DEPARTMENT OF FINANCE
CALIFORNIA
ARNOLD SCHWARZENEGGER, GOVERNOR
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July 28, 2010

Mr. David E. Wilson, Chief Executive Officer
Conservation & Liquidation Office
425 Market Street, 23rd Floor
San Francisco, CA 94105

Dear Mr. Wilson:

Final Report—Executive Life Insurance Company Financial Statement Review, December 2009

The Department of Finance, Office of State Audits and Evaluations, has completed its review of the Executive Life Insurance Company Estate assigned to the Conservation & Liquidation Office (CLO) for the period January 1, 2009 through December 31, 2009.

The enclosed report is for your information and use. We appreciate the assistance and cooperation of CLO staff and management. If you have any questions regarding this report, please contact Kimberly Tarvin, Manager, or Rick Cervantes, Supervisor, at (916) 322-2985.

Sincerely,

Rick Sierra
for David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Mr. Ray Minehan, Chief Financial Officer, Conservation & Liquidation Office
Mr. Ed Hahn, Vice President Estate Finance Group, Conservation & Liquidation Office
Mr. Keith Nelson, Chief, Ethics and Operational Compliance Office, California Department of Insurance
Mr. Jesse Huff, Audit Committee Chair and Chief Deputy Insurance Commissioner, California Department of Insurance

FINANCIAL STATEMENT REVIEW

Executive Life Insurance Company Estate
Conservation & Liquidation Office
For the Period January 1, 2009
through December 31, 2009

Prepared By:
Office of State Audits and Evaluations
Department of Finance

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Executive Summary

The California Department of Insurance (Department) takes a leading role to conserve, rehabilitate, or liquidate licensed California financially distressed and insolvent insurance enterprises under appointment by the Superior Courts. The Department's involvement helps secure consumer interests and provide for a stable, consistent insurance market.

The Conservation & Liquidation Office (CLO), created in 1994 to be the successor of the Conservation & Liquidation Division of the Department, is appointed by the California Insurance Commissioner (Commissioner) to oversee the affairs of financially impaired insurance enterprises domiciled in California. Financially impaired insurance enterprises are usually subject to a period of court supervised conservation under CLO administration. During this time, CLO, along with the regulators, explore opportunities for rehabilitation. Financially distressed life insurance enterprises are frequently conserved, with policyholder liabilities and related invested assets transferred to a third party acquirer. However, for the vast majority of financially distressed property and casualty insurance enterprises, the enterprises will not be conserved, but liquidated.

For enterprises liquidated, the Commissioner, acting through CLO, assumes title of the enterprise's assets. The insurance enterprise offices are closed, all outstanding policies are cancelled, and the process of obtaining and liquidating the enterprise's remaining assets begins. The books and records of the enterprise are acquired by CLO for use during this process. The goal of liquidation is to apply the money acquired from liquidating the enterprise's assets toward the enterprise's debts and outstanding insurance claims. Upon issuance of a liquidation order, CLO issues a notice to all interested parties, including the enterprise's policyholders, creditors, and shareholders. The notice requests proofs of claim be filed with CLO in order to participate in a distribution of assets. An enterprise subject to a conservation or liquidation order is referred to as an estate. The costs of CLO administration are borne by the estate of the insolvent entity. For estates with no assets, the California Insurance Fund supplements the costs. The process of conservation and subsequent liquidation can take several years.

The Commissioner, under California Insurance Code section 1060, is required to transmit an annual report of information on the estates under his supervision to the Governor. These estates include those for which the Commissioner is fully responsible; those for which the Commissioner is partially responsible; those for which the Commissioner has custodial responsibilities; and those for which the Commissioner is fully responsible, but are operated separately. As of December 31, 2009, 23 open estates and 3 trusts of liquidated insurers are subject to the oversight of CLO. In 2009, CLO made interim and final distributions totaling $149 million and closed three estates.

The California Insurance Code sections 1060 and 1061 authorize and require the Department of Finance to conduct biennial examinations of the Commissioner's books and accounts in support of the annual report transmitted to the Governor.

Specifically, the objectives of the engagement were to perform a review of the open estates' Statement of Assets and Liabilities, Statement of Operations, and Statement of Cash Flows (Statements) as of December 31, 2009, in accordance with attestation standards established by the American Institute of Certified Public Accountants. An individual report for each estate reviewed, including any applicable restrictions on its use, will be issued.

Our review included those estates assigned to CLO's Special Deputy Insurance Commissioner and considered open by the Superior Court; and did not include estates assigned to other Special Deputy Insurance Commissioners. Financial reports for estates assigned to other Special Deputy Insurance Commissioners are issued under separate cover by separate entities.

Review Results

Based on our review, nothing came to our attention that caused us to believe that the Statements for the year ended December 31, 2009 are not presented, in all material respects, in conformity with Generally Accepted Accounting Principles.

This report is intended for the information and use of the California Department of Insurance, CLO, and the courts, and should not be used for any other purpose. However, the report is a matter of public record and its distribution is not limited.

DEPARTMENT OF FINANCE

ARNOLD SCHWARZENEGGER, GOVERNOR

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Independent Accountant's Report

Mr. David E. Wilson, Chief Executive Officer
Conservation & Liquidation Office
425 Market Street, 23rd Floor
San Francisco, CA 94105

We have reviewed the Statement of Assets and Liabilities, Statement of Operations, and Statement of Cash Flows (Statements) for the Executive Life Insurance Company Estate for the year ended December 31, 2009. The Conservation & Liquidation Office (CLO), as assigned conservator/liquidator, is responsible for the Statements.

Our review was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. A review is substantially less in scope than an examination, the objective of which is the expression of an opinion on the Statements. Accordingly, we do not express such an opinion.

Based on our review, nothing came to our attention that caused us to believe that the Statements of the Executive Life Insurance Company Estate for the year ended December 31, 2009 are not presented, in all material respects, in conformity with Generally Accepted Accounting Principles.

As discussed in Note 3 to the financial statements, the Executive Life Insurance Company Estate corrected its policyholder liability to reflect the actual liability as established by the Court in 1993.

This report is intended solely for the information and use of the California Department of Insurance, CLO, and the courts, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Nicole Lean, CPA

for David Botelho, CPA
Chief, Office of State Audits and Evaluations

June 8, 2010

Executive Life Insurance Company Estate
Statement of Assets and Liabilities
As of December 31, 2009

Assets	**Balance**
Participation in Pooled Investments, at Market	$ 35,589,666
Restricted Investments, NOLHGA[1]	9,387,091
Restricted Investments, Opt-In Only	295,746
Restricted Investments, Aurora-Penn	5,894,606
Accrued Investment Income	208,382
Other Receivables	1,605,755
Total Assets	$ 52,981,246
Liabilities	
Secured Claims	$ 6,757,636
Accrued Administrative Expenses	1,727,163
Policyholder Liability	5,469,371,504
Other Claims	428,836
Total Liabilities	5,478,285,139
Net Assets (Deficiency)	$(5,425,303,893)

The notes are an integral part of the financial statements.

[1] NOLHGA represents The National Organization of Life and Health Guaranty Associations

Executive Life Insurance Company Estate
Statement of Operations
For the Year Ended December 31, 2009

Investments	
Investment Income	$ 1,557,787
Investment Expenses	(38,462)
Gain (Loss) on Securities	1,149,635
Net Investment Income	2,668,960
Expenses	
Legal Expenses	9,387,019
Consultants and Temps	345,601
Office Expenses	133,173
Allocated Overhead Expenses	437,124
Federal Income Taxes	229,375
Accrued Interest on Policyholder Liability	227,623,289
Total Expenses	238,155,581
Net Income (Loss)	**$(235,486,621)**

The notes are an integral part of the financial statements.

Executive Life Insurance Company Estate
Statement of Cash Flows
For the Year Ended December 31, 2009

Cash Flows from Operating Activities	
Net Income (Loss)	$ (235,486,621)
Decrease (Increase) in Other Receivables	47,656
Increase (Decrease) in Secured Claim Liabilities	104,024
Increase (Decrease) in Accrued Administrative Expenses	213,725
Increase (Decrease) in Policyholder Liability	227,623,289
Net Cash Flows from Operating Activities	(7,497,927)
Cash Flows from Investing Activities	
Decrease in Accrued Investment Income	92,405
Cash Flows from Financing Activities	0
Net Decrease in Cash	**(7,405,522)**
Cash at Beginning of Period	58,572,631
Cash at End of Period	**$ 51,167,109**

The notes are an integral part of the financial statements.

1. Organization

The California Insurance Commissioner (Commissioner), an elected official of the State of California, acts under the supervision of the Superior Court (Court) when conserving and liquidating insurance enterprises. In this capacity, the Commissioner is responsible for taking possession (conservation) of the assets of financially troubled insurance enterprises domiciled or incorporated in California. An enterprise subject to a conservation or liquidation order is referred to as an estate.

Executive Life Insurance Company (ELIC) was placed in conservation by order of the Los Angeles County Superior Court on April 11, 1991. At the time, ELIC, which had more than 350,000 policyholders, was the largest life insurance insolvency in United States history. In the summer and fall of 1991, the Commissioner conducted an auction seeking bids to acquire the junk bond portfolio and insurance assets of ELIC. In December 1991, the Commissioner's selection of a group of French and European investors (the Altus/MAAF group) as the winning bidder was approved by the Superior Court.

In March 1992, ELIC's junk bond portfolio was transferred to Altus Finance for a total purchase price of approximately $3 billion. In August 1993, the Superior Court approved a final Rehabilitation Plan under which the majority of ELIC's assets and its restructured insurance policies were transferred to a new California insurance company created by the European consortium that had won the 1991 bid. The Rehabilitation Plan became effective in September 1993. Under the terms of the Rehabilitation Plan, former ELIC policyholders were given a choice either to accept new coverage (Opt In) from Aurora National Life Assurance Company (Aurora) or to terminate their ELIC policies (Opt Out) in return for a pro rata share of ELIC's assets. The Rehabilitation Plan also provided for the establishment of various trusts, collectively known as the Enhancement Trusts, to marshal and distribute assets for the benefit of former ELIC policyholders.

2. Basis of Presentation

During 2009, CLO managed three trusts in addition to the ELIC estate: ELIC Holdback Trust, ELIC Opt Out Trust, and ELIC FEC Litigation Trust. This report presents the results for the ELIC estate (Estate) only.

The accompanying financial statements of the Estate have been prepared in conformity with generally accepted accounting principles. These financial statements reflect the financial position and activity of the Estate, which has been assigned to CLO by the Commissioner in his role as liquidator.

3. Summary of Significant Accounting Policies

ASSETS:

Cash and Cash Equivalents
Cash and Cash Equivalents consist of cash in banks, investments in money market funds, and all investments with original maturities of three months or less. Investments with maturities of greater than three months, but due in one year or less, are classified as short-term investments. Restricted cash is segregated in accordance with restrictions imposed by court order, a loan or security agreement, California statute, or escrow agreements, and is generally unavailable for administrative expenses. The Estate held no restricted cash as of December 31, 2009.

Pooled Investments
All investments, including short-term investments and debt and equity securities, are stated at market value. Market values are those provided by the depository trust institution in possession of the securities at the balance sheet date or through brokerage institutions.

The majority of the invested assets of the estates are combined for investment purposes into an investment pool, divided equally between two investment management firms. Each of the participating estates owns a percentage of the pool based on its proportionate share of the fair value of the pool's net assets. The net assets are valued at fair value on a monthly basis and estate ownership is computed monthly based on contributions and withdrawals by participating estates. Realized and unrealized gains and losses are allocated monthly based on the estate's ownership percentage in the pool at month end.

Pooled investments may be considered restricted. However, the Estate held no restricted pooled short term investments as of December 31, 2009.

Non-Pooled Short-Term Investments
Non-Pooled Short-Term Investments consist of investments with maturities greater than three months but less than one year and are funds that cannot be commingled with other funds. Non-pooled investments are held by a custodian bank, and for larger non-pooled investment accounts, an investment manager oversees the investment.

Non-pooled investments are stated at market value. Market values are those provided by the depository trust institution in possession of the securities at the balance sheet date or through brokerage institutions. Where market values are not readily determinable, book values are used.

Restricted investments are either restricted by court order, held in trust, or represent a deposit whose use is restricted by statute. The Estate held $15,577,443 in restricted non-pooled short-term investments as of December 31, 2009.

Accrued Investment Income
Accrued Investment Income represents monthly estimates of interest and dividends earned on cash and investments held by the Estate. For pooled investments, interest accruals are allocated based on the Estate's percentage of ownership in the pool. Non-pooled interest accruals are on an estate by estate basis. Each month interest and dividends are accrued and posted to the Estate’s account. Upon receipt of the earnings, the accruals are reversed and actual amounts received are posted.

Other Receivables
Other Receivables consist of an account held by Aurora reserved for covering the additional costs to policyholder adjustments for Opt In contracts as may be required. Any remaining amount will be returned to the ELIC estate for distribution to all Opt In policyholders.

LIABILITIES:

Secured Claims
Secured Claims represents funds allocated to Opt In policyholders involved in the Pennsylvania Class Action suit, where the Pennsylvania Life and Health Insurance Guaranty Association (PLHIGA) has certain subrogation rights, and unclaimed funds payable, which are funds distributed to claimants that were returned as undeliverable and/or an accurate address could not be located. Unclaimed funds are eventually escheated to the California State Controller's Office or the state treasurer of the claimants' last known address.

Accrued Administrative Expenses
Accrued Administrative Expenses represent administrative expenses which have been accrued but not yet paid. Generally accepted accounting principles require that the financial statements of entities in liquidation provide for an estimate of future administrative costs. Because the final resolution of litigation and other matters which impact the closure of an estate will take an indefinite time to resolve, it is CLO's policy not to accrue estimates of future administrative costs except when the Court has approved a final distribution order and the estate is scheduled to be closed within the following twelve months.

Policyholder Liability
In preparation for the eventual final distribution and closing of the estate, a detailed review of the liability to policyholders was performed based on examination of the Modified Rehabilitation Plan and relevant judicial decisions. In 2009 the Estate corrected its policyholder liability to reflect the actual liability, as established by the Court in 1993. This correction was made as a prior period adjustment of $2,980,353,492 to net asset balance. In addition, interest of $227,623,289 as shown on the Statement of Operations was accrued in 2009. As of December 31, 2009, the revised amount includes accrued but unpaid interest owed to former ELIC policyholders of approximately $2.2 billion.

The revision is consistent with the methodology specified in the Rehabilitation Plan, approved by the Court, which has been used to make all distributions from the ELIC estate. The revision will have no impact on individual policyholders or their right to a proportionate share of any future distributions.

Other Claims
All Other Claims represent pre-liquidation accounts payable and claims due to general creditors. It is not likely these claims will be paid.

INVESTMENTS:

Investment Income
Investment Income is comprised of interest and dividends earned on cash and investments held by the estate. For estates with investments in the pool, income is allocated based on the estate's proportional share in the pool.

Investment Expenses

Investment Expenses is comprised of investment and interest expenses related to cash and investments held by the estate. For estates with investments in the pool, the expenses are allocated based on the estate's proportional share in the pool.

Gain (Loss) on Securities

Gain (Loss) on Securities consists of long and short-term gains and losses incurred as part of the investment pool, mark to market adjustments, gains and losses on non-pooled reappraisals of securities, and gains and losses incurred on the transfer of non-pooled securities into the pool. The long and short-term gains and losses and mark to market adjustments are allocated based on the estate's proportional share in the pool. Gains and losses on the reappraisal of non-pooled securities and the transfer of non-pooled securities into the pool are reported on an estate by estate basis.

Unrealized and realized gains and losses are included as a component of net investment income. The cost of securities sold is based on specific identification and realized gains or losses are computed based on the securities' original cost. Transfers of non-pooled investments to a pool are a sale resulting in non-pooled realized gains or losses and a noncash transfer. Transfers from one pool to the other are a sale resulting in pooled realized gains or losses and a non-cash transfer.

EXPENSES:

Administrative Expenses

Administrative Expenses consists of both direct and indirect expenses.

Direct Expenses are those expenses which are directly charged to the Estate, such as legal costs, consultants and contractors, office expenses, and federal income taxes.

Indirect expenses are administrative expenses not directly charged to an estate but allocated to each estate on a proportional basis. Allocated expenses applicable to all of the estates include CLO employee compensation and benefits, payroll taxes, rent, utilities, and other general overhead costs. These shared expenses are allocated to each estate based on factors derived from the direct CLO labor hours and contractor hours charged to each estate.

4. Litigation

The Commissioner, in his capacity as conservator, rehabilitator and liquidator of the Estate, commenced a civil action in 1999 against Altus Finance S.A. (Altus) and other defendants alleging that they had acquired the junk bond portfolio and insurance assets of ELIC through fraud. Settlements were reached with Altus and some of the other defendants in 2004 and 2005.

A trial against the remaining defendants in 2005 resulted in a jury verdict finding Artemis S.A., a two-thirds owner of Aurora, liable for knowing participation in a conspiracy with members of the Altus/MAAF group to defraud the Commissioner. In August 2008, the jury’s verdict of liability was upheld on appeal and the case was remanded to the District Court for a new trial on the issue of damages.

At present, no trial date has been set.

5. Subsequent Events

There are no reportable subsequent events for this Estate.