Funeral Trust Division
2602 Iron Gate Drive
Suite 202
Wilmington, NC 28412
(910) 550-0542
ArgentFinancial.com

January 12, 2021

Chair Kelley
Vice Chair Feldman
Senate Finance Committee
Miller Senate Office Building, 3 East
Annapolis, Maryland 21401

Chair Pendergrass
Vice Chair Peña-Melynk
Health and Government Operations Committee
House Office Building, Room 241
Annapolis, Maryland 21401

RE: SB192 | HB5 – (Cemeteries – Perpetual Care – Distribution from Perpetual Care Trust Fund)

Dear Chair Kelley, Chair Pendergrass, Vice Chair Feldman, Vice Chair Peña-Melynk, Members of the Senate Finance Committee, and Members of the House Health and Government Operations Committee:

I was recently made aware that Maryland was considering the implementation of a Total Return Distribution Method for perpetual care cemeteries in the state pursuant to proposed Senate Bill 291 and House Bill 85. Our institution has reviewed this proposed legislation and would like to provide some additional insights, from the perspective of an independent trustee, as to why such a change would be in the interest of Maryland cemeteries and its citizens.

I. Argent Trust Company – (About Us)

Argent Trust Company ("Argent") is a Tennessee state-chartered trust company that administers over $23 billion in trust assets for our various personal and institutional trust clients. Argent also maintains a dedicated funeral and cemetery trust division (the "Cemetery Trust Division") that administers over $2 billion in funeral and cemetery trust assets for 160 clients across 35 states (excluding Maryland). The Cemetery Trust Division is composed of 12 trust professionals, which include:

- Dedicated legal team that reviews state regulations for the administration of funeral and cemetery trust assets in compliance with state law;
- Dedicated trust administration personnel to oversee any required annual reporting and the timely deposit, investment and withdrawal of funds in accordance with state regulations; and
- Dedicated investment management with an experienced team of portfolio managers that are familiar with the various state-specific investment requirements.

Argent's Cemetery Trust Division has over 150 years of combined experience in the administration and investment funeral and cemetery trust accounts. For more information about Argent or its Cemetery Trust Division, please visit our website at https://argentfinancial.com.

II. Trustee's Fiduciary Duty to a Perpetual Care Cemetery Trust

Perpetual care cemeteries have a profound responsibility to their clients and their communities to provide

a well-maintained final resting place, in perpetuity, for the departed. To accomplish this, states have tasked third-party fiduciaries with the responsibility, as trustee, for the oversight and administration of the perpetual care trust fund. The trustee's fiduciary obligations are ongoing duties that begin at the fund's inception and continue into perpetuity.

As you know, the perpetual care cemetery trust fund is the funding vehicle that covers the costs of lawn maintenance and the general upkeep of the cemetery grounds. As such, the trustee owes a fiduciary duty to ensure that the perpetual care cemetery trust fund is invested in a prudent manner and that distributions that are permitted under state law are made to the cemetery company in a timely manner. For the reasons mentioned below, Argent has taken the position that a Total Return Distribution Method is not only preferable for providing increased distributions to the cemetery company, but it also grows the corpus of the trust fund over time.

III. Benefits of Total Return Method vs. Net Income Method

A. Net Income Distribution Method

For generations, perpetual care cemetery trust funds have been limited to only distributions of net income, that is, the interest and dividend yielded after the payment of fees, expenses and taxes. As a result, the typical investment portfolio for Net Income Distribution Method trusts is heavily weighted toward income-producing investments. The cemetery company is entitled to receive all available net income, which generally varies from month to month. Over the past decade, low interest rates have meant that these investments have dramatically underperformed. Accordingly, cemeteries are receiving far less from their trusts' investments than in previous years, hampering their ability to pay for the upkeep and maintenance required in a perpetual care cemetery.

While the Net Income Distribution Method approach may have been satisfactory for many newer cemeteries, there has been a growing concern for older cemeteries that have either sold out or are close to selling out of their available lots and/or grave spaces. Perpetual care cemetery trusts are funded with a portion of the sale of each lot and/or grave space in accordance with state law. Such deposits are the main source of corpus appreciation for a Net Income Distribution Method trust fund since the investment of the fund is weighted toward income producing investments. If trust corpus has not grown adequately over time, then there may not be enough income generated in later years to care for the cemetery in perpetuity.

Furthermore, once a cemetery sells out of its available lots and/or graves, then there is less incentive for the cemetery company to cover the costs themselves for any required maintenance if the net income from the trust is inadequate. Argent continues to see various instances across the nation where a cemetery that is at full capacity becomes a public nuisance due to lack of proper upkeep and maintenance. In such instances, the city or township where the cemetery is located is then tasked with taking over the maintenance of the cemetery grounds. In such a scenario, the city or township must supplement, at the expense of the taxpayers, the difference between available trust income and actual cost of the cemetery maintenance.

B. Total Return Distribution Method

Under a Total Return Distribution approach, the cemetery elects a fixed percentage of income, capital gains, and/or principal based on the average annual fair market value of the trust. Accordingly, the investment portfolio under such an approach will be a balanced portfolio that focuses on a combination of stocks and interest-bearing investments with the main objective of maximizing the growth of the entire trust.

The main benefits for the Total Return Method are as follows:

- Diversified portfolio under a Prudent Investor Standard encourages both growth of corpus and income generation;
- Trust investment portfolio not completely dependent on interest rates;

- Consistent amount distributed each period to the cemetery, which allows for ease of managing and budgeting;
- Typically, the Total Return Distribution amount exceeds the amount of net-income generated under the Net Income Method; and
- The cremation rate is dramatically increasing nationwide, which correlates to fewer sales of lots and/or grave spaces per year. However, under a Total Return approach, the cemetery is no longer completely reliant on growing the trust corpus via deposits from sales of new lots and/or grave spaces.

In our experience, issues with utilizing the Total Return Distribution Method only appear to occur when:

- The trustee and/or investment manager are not familiar with the Total Return calculation and/or the associated diversified growth investment strategy; or
- During periods of a prolonged market downturn, this method could result in the possible overpayment of trust corpus.

After reviewing SB 192 and HB 05, it is our belief that these proposed bills contain the necessary provisions for the Office of Cemetery Oversight to review these trust funds on a regular basis and intervene if either issue noted above is found for a particular perpetual care trust fund. Specifically, these bills permit the Director of the Office of Cemetery Oversight to limit or prohibit any distribution after a review of the trust fund found either deficiency noted above.

IV. Conclusion

It is Argent's position that a Total Return Distribution Method is the preferable choice for providing consistent, increased returns to the cemetery company, while at the same time enhancing the fund's long-term viability by growing the corpus of the trust fund over time. After reviewing SB 192 and HB 05, Argent believes that they are similar in nature to Total Return/Unitrust laws that have been passed in other states for which we currently act as a cemetery trustee. At this time, Argent would recommend that SB 192 and HB 05 be passed since they would increase the monthly/quarterly distributions to cemetery companies, they would grow the corpus of the perpetual care cemetery trust fund, and they contain adequate regulatory safeguards to prohibit the excess invasion of principal during periods of lower investment returns.

If you should have any questions, please feel free to contact me at jwilson@argenttrust.com or (910) 550-0542.

Respectfully submitted,

Justin D. Wilson | SVP & Senior Legal Counsel
Argent Trust Company

Total Return Method

For Perpetual Care Trusts

Perpetual Care Trusts are created to ensure cemeteries remain properly maintained, attractive and safe for consumers into perpetuity. A percentage of each burial plot sale funds them.

Historically, once funded corporate trustees invest under Prudent Person Rule to seek income while preserving capital to support net income distributions. The current low interest environment does not support perpetual care trusts with net income method.

The net income method yields lower total rate of return which results in lack of funds to maintain cemetery (i.e. mowing grass, planting flowers, trimming trees, paving roads, etc.)

Perpetual care trust accounts are not generating enough funds to maintain the cemetery and build a nest egg for unpredictable maintenance costs.

This causes consumer concern and complaints. It also results in cemeteries being turned over to municipalities and states because of insufficient funds to continue maintaining them. Taxpayer money is then thwarted.

A MORE VIABLE OPTION IS THE TOTAL RETURN METHOD.

Why is the Total Return Method a better option?

The total return method allows for creation of broader diversification (which can reduce volatility and spread market risk) by owning various asset classes, market capitalizations (large, mid, small) and investment styles (value, growth). Perpetual care is a marathon, not a sprint. It is "perpetual care" not "next year's" care. It is crucial to be prudent to protect the cemetery and the consumers utilizing it.

How does the Total Return Method differ from the current Net Income Method?

The total return method allows distribution to cemeteries in the form of a percentage of total market value. It allows for no less than 3 percent and no more than 5 percent. The net income method only distributes interest and dividends, and so forces asset allocation into certain types of investments, which may be less desirable.

What are safeguards to protect consumers and the public in a downturn?

- A rolling average for distributions keeps trustees from distributing excessively high amounts in good years or low amounts in bad years. It evens the playing field.
- Built in protections require the cemetery to temporarily revert back to net income method if facts warrant such a move.
- The Office of Cemetery Oversight reviews each cemetery's annual report to ensure funds are protected and growing for the life of the cemetery.

Are other states utilizing the Total Return Method?

Yes: Arizona, Colorado, Delaware, Florida, Georgia, Indiana, Iowa, Missouri, Nevada, North Carolina, Oklahoma, Tennessee, Texas, Virginia and Washington have passed into law the total return statutes applicable to Cemetery Perpetual Care Trusts or have unitrust provisions. California has passed legislation that will become effective in 2021. Several other states are reviewing it.

What are benefits of Total Return Method?

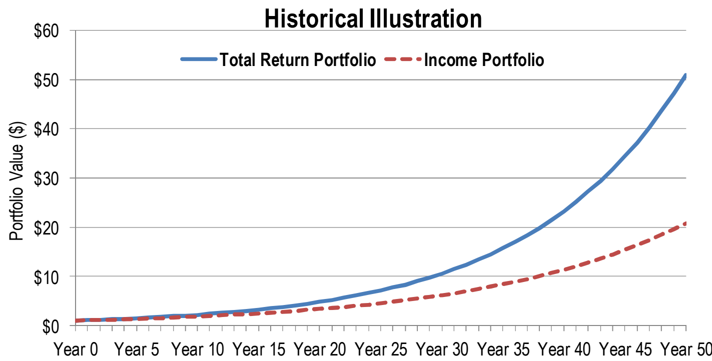
- Total return method has historically produced 2 to 4 percent greater than net income method.
- Allows for higher and more sustainable distributions to the cemetery to be utilized for the care and maintenance of the cemetery pursuant to Maryland Statute 5-603(e). ALL distributed funds must be used for the perpetual care of the cemetery.
- Principal can grow at a greater rate than net income method.
- Reflects exactly how much funds will be available, in advance, which is key for budgeting and planning purposes for the cemetery.

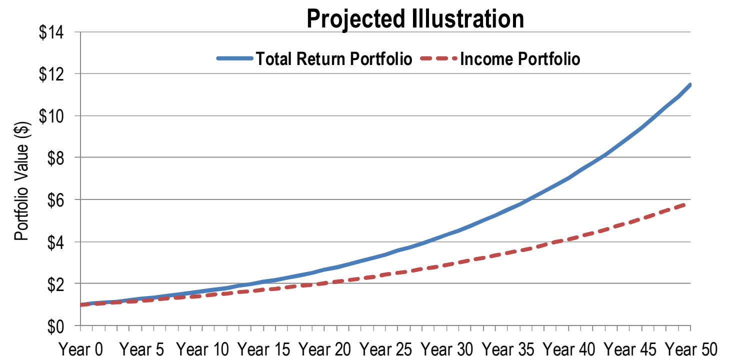
Why should the change be made now?

The total return method provides a sustainable and stable cash flow allowing cemeteries to make future financial decisions efficiently to serve the consumer. This should be an option. It is not mandatory. The individual cemeteries can choose what option best fits their specific needs

Representative Illustrations

- The graphs below illustrate the hypothetical growth of $1 for a Total Return portfolio versus an Income-oriented portfolio, in both historical and projected scenarios. In both cases, the Total Return portfolio yields a higher portfolio value and cumulative distributions over the long term.





Cumulative Distributions	
Total Return Portfolio	$30.55
Income Portfolio	$13.93
Difference	**$16.62**

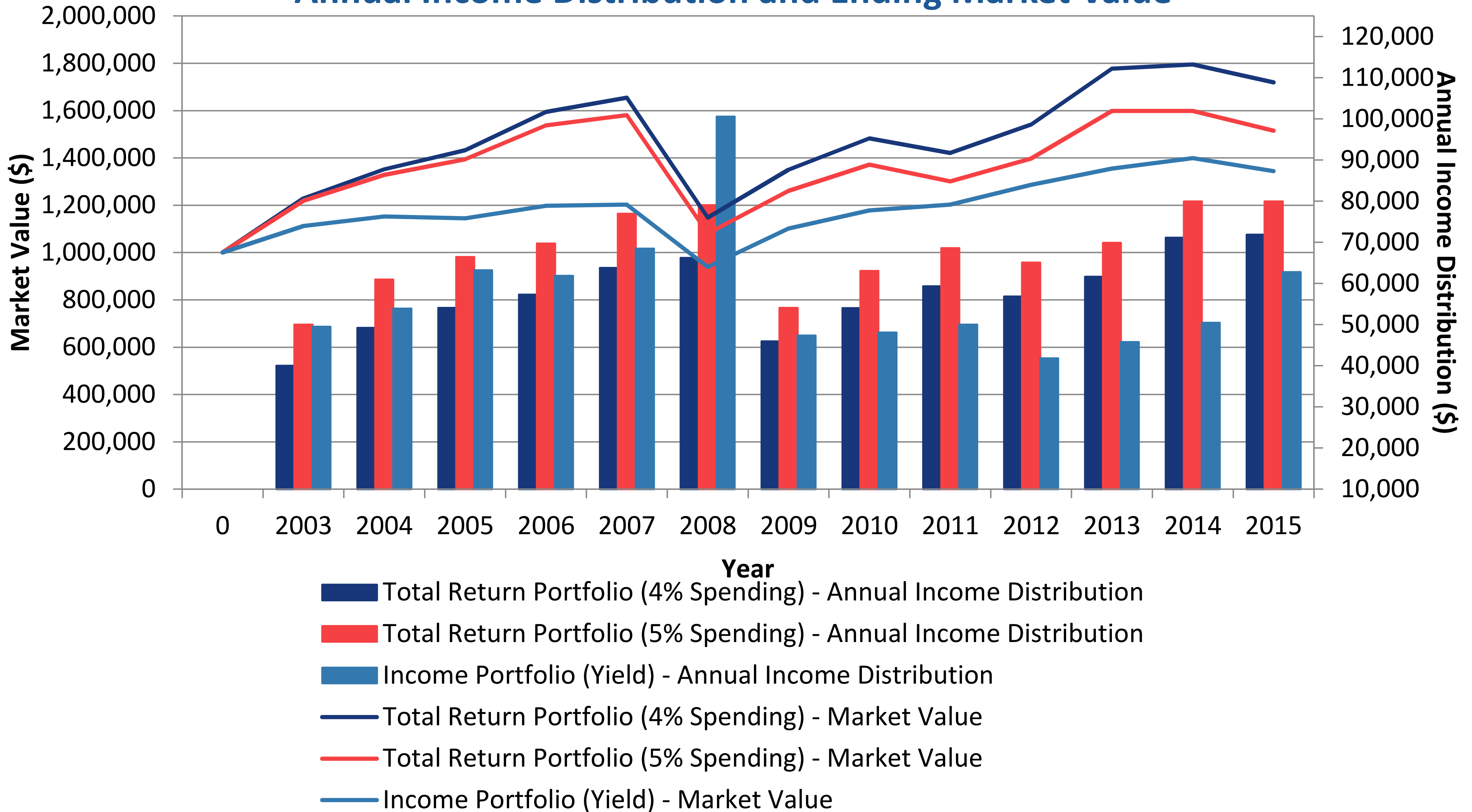
Cumulative Distributions	
Total Return Portfolio	$10.47
Income Portfolio	$3.72
Difference	**$6.75**

Note: The Total Return Portfolio consists of 60% Stocks/40% Bonds and the Income Portfolio consists of 20% Stocks/80% Bonds. Rate of returns (capital appreciation and income) used for illustration purposes are held constant each year with portfolios rebalanced annually. The Total Return Portfolio assumes a 5.0% annual distribution rate, while the Income Portfolio distributes only current income. The Historical Illustration is based on data from Ibbotson Associates, 1926-2014. The Projected Illustration is based on data from LCG Associates and Standard & Poor's.

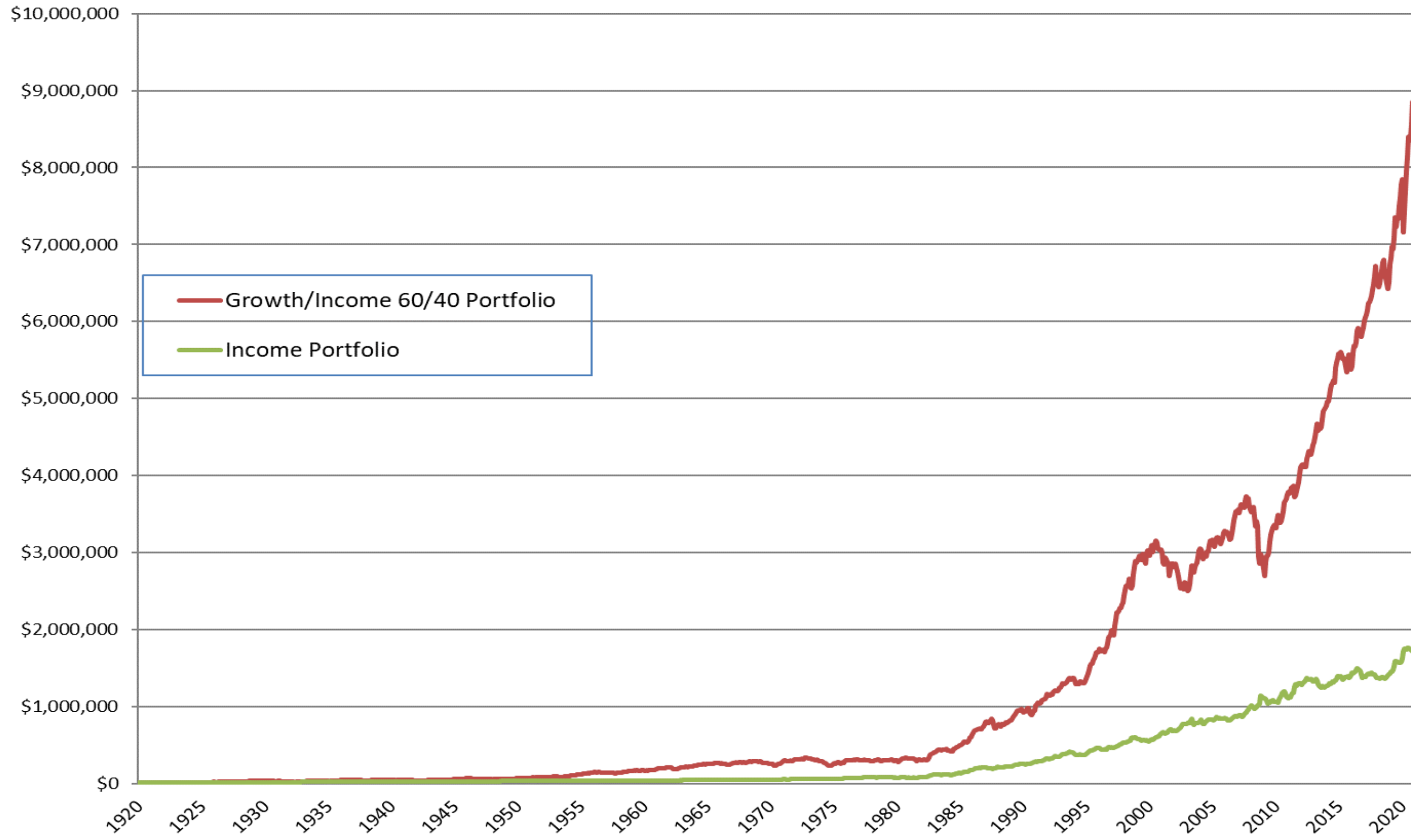
Illustration – Distributions and Growth of $500,000

YEAR	TOTAL RETURN PORTFOLIO 4% SPENDING RATE			TOTAL RETURN PORTFOLIO 5% SPENDING RATE			INCOME PORTFOLIO	
	Total Return Portfolio (4% Spending) - Market Value	**Total Return Portfolio (4% Spending) - Annual Income Distribution**		**Total Return Portfolio (5% Spending) - Market Value**	**Total Return Portfolio (5% Spending) - Annual Income Distribution**		**Income Portfolio (Yield) - Market Value**	**Income Portfolio (Yield) - Annual Income Distribution**
0	500,000			500,000			500,000	
2003	614,605	20,000		609,605	25,000		556,169	24,739
2004	675,867	24,584		664,273	30,480		576,390	26,932
2005	716,162	27,035		697,234	33,214		572,530	31,606
2006	797,101	28,646		769,061	34,862		598,691	30,934
2007	827,159	31,884		790,371	38,453		601,267	34,224
2008	573,815	33,086		540,391	39,519		469,632	50,278
2009	675,167	22,953		630,435	27,020		550,689	23,656
2010	741,259	27,007		685,844	31,522		589,207	24,038
2011	710,537	29,650		650,560	34,292		601,284	24,981
2012	770,147	28,421		698,633	32,528		643,033	20,908
2013	888,870	30,806		799,346	34,932		677,454	22,870
2014	897,706	35,555		799,298	39,967		699,747	25,228
2015	859,733	35,908		757,494	39,965		671,935	31,378
TOTAL		**375,536**			**441,752**			**371,771**

Total Return and Income Portfolio Expectations



Note: The Total Return Portfolio consists of 60% Stocks/40% Bonds and the Income Portfolio consists of 20% Stocks/80% Bonds. Rate of returns (capital appreciation and income) used for illustration purposes are held constant each year with portfolios rebalanced annually. All illustrations and assumptions provided by Trust Advisors, Inc., a subsidiary of SCI, and LCG, a registered investment advisor.


Growth of $10,000
$10,000,000
$9,000,000
$8,000,000
$7,000,000
$6,000,000
$5,000,000
$4,000,000
$3,000,000
$2,000,000
$1,000,000
$0
Growth/Income 60/40 Portfolio
Income Portfolio
1920
1925
1930
1935
1940
1945
1950
1955
1960
1965
1970
1975
1980
1985
1990
1995
2000
2005
2010
2015
2020

PERPETUAL CARE PART 1

Perpetual or endowment care involves the continued preservation, improvement, embellishment and maintenance in a proper manner markers, lots, compartments, crypts or other space in a cemetery, columbarium or mausoleum.

How to Put Aside Enough Now To Cover Cemetery Costs Later

by Hayden Burrus

Editor's note: This is the first in a three-part series about how to set up and maintain a perpetual care or endowed care fund for a cemetery.

Perpetual care funds were originally established by some forward-thinking cemeteries. They were later mandated by virtually all state governments, with certain cemeteries, such as those run by religious or fraternal organizations, exempted. They are also referred to as endowment care funds, but for the purposes of this article we will use the term "perpetual care fund."

Hayden Burrus

The funds were created and are designed to ensure that enough money will be set aside from today's cemetery revenue to pay for the care of cemeteries in the future. To achieve that goal, a forward-thinking cemetery must do much more than simply set aside the state-mandated amount of money—or more than that amount. The money in the fund must be properly invested.

These funds must cover three very different types of expenses:

• **Continual, standard cemetery maintenance.** These expenses include mowing the cemetery grounds, regular custodial care, landscape and grounds maintenance and any other expenses that occur regularly, on a monthly, quarterly or annual basis. They are the easiest to work with and project. Although these periodic expenses may not currently be that high, the effect of costs rising slowly but indefinitely can be very significant. This is illustrated in Table 1.

TABLE 1: ANNUAL EXPENSE $1,000

In a moderate inflationary environment of 5% per year, even a small annual expense of $1,000 will cost a cemetery almost $3 million during this century.

	4% ANNUAL INFLATION		5% ANNUAL INFLATION	
YEAR	ANNUAL EXPENSE	CUMULATIVE EXPENSE	ANNUAL EXPENSE	CUMULATIVE EXPENSE
2000	$ 1,000	$ 1,000	$ 1,000	$ 1,000
2010	$ 1,480	$ 12,486	$ 1,629	$ 13,207
2020	$ 2,191	$ 30,969	$ 2,653	$ 34,719
2050	$ 7,107	$ 158,774	$ 11,467	$ 219,815
2100	$ 50,505	$ 1,287,129	$ 131,501	$ 2,740,526

• **Periodic "one-time" expenses.** These expenses include all maintenance and improvement expenses occurring on an infrequent and sometimes irregular basis. Examples include road repaving, major landscaping work and new roofing for cemetery buildings. Even when cemetery grounds are currently well maintained, the infrastructure gradually decays and requires major restoration efforts or replacement. Consider that if restoration work on cemetery structures must occur once every 20 years, the work must be done five times during the next century. At a cost (in today's dollars) of $25,000 to $50,000, the total cost for this work could be as high as $10.7 million after considering inflation. (With an inflation rate of 5 percent, a $50,000 restoration expense occurring every 20 years will cost $133,000 in 2020, $352,000 in 2040, $934,000 in 2060, $2,478,000 in 2080 and $6,575,000 in 2100.)

• **Unplanned, unexpected costs.** In addition to the expected expenses mentioned above, over the course of time, unexpected and sometimes catastrophic costs may be caused by fire, explosion, flood, earthquake, tornado, vandalism, etc. The trust fund must have the ability to pay for the repairs associated with these events unless the cemetery has insurance to cover all of these eventualities. The size of the policy deductible should rise as the value of the trust fund rises.

Regulations

As a part of my work with cemetery perpetual care funds, I have had the opportunity to speak with more than 40 regulators and legislators in jurisdictions across the United States and Canada. The laws in these jurisdictions have the same general structure, but the regulators' attitudes toward cemetery regulation vary widely.

Perpetual care fund regulations universally require a fixed percentage of sales to be contributed into the care fund. In most cases, this percentage varies between 10 percent and 20 percent. Some jurisdictions have different contribution rates for different categories of cemetery space. In addition, some jurisdictions require cemeteries to collect a fixed fee from each purchaser of cemetery property.

Funding of this type has many benefits, from an actuarial and financial viewpoint.

TABLE 2: INITIAL VALUE $100,000

An investment income maximization strategy can be catastrophic.

YEAR	VALUE OF TRUST FUND EMPHASIZING INVESTMENT INCOME	VALUE OF TRUST FUND EMPHASIZING TOTAL RETURN	LOST VALUE IF TOTAL RETURN IS NOT EMPHASIZED
2000	$ 100,000	$ 100,000	$ 0
2010	$ 183,354	$ 275,115	$ 91,761
2020	$ 336,185	$ 756,882	$ 420,697
2050	$ 2,072,273	$ 15,760,533	$ 13,688,261
2100	$ 42,943,147	$ 2,483,944,148	$ 2,441,001,000

■ In contrast to the wide latitude the prudent investor rule provides, regulations governing withdrawals from perpetual care funds are very stringent and narrow.

First and foremost, it leads to the sharing of perpetual care expenses among all cemetery plot owners. It also results in social equity, since people purchasing more desirable (and costly) cemetery property contribute more toward the perpetual care of the cemetery as a whole. A further benefit of the percentage of sales contribution plans is that they are inflation sensitive—no adjustments need to be made to the legislation to account for the effect of inflation on the cost of perpetual care. As the expenses related to perpetual care rise, so will the cost of cemetery plots and the contributions to the perpetual care trust fund.

Some states do not require any funding of individual cemetery perpetual care funds by people who bought cemetery plots before the cemetery established a perpetual care fund (i.e. their exclusion from cemetery perpetual care fund legislation was grandfathered in). This addendum to perpetual care legislation is inherently unfair. It shifts the burden of funding the perpetual care of the entire cemetery onto future purchasers of cemetery property. This burden is especially great for property purchasers in cemeteries that are close to full capacity.

The specifics of legislation pertaining to contributions into perpetual care funds in most jurisdictions are based on political compromise and legislative fiat rather than sound actuarial and financial theory.

Investment practices for cemetery perpetual care funds are not usually specifically stated. Instead, they are governed by a doctrine known as the "prudent investor rule." This rule normally contains language similar to the following:

"In acquiring, investing, reinvesting, exchanging, retaining, selling and managing property for the benefit of another, a fiduciary shall exercise the judgment and care under the circumstances then prevailing which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds considering the probable income as well as the probable safety of their capital. Within the limitation of the foregoing standard, a fiduciary is authorized to require and obtain every kind of property ...."

In essence, this rule allows complete flexibility for the perpetual care fund investment officer to adjust investment practices as the condition of the fund and the financial climate change. It acknowledges that there are a variety of reasonable and intelligent investment strategies and allows investment strategies to change over time. It is sound legislation.

In contrast to the wide latitude the prudent investor rule provides, regulations governing withdrawals from perpetual care funds are very stringent and narrow. I have found no jurisdictions that permit any withdrawals of principal from perpetual care trust funds. The logic behind this is that contributions into perpetual care trust funds are intended to support cemetery maintenance indefinitely, therefore initial contributions should remain indefinitely. In most cases, this rule is sound and instrumental in ensuring the long-term solvency of perpetual care funds.

Most jurisdictions distinguish trust fund income between investment income (arising from interest and dividends on securities) and capital gains (arising from the increase in value of stocks, bonds and other assets). Withdrawal of capital gains is often prohibited by legislation, while withdrawal of at least part of the investment income is permitted. The investment vehicles generating the largest portion of their income through investment income are bonds and cash investments. The investment vehicles generating the largest portion of their income through capital gains are common stocks.

This distinction is arbitrary, unnecessary and harmful to the long-term solvency of perpetual care trust funds. All appreciation (or depreciation) in the value of a trust fund affects the trust fund equally, regardless of whether it comes from investment income or capital gains. This legislation, in effect, forces trust fund managers to ignore capital gains and adjust their portfolios to ensure that the investment income from the funds will be high enough to allow for the withdrawals the cemetery must make.

The time horizon for cemetery trust funds is very long. Vanguard Investment Group, the largest mutual fund provider in the world, advises in its brochure "Creating the Right Investment Mix": "The longer your investment time frame, the more you can ignore short-term risks and focus on long-term results. In other words, the further you are from your investment goal, the more it's worth taking risks with stocks." To further support that point, let me point out two additional items about the long-term performance of the Standard & Poor's (S&P) 500 common stocks:

- Between 1926 and 2000, there has been no 20-year historical period—not even during the Great Depression of the 1930s—when the bond market has outperformed the S&P 500.
- Between 1926 and 2000, there has been no 20-year historical period where the S&P 500 has not appreciated in value faster than inflation.

Ignoring the long-term potential for common stocks can be catastrophic. Consider two trust funds valued today at $100,000. One is focused on maximizing investment income; it has invested 90 percent of its portfolio in the bond market and 10 percent in common stocks. The other is focused on maximizing its total return without regard to the mix between investment income and capital gains; it has invested 90 percent of its portfolio in

common stocks, and 10 percent of its portfolio in the bond market. Table 2 shows the future values of each of these portfolios.

Table 2 illustrates that an investment income maximization strategy can be catastrophic. Even after a medium time horizon of 20 years, the investment income maximization strategy will cost the sample trust fund in this example over $400,000 in lost investment return—more than four times the value of the original investment. Over the 50- and 100-year time horizon, the loss is in the millions.

Coming next issue: The mismatch of perpetual care costs, cemetery revenues and perpetual care fund revenues.

Hayden Burrus is the principal actuary of HB Actuarial Services in Delray Beach, Florida. He is an associate of the Casualty Actuarial Society (ACAS) and a Member of the American Academy of Actuaries (MAAA). HB Actuarial Services specializes in stochastic simulations of financial results, forecasting of uncertain cash flows and non-traditional forecasting methodologies, as well as standard property and casualty pricing and reserving issues. He can be reached at (561) 279-2323, or through e-mail at burrus@Hbactuarial.com.