?
>
> A: I believe, yes.
>
> * * * * * * * * * * * * * * * * *
>
> Q: But did you conclude in your report that the documents that were actually filed by these companies in

the public records were clearly false?

A: Absolutely.

Q: And isn't it also the case that you conclude that the [DOI] had to know they were false when they were filed?

A: We felt that was the case.

Q: And isn't it also the case with the [OFI], in its approval of the IPAC, APAC transactions?

A: We felt they knew.

* * * * * * * * * * * * * * * * *

Q: There are several paragraphs on that page, Mr. Lynch, that deal with an effort to "cure a $45 million debt which IPAC had with [PILICO] and [FF&C], incurred through the issuance of certificates of deposit for cash from those companies." Do you see that, Sir?

A: Yes.

Q: You are familiar with that from your investigation, with that transaction from your investigation?

A: Correct.

Q: What happened in that transaction was that $28 million worth of worthless certificates of deposit were exchanged for a worthless "debenture" for $28 million; right?

A: (Witness nods head affirmatively.)

Q: Isn't that right, sir?

A: Correct.

Q: And that was a paper transaction that you concluded was designed to give the appearance that this company was solvent, so that it could remain open; right?

A: That's right.

Q: And this is one of the --

A: Seems to me that there was, they were involved in conversations together with these transactions.

Q: You mean that the OFI and the [DOI] were consulting together on this?

A: Seems to me that was the case.

Q: And this is one of the transactions that you concluded that the regulatory authorities, if we can speak of it that way, had to have known was a fraudulent transaction at the time they approved it?

A: Correct.

* * * * * * * * * * * * * * * * * *

Q: Did your investigation reveal any legitimate reason why the state regulatory authorities would approve this certificate of deposit for debenture transaction?

A: Not in my judgment.

Deposition of Inspector Lynch, Exhibit "PP" (attached and incorporated herein in its entirety).

Testimonial Admissions By Officials And
<u>Employees Of The State Of Louisiana</u>

73.

In addition to those items of testimony already mentioned, Mr. Green has also given deposition testimony concerning his contacts in late 1988, or early 1989, with William McCartney, the Nebraska Insurance Commissioner. Mr. Green has testified that he was contacted by Mr. McCartney concerning problems with Midwest that had been detected by examiners of the Nebraska Department of Insurance. (Green Deposition, Exhibit "D" at p. 102). The Nebraska Commissioner arranged a meeting, which Green attended, along with DOI Chief Examiner Malcom Ward and other DOI staffers, to discuss the problems with Midwest. (Exhibit "D" at p. 100). The Nebraska officials were concerned about the intercompany transfers that were being made between and among Midwest and other members of the Southshore Group. Exhibit "3" to the Green Deposition sets forth in three (3) numbered paragraphs the type of intercompany transactions in question:

(1) On December 29, 1987, Bilbruck, Herman and Lafont caused Midwest to purchase from its affiliate, Alliance Life Insurance Company, a mortgage participation certificate issued by another affiliate, Riverside Corporation. [Midwest] paid $3,392,983 for this certificate. All but $280,700 of the individual mortgages serving as collateral for the participation certificate were double pledged since Alliance Life already owned most of those mortgages outright. Bilbruck, Herman and Lafont caused [Alliance] to sell the participation certificate to [Midwest] in response to contentions by the Kansas insurance examiner that the collateral was double pledged. The timing of this transaction is particularly important. The transaction was accomplished because of criticism by the Kansas examiner and just two days before the end of calendar year 1987. These individuals then caused [Midwest] to sell substantially all of the mortgage participation certificate to another affiliate in August, 1988, just days before the Nebraska examination of [Midwest] started;

(2) Beginning on November 8, 1988, and continuing until December 20, 1988, Bilbruck, Herman and Lafont caused a series of material transactions to take place between [Midwest] and one of its affiliates, Universal Guaranty Life Insurance Company. Ten loans were made by [Universal] to [Midwest], but were not evidence by promissory notes, and were not reported or filed as such by [Midwest]. The books of Midwest described these as "advances from parent";

(3) On November 4, 1988, Bilbruck, Herman and Lafont caused [Midwest] to transfer $17,000,000 to Bomar Investment Corporation to fund the purchase of Universal Guaranty Life Insurance Company. This transaction was never file [sic] or reported. Upon discovery of this transaction by the [DOI] examiners, Bilbruck, Herman and Lafont denied knowledge of the transaction. Subsequently, Bilbruck provided the [DOI] with a sworn statement, dated December 23, 1988, which stated that the $17,000,000 which was wire-transferred from [Midwest] on November 4, 1988, was presently in a bank account in the name of [Midwest] and was free and clear of any encumbrance. The examiners discovered evidence that, in fact, the $17,000,000 was wire-transferred from Universal Guaranty to [Midwest] on December 23, 1988, to be held by [Midwest] only until December 30, 1988, when it was wired back to Universal Guaranty. Pursuant to this wire transfer, Bilbruck then provided the [DOI] with a letter, dated December 27, 1988, which stated that the $17,000,000 never left the balance sheet of [Midwest]. He further stated that the funds had been transferred to

> [PILICO], another affiliate, to purchase certain investments that he would provide details on later. By letter of January 22, 1989, Bilbruck provided the [DOI] with a six-step explanation of what happened to the $17,000,000 in funds. This explanation was inconsistent with bank records from Hibernia Bank which the examiners obtained in attempting to document this transaction. [Midwest] funds of $17,000,000 were used to purchase Universal Guaranty Life Insurance Company. The advance from [Midwest] was not evidenced by any legal documentation generally associated with such transactions.

Exhibit "QQ" at pp. NDI101789-NDI101792.

74.

This same document further characterizes this series of transactions as follows:

> In essence, Bilbruck, Herman and Lafont operated [Midwest] and their other affiliates without regard to them be [sic] separate corporate entities. Funds and assets were transferred without following usual business formalities and without being fair and reasonable to all involved.

Exhibit "QQ" at p. NDI101791 (emphasis added).

75.

Thus the DOI was early on -- almost a full calendar year before the fateful transactions engineered by the OFI and OFI in December, 1989 -- fully aware of the impropriety of the intercompany transactions in which these companies engaged.

76.

It is clear that, not only did the DOI not take appropriate steps to rectify this course of action, but, instead, acquiesced and participated in similar transactions that were not fair and reasonable in violation of statutes and regulations. See, e.g., La.R.S. 22:843 and La.R.S. 22:844(H) (rules governing concentration of investments); La.R.S. 22:1214 (Louisiana Insurance Code's prohibition on unfair and deceptive practices); La.R.S. 22:731(2)(e) (failing to investigate properly the competence, experience, and integrity of the persons who controlled Midwest);

and Regulation 31:3(a)(1) of the Louisiana Insurance Regulations ("Transactions with affiliates ... shall be fair and reasonable").

77.

In addition, Commissioner Green also testified as follows:

Q: So it would be a violation of the insurance code for an insurance company to have included on its financial statement an asset or security that was a security that was issued by an insolvent company; isn't that correct?

A: I think so, yes.

Green Deposition, Exhibit "D" at p. 177.

Q: So you are not aware of anyone asking for any other valuation of the CD's, but you would agree with me that an excessive valuation of an admitted asset of an insurance company would be misleading to the policyholders and --

A: That is correct.

Q: And you would agree with me that it's important to policyholders and annuity holders and any other person who deals with a life insurance company for them to know the truth or accuracy of the valuation of the admitted assets of that insurance company?

A: Correct.

. . . .

Q: It would be important to the public that a life insurance company have the public's confidence in that company's ability to invest funds that annuity holders or policy holders had on deposit with that company; isn't that correct?

A: That's correct.

. . . .

Q: So it would be a violation of the insurance code for an insurance company to have included on its financial statements an asset or security that was a security that was issued by an insolvent company; isn't that correct?

A: I think so, yes.

Q: At the time that you were commissioner of the [DOI], it would have been a violation of the insurance code for a company, an insurance company, to include on its financial statement a value of 28 million dollars for an admitted asset if it were known that that asset was worth no more than 5 percent of that amount?

A: I would think that's correct.

Exhibit "D" at pp. 175-178 (emphasis added).

78.

In addition to Mr. Green's testimony in this regard, the Attorney General of the State of Louisiana concluded that:

> Commissioner Green has failed to conduct an independent audit of Midwest and secure an expert appraisal of its assets or take any other action to enforce provisions of the Louisiana Insurance Code to protect the interest of the policyholders.

Exhibit "RR".

Background of IPAC

79.

Insurance Premium Assistance Company, or "IPAC", was a finance company which primarily financed the insurance premiums generated by the activities of FF&C. It was a wholly owned subsidiary of PI. In 1988, the owners of these affiliated companies decided that IPAC should apply for a license to become a Limited Function Financial Institution, or LFFI. The Limited Function Financial Institution program was created by statute as a result of intense lobbying by the Champion insurance group, and the first LFFI license was issued on November 27, 1987, to United Financial Services, the premium finance company of the Champion insurance group. Louisiana's LFFI statute is believed to be unique among the fifty states, in that it permits insurance companies to finance their own premiums by the sale of so-called "Certificates of Deposit" issued by the finance company to the insurance company. The State Regulatory Defendants should have realized the inherent potential for abuse in this arrangement, and should have been put on notice by the uniqueness of Louisiana's approach that a heightened degree of scrutiny was required. In fact, the State Regulatory Defendants, and particularly the OFI, reacted to the IPAC LFFI license with heightened recklessness, instead of heightened scrutiny.

80.

The entire brief life of IPAC as an LFFI (from December 1988 to January 1990--a period of slightly over one year) was fraught with irregularities and highly unusual conduct by the OFI.

81.

For instance, on November 22, 1988, the Defendant Fred Dent, by letter to IPAC's counsel, effectively waived the statutory requirements and delays for IPAC to become able to issue "Certificates of Deposit", and interprets the Louisiana statute in such a way that it effectively eliminated the restrictive oversight purposes of the licensing procedure. In this letter, Mr. Dent, who was at that time Commissioner of Financial Institutions, notes that the OFI required "additional time to work out the inter-company lending issue", thereby acknowledging as of November 22, 1988, that there were inter-company investment limit problems involved with IPAC and its related companies.

82.

The Defendant Dent further accommodated the RHC/Bomar/PI management's efforts to engage in the corporate shell game by construing La. R.S. 6:451 et seq., and the Rules promulgated thereto, in such a way so that IPAC could operate indefinitely as a LFFI without having to apply to OFI for a license. He did this by construing the statute to mean that banking business could be engaged in by IPAC for an indefinite period without a LFFI license, until the income derived from its banking activities exceeded $50,000. This permitted the issuance of CD's, which the OFI knew were intended to be issued to affiliated companies, without the license contemplated by the Legislature. In fact, Mr. Dent's blanket waiver of regulatory control would have permitted IPAC, or anyone else, to lend money, receive deposits, and pay checks to anyone, anywhere, without any control or regulation by the OFI, so long as that person's income did not exceed $50,000. Mr. Dent's letter plainly states that until that $50,000 threshold is reached, no license even need be applied for. Obviously, there could be many ways for companies to evade regulation under this interpretation. Among others which come to mind are the creation of numerous companies, with a new banking institution springing up as soon as the preceding banking institution reached an income level of $49,999. By taking this interpretative stance, OFI also encouraged the RHC/BOMAR/PI management's efforts to obscure the source of either MIDWEST and/or PILICO's funding of the Universal Guaranty Life purchase through IPAC. Such a construction of the law was tantamount to a repeal of the statute by covert administrative fiat.

83.

On December 19, 1988, the OFI finally issued its License and Certificate of Authority to IPAC to act as an LFFI, with three provisos: (a) IPAC could issue CD's for cash or cash equivalents only; (b) IPAC could only accept deposits from three companies, namely PILICO, FF&C and Liberty Underwriters, another affiliated company of the Bomar Investment Group; and © upon receipt of cash or cash equivalents from the three above-mentioned companies, IPAC was authorized to make reinvestments.

84.

At the time the OFI issued this license, authorizing IPAC to take funds from PILICO and issue back to PILICO "Certificates of Deposit", PILICO's publicly-filed 1987 Annual Statement revealed that it had already been heavily laden with investments in affiliates, and that it had illegally issued two separate cash dividends of $1 million to an affiliate.

85.

The OFI further allowed IPAC to function as an LFFI before the appropriate administrative time constraints had run, and also allowed IPAC to circumvent even the watered-down requirements set down by the OFI. By way of example only, Universal Guaranty Life (yet another affiliate) bought a thirty-day certificate of deposit from IPAC in the amount of $3 million, on November 29, 1988. But Universal Guaranty Life was not one of the three companies authorized to purchase CD's from IPAC.

86.

In issuing the licenses on December 19, 1988, the OFI recklessly made the following findings, while having every reason to believe and understand that these findings were false:

(1) that the planned LFFI activities (<u>i.e.</u>, taking money from PILICO, FF&C, and Liberty Underwriters, and giving them back pieces of paper called CD's) were merely "incidental" to IPAC's other business activities, when the deposits from these companies financed virtually the entirety of IPAC's premium finance business;

(2) that the public interest would be served, when OFI's year's of experience with Champion's LFFI, United Financial Services, was indicating otherwise, and when no conceivable public interest could have been involved;

(3) that IPAC exhibited financial responsibility and fitness to command confidence in the community; and that IPAC proposed to conduct its activities in a safe and sound manner, when a cursory investigation of the BOMAR/PI/IPAC executive team's 1988 financial transactions would have revealed a plethora of regulatory violations in many states, as evidenced by Consent Orders issued against them by February of 1989 in Nebraska, Ohio, and Kansas.

87.

Further, on April 24, 1989, the OFI approved Certificates of Deposit in the amount of $40 million which had been "sold" by IPAC between December 28 and December 31, 1988, to its affiliates FF&C and PILICO, despite delinquency and irregularities in the reporting of these Certificates of Deposit and despite IPAC's failure to file the requisite unqualified, audited financials by March 30, 1989, as required by law. This "sale of CD's" by IPAC amounted to nothing more than a way to drain cash from its affiliates FF&C and PILICO (and ultimately from these Class Plaintiffs) and put it into IPAC, so that it could be further manipulated by the owners of these affiliated companies. This was done with the full actual knowledge and encouragement of the State Regulatory Defendants, as part of their own criminal purposes.

88.

As noted earlier, IPAC's license from the OFI limited IPAC to issuing CD's <u>only upon receipt of cash or cash equivalents</u> from the three specified companies. Yet, in May of 1989, OFI had knowledge that $17 million of the $40 million worth of CD's had been illegally issued by IPAC in exchange for "unsecured non-cash equivalents," which amounted to nothing more than journal entries in the books of PILICO. Notwithstanding this certain knowledge of OFI, OFI failed to issue a Cease and Desist Order and failed to revoke IPAC's license. These journal entries permitted PILICO to show millions of dollars worth of "CD's" on its books as assets, when in fact, no value had been given for the "CD's" other than a bookkeeping entry.

89.

The DOI, with the assistance and collaboration of the OFI, knowingly and deliberately chose to allow these "investments" to be carried as admitted assets, knowing the great potential for the public to be confused and deceived into the impression that these "assets" were conventional certificates of deposit from a legitimate and insured financial institution. Further evidence of management's fraudulent intent to pass off these "CD's" as legitimate bank instruments is the fact that they were shown on the books as separate $100,000 CD's, thereby encouraging the reader to believe they were prudently purchased so as to be protected by the $100,000 maximum insured amount for FDIC-insured financial institutions. In fact, PILICO's management used precisely this inference to extract more money from the Plaintiffs, as evidenced by correspondence from PILICO's Policyholder Service Department

Manager. That letter, dated December 31, 1989, fraudulently states, among other things, "We have had the greatest year in the history of the company," and further states as follows:

> If you have not contributed to your IRA for the 1989 or 1990 tax year, this is a perfect time. As you know, Public Investors is a Legal Reserve Company. We currently have $28,250,000 in CD's, $8,920,000 in Bonds, and $1,050,000 in debentures.

90.

This letter was blatantly fraudulent in its purpose and intent. It was designed to deceive the Petitioners into believing that PILICO owned $28,250,000 in legitimate and valuable bank CD's. It was made possible by the intentional, reckless, willful, and outrageous misconduct of the DOI and OFI in assisting the Southshore Management Group to make these representations, by permitting them to operate and to assert that their "CD's" had value, when these State Regulatory Defendants knew them to be valueless. Indeed, the situation is even worse, since PILICO did not even hold the worthless IPAC CD's when the letter was written, since OFI and DOI had permitted them to be swapped for equally worthless IPAC "debentures" on December 15, 1989. This sham transaction is discussed below. The State Regulatory Defendants knew that the illegal structure which they permitted and encouraged would be used to mislead and defraud the Petitioners. If they did not know this, then this failure is itself outrageous and scandalous misconduct.

91.

OFI also failed to issued a Cease and Desist Order in May of 1989, despite knowing that IPAC had failed to maintain the requisite ratio of equity to deposits of at least 10%. In fact, the ratio was only 8.5% as of 12/31/88.

92.

Despite all of the above knowledge, the State Regulatory Defendants permitted illegally-issued CD's to remain outstanding for almost a year. OFI and DOI knew that these were being shown on the books of Louisiana insurance companies, and that they were being represented to the public as assets of those companies. By June of 1989, the OFI had certain knowledge that IPAC was unable to honor these CD's, if PILICO or FF&C should turn in the "Certificates of Deposit" and demand the return of their cash plus interest. These "Certificates of Deposit" expired in June of 1989. Rather than expose the fact that PILICO's & FF&C's funds were irretrievably lost, the State Regulatory Defendants permitted IPAC to "rollover", or renew these CD's, thereby participating in a cover-up of the financial house of cards involving these affiliated companies. By this date, the nature and extent of the Champion insurance group's fraud, which was carried out in virtually the same way as set out above, was apparent to DOI and OFI. They knew or should have known the danger of permitting the IPAC arrangement to continue.

93.

By the end of May, 1989, the State Regulatory Defendants had actual knowledge of a valuation from the National Association of Insurance Commissioners' Securities Valuation Office, placing a value of "five cents on the dollar" ($.05/$1.00) on the IPAC Certificates of Deposit. In an outrageous breach of its regulatory responsibility, OFI still approved the rollover of the CD's on June 30.

94.

Throughout this period, the State Regulatory Defendants also allowed unlimited extensions of time for IPAC to fulfill its statutory obligation to file unqualified, audited financials. In other words, having actual knowledge that IPAC was insolvent, OFI gave IPAC permission to hide that fact from the public, including the Petitioners, although the law provided that IPAC was to reveal this information. OFI deliberately permitted this, without any justification whatsoever.

95.

When IPAC was allowed to sell CD's to PILICO ($28.6 million) and FF&C ($11.9 million) in December of 1988, as described above, the State Regulatory Defendants violated their duties to the Petitioners by allowing the following, inter alia, to occur:

1) allowing affiliated companies to disguise the source of funding of the Universal Guaranty Life Insurance ("UGL") purchase by RHC/BOMAR/PICO;

2) allowing the controlling holding companies to deplete subsidiaries PILICO, FF&C, and MIDWEST of high quality assets, in order to illegally finance a spectacular buying spree orchestrated by the officers and directors of the RHC/BOMAR/PICO holding company;

3) allowing the investments of policyholders, annuitants, and note holders of PILICO, MIDWEST, and PICO to be unsafely and unsoundly invested in affiliated companies under terms that were unfair and unreasonable, and which illegally exceeded the single entity investment limits;

4) allowing petitioners' invested monies, and often lifetime savings, to be used to purchase the IPAC CD's, at complete risk to petitioners' monies, which should have been conservatively and safely invested and/or held in safe and sound assets;

5) allowing the $28.6 million of Certificates of Deposit, and the subsequent $28.6 million debenture issued to replace them, to stand as admitted assets until the date of the 1988 year-end Examination Report of PILICO, thereby misleading petitioners and the public to believe that PILICO had capital and surplus (net worth) of $5,092,329, as reported in its 1988 year-end Annual Report, as opposed to being ($31,805,488) insolvent, as determined by the 1988 year-end Examination Report for PILICO; and

6) subsequently collaborating with the Southshore management to permit the replacing of the admittedly worthless IPAC CD's (classified as "short-term investments") by equally worthless IPAC "debentures" (misleadingly classified, with the State Regulatory Defendants' blessings, as "bonds.") Furthermore, the State Regulatory Defendants permitted these "bonds" to be completely omitted from PILICO's Part Two, Schedule Y of the 1989 year-end Annual Statement, which supposedly listed all transactions with affiliates.

96.

These IPAC "CD's" figure prominently in the State Regulatory Defendants' considered plan to drain assets away from PILICO and to favor FF&C at the expense of PILICO and the petitioners. For instance, in December of 1989, the Riverside/Bomar Group (which had owned all of the affiliated companies mentioned herein) arranged to sell these companies to a new set of investors known as the Southshore Group. The OFI and DOI were heavily involved in every facet of this transaction; indeed, the DOI appears as "Intervenor" in the ultimate sales transaction. Furthermore, the Defendant Fred Dent originated the idea that IPAC should issue the unsecured and worthless "debenture" in the amount of $28.25 million, and exchange it for the equally worthless IPAC "CD's" then held by PILICO. While PILICO'S "CD's" were exchanged for the worthless IPAC "debenture", at the suggestion of the Defendant Dent, a different treatment was accorded to Fidelity Fire's IPAC CD's. These were exchanged for valuable assets. At this time, the State Regulatory Defendants all knew, to a certainty, that IPAC could not pay the "debenture", and also knew that the National Association of Insurance Commissioner's report, valuing the "CD's" at five cents on the dollar, had already been noted in the year end 1988 examination report of Fidelity Fire by DOI, filed on June 2, 1989. Yet, the charade continued and the false and worthless "debenture" was created to be used as a plug figure, with the actual complicity and direct management involvement of the State Regulatory Defendants, so as to allow these interrelated companies to appear solvent, so that the public would not have the benefit of knowing the truth about their perilous investments.

97.

Numerous meetings were held between the purchasers, sellers, and these State Regulatory Defendants, and many of these meetings are documented. It is beyond a doubt that the State Regulatory

Defendants had a complete understanding of the financial consequences of this matter. Yet, fully understanding the matter, these State Regulatory Defendants allowed the IPAC CD's then held by PILICO--which were on the verge of expiring once again and thus of being exposed as utterly worthless--to be exchanged for an unsecured and equally worthless "debenture" also issued by IPAC, in the amount of $28.25 million. The purpose of this was nothing more than to deliberately give the <u>appearance and false impression</u> that PILICO was holding a valuable asset--a "debenture"--when in fact the State Regulatory Defendants fully knew this to be nothing more than a charade designed to hide the truth from these Petitioners and others in their position, and to induce more money from them. This action also served the purpose of saving the OFI from severe political embarrassment for its having allowed these worthless CD's to exist, knowing them to be worthless. Thus, the State Regulatory Defendants' actions here were part of a cover-up of their own failure to regulate according to law, and served further to cover up the damage their failures had caused, and were continuing to cause, to the Petitioners.

98.

At the same time that <u>PILICO's</u> "CD's" issued by IPAC were being exchanged for the worthless IPAC "debenture", <u>FF&C's</u> "CD's" issued by IPAC were exchanged for valuable assets, thereby furthering the planned illegal program of political preference, to the direct prejudice of the Petitioners.

99.

The aforementioned debenture transaction was approved by DOI and OFI, despite their own knowledge that IPAC could not of its own repay this debenture, and that the issuance of the debenture was a violation of PILICO's asset reserve requirements, the maximum single entity investment limitations, and the "fair and reasonable" requirement of affiliated transactions pursuant to Regulation 31, which the DOI is charged with enforcing.

100.

Furthermore, the State Regulatory Defendants were at least reckless in allowing anything at all to be exchanged for the IPAC CD's at this time, since the NAIC Securities Valuation Office report (valuing these CD's at five cents on the dollar) had already been noted in the year-end 1988 Examination Report of FF&C by DOI, which was filed on June 2, 1989.

101.

It is clear that the BOMAR and Southshore managements, who owned all these affiliated companies, knew and contemplated the result of this transparent transaction. Likewise, it is plain that the State Regulatory Defendants knew and contemplated the result of it. The only interested parties who did not know and contemplate the result of this transaction were those members of the public in the position of the Petitioners. These persons were prevented from understanding the transaction due to a deliberate, recorded, and acknowledged plan by the State Regulatory Defendants to conceal these machinations from the public, for their own purposes.

Specific Failure With Respect to the PICO Credit Companies

102.

The DOI and OFI further allowed the sale of assets of the various PICO Credit companies (e.g., PICO Credit Company of Many, PICO Credit Company of Jena, etc.) on June 30, 1989, for $35,300,000. These were also premium finance companies affiliated with PICO, PILICO, FF&C, and MIDWEST. They were subject to regulation by the OFI. None of the funds from this sale reached PILICO, despite the fact that PILICO had purchased $7,030,000 worth of PICO Credit bonds on January 1, 1989. Incredibly, on the same date that DOI and OFI allowed this sale of PICO Credit assets to take place and failed to oversee the distribution of the realized sums, OFI allowed the rollover of IPAC's CD's, $28 million of which had been issued to PILICO, knowing full well they were virtually worthless.

103.

The funds raised by the PICO Credit sale, on information and belief, went to assist the temporary "cure" of MIDWEST's impairment, which had been ordered in April, 1989, by Nebraska's DOI, and also went to shore up FF&C's continued financial hemorrhaging. None of the details, terms, and distribution of the PICO Credit sales transactions were reported clearly and concisely in a holding company registration statement and/or amendment and/or any annual report of PICO, PILICO, FF&C and/or MIDWEST.

<u>Other Instances of Outrageous, Malicious, Reckless Willful, Intentional, Flagrant And Fraudulent Misconduct By The DOI And OFI</u>

104.

Between November, 1986, and September 4, 1991, when the last of these companies was finally placed in liquidation, PICO, PILICO, FF&C, IPAC and MIDWEST engaged in numerous and flagrant violations of Louisiana Insurance, Banking, OFI, LFFI, and LIGA Statutes and Regulations, all of which were approved, encouraged, condoned, orchestrated, and permitted by the State Regulatory Defendants.

105.

These violations committed by these companies include, but are not limited to, the following: entering into unauthorized investments with affiliates; receiving uncollateralized promissory notes, certificates of deposit, and/or debentures from affiliates; purchasing overvalued real estate from affiliates and others; improperly receiving and advancing funds to affiliates; failing to pay LIGA assessments timely, if at all; misrepresenting the terms and conditions of various transactions between affiliates; making fraudulent and negligent representations as to the management and financial condition of these companies in order to induce the purchase of policies, annuities, and corporate notes; entering into material transactions with affiliates which were not on fair and reasonable terms and the precise nature and details of which were not clearly and accurately disclosed; substituting non-admitted assets for admitted assets; and failing to file timely and/or accurate annual statements and/or audited, unqualified financials and/or holding company registration statements and/or amendments, and other required statements and reports with DOI and/or OFI.

106.

The State Regulatory Defendants were at all relevant times aware of, supported, and caused the number and extent of the statutory and regulatory violations in the management and transactions of PICO, PILICO, FF&C, IPAC and MIDWEST.

107.

The State of Louisiana, and its Department of Insurance, through its Commissioner, breached its duties to the Petitioners by failing to administer and enforce the provisions of the Insurance Code and by failing to examine, supervise, and regulate all phases of PICO, PILICO, FF&C, IPAC, and MIDWEST; by acting negligently and by making negligent misrepresentations to the Petitioners during the course of its administration of the non-discretionary provisions of the Louisiana Insurance Code and Regulations as to PICO, PILICO, FF&C, and MIDWEST; and by exhibiting reckless, willful, outrageous, and malicious disregard and misconduct towards the Petitioners in conducting its discretionary functions; and by aiding others to negligently and/or intentionally and fraudulently violate provisions of the Insurance Code, including unfair and deceptive acts and practices; all by means of the following actions and inactions, among others:

a. Failing to enforce its own regulations;

b. failing reasonably to monitor the management of these companies;

c. ignoring historical financial data reported by PICO, PILICO, FF&C, and MIDWEST which reflected, as early as 1986, the diminution of admitted assets, and the flagrant violations of allowable affiliate transactions;

d. failure to invoke its regulatory powers at all; or, in the alternative, failure to regulate by its failure to take any of the following steps, among others, in a timely fashion: issuing consent orders, notices of impairment and/or cease or desist orders; suspending, revoking or not renewing certificates of authority; ordering target examinations; imposing monetary penalties, placing into conservation, rehabilitation or liquidation; and/or evaluating and disallowing non-admitted assets, as to the following companies, for the following periods relevant to this Petition:

(I) PICO, for violations in 1986, 1987, 1988, 1989, 1990, and/or 1991;

(ii) PILICO, for violations in 1986, 1987, 1988, 1989, 1990, and/or 1991;

(iii) MIDWEST, for violations in 1988, 1989, 1990, and/or 1991;

(iv) FF&C, for violations in 1988, 1989, 1990, and/or 1991;

(v) BOMAR, for violations in 1986, 1987, 1988, 1989, 1990, and/or 1991;

(vi) RHC, for violations in 1987, 1988, 1989, 1990, and/or 1991;

(vii) SHC, for violations in 1989, 1990, and/or 1991;

(viii) PRC, for violations in 1990 and/or 1991.

e. ignoring information regarding PICO, BOMAR, RHC, SHC, PRC, MIDWEST, ALI, and UGL, and their affiliate dealings, transmitted by other state departments of insurance (including, but not limited to, those of Texas, Ohio, Kansas, Oregon, and/or Nebraska), as early as 1986, which reports indicated severe impairments, statutory violations, and financial mismanagement;

f. failing to comply with Regulation 5, wherein DOI lists the protection to policyholders purportedly afforded by registration of insurance companies with the State of Louisiana Department of Insurance;

g. ignoring IRIS reports on PILICO, MIDWEST, and FF&C indicating non-compliance with NAIC ratios sufficient to require immediate regulatory attention;

h. issuing Certificates of Compliance to companies which were not, in fact, in compliance with the law;

I. failing to act in the face of mounting evidence of statutory violations, massive irregularities, and financial mismanagement;

j. ignoring multiple consumer requests and reports regarding these companies which indicated financial instability and mismanagement, and making misleading statements to consumers;

k. failing to administer the provisions of the Holding Company Law, Regulation 31, such that between January of 1986 and February 1 of 1990, with the exception of a single undated registration statement filed at least nine months late on the part of BOMAR/PICO, not another registration statement, and not a single amendment was filed on behalf of PILICO, FF&C, MIDWEST, PI, BOMAR, RHC, and/or PRC, despite the statutory requirement that such statements be filed within 15 days of any transaction among affiliates in excess of $150,000, which transactions regularly occurred. This severely prejudiced the Petitioners;

l. although knowing that the holding company registration statements and amendments were confidential and not subject to Public Records requests, and knowing that the DOI was therefore the single outside party with access to knowledge of intercompany transactions and with regulatory power to ensure their lawfulness, the DOI nevertheless failed to enforce registration of affiliate transactions and holdings as to PILICO, MIDWEST, FF&C, PICO, RHC, PRC and BOMAR, pursuant to Regulation 31.

108.

Many of the activities undertaken by the individuals manipulating the subject insurance companies, and permitted by the State Regulatory Defendants, involve a concerted effort to drain assets out of PILICO, and into various other companies. On January 18, 1987, PILICO illegally issued a $1 million cash dividend to an affiliated company. Less than a year later, on December 30, 1987, it illegally issued another $1 million cash dividend to an affiliated company, thereby contributing to its state of insolvency, as defined by the DOI's 1988 year-end Examination Report of PILICO. DOI learned of the first dividend declaration on March 1, 1987, at the latest, by means of PILICO's annual statement, and learned of the second dividend, at the latest, on March 1, 1988. The DOI took no regulatory action in response to either of these illegal dividend declarations, despite the fact that they appear to be prima facie illegal. Knowledge of these dividends <u>would</u> also have been available within 15 days of each dividend declaration, <u>if</u> PILICO had filed a Holding Company

Registration Statement and/or Amendment as required by law, or had DOI properly enforced such filings. In fact, DOI's failure to require these filings, even with actual knowledge of transactions which triggered them as a matter of law, further contributed to both the insolvency of PILICO and the ability of the owners of these companies to conceal the true intent and effect of their transactions.

109.

Allowing these dividends was particularly egregious as PILICO was thereby permitted to illegally distribute monies to PICO, its parent holding company, which was simultaneously raising monies by the sale of corporate notes to certain of the Petitioners, during the same time frame. A Prospectus pertaining to Corporate Notes, dated October 25, 1986, and issued by PICO, was supplemented on August 12, 1987. This was the date of BOMAR's purchase of PICO, which occurred after the first million dollar dividend issued in January, 1987, but before the second in December of that year. Advertisements in the Alexandria Town Talk regarding these securities guaranteed interest rates at 10.03 % for 5 years.

110.

The Supplement stated that PICO would continue to be conducted after the Merger in substantially the same manner as it was being conducted "at the present time." This was a material and negligent misrepresentation, in violation of the Insurance Code's prohibition on unfair and deceptive practices, La.R.S. 22:1214, especially given the fact that the very consummation of the Merger put Petitioners' investments precariously at risk, as the entire purchase price of $12,350,000 was being financed, 25% of which PI funded. Thus, with BOMAR's purchase, PICO's stockholders (i.e., the equity owners) were safely being bought out at a time when the company was steadily losing money, and Petitioners' investments (i.e., the debt instruments) were funding the buyout. Furthermore, despite purported concern for PICO and its subsidiaries' liquidity, which was jeopardized by the DOI-approved buyout, another million dollar dividend was illegally distributed within five months by PILICO. The State Regulatory Defendants still took no action as to the sale of the corporate notes, the distribution of the dividends, the blatant violations of La. R.S. 22:1214, and/or the fact that none of this activity was being reported to DOI in a holding company registration statement.

111.

Even after these companies were placed in liquidation, and were under the direct supervision of the Department of Insurance, the State Regulatory Defendants continued to participate in the direct solicitation of premium payments from the Petitioners, through the commission of thousands of acts of individual mail fraud by the mailing of deliberately false and misleading instructions and requests to the Petitioners that they should send in their premium payments, with the full knowledge that the companies were insolvent and the payments would be irretrievably lost.

<u>Specific Failure With Respect To The Riverside/BOMAR Purchase Of PICO</u>

112.

The DOI approved the acquisition of PICO by the Riverside/BOMAR group on August 12, 1987, and thereby flagrantly violated various statutory provisions. Among others, the DOI violated La. R. S. 22:731(2)(e) by failing to properly investigate the competence, experience, and integrity of the persons who controlled BOMAR; if it had conducted such an investigation, it would have discovered that the acquisition of PICO by these individuals was not in the interest of the policyholders of PILICO.

113.

The DOI further violated its duty to hold a public hearing before approving the aforementioned acquisition. Instead of holding a public hearing, notice of the hearing was purportedly "waived" with the result that only two persons were present at the hearing on July 29, 1987, namely counsel for BOMAR, the purchaser, and John Fontenot, General Counsel and Hearing Officer for DOI (who subsequently played a similar role in approving the purchase of PICO, RHC/BOMAR by SHC in December, 1989). No one was present to represent the interest of the companies being sold, their policyholders, or note holders, including the policyholders of PILICO, and the DOI representative utterly failed to do this.

114.

The DOI further failed in its duty by approving this transaction when the financial condition of the acquiring party was such as would necessarily jeopardize the financial stability of the resulting companies and prejudice the interests of their policyholders. Specifically, <u>the entire purchase price</u> for PICO ($12,350,000) was loaned to BOMAR as follows: approximately $7,300,000 was borrowed from the Hibernia National Bank, approximately $2,050,000 was borrowed from the BOMAR affiliate Alliance Life Insurance, and approximately $3,000,000 was borrowed from PI or its subsidiaries. Thus, the entire purchase was over-leveraged, and financing this purchase threatened the financial stability of both the acquired company and those companies from whom the borrowings were made, and adversely affected the liquidity of PI and its subsidiaries, as well as the financial stability of the entire BOMAR group.

<u>Failure With Respect To</u> <u>Reporting And Examination Requirements</u>

115.

In addition to the gross negligence, recklessness, wrongful acts, outrageous and malicious conduct, and breaches of duty in the preceding paragraphs, the DOI also breached its duty to the Petitioners in the following ways:

a. Failing to ascertain the extent of PILICO's impairment from 1987 on, FF&C's impairment from 1988 on, and MIDWEST's impairment from 1988 on, and then failing to issue a written requirement to each company for the impairment to be remedied, pursuant to La. R.S. 22:77, and thereby protecting the remaining assets of each company;

b. Failing to respond to violations on the part of PILICO and MIDWEST, their affiliates and holding companies, involving the amount and extent of investments in single entities, pursuant to La. R.S. § 22:843 and Regulation 31;

c. Failing to respond to the flagrant violations of the reporting requirements pursuant to L.R.S. 22:161, 22:1070; and 22:1451 on the part of PILICO, FF&C, and MIDWEST, whose officers verified by oath and certified to the amounts reported in the Annual Statements of these companies, which consistently omitted, distorted, and internally contradicted the financial transactions reported by these companies. These omissions, distortions, and contradictions include the following:

(I) On the 1987 year end PILICO Annual Statement is reflected a net gain of $759,328 for that year. On each year's Annual Statement, there is a column for reporting the previous year's results, for purposes of comparison. On the 1988 year-end report for PILICO, this figure for 1987 results is changed to reflect a net <u>loss</u> of ($759,328). The <u>1988</u> year end result is listed on the 1988 report as a net loss of ($959,000). Recording the previous year's result on the current year's Annual Statement is intended to allow the reader of that Annual Statement to compare the reported results of the current year with that of the prior year. By recording the 1987 result as a net <u>loss</u> of ($759,325), and by comparing it to the reported current year loss of ($959,000), the PILICO management gave the misleading impression that only an additional $200,000 was lost in 1988 over and above the amount lost in 1987; when, in fact, recourse to the actual Annual Statement of 1987 would show the reader that 1988 had resulted in an additional loss of $1.6 million;

(ii) On the 1988 year-end Annual Report for MIDWEST, in Part II of Schedule Y, the figure

$5,190,000 is shown in the column for purchases, sales, exchanges of loans, etc. For the same year in the PILICO Annual Report, the same exact figure is reported in the same column. Despite the fact that these two companies were commonly owned, and that it would be extremely unlikely that both companies had the same figure for this entry, apparently no effort was made by DOI to investigate the accuracy of either Report;

(iii) In the 1989 year end PILICO Annual Report, there is no mention of the $28 million debenture issued by IPAC on Schedule Y, Part 2 for affiliated transactions;

(iv) and most egregiously, at no time did the DOI insist that these companies reflect the corrected figures required to be made as per examination adjustments, on the subsequent annual reports available to the public. This resulted, by way of example only, in the continued misrepresentation to the public that PILICO had a net worth of over $5 million at the end of 1988 as reported by PILICO, rather than a <u>negative</u> net worth of over $32 million as adjusted by the examiners. Thus, even such inadequate regulatory examination as did occur regarding these companies was rendered useless by the DOI's failure to insist upon the implementation of its own conclusions.

d. By breaching its ministerial duty to annually ascertain the surplus and reserves of PILICO, FF&C, and MIDWEST as required by L.R.S. 22:162, which failure prevented the rehabilitation and/or conservation of these companies in a timely fashion, such that Petitioners would not have suffered the total loss they have suffered today. Specifically:

(I) by March 1, 1988, the DOI knew from PILICO's Annual Report that two separate million dollar cash dividends had been illegally issued by PILICO, and had thereby jeopardized its surplus;

(ii) by March 1, 1989, the DOI knew from PILICO's Annual Statement that it had liquidated high quality assets of $33 million and had illegally invested $28.6 million of the proceeds into affiliate IPAC's Certificates of Deposit of questionable value, if indeed they had any value at all;

(iii) by March 1, 1990, the DOI knew from PILICO's 1989 Annual Statement that over 86% of its invested assets were actually invested in affiliated companies, 98% of which was represented by the bogus IPAC "debenture" described above;

(iv) by March 1, 1989, the DOI knew from FF&C's 1988 Annual Statement that it was suffering "losses incurred" of 90% of premiums earned, and "other underwriting expenses incurred" of 40.7% and therefore was not viable as a profitable company;

(v) by March 1, 1989, the DOI knew from FF&C's 1988 Annual Statement that $11.9 MM of its assets had been illegally invested in affiliate IPAC's CD's of questionable worth, and shortly thereafter DOI knew that these CD's had almost no worth at all;

(vi) from FF&C's 3rd and 4th Quarter, 1988 Reports, the DOI was aware of FF&C's financial instability;

(vii) by February 6, 1989, the DOI was aware of the Consent Order issued against MIDWEST by the Nebraska Insurance Department, and other such Orders from Ohio and Kansas; and by April 11, an Order to Cure Impairment of $5 million had been issued against MIDWEST by the Nebraska DOI. These events could and should have been sufficient to cause the State of Louisiana to order its own target examination, whereby the extent of MIDWEST's impairment, insolvency, and/or unfair, unsafe and unsound dealings hazardous to its policyholders, could and should have been scrutinized and ascertained;

(viii) The actual degree of insolvency for PILICO, MIDWEST, and FF&C at the time of their ordered rehabilitations in 1991 was not at great variance with the figures established by DOI examination of these companies in 1988. By the DOI failing to act timely and responsibly with respect to PILICO and MIDWEST, petitioners have suffered the total loss they have today.

e. By failing to invoke the penalties provided by L.R.S. 22:1315(B) against officers, agents, or legal entities which perform services for an Insurer, who represent falsely, directly or indirectly, information to the DOI regarding assets, and/or materially misrepresent to the DOI the value of assets of the Insurer <u>or affiliate</u>, etc. in violation of La. R.S. 22:1315 (A).

f. By failing to invoke La. R.S. § 22:7 against PILICO, MIDWEST, FF&C, PICO, RHC, BOMAR, SHC and/or PRC, which provides for financial fines as well as the revocation of licenses against one who intentionally violates or aids another in violating the provisions of the Insurance Code. This statute is invoked by Petitioners against DOI, OFI, LIGA, and the State of Louisiana for aiding the officers and directors of PILICO, MIDWEST, PICO, BOMAR, RTC, SHC, PRC, and FF&C to violate the provisions of the Insurance Code.

g. By failing to salvage any value for policyholders and note holders of PILICO and MIDWEST by taking basic, prudent steps to conserve, preserve, market, and develop the remaining assets of these companies when every indication could and should have led them to do so as early as 1988 for PILICO, MIDWEST and FF&C. By way of example only, the State Regulatory Defendants squandered the opportunity to realize value from the licenses to do business which MIDWEST held in some 40 jurisdictions, by unconscionable delay, incompetence, and/or reckless disregard of every standard of the Insurance Code, the NAIC, and comparably funded and staffed state insurance departments. MIDWEST had value as a going concern which could have been realized through an orderly sale to persons who engage in the business of purchasing such assets of troubled insurance companies. MIDWEST's 40 licenses to do business alone had a value of approximately $50,000 each, for an aggregate of some $2 million, which could and should have been conserved for Petitioners. This conservation could and should have occurred by the timely and prudent transfer to interested third party purchasers who were, upon information and belief, actually presented to the State Regulatory Defendants.

h. Contributing to the financial demise of MIDWEST by allowing depletion and diversion of over $21 million of bona fide assets to other affiliated companies;

I. Responding to direct inquiries from consumers as late as Fall of 1990 that these companies were "in good standing, as per the Tax Department," thereby giving the misleading impression that the companies were solvent and in compliance with Louisiana law;

j. Allowing PRC Holding Company to be chartered on January 26, 1991, to hold PICO, PILICO and others, known by DOI to be insolvent, with the intent of providing yet another layer of insulation between PICO and PILICO, which had failed, and FF&G, MIDWEST, and IPAC, which were close to being insolvent if not already so, and LIGA, which was still reeling from the Champion claims;

k. Giving the approval, value, credibility, and respectability of the Department of Insurance to PI, PILICO, MIDWEST, FF&C, and IPAC, through inaction, delinquency, malfeasance, misfeasance, gross negligence, and/or wanton misconduct thereby misleading the policyholders and note holders it was mandated by law to protect;

l. And other actions or failures to act by the Department of Insurance, which Petitioners will bring in by way of amendment at the appropriate time.

Other Examples Of Inter-Company Abuse Sanctioned And/Or Permitted By The State Regulatory Defendants

116.

On November 7, 1988, the State Regulatory Defendants allowed PICO to purchase Universal Guaranty Life for $27.75 million, despite the knowledge of these Defendants that PICO could not afford to pay this purchase price, and must of necessity turn to its affiliates or subsidiaries for financing.

117.

In fact, the purchase of Universal Guaranty Life was financed by liquidating $33 million worth of valuable assets owned by PILICO. Another $17 million of assets owned by Midwest were liquidated, and $11.9 million of FF&C's assets were liquidated, thus raising a total amount of $61.9 million.

118.

Contradictory explanations were offered by the owners of these affiliated companies as to the timing, course, and path of Universal Guaranty Life's acquisition financing, as well as additional monies allegedly ear-marked for that purpose. These inconsistent explanations were proffered to DOI and wholly available to the DOI, yet DOI never demanded any explanation or conducted any investigation sufficient to explore the inconsistencies. By way of example only, one explanation offered was that, on November 4, MIDWEST transferred $15.75 million of the purchase price ($17 million, according to another version) through a complex series of transactions spanning five separate affiliated companies, ultimately transferring the funds to PICO. According to this explanation of the financing of Universal Guaranty, this $15.5 million (or $17 million) was put together with $7 million from the sale of MIDWEST to Universal Guaranty, and $3 million borrowed by IPAC on its credit line.

119.

Yet another explanation proffered by the Bomar Group is that the very purpose of PILICO's and FF&C's purchase of $40 million of IPAC CD's was to finance the UGL purchase. Yet, according to the public filings available to the State Regulatory Defendants, these CD's were reportedly purchased on December 28 and December 31, 1988, seven weeks <u>after</u> the Universal Guaranty Life purchase.

Furthermore, although PILICO did in fact liquidate $33 million worth of good and valuable assets in 1988, only $12.5 million of actual cash went toward the purchase of CD's from IPAC. The remainder of the $28.6 million of CD's which were purchased from IPAC for PILICO were illegally "purchased" via journal entry. Incredibly, the fate of the remaining cash generated by the sale of PILICO's assets remains a mystery. On PILICO's Annual Report for year-end 1988, schedule DA, Part 1, under the heading "All Short-Term Investments Owned as of 12/31," the purchase of $28.65 million worth of IPAC CD's, maturing June, 1989, was noted without any NAIC designation listed. In June of 1989, an OFI examination of IPAC's books revealed that $17 million of this $28.6 million amount was not purchased by cash, but merely purchased by a journal entry. It should have been obvious to persons having the sophistication and expertise of the State Regulatory Defendants that, in a very short period, $17 million in cash had been drained from PILICO, and was utterly unaccounted for in the inconsistent public filings made by PILICO and these other affiliated companies. The grossly reckless, or deliberate, failure by the State Regulatory Defendants to investigate and account for this missing cash, at a time when it might have been located, constituted a direct cause of the Petitioners' loss. Furthermore, if the purchase of UGL was indeed financed by PILICO's liquidation of $33 million in assets, DOI recklessly failed to trace or account for the $17 million that was transferred out of MIDWEST, which was also allegedly used to purchase UGL.

120.

Other suspicious and odd transactions were also ignored by the State Regulatory Defendants. For instance, the Riverside/BOMAR/PI Group purchased MIDWEST in late 1987 for $13 million, and within a year sold it to Universal Guaranty Life for $7 million as part of the Universal Guaranty Life acquisition, hardly fair and reasonable terms between affiliates, as required by Regulation 31. This last transaction was not reported to or approved by Nebraska's DOI, where MIDWEST was domiciled at the time. It was also unreported on any holding company registration statement in Louisiana, as required by law.

121.

During the months of November and December, 1989, approximately $40 million was transferred from Universal Guaranty Life to MIDWEST, and transferred back to Universal Guaranty Life within a few days, as reported in Universal Guaranty's Notes to Financial Statements in its 1988 Annual Report. These transfers were <u>not</u> reported in MIDWEST's Annual Report. These transfers appear to have been made by the owners of these companies with the deliberate aim of creating the false impression that MIDWEST owned the assets which were very briefly "parked" in MIDWEST from Universal Guaranty. This was evidently done to circumvent regulatory requirements in Nebraska, and to mislead regulatory authorities and the public there. The State Regulatory Defendants allowed it to occur. It could easily have been ascertained, if the State Regulatory Defendants had been performing their appropriate regulatory functions in requiring that appropriate reports be filed according to statute, and in conducting appropriate and prudent examinations of these companies. The failure of these State Regulatory Defendants to do so has led to direct losses by the Petitioners, and could easily have been avoided, given the in-depth groundwork exposing these violations provided by the Nebraska Insurance Department 1988 and 1989 year-end Examination Reports, which DOI had in its possession.

122.

None of these transactions was given the required approval of the Nebraska DOI, where MIDWEST was domiciled at the time, nor was it reported clearly, concisely, or consistently to the Louisiana

DOI in the year-end 1988 Annual Statements of these participating companies. Further, there was never any holding company registration filed with DOI, as required by law, to report any or all of the intricacies of this acquisition.

123.

It was, or should have been, grossly obvious to persons with the sophistication, expertise, and information available to the State Regulatory Defendants herein that complex inter-company affiliate transactions were occurring here, which should have been explored until satisfactory answers were given.

Further Violations With Respect To The Purchase Of These Companies By Southshore Holding Company

124.

Throughout the summer and fall of 1989, the State Regulatory Defendants assisted in orchestrating and approving the purchase by Southshore Holding Company of the Public Investors/BOMAR/Riverside group of companies on December 15, 1989. This purchase was conducted in violation of La. R.S. 22:731(2)(d), since the plan or proposals which Southshore had, to liquidate the various companies bought, sell their assets, or consolidate and merge them with other entities, or to make other material changes in their businesses and corporate structure, were unfair and unreasonable to policy holders of these insurers. Illustrative of this was the exchange of $28 million of IPAC CD's for a debenture of like amount, discussed at length above. Additionally, these plans were unfair, unreasonable, and/or fraudulent as to the Petitioners, in a variety of ways. For instance, Southshore attributed approximately $10 million dollars of value to a San Antonio, Texas building known as Parkway Plaza, when it was known to be worth no more than $1.5 million. If the DOI was unaware of the inflated value of this building, which was transferred to FF&C, then the DOI evidently believed that it was preferring FF&C to PILICO by allowing PI to transfer, through IPAC, what it believed to be $15.9 million of substantial assets to pay off the illegally-issued $11.65 million of CD's and $4.25 million of agents' balances owed to FF&C. Alternatively if the DOI was indeed aware of the inflated value of the Parkway Plaza building (which would have amounted to State-approved fraud), then it still was deliberately preferring FF&C to PILICO, by allowing a total of $7 million to be transferred to FF&C in this transaction, and zero to PILICO.

125.

As a further example of the State Regulatory Defendants' complicity in this matter, by an agreement made on or about November 17, 1989, the DOI allowed the Parkway Plaza building to be substituted on April 3, 1990 by a ranch in Weld County, Colorado, listed in FF&C's year-end 1990 Annual Statement as having a value of over $13 million, when said ranch was ultimately appraised at $636,000. In essence, the State Regulatory Defendants deliberately and carefully structured the Southshore/Riverside Sale, with the primary goal being to shore up FF&C, and thereby to avoid another draw upon the LIGA Fund, which had been recently diminished by the Champion disaster. This action was undertaken at the expense of PILICO and to the direct disadvantage of the Petitioners.

The "Single Business Enterprise" Treatment Of These Entities By The State Regulatory Defendants

126.

Numerous lawsuits were filed pursuant to the failing of the Southshore- and PRC-affiliated companies. Indeed, there have been several criminal proceedings in various Federal Courts over this matter. One of the lawsuits over these same transactions was State of Louisiana v. Public Investors Life Insurance Company, et al., bearing Civil Action No. 165,746, in which the State of Louisiana sought a declaratory judgment declaring the Southshore affiliated defendants to be a "single business enterprise."

127.

Without commenting upon the parties named or the merits of the State's suit, the Petitioners allege that the State Regulatory Defendants, as a matter of practice, and in direct disregard of their statutory and regulatory obligations, have indeed themselves routinely treated the Southshore and PRC affiliates as a "single business enterprise" at all times relevant hereto, to the great financial detriment of PICO, PILICO and MIDWEST annuitants, policyholders and note holders.

128.

The State Regulatory Defendants accomplished this treatment of the Southshore and PRC affiliates as a "single business enterprise" by failing to honor the corporate formalities between and among these entities, failing to insist upon arms-length transactions between the affiliates, failing to observe proper and legally-mandated distinctions between these entities, failing to insist upon proper documentation and financial reconciliations of their transactions, ignoring the plethora of affiliated transactions listed (even if incorrectly, incompletely or inconsistently) in the Annual Statements of the various companies, and in other ways. In this way, the State Regulatory Defendants compounded whatever misuse of funds, misappropriation of funds, and illegal transfers had already been effectuated by other parties, and actually encouraged them to further and perfect their unlawful conduct.

129.

However, regardless of the treatment of the affiliated companies by their officers and directors and by the State Regulatory Defendants, the Petitioners did not view PICO, PILICO, or MIDWEST as part or parcel of a larger "single business enterprise" to be toyed with, manipulated, depleted, and stripped of their assets at the whim of their officers, directors or the State Regulatory Defendants, whether motivated by greed, ambition, or fear of political scandal or criticism. When the Plaintiffs invested part or all of their life savings in PICO, PILICO or MIDWEST, they reasonably believed they were doing business with an individual company, standing alone, with its own assets and corporate formalities, and with a regulatory structure which each company had to comply with on its own. The Plaintiffs were never advised that the State Regulatory Defendants were actually treating these companies as one "single business enterprise" and allowing their owners to transfer assets between the companies without any regulation or proper accounting. Thus, the State Regulatory Defendants violated the Plaintiffs' legal expectations and rights by illegally treating the affiliated companies as a "single business enterprise," and by directing or allowing the assets of the various affiliated companies to be moved around in a sophisticated but corrupt corporate "sleight of hand." The State continues this conduct today by bringing its action for a declaratory judgment.

130.

In direct contravention of law, the State Regulatory Defendants manipulated PICO, PILICO, MIDWEST, FF&G, IPAC and their assets in an unsuccessful attempt to keep FF&G solvent and thereby to prevent another expensive and politically embarrassing tap of the LIGA Fund, following the Champion disaster.

131.

As evidenced by the terms of the Southshore/Riverside/PICO purchase in which the Commissioner of Insurance appeared as Intervenor, PICO, PILICO, MIDWEST were looted whenever FF&C threatened the LIGA Fund. The State Regulatory Defendants thereby reversed their statutory roles, and ensured that the assets of

PICO, PILICO, and MIDWEST would serve as insurance to the LIGA Fund, preventing its insolvency, rather than the other way around.

132.

The State of Louisiana, and its Office of Financial Institutions, through its Commissioner, breached its specific duty to Petitioners to administer and enforce the provisions of the Louisiana Banking Law, and to license, examine, and regulate all phases of IPAC by being negligent and making negligent misrepresentations during the course of its administration of the non-discretionary provisions of the Louisiana banking law and regulations and the Administrative Procedures Act; by exhibiting reckless, willful, wanton, and malicious disregard and misconduct disregard, pursuant to La.R.S. 9:2798.1, in its application of the Banking Law and Regulations to IPAC; and by aiding others to negligently and/or intentionally violate provisions of the banking law and the Insurance Code, including unfair and/or deceptive acts and/or practices, all by means of the acts and omissions articulated in the foregoing paragraphs of this Complaint, including the following, among others:

a. failing to enforce its own regulations;

b. failing reasonably to monitor the activities of IPAC;

c. failing, like DOI, to invoke its broad regulatory powers at all, or, in the alternative, failing to invoke them in a timely and effective fashion;

d. discharging its regulatory functions with the protection of the Louisiana Insurance Guaranty Fund as its primary objective, as opposed to the protection of the financial integrity and security of financial institutions and insurance companies permitted by OFI to invest in IPAC;

e. lending and conferring the OFI's approval, value, credibility, and respectability to IPAC, PICO, PILICO, MIDWEST, and FF&C through its participation in the approval of the Southshore/Riverside purchase, and by its inaction, delinquency, malfeasance, misfeasance, gross negligence and/or wanton misconduct, thereby misleading Petitioners whose interest it allegedly protected;

f. and other actions or failures to act by the Office of Financial Institutions, which Petitioners will bring in by way of amendment at the appropriate time.

133.

Jim Brown filed a RICO suit captioned James H. "Jim" Brown v. Kenneth D. Ross, et al., No. CV-92-1618 "A" (U.S.D.C. W.D. La. March 1, 1993). None of the companies or individuals named as Defendants in the Jim Brown RICO suit could have practiced their fraud on the members of the public or the Petitioners without the direct, deliberate, and active involvement of the State Regulatory Defendants in the structure, activity, and management of the enterprises involved herein. The ability of the Defendants named in the Jim Brown RICO suit to practice their deception hinged on the Office of Financial Institutions' approval, the Department of Insurance's approval, and the approval of Green, Dent, Ward, Wagner, and others. Among other particulars, the scheme and the success of the enterprise, could not have been made possible without the substitution of fake assets for the "CD's", all as described above. This was knowingly effected by the State Regulatory Defendants, for the direct pecuniary interest of the State and the State Regulatory Defendants.

134.

The initial problems of these insurance companies began to arise in late 1986. Based on annual reports filed with the DOI, PILICO had $34,000,000 in assets and $27,860,000 in liabilities for a capital surplus of $6,140,000. On December 29, 1986, a $1 million cash dividend was declared, and ultimately paid on January 18, 1987 to PICO (PILICO's 100% owner). This cash dividend exceeded 15% of PILICO's surplus at its most recent fiscal year-end (December 31, 1985), and thus required consent and approval of the Commissioner of the DOI, pursuant to Regulation 31:3(c). No such approval was ever sought or given, and the DOI never questioned the financial soundness of the decision to declare and pay the dividend, although the payment of this money was undisputably made. The DOI was well aware of such payments, since the Annual Reports of these companies demonstrating these payments were on file and reviewed by the DOI.

135.

In addition, as of December 31, 1986, PILICO's assets included "bonds" with a face amount of $8,046,819. Of this number, bonds with a face amount of $4,230,000, or 52.5% of the total, were issued by PICO credit companies. PILICO's total assets were stated at $33,940,582. Thus, the face amount of bond-holding investment in PICO (PILICO's 100% parent) represented 12.5% of PILICO's total assets. The statutory limitation on investment by an insurance company in a single entity is 5%, pursuant to La.R.S. 22:843 and La.R.S. 22:844(H). The DOI was aware of these facts and intentionally failed to take action to protect the Petitioners.

136.

Additionally, DOI either knew or should have known, or was deliberately ignorant of the fact that the financial condition of Bomar/Riverside, the acquiring party of the Southshore group, was such as would necessarily imperil the financial stability of the surviving entity, and thus prejudice the interests of PICO and/or PILICO policy holders such as Petitioners. Specifically, <u>the entire purchase price</u> paid for PICO ($12,350,000) was borrowed by Bomar, as follows: (approximately) $7,300,000 for the Hibernia National Bank; (approximately) $2,050,000 from PICO's own affiliate Alliance Life Insurance; and -- most astonishingly of all from the standpoint of regulatory prudence -- (approximately) $3,000,000 from PICO and/or its subsidiaries. (Exhibit "II", at p. A00101) Thus, as the <u>entire</u> purchase price was borrowed, this acquisition was grossly over-leveraged, and the financial stability of both

PICO and its subsidiaries, including PILICO, was unreasonably threatened. Moreover, the imprudence of this acquisition also adversely affected the liquidity of PICO and its subsidiaries, including PILICO, as well as the financial stability of the entire Bomar Group.

137.

Pertinent information about the over-leveraged acquisition of PICO was available to both DOI and OFI and deliberately ignored. The details of the highly leveraged purchase price, along with other pertinent information, were provided to DOI in a document entitled "Public Investors, Inc. Acquisition Information", and prepared in July, 1987. Exhibit "JJ". Specifically, page D000500 of this document, under the heading "Summary of Proposed Transaction" sets forth the source of the purchase price, i.e., borrowings from Hibernia National Bank ($7,300,000); Alliance Life Insurance Co., an affiliate of PICO ($2,600,000); and PICO itself ($3,000,000). Subsequently, PICO issued a Prospectus describing the offer of certain corporate notes on October 25, 1986 (Exhibit "KK"), and a Supplement to that Prospectus dated August 12, 1987 (Exhibit "II"). The date of the Supplement to the Prospectus was the date of Bomar's acquisition of PICO -- after the first $1 million dividend, paid in January, 1987, but before the second $1 million dividend, paid in December, 1987. Both the Prospectus and the Supplement were filed with OFI on August 17, 1987 (Harry C. Stansbury, Deputy Securities Commissioner).

138.

Given the additional information the DOI and OFI were privy to, the Supplement to the Prospectus conferred information sufficient to show that the transaction should never have been approved. Thus, the DOI and OFI were at least negligent in granting this approval and contributed to the unsecure and uncertain financial condition of this insurance holding company. The Supplement states in pertinent part as follows:

> If the merger is consummated, Bomar will be the sole stockholder of [PICO] and it is expected that Bomar will cause the registration of [PICO]'s shares under the [SEC] Act of 1934 to be terminated. Thereafter [PICO] will not be required to file periodic reports and proxy materials with the [SEC] and such information will not be publicly available.
>
> All of the money paid by Bomar to the shareholders of [PICO] in exchange for their shares of [the Common Stock] and the [Preferred Stock] of [PICO]will be borrowed from the following sources: (I) Approximately $7,300,000 from Hibernia National Bank ... ; (ii) approximately $2,050,000 from a company affiliated with Bomar; and (iii) approximately $3,000,000 from [PICO] or its subsidiaries. **The $3,000,000 to be loaned to Bomar by [PICO] or its subsidiaries will delete the amount of cash available to [PICO] and its subsidiaries for other uses and, to that extent will adversely affect the liquidity of [PICO] and its subsidiaries**.

Supplement to the Prospectus, Exhibit "II" at p. A001001 (emphasis added).

139.

Even the final disclaimer in the above quote from the Supplement is actually misleading on its face. Because, as noted, an additional $2,600,000 was borrowed from PICO affiliate Alliance Life Insurance (as set forth in the information provided to the DOI), a total of $5,600,000 (not merely $3,000,000 as the Supplement states) was borrowed from PICO and/or its affiliates. Thus, the financial stability of PICO was affected even more than the Supplement admits to, and the DOI knew this as much as a month before the acquisition took place.

140.

The Supplement also states that the affairs of PICO would continue to be conducted after the acquisition in substantially the same manner as they were being conducted "at the present time". This was a material and (at least) negligent misrepresentation, in violation of the Louisiana Insurance Code's prohibition on unfair and deceptive practices. La.R.S. 22:1214. The resulting merger put investments in PICO, including those of Petitioners, precariously at risk because a minimum of 25% ($3,000,000) of the purchase price was to be financed by PICO itself. Moreover, when the $2,600,000 loan from the PICO affiliate is considered, the total percentage of PICO's portion of the acquisition financing rises to 44.8%. As a result of the acquisition, PICO's stockholders, i.e., the equity owners, were safely bought out of their investment at a time when PICO was steadily losing money, and Petitioners' investments, i.e., the debt instruments, were funding the buy out.

141.

Furthermore, despite the purported concern for PICO and its subsidiaries' liquidity -- which was already severely jeopardized by the DOI-approved buy out -- another $1 million dividend was illegally distributed within five months by PILICO. The State Regulatory Defendants still took no action against the sale of the corporate notes, the illegal distribution of the dividends, the blatant violations of La.R.S. 22:1214, nor the fact that none of this activity was being reported to the DOI in a Holding Company Registration Statement, which was by itself a clear non-discretionary breach of Regulation 31 of the Louisiana Insurance Regulations.

142.

DOI either was or should have been aware that even PICO's pre-acquisition stockholders were concerned about the over-leveraged transaction and the potential after-merger liquidity problems. The selling shareholders originally were to finance $2.5 million, or 20% of the purchase price. These shareholders reconsidered, however, and requested that they be paid in cash. See no. 4 on page D000501 of Exhibit "JJ".

143.

In addition to the problems of overleverage and regulatory reporting violations, the DOI's approval also flagrantly violated various other regulatory provisions. The DOI violated, inter alia, La.R.S. 22:731(2)(e) by failing to investigate properly the competence, experience, and integrity of the persons who controlled Bomar. If the DOI had conducted such an investigation, it would have discovered that the acquisition of PICO by these individuals was undeniably not in the best interest of the policyholders of PICO, including Petitioners, to whom the DOI owed its primary duty. Indeed, knowledge of the lack of experience, competence, integrity, and financial wherewithal of the Bomar Group was available from a simple reading of the Supplement filed with the OFI in August of 1987. Thus, this knowledge was either known or should have been known to the DOI. For example, the Supplement states in pertinent part as follows:

> Bomar and Acquisition were each organized ... in June of 1987, for the purpose of facilitating the merger [with PICO]. Bomar and Acquisition have not engaged in any business since their incorporation other than in connection with the transactions contemplated by the Merger Plan and the Joint Agreement [with PICO].

Exhibit "II" at p. A001002.

144.

The DOI further violated its duty to Petitioners to hold a public hearing before approving the acquisition of PICO. Instead, notice of the hearing was purportedly "waived", with the result that only two persons were present at the "hearing" on July 29, 1987, namely: counsel for Bomar and one John Fontenot, General Counsel and Hearing Office of the DOI itself. There was no independent counsel present, nor indeed anyone at all, to represent the interests of the companies to be acquired, nor their policyholders, or their note holders, including Petitioners as note holders and policyholders of PILICO. The DOI representative, Mr.

Fontenot, failed utterly in this responsibility which was his by statute and regulation.

145.

Despite an extremely over-leveraged acquisition, and an inexperienced and unqualified management, the Bomar Group from the very beginning had plans for aggressive growth and expansion which were known to the DOI and OFI. For example, the Supplement, at page A001002 states: "... Bomar is hopeful that the reorganization and Merger [with PICO] will provide [Bomar] with opportunities for growth that it might not otherwise have". <u>See also</u> p. D000503, <u>et seq</u>. of Exhibit "JJ".

146.

The financial problems of the PICO/PILICO companies actually did arise as the result of mismanagement subsequent to 1987. This fact has been conceded by the State itself, as follows:

> While the focus of investigations is on Southshore, there is cognizance that a previous holding company called Bomar Investment Co., which changed its name to Riverside Holding Co., <u>had mismanaged the group in the period 1987-89</u>.
>
> . . . .
>
> Most of these companies were subjected to financial shock during the period of 1987-89 when they were under the control and management of Bomar Holding Co. which later changed its name to Riverside Holding Co. Southshore acquired the group from Riverside. <u>While the period these companies were under the control of Riverside/Bomar is replete with mismanagement</u>, the focus of this investigation has been on the activities of Southshore.

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A" (emphasis added).

147.

The financial shocks and abuse suffered by PICO, PILICO, and the other PICO affiliates -- as conceded by the State itself -- would not have happened but for (at least) the intentional, flagrant, outrageous misconduct of the DOI and OFI in carrying out their ministerial duties of reviewing the readily available data and information which raised numerous red flags and should have resulted in (at least) more careful regulatory oversight.

148.

As bad as it was, the actions and inactions of the State Defendants, during 1986-1987, pale in comparison to what occurred in 1988-1989, when violations regarding investment limitations and affiliated transactions had become known to regulatory authorities all over the United States, and with actual examinations being conducted in Nebraska, Ohio, Kansas, and South Carolina. Indeed, the DOI's own 1988 year-end reports of PILICO and FF&C found these companies to be <u>insolvent at that time</u> (<u>See</u> Exhibits "BB" and "CC"), yet they were not put into liquidation, nor was any other appropriate or reasonable action taken. False figures were known by the DOI and OFI to exist in the Annual Reports of these companies and their various affiliates, but these false figures were allowed to remain in the public records, so as to give a false impression of financial stability.

149.

In late 1988, or early 1989, the Nebraska Commissioner of Insurance, William McCartney, contacted DOI Commissioner Doug Green and informed him of problems with this group of insurance companies (referred to as the Bomar/Riverside Group at that time). Exhibit "D" (Green depo.) at p. 100. Green and Malcom Ward, Chief Examiner of the solvency division of the DOI, traveled to Kansas City, met with Mr. McCartney and commissioners of other states involved, and engaged in a frank and open discussion of the problems with the Bomar/Riverside Group. Exhibit "D" at pp. 100-101. Green and Ward, and thus the DOI, were made fully aware of these companies' problems (if indeed they did not already know of them) relating to illegal or improper intercompany transactions. Exhibit "D" at pp. 103-104. As a result of this meeting, Green instructed the DOI's

Chief Examiner (Ward) to put these companies on a priority basis and to conduct an examination. Exhibit "D" at p. 104. So, as previously discussed, in early 1989, the DOI commenced an examination of the Bomar/Riverside companies. Exhibit "D" at pp. 105-108.

150.

On December 2, 1993, Mr. William McCartney, the Nebraska Commissioner of Insurance, gave deposition testimony in an Iowa lawsuit, entitled Noel v. Dane Bosworth, Inc. In that deposition, Mr. McCartney testified that DOI Commissioner Green represented to him as follows:

> Q: Can you tell us what [the DOI] represented they would do?
>
> A: Yeah, that they wouldn't engage anymore in these borderline interaffiliate transactions, that the bad assets in the company would be -- well, at the time we looked at it year-end 1989, they were taken out of the company and replaced with good assets.
>
> That as you are aware, I hope you are aware, if you are not, <u>we also permitted that redomestication upon some representations to us from the Commissioner of Insurance in Louisiana that this company wouldn't be permitted to invest in the kinds of assets that had gotten it in trouble anymore, and they would effectively oversee and monitor the company, and, in fact, that didn't happen</u>.

Excerpts of the deposition of Mr. McCartney, attached hereto as Exhibit "NN", at pp. 14-15 (emphasis added).

151.

In fact, the DOI did not either keep its promise to the Nebraska Commissioner, <u>or</u> fulfill its duty to regulate these companies properly. The State has actually conceded as follows:

> Southshore officials manipulated millions of dollars in premium income and valid assets, exchanging them for worthless or low quality assets when they took control of the group of

> companies that included Midwest ..., [PILICO], [FF&C], and [PICO].
>
> <u>[DOI] officials failed to take proper action to prevent the series of events which included the take-over of that group of companies by Southshore</u>. From the outset, the [DOI] should have challenged the inclusion of questionable assets, such as $10 million for a still unfinished office condominium called Parkway Plaza in San Antonio, Texas, and $13.69 million for a Colorado ranch that is valued at less than $750,000 purchase price, <u>which enabled the insurance firms to continue collecting premiums from the public</u>.

Report of the Louisiana Inspector General (December 11, 1991), Exhibit "A".

152.

Thus the State's regulatory failures and breaches of its duty to Petitioners, motivated by the State's own pecuniary interest to favor FF&C and the LIGA, set the stage for the financial transactions, including further breaches of the State's duty to Petitioners.

153.

In addition, OFI participated in yet other illegal and improper transactions between and among the Southshore Group of companies, all to the detriment of PILICO and/or Midwest. At least some of these transactions were actually suggested by OFI Commissioner Fred Dent.

154.

In Mr. Dent's June 15, 1989, meeting with Mark Herman of Bomar and other IPAC officials, Mr. Herman reported that the PICO sale had concluded with $9,358,000 in cash proceeds retained. <u>See</u> Exhibit "OO". Commissioner Dent asked how leveraged the companies were. Mr. Herman replied that the debt to Hibernia Bank, which was $1.8 million a month previously, had increased to $7.3 million. <u>Id</u>. Mr. Herman then stated that the purpose of the present meeting was to discuss the routing of the $9.3 million sales proceeds, which were being held by Hibernia.

155.

At this point, PICO owed $6.93 million in debentures to PILICO and $1.55 million to FF&C. Mr. Dent asked why the money could not be paid directly to Hibernia, and was told that in that event, PICO would not have the cash to repay the debentures due to PILICO and FF&C. See Exhibit "OO".

156.

In fact, subsequently in 1989, the assets and businesses of PICO, and its affiliate consumer finance companies, were sold for cash, but none of the cash was remitted to PILICO. The PICO affiliates were effectively reduced to shell companies without paying off their debenture obligations to PILICO. The OFI's own examination report of PILICO determined the debentures not to be adequately secured and thus not allowable as admitted assets.

COUNT I: OUTRAGEOUS, RECKLESS, WILLFUL, INTENTIONAL, FLAGRANT AND/OR FRAUDULENT MISCONDUCT BY THE STATE REGULATORY DEFENDANTS

157.

The foregoing paragraphs of this Petition are hereby incorporated by reference.

158.

The State Regulatory Defendants breached their duties to the Petitioners by failing to administer and enforce the provisions of the applicable laws, acted negligently and made negligent misrepresentations during the course of their administration of the non-discretionary provisions of the laws, and exhibited intentional, reckless, willful, outrageous, and malicious disregard and misconduct toward the Petitioners in conducting their discretionary functions, and by aiding others to negligently and/or intentionally and fraudulently violate provisions of the Louisiana laws, including unfair and deceptive acts and practices by said others, all as set out in the preceding paragraphs of this Petition.

159.

These activities directly and proximately caused the damages to these Petitioners, all as set out herein. The State Regulatory Defendants are solidarily liable for these damages.

160.

The State Regulatory Defendants aided and abetted the illegal activities of the RHC/BOMAR/PICO group and the Southshore/PRC group, among others, all to the direct pecuniary loss of these individuals.

161.

The State Regulatory Defendants were aware of the aforementioned irregularities and illegal activities, and knowingly rendered substantial assistance to them. These activities caused substantial damage to the Petitioners, all as set out above, and the State Regulatory Defendants are solidarily liable for these damages.

COUNT II: OUTRAGEOUS, RECKLESS, WILLFUL, INTENTIONAL, FLAGRANT AND/OR FRAUDULENT MISCONDUCT BY OFFICIALS OF THE STATE FOR WHICH THE STATE REGULATORY DEFENDANTS ARE LIABLE

162.

The foregoing paragraphs of this Petition are hereby incorporated by reference.

163.

Official of the State Regulatory Defendants, such as Fred C. Dent, Douglas D. Green, Thomas Bently, Malcolm Ward, while acting within the course and scope of their employment by the State (by and through the DOI or OFI), systematically engineered, manipulated and acquired control over the group of companies at issue herein, and further engaged in intentional, malicious, willful, and outrageous misconduct all for the benefit of the State, as outlined above.

164.

These activities directly and proximately caused the damages to these Petitioners, all as set out herein. The State Regulatory Defendants are solidarily liable for these damaging activites of its own officials and employees.

165.

The State Regulatory Defendants were aware of the aforementioned irregularities and illegal activities of its own officials, and knowingly rendered substantial assistance to them. These activities caused substantial damage to the Petitioners, all as set out above, and the State Regulatory Defendants are solidarily liable for these damages.

PRAYER FOR RELIEF

The acts and omissions of the Defendants, as described herein, entitle the Petitioners to a Judgment against the Defendants jointly, severally, and in solido, as follows:

a. Rescinding their purchases of insurance policies, annuities, and notes, as the case may be, awarding them restitution of all monies tendered and consideration paid therefor, and ordering legal interest from the date the consideration was paid by each Petitioner; and

b. Alternatively, for all damages, including, but not limited to, the following:

(I) Loss of insurability by certain Petitioners who became uninsurable over an extended period of time during which Defendants continued to engage in acts and omissions as herein alleged, and concealment by the Defendant of the financial condition of the insurance companies named herein;

(ii) Loss of payment of insurance and annuity proceeds and other amounts due and payable, as a consequence of the occurrence of events covered by insurance and annuity contracts between certain Petitioners and the insurance companies referred to herein;

(iii) Loss of cash values and any other amounts (together with any and all additions thereto, including, but not limited to, dividends and interest) accrued under and in accordance with insurance and annuity contracts between certain Petitioners and the insurance companies referred to herein;

(iv) Loss of premiums and any other consideration paid for all insurance and annuity contracts that were in fact worthless when purchased or which became worthless during such time periods that the companies named herein were hopelessly insolvent and during which time period such insolvency was concealed by the Defendants and/or such companies were misrepresented by the Defendants to be solvent thereby causing and/or inducing Petitioners to pay said premiums;

(v) Loss of principal and any other consideration invested in annuity contracts and income and additions accrued and accumulated on said amount or amounts invested in annuity contracts issued by the insurance companies referred to herein to certain Petitioners;

(vi) Loss of principal and any other consideration invested in notes and other securities, instruments, and contracts together with all income and additions accrued and accumulated on or in connection with same, between certain Petitioners and companies referred to herein;

(vii) Impairment of the financial condition and credit worthiness of certain Petitioners;

(viii) Losses of homes, farms, businesses, income, profits and any and all immovable and movable property by certain Petitioners resulting from the financial ruin of these certain Petitioners due to the failure and collapse of the companies named herein;

(ix) Damages to financial standing and reputation of certain of the Petitioners;

(x) Pain, suffering, embarrassment, humiliation, emotional distress, and mental anguish resulting from the financial from the financial chaos and ruin experienced by the Petitioners;

(xi) Any and all other damages of every nature and kind suffered and to be suffered by Petitioners as a consequence of the acts and omissions of the Defendants.

166.

Petitioners also pray for Judgment against the Defendants jointly, severally, and in solido for attorneys' fees, judicial interest, costs, and all expenses of these proceedings and for any and all other general and equitable relief.

WHEREFORE, the Petitioners pray that there be judgment for monetary damages in their favor and against the Defendants, that the Petitioners be awarded their reasonable attorneys' fees and costs, and for such other and further relief as law, equity and the nature of the case may require.

The Petitioners respectfully pray for a trial by jury, to the full extent permitted by law.

Respectfully submitted, this 1st day of March, 1999.

PERCY, SMITH, FOOTE & GADEL

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ATTORNEYS FOR PLAINTIFFS

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing has been served on all counsel of record by placing same in the United States mail, postage prepaid and properly addressed, this 1st day of March, 1999.

Dan B. McKay, Jr.
John Gregory Odom
David P. Smith
Stuart E. Des Roches

PLEASE SERVE:

1. **The State of Louisiana,** through the Department of Insurance by serving James H. Brown, its Commissioner, Baton Rouge, Louisiana.

2. **The Department of Insurance of the State of Louisiana,** by serving James H. Brown, its Commissioner, Baton Rouge, Louisiana.

3. **The State of Louisiana,** through the Office of Financial Institutions, by serving Larry L. Murray, its Commissioner, Baton Rouge, Louisiana.

4. **The Office of Financial Institutions,** by serving Larry L. Murray, its Commissioner, Baton Rouge, Louisiana.

5. **The State of Louisiana,** by serving its Attorney General, Richard Ieyoub, Baton Rouge, Louisiana.