

ANNUAL REPORT
OF
EDUARDO S. ESPINOSA,
RECEIVER
FOR
RETIREMENT VALUE, LLC

As of
December 31, 2018

State of Texas v. Retirement Value, LLC, et al.
Cause Number D-1-GV-10-000454
126th Judicial District Court of Travis County, Texas

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This report updates the investors, the Court and the public as to the Receivership's status as of December 31, 2018. This report supplements all prior reports by the Receiver and should be read in conjunction with those reports.

I. Introduction

This case arises out of an investment scam perpetrated by Retirement Value and its principals. The Texas State Securities Board ("TSSB") shut down the scam at the end of March 2010 and the Court appointed the Receiver in May 2010. Since that time, the Receiver has worked to recoup as much as possible from Retirement Value's assets and principals. The Receiver has been administering the estates assets in accordance with the Plan of Distribution adopted by the Court on July 20, 2012.

II. The Underlying Scam

From April 2009 through March 29, 2010, Retirement Value raised more than \$77 million from more than 1,100 investors through the sale of securities. Each security was structured as a loan to Retirement Value, whereby the investors provided Retirement Value with funds in exchange for Retirement Value's promise to pay a fixed sum of money at an undetermined date in the future. The amount that Retirement Value agreed to pay was tied to the calculated life expectancy of insureds under life insurance policies owned by Retirement Value. In all instances, Retirement Value agreed to pay a return of 16.5% simple interest per year for the insured's projected life expectancy. Thus, if the insured had a projected life expectancy of 64 months, Retirement Value would pay \$18,800 on a \$10,000 investment. The date on which the insured under the policy died set the date that the loan matured and when Retirement Value would be required to repay the loan. The loan's maturity date did

not affect the amount of money that Retirement Value was obligated to pay the investor, except that investors were entitled to a return of unused premiums, if any. Each investor was allowed to select a life insurance policy or policies to which to tie his or her investment from a rotating portfolio of ten policies maintained by Retirement Value.

Retirement Value made significant misrepresentations as well as omissions of material facts as to the nature and value of the investments it sold, including the following:

- Retirement Value falsely claimed that investors were irrevocable beneficiaries in the policies.

As an inducement to purchase the policies, Retirement Value represented that each investor would be an irrevocable beneficiary in the policy in which he or she invested. As irrevocable beneficiaries, the investors would be entitled to direct payment from the insurers and Retirement Value, as owner of the policies, would be unable to change beneficiaries. In fact, however, the named beneficiary was a law firm, Kiesling Porter Kiesling & Free, that owed no duty to the investors and was itself only a revocable beneficiary.

- Retirement Value falsely claimed to escrow investor funds.

Retirement Value represented that all investor funds would be deposited in “escrow accounts” that would be managed by Kiesling Porter in its role as an “independent escrow agent” and that Retirement Value would not receive or handle investor money. In addition, Retirement Value represented that funds would be placed in sub-accounts tied to each policy. These representations were untrue. First, the funds loaned to Retirement Value by the investors were not held in escrow and Kiesling Porter did not act as an escrow agent. Second, Retirement Value (with the acquiescence of Kiesling Porter) repeatedly commingled the funds held in the sub-accounts.

- Retirement Value falsely claimed that the insureds had less than a 10% chance of surviving beyond Retirement Value’s projections.

When selling the investments, Retirement Value provided life expectancy projections from a third-party provider, Midwest Medical, representing that there was a 90-95% chance that the insured would be dead by the projected life

expectancy and a 95-98.5% chance of death within twelve months. Retirement Value's representations as to this risk were wholly false. The life expectancy projection used by Retirement Value and presented to the investors was Midwest Medical's calculation of the insured's median life expectancy. It is the point at which 50% of the people who are statistically similar to the insured are expected to have died and 50% are expected to remain alive. Retirement Value actively hid its use of median life expectancies.

- Retirement Value did not disclose that Midwest Medical's projections were far outside industry norm

At the time that it was touting the reliability and good reputation of Midwest Medical and its projections, Retirement Value knew that Midwest Medical was an industry outlier and that projections from other providers were routinely two to three times longer.

- Retirement Value did not disclose that Midwest Medical's principal was a convicted felon who had repeatedly been accused of falsifying life expectancy projections.

At the time that it was touting the reliability and good reputation of Midwest Medical and its projections, Retirement Value knew Midwest Medical's principal, George Kindness, was a felon and that he had been accused of falsifying life expectancy projections and misrepresenting himself as a physician. When potential investors became aware of Midwest Medical's reputation, Retirement Value hid the fact that it was relying on Midwest Medical's projections.

In addition to these misrepresentations and omissions, Retirement Value made numerous others. For further details, please see the Receiver's Initial Report at pages 7-20.¹

The principals of Retirement Value – Ron James, Don James, Richard Grey, Wendy Rogers, Michael McDermott and Michael Beste – have been indicted for their roles in Retirement Value's fraudulent scheme. Trials are set to begin in November 2019.

¹ The Receiver has filed all of his narrative reports with the Court and posted them on the Receiver's website, www.rvllreceivership.com.

III. Plan of Distribution

After significant litigation and review of several alternatives, the Court confirmed a plan of distribution (the “Plan”) recommended by the Receiver in July 2012. The Plan provides that the Receiver will manage all of the policies owned by Retirement Value and those owned by an affiliate, Hill Country Funding, for the benefit of the creditors of both entities. No investor has an interest in any particular policy; instead, they (and the remaining creditors) have a claim against all assets of the estate. The Receiver is to manage the portfolio so that the proceeds from the first policies to mature will be used to pay premiums on the remaining policies. When (and only when) the Receiver has more cash available than is needed to ensure the continued payment of premiums may the Receiver make a distribution.

Each investor holds a claim against the estate equal to the amount that he or she invested less any payments received from Retirement Value or the estate. There are currently \$69.5 million in investor claims against the estate.

IV. Financial Report

The estate began 2018 with about \$3.7 million in cash, policies worth about \$19.0 million and uncollected judgments and settlements. During the year, the estate’s largest expense was \$4.8 million in portfolio premiums; and its largest collection was \$12.0 million in death benefits. The estate ended the year with \$10 million in cash, policies worth \$14.8 million and uncollected litigation recoveries. The estate’s sources and uses of cash since the receivership’s inception and for the year are summarized below.

Cash

	<u>5/5/10 thru</u> <u>12/31/2017</u>	<u>1/1/2018 thru</u> <u>12/31/2018</u>
Beginning Balance	23,150,192	3,662,719
<i>Plus</i>		
Death Benefits	27,661,497	12,000,000
Estate Recoveries	13,074,957	77,924
Interest Rec'd	<u>466,961</u>	<u>115,532</u>
<i>Sub total</i>	41,203,415	12,193,456
<i>Less</i>		
Premiums Paid	(35,171,206)	(4,842,680)
RV Mortgage (P&I)	(45,488)	
Taxes	(3,093,989)	(815,700)
Fees and Expenses	(10,537,621)	(201,154)
3rd Party Disb.	(950,929)	
Distributions	<u>(10,891,655)</u>	<u> </u>
<i>Sub total</i>	(60,690,888)	(5,859,534)
Ending Balance	3,662,719	9,996,641

Since its inception, the Receivership's primary expense has been premiums on its life insurance policies. Its second highest use of cash has been distributions to Retirement Value's investor-victims. The receivership has paid over \$40,000,000 in premiums and \$11,000,000 in distributions. These disbursements were funded exclusively from: (i) the cash-on-hand at inception; (ii) the death benefits collected from matured policies; and (iii) the Receivership's settlements and litigation recoveries.

V. The Portfolio

The estate's primary asset is the portfolio of life settlement policies that it holds for the benefit of the investors. Through December 31, 2018, the portfolio has experienced \$39.5 million in maturities leading to \$10.9 million in distributions. There are 43 policies on 36 insureds remaining in the portfolio, which have a face value of \$102.1 million and a liquidation value of \$14.8 million.²

A. Profile

1. Matured Policies

As of the end of 2018, the following policies had matured.

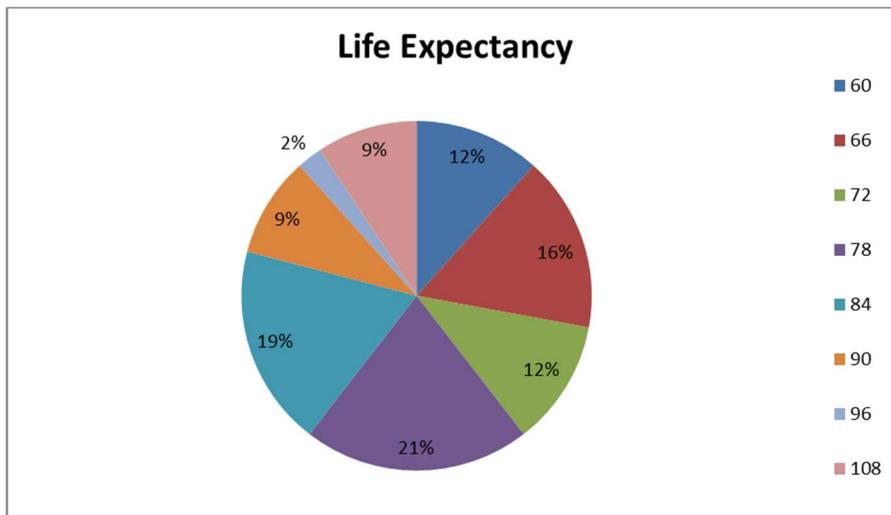
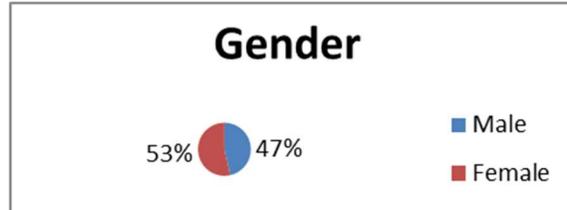
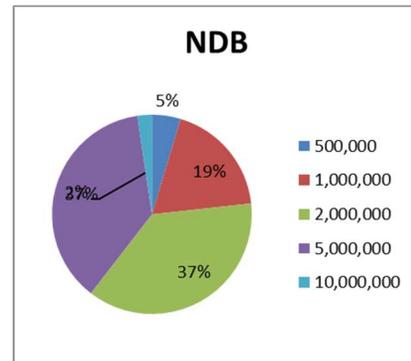
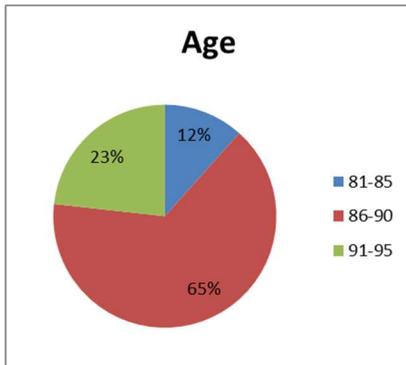
Matured Policies				
Internal Code	Carrier	Face Amount	Matured	
PLI140-111109-DM	Pacific Life	\$ 10,000,000	11/2/2010	
AXA597-110209-HM	AXA Equitable	\$ 1,250,000	4/22/2013	
PLI930-102009-HM	Pacific Life	\$ 1,250,000	4/22/2013	
AGL06L-102009-LM	American General	\$ 2,500,000	7/21/2014	
LFG735-030510-AS	Lincoln Financial	\$ 5,000,000	3/20/2015	
AXA804-031909-RM	AXA Equitable	\$ 4,500,000	8/8/2015	
SLA338-112009-CD	Sun Life Assurance	\$ 2,000,000	9/1/2015	
ANI521-102209-BW	American National	\$ 1,000,000	12/22/2016	
LFG782-090409-HO	Lincoln Financial	\$ 5,000,000	2/3/2018	
ING201-071509-AG	ING	\$ 5,000,000	2/9/2018	
AGL130-012110-PM	American General Life & Accident Ins. Co.	<u>\$ 2,000,000</u>	6/6/2018	
		\$ 39,500,000		

Due to the relatively few number of lives underlying the portfolio, maturities do not occur on a regular basis. As an example, there were only \$1 million in maturities during the 28 months between October 2015 and January 2018 but \$12 million in the next five months.

² Two additional policies -- LFG177-031909-MC (\$1.5 million) and HLI814-092509-MI (\$1.5 million) -- matured since the date of this Report raising total maturities to \$42.5 million and reducing the total number of remaining policies to 41 with a face value of \$99.1 million.

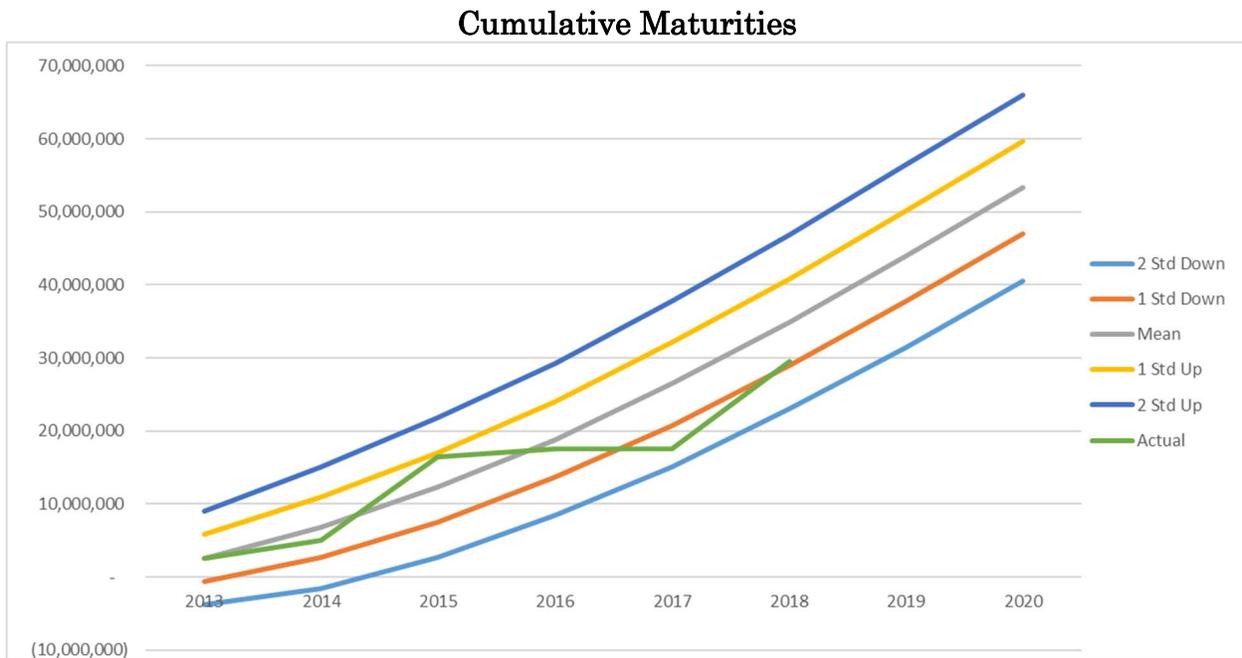
2. Active Policies

As of the date of this report, the active portfolio contained 43 policies on 36 individuals with an aggregate face value of \$102.1 million. The average age of the insureds is 88.3 years with an average median life expectancy of 75.22 months. All insureds are non-smokers. The following graphs depict additional details:



B. Progress against the 2012 projections

In 2012, the Receiver projected that the portfolio would return roughly 100 cents per dollar invested with an expected range between 80 and 120 cents. Actual maturities to date suggest that the portfolio's returns will be in the lower end of that range.



The grey line in the center represents the expected performance and the blue lines at the top and bottom represent the outer limits of the outcomes predicted in 2012. While actual maturities have exceeded predictions at times, the overall trend is currently below the expected performance. It is, however, still within the expected range of the projections.

As the big swings in the green “actual” line show, maturities in the portfolio vary significantly from year to year due to the relatively small number of insureds. Thus, a run in maturities (such as occurred in the first half of 2018) could significantly

impact the projections. Notably, the estate holds \$14.7 million in insurance on one insured, \$8 million on another insured and \$7 million on a third.³ The death of any of these insureds would have a significant impact.

In addition to maturities, the overall performance of the portfolio and, thus, the amount ultimately available for distribution depends upon premium costs and taxes. As discussed below, premium costs have increased for certain of the policies because some insurers have increased the cost of insurance above that originally used to set premiums. But, the corporate tax rate that Retirement Value pays on profits from maturities dropped significantly beginning in 2018.

C. Changes affecting the portfolio

1. The Receiver recently increased the longevity estimates used to model the portfolio's performance due to the availability of better statistical information

The Receiver uses life expectancy or longevity estimates to determine the reserves that he needs to maintain in order to comply with the Plan and to protect the estate from running out of money. This year, he increased the portfolio's longevity estimates for two reasons. First, the American Society of Actuaries recently finalized a new mortality table, the 2015 Valuation Basic Table (2015 VBT), that replaced the old mortality table, the 2008 Valuation Basic Table (2008 VBT), used to determine life expectancies. Second, the life expectancy estimates that the Receiver obtained in

³ The Receiver is considering ways in which to reduce these concentrations in order to reduce the risk in the portfolio.

2011 and 2012 are no longer reliable. These changes have had the effect of lengthening the Receiver's estimate of each insured's life expectancy.

a. The 2015 VBT predicts that insureds will live longer

The Society of Actuaries periodically publishes Valuation Basic Tables based on information provided by life insurance companies regarding the mortality experience of the individuals they insure. As a general matter, the Valuation Basic Tables project that individuals with life insurance live longer than comparably aged persons in the general American population. While there is some debate as to why this is true, the consensus is that insured persons are wealthier than non-insured persons are and, thus, have access to better health care and nutrition enabling them to live longer.

Over the last several decades, the trend has been for all Americans to live longer. This trend is particularly evident among Americans with life insurance. As a result, the 2015 VBT projects that people will generally live longer than the 2008 VBT did.⁴ These same general trends affect the Retirement Value portfolio.

b. The LEs used to develop the Plan are no longer reliable

The passage of time affects the reliability of a life expectancy estimate (an "LE"). The LEs that the Receiver obtained in 2011 and 2012 are stale and no longer reliable. An LE is a statistical analysis of an insured's life expectancy based on his age and health. In simple terms, an underwriter determines whether the insured is

⁴ In addition, the 2015 VBT is based on significantly more data than the 2008 VBT and is thus considered more accurate.

more or less healthy than the average person of the same age and gender. Based on this analysis, the underwriter will assign a multiplier to be applied to standard mortality estimates for persons the insured's age. For example, a multiplier of 150 means that the insured is 50% more likely to die in a given time period than the average person his age. As time passes, however, the insured's health changes. He may recover from old ailments or develop new ones. As a result, an LE becomes less reliable over time.

Moreover, the 2011 and 2012 LEs were based on the 2008 VBT rather than on the 2015 VBT. As discussed above, the 2015 VBT predicts that insureds will live longer than the 2008 VBT did. Accordingly, the projections that were based on the 2008 VBT are too short even if the insured's health has not improved relative to others his age.

For all of these reasons, the LEs that the Receiver obtained in 2011 and 2012 are no longer reliable. Rather than spend the money to obtain updated health information and new life expectancy estimates, the Receiver has elected to use the standard life expectancy for each insured as projected by the 2015 VBT. In so doing, the Receiver is assuming that each insured is of average health for his or her age.

c. As insureds age, their life expectancy increases

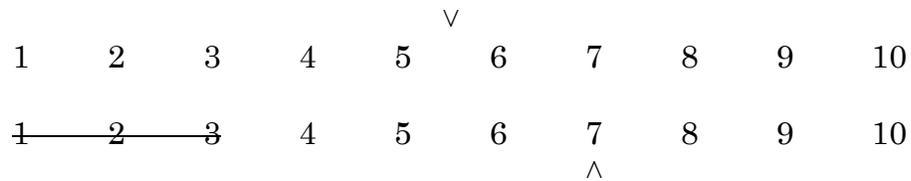
There is another factor at play here as well. As a person ages, his life expectancy increases. A 77-year old male in 2010 had a base life expectancy of 156 months, i.e., he had a 50% chance of living to age 90. The same man, now 85, has a

base life expectancy of 96 months, i.e., he has a 50% chance of living to age 93.⁵ Simply by living for eight years, the insured increased his life expectancy by three years.

This increase in estimated life expectancy is statistical. A life expectancy projection says little about an individual insured's mortality, it simply predicts the timing of deaths within a large group of people. The projection predicts that a certain percentage of the group will die each year. The point at which 50% are expected to have died is the median life expectancy. Some in the group will live a shorter time and some will live a longer time. At the beginning of the period, we have no way of knowing whether our insured will die sooner or later than the others in his group.

Eight years in, we know a bit more. While we do not know when the insured will die, we do know that he survived the first eight years. Thus, we know that he is not one of the ones that will die sooner and is more likely to be one of the group that lives longer. As a result, we expect that he will live longer than the median life expectancy of his original group.

To illustrate this concept, we can use a simple mathematical example of the numbers between one and ten. The median (or middle) number is between 5 and 6.



But, if we eliminate 1, 2 and 3, the median (or middle) number moves to 7.

⁵ Both estimates are based on the 2008 VBT.

Due to all of these factors, the Receiver has extended his longevity estimates for purposes of analyzing the portfolio.

2. Increases in the cost of insurance have affected the portfolio's performance.

Over the last several years, a number of insurance companies have announced that they either have or are considering raising the cost of insurance on certain of their life insurance policies. When issuing a class of policies, insurers create two cost of insurance tables that determine the premiums required to keep the policy in force throughout the insured's life. The first table, the guaranteed table, sets out the maximum amount the insurer can charge per \$1,000 of coverage for each year of the insured's life based on the insured's age. The guaranteed table is included in the insurance contract and is used for guaranteed illustrations but is not used to set the actual insurance cost.

To set the actual insurance cost, the insurer creates a second cost of insurance table, the actual table, that it believes is actuarially sound, i.e., the payment of premiums plus anticipated investment income will provide sufficient funds to the insurer to pay death benefits as they come due. The insurer does not publish this table but it works just like the guaranteed table setting a cost per \$1,000 of insurance based on the insured's age. Under most insurance contracts, the insurer may raise the actual table in certain circumstances such as when insureds are dying more frequently than expected.⁶

⁶ The circumstances in which an insurer can or must change the actual table vary by insurance contract.

These cost of insurance increases have been highly controversial and have led to significant litigation. Although not a party to any of this litigation, the Receiver is monitoring these cases to see how they may impact the estate. In an appropriate circumstance, the Receiver may consider filing or joining such a suit.

To date, insurers have announced cost of insurance increases that impact the following policies in the portfolio.

Policy	Carrier	Face Amount
AXA826-110509-IC	AXA Equitable	\$ 1,250,000
AXA091-012110-PC	AXA Equitable	\$ 5,000,000
AXA994-011510-BD	AXA Equitable	\$ 2,100,000
HCF-AXA058-PF	AXA Equitable	\$ 2,500,000
AXA729-112009-SF	AXA Equitable	\$ 2,000,000
AXA146-090409-GJ	AXA Equitable	\$ 2,000,000
AXA335-022410-PS	AXA Equitable	\$ 3,000,000
ING036-071509-EB	ING	\$ 3,000,000
<u>LFG591-031909-DH</u>	Lincoln Financial	<u>\$ 1,000,000</u>
9 Policies		\$ 21,850,000

Due to the ongoing litigation, the Receiver does not know whether these cost increases will remain in effect. The Receiver has not calculated the impact of the cost of insurance increases separately from that of the longer longevity estimates. Based on his experience with this and other portfolios, the Receiver believes that the longer longevity estimates have a greater impact, however.

D. New Projection

1. The Receiver anticipates that distributions may be lower than anticipated in 2012

Because the longevity estimates have lengthened and the cost of insurance for certain policies has increased, the Receiver had his actuary revised the stochastic analysis of the portfolio to incorporate the new information. The new analysis predicts that the estate will return about 81% of the funds invested with likely results between 73% and 93%.⁷

	Expected	High	Low
Portfolio	\$ 44,409,091	\$ 53,793,686	\$ 37,603,153
Cash	\$ 9,996,641	\$ 9,996,641	\$ 9,996,641
Distributed	<u>\$ 10,985,790</u>	<u>\$ 10,985,790</u>	<u>\$ 10,985,790</u>
Total	\$ 65,391,522	\$ 74,776,117	\$ 58,585,584
Claims	\$ 80,361,992	\$ 80,361,994	\$ 80,361,995
Percentage	81.37%	93.05%	72.90%

The reserves required by the Plan are \$16.1 million⁸. These reserves are sufficient to cover premiums in 97.5% of anticipated scenarios.

This projection is very conservative. Notably, it assumes that each of the insureds is as healthy as the average person of his or her age. The data from 2011 and 2012 suggests that the insureds may not be that healthy. Moreover, the actual maturities are still within the levels projected in 2012. Finally, the portfolio remains

⁷ As with all of the Receiver's projections, the new model takes into account income taxes owed on maturities.

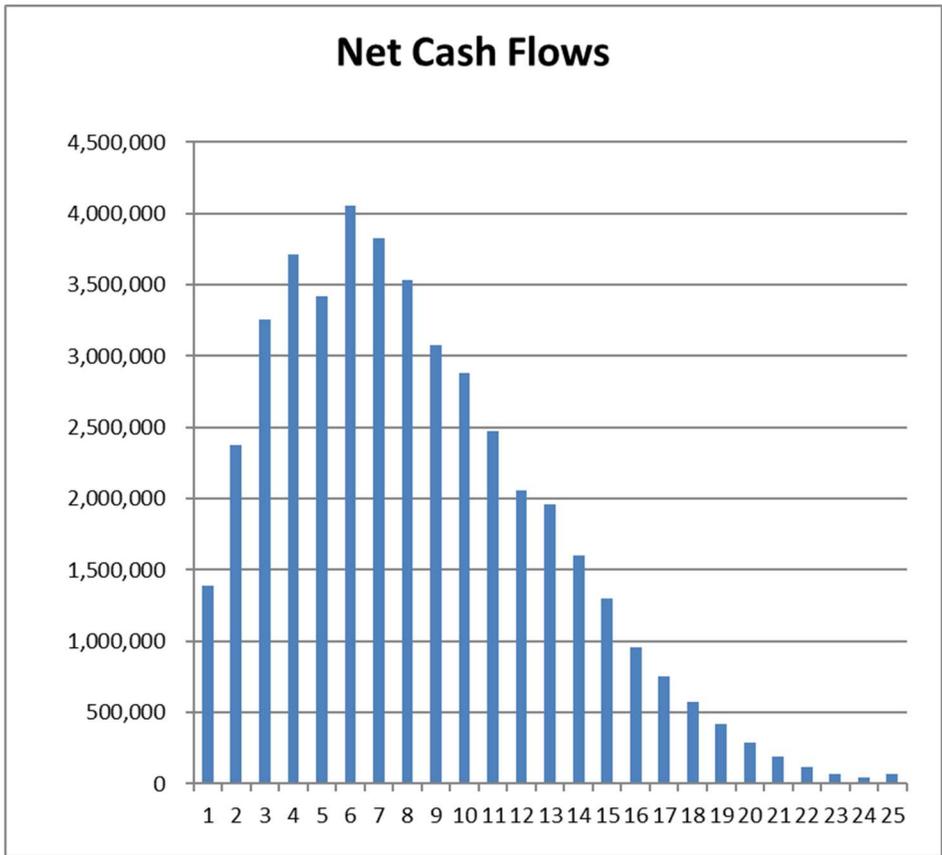
⁸ The December 31, 2018 actuarial analysis identifies the mean Premium Reserve Requirement as \$5,258,133 and a standard deviation as \$5,413,898. With \$5.3 million in reserve the estate has a 50/50 chance of not running out of cash. The Plan requires the reserve to be set to a 97.5% confidence interval, which translate to the mean plus 2 standard deviations or \$16,085,928.

very highly concentrated in just a few lives. Three insureds represent \$29.7 million in face – 29.1% of the portfolio. The death of one or more of these insureds in the near term would dramatically change the projections.

2. The timing of anticipated distributions remains uncertain

It is impossible to tell “when” the estate will have adequate excess cash flow to make the distributions forecasted by the model. The actual distributions are dependent on which policies mature when. The model looks at the portfolio as a portfolio and cannot be interpreted as identifying a maturity date for any particular policy or each policy. That said, the model does generate an anticipated Net Cash Flow. Net Cash Flows refers to each year’s expected (i) maturity proceeds; less (ii) premiums paid; and (iii) taxes. In other words, whether the estate is expecting to increase or decrease its cash on hand. A warning about statistics: the Net Cash Flow discussed below is the model’s forecasted mean (or average) results. By their nature, the actual results will vary from (but should bounce around) the mean. Actual Net Cash Flow should track the mean, but will not mirror it. Accordingly, the actual results in Year 1 will affect the results in each subsequent year, the same is true for Year 2, Year 3 and so on.

The following chart depicts the portfolio’s anticipated Net Cash Flows over the next 25 years.



The forecasted mean Net Cash Flow should restore the Premium Reserve to its requisite level by mid-2021. The Receiver anticipates continuing to use Net Cash Flow throughout 2019 and 2020 to rebuild the Premium Reserve.⁹ However, each time a policy matures the mean and standard deviation used to establish the Premium Reserve are affected, thus the requisite Premium Reserve may increase or decrease while being reloaded. Accordingly, though the Receiver does not expect to make a distribution before 2021; the timing of a distribution remains a function of and dependent upon which policies mature and when.

⁹ The Receiver is exploring the possibility of obtaining a back-up line of credit to meet part of the reserve requirements. If he can do so, the Receiver would be able to make distributions sooner.

The Portfolio has a forecasted maturity horizon (i.e. when the last insured is expected to pass) exceeding 25 years. The Net Cash Flow forecast reflects an expectation that the Portfolio will generate most (about 80%) of the distributable cash within the next 12 years.

VI. Litigation and other recoveries

In addition to the portfolio, the estate also holds judgments and settlements in its favor against various persons who were involved with RV. To date, the Receiver's litigation efforts have yielded collections exceeding \$10.7 million.

Litigation Recoveries

Settlements

Collins, Bruce	322,078.97
Gray, Richard H	623,099.56
James Settlement Services, et al	5,500,000.00
Kiesling Porter Kiesling & Free	710,000.00
Licensees	2,133,887.13
Rogers, Wendy	182,963.63
Total Settlements	9,472,029.29
(To Be Funded)	(46,589.96)
Collected	9,425,439.33

Judgments

Total Judgments	6,086,239.49
Adjustments	(799,764.87)
(To Be Collected)	(3,973,356.19)
Collected	1,313,118.43

Total Litigation Recoveries

10,738,557.76

Non-Litigation Recoveries

James Settlement Servi Disputed Assets	1,659,304.12
Pacific Life Disputed policy	10,117,534.00
Special Acquisition Hidden Assets	1,231,925.00
State of Texas Franchise Tax	34,564.00
Total Non-Litigation Recoveries	13,043,327.12

Total Recoveries

23,781,884.88

Although he is continuing to pursue recovery, the Receiver projections do not rely on collection of the approximately \$4.0 million in outstanding accounts receivable.

VII. Conclusion

The estate is operating more or less as planned. As time has passed and more information known, the Receiver believes that additional steps are necessary to improve the portfolio's performance. Accordingly, he is exploring the following transactions:

- Trading policies on insureds on which the estate is concentrated for policies on other persons. For example, the estate holds \$14.7 million on a single insured. By trading \$10 million of this coverage for \$10 million of coverage on 6 to 8 insureds, the Receiver could significantly reduce the risk in the portfolio and likely lower the required reserves.
- Obtaining a back-up line of credit for about \$5 million. While the Receiver does not expect to need to use the line, having the line would enable him to reduce his cash reserves and to make distributions sooner.

The Receiver will seek the Court's permission before engaging in either potential transaction.