DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

P.O. Box 690, Jefferson City, Mo. 65102-0690

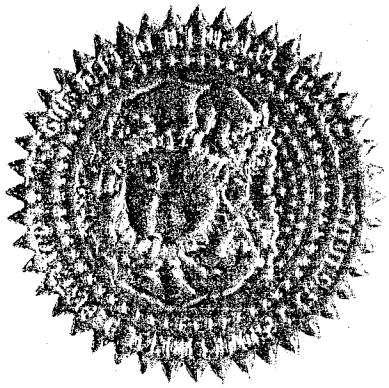
RE: Examination Report of Capital Reserve Life Insurance Company as of March 31, 2007

ORDER

After full consideration and review of the report of the financial examination of Capital Reserve Life Insurance Company for the period ended March 31, 2007, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, Douglas M. Ommen, Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 374.205.3(3)(a), RSMo., adopt such report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, the findings and conclusions of the examination report are incorporated by reference and deemed to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo.

Based on such findings and conclusions, I hereby ORDER Capital Reserve Life Insurance Company, to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed by such report: (1) implement, and verify compliance with, each item mentioned in the General Comments and/or Recommendations section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions.

So ordered, signed and official seal affixed this September 26, 2007.



DOUGLAS M. OMMEN, Director
Department of Insurance, Financial Institutions
and Professional Registration

REPORT OF

LIMITED SCOPE EXAMINATION OF

CAPITAL RESERVE LIFE INSURANCE COMPANY

AS OF

MARCH 31, 2007

STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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July 19, 2007
Jefferson City, Missouri

Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance
Chairman, (E) Financial Condition Committee, NAIC

Honorable Merle Scheiber, Commissioner
South Dakota Division of Insurance
Midwestern Zone Secretary

Honorable Douglas M. Ommen, Director
Missouri Department of Insurance, Financial
Institutions and Professional Registration
301 West High Street, Room 530
Jefferson City, Missouri 65101

Gentlemen:

In accordance with your financial examination warrant, a limited scope financial examination has been made of the records, affairs and financial condition of

Capital Reserve Life Insurance Company

also referred to as "CRL" or as the "Company." The examination was conducted at the Company's home office at 812 Madison Street, Jefferson City, Missouri 65101, telephone number (573) 636-3913. This examination began on June 18, 2007 and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The prior full scope association financial examination of Capital Reserve Life Insurance Company was performed as of June 30, 2005. The examination was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC) with no other zones participating.

The current limited scope examination covers the period from July 1, 2005 through March 31, 2007, and was conducted by an examiner from the State of Missouri representing the Midwestern Zone of the NAIC with no other zones participating.

Areas Covered

The current examination was a limited scope examination which objectives were to analyze the Company's operating performance subsequent to the prior examination and evaluate management's ability to return the Company to a profitable status. The examination included the following:

(1) a review and summarization of the Company's operating performance based on its monthly financial statements for the period subsequent to the prior examination;
(2) a review of the Company's Business Plan as submitted to the Missouri Department of Insurance, Financial Examination and Professional Registration (DIFP);
(3) a review of the current status of legal actions brought by and against the Company;
(4) a review of the management letter findings of the Company's independent CPA and the independent CPA's workpapers relating to the year end 2006 audit.

This is a limited-scope examination, and as such, is limited to those areas identified above and is not intended to communicate all matters of importance for an understanding of the Company's financial condition.

Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance, Financial Institutions and Professional Registration and statutes of the State of Missouri prevailed. Specific procedures utilized in review of the individual areas covered by this examination are summarized in the related subsections of this report.

DESCRIPTION OF COMPANY

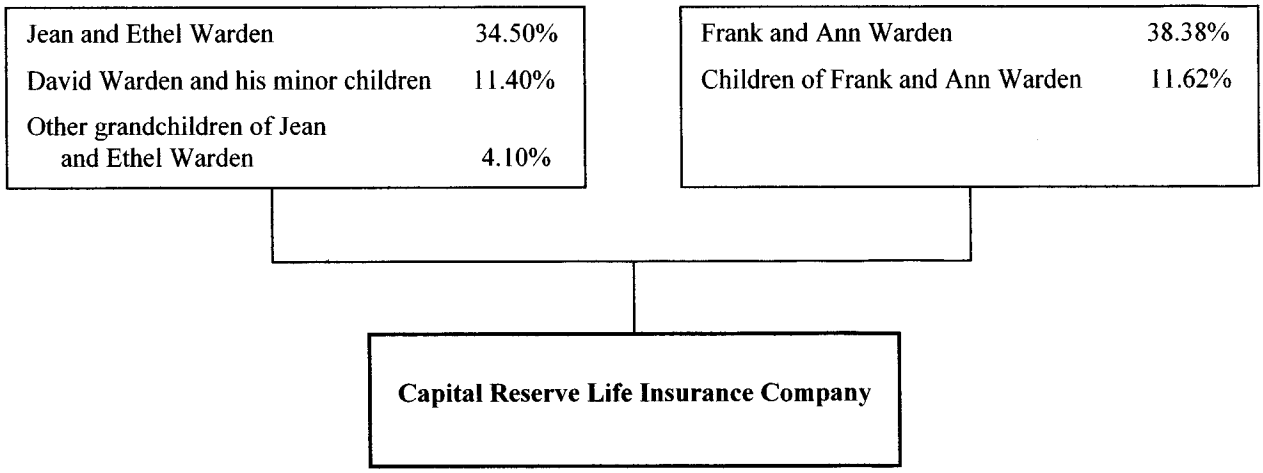
General

Capital Reserve Life Insurance Company was originally incorporated under the Mutual Assessment laws of Missouri in 1922, as the Capital Mutual Association. In 1949, the Company was reincorporated as a Stipulated Premium Life Insurance Company and changed to its current name. In 1955, the Company became a Joint Stock, Legal Reserve Life Insurance Company qualified to do business under the provisions of Sections 376.010 to 376.670 RSMo.

Management and Control

Prior to April 2004, the ownership of the Company was divided equally between members of two families, the Rileys and the Wardens. By agreement, the ownership of the Company was to remain equally divided between the two families with each family voting as a block. Therefore, no individual owner had a controlling interest in the Company. In March 2002, the Company reached an agreement with the Riley family to repurchase their 50% of the outstanding stock for a total price of $9,169,000. The result of the repurchase was to decrease the total surplus of the Company by the $9,169,000 amount paid for the stock repurchase.

Subsequent to the repurchase, the ownership of the Company was split equally between two controlling groups of the remaining shareholders who are all members of the Warden family. Frank and Ann Warden are considered the ultimate controlling entity as they hold 38.38% of the total shares of stock outstanding. The current ownership, as of March 31, 2007 is depicted in the following organizational chart.



The management of the Company is vested in a nine member Board of Directors elected by the shareholders. As of March 31, 2007, five of the directors were shareholders and/or employees of CRL and four of the directors were individuals not otherwise affiliated with the Company.

The Company's daily operations are managed by its officers consisting of the following individuals:

Joseph Warden	President
Frank Warden	Vice President and Director of IS Operations
Anthony Hutchinson	Chief Executive Officer

Besides the officers, the Company also has seven other employees consisting of three office employees, a Marketing Director, Underwriting Clerk and Premiums Receipts Clerk, and four Sales Field Representatives.

Company Operations

The Company is licensed in Missouri under Chapter 376 RSMo for life and accident and health insurance. The Company is also licensed in Kansas and Iowa; however, the Company has not written business in Iowa in several years and currently does not meet that State's minimum surplus requirements for writing new business. For the year ending December 31, 2006, Missouri direct premiums and annuity considerations accounted for 85.4% of all direct premiums and annuity considerations with Kansas accounting for the remaining 14.6% percent

Prior to the repurchase of the Riley family stock, the Company traditionally wrote whole life, 20-pay and other long-term pay life products through independent agents. Subsequently, the Company shifted its marketing focus by terminating its relationships with independent insurance agents and entering into agreements with funeral home directors to sell pre-need funeral coverage in the form of single premium annuities and interest sensitive life products.

The Company experienced a substantial growth in premium and annuity considerations volume due mainly to increased sales of its annuity products. However, due to the high reserve requirement of these products and the significant increases in the Company's general and administrative expenses, the increase in premiums and annuity considerations has not translated into increased profitability.

Prior Examination Findings

The prior examination report, dated June 30, 2005, noted over $600,000 in questionable reimbursements made to the Company's former President and his wife. As a result of these reimbursements and other concerns, the Board of Directors removed the former President in September 2005, and subsequently filed a lawsuit to recoup the misappropriated amounts.

The prior examination report also included examination changes totaling $505,957 as well as numerous comments and recommendations relating to internal controls, corporate governance, overall management competence and errors made in the Company's Annual Statement reporting.

ANALYSIS OF OVERALL OPERATING PERFORMANCE

The objective of the overview of the Company's overall operating performance was to determine and document the trends in the Company's net losses and declines in surplus since the prior examination. Procedures included obtaining the Company's monthly financial statements and scheduling the monthly net profit/loss amounts as well as the monthly ending capital and surplus. In addition, the Company's Quarterly and Annual Statements were obtained and reviewed.

Significant losses and declines in capital and surplus have been noted for each of the past five years as follows:

Year	Net Loss Incurred	Ending Capital and Surplus
2002	$(232,254)	$6,605,994
2003	(505,290)	6,003,509
2004	(1,173,550)	4,598,927
2005	(2,257,669)	2,194,599
2006	(244,448)	1,960,470
2007 (through March 31st)	(152,754)	1,750,249

Although the Company was able to reduce the amount of the annual net loss and rate of surplus decline in 2006, it was noted per review of the Company's monthly financial statements, that the Company has incurred operating losses in all but three of the 21 months subsequent to the prior examination date. Additional losses were also incurred for the three month period subsequent to the current examination.

The Company's capital and surplus as of the examination date was only $550,249 above the minimum capital and surplus level of $1.2 million required by 376.280 RSMo (Capital necessary to do business). Should CRL continue to sustain surplus declines, the Company could eventually drop below the minimum capital and surplus requirements.

The Company's current weak surplus position limits the actions the Company can take in order to grow its business and threatens possible action from the DIFP should the capital and surplus continue to deteriorate. The Company should take immediate steps to stabilize and increase its capital and surplus levels such actions could include obtaining additional capital contributions from current shareholders, obtaining additional capital contributions from outside investors, sale of part of the Company's real estate assets or a sale of the Company itself.

REVIEW OF BUSINESS PLAN

The objective of the review of the Company's business plan was to determine the reasonableness of management's plan to return the Company to a profitable status. Procedures included reviewing the business plan filed with the DIFP, interviewing Company management regarding the business plan and marketing efforts, reviewing the Company's budget and forecast and reviewing the Company's income and expense amounts during the examination period.

As a result of concerns relating to operating performance, the Company was required by the DIFP to file a business plan in April of 2007. The business plan was submitted to the DIFP on April 30, 2007 and consisted of three narrative pages and a one page budget and forecast. The business plan was prepared by the Company's CEO and focused mainly on the Company's marketing and investment efforts.

It was noted in the prior examination, that the Company's Sales Department consisted of a Director of Training and Marketing, a Sales Director and three Field Sales Representatives. The Director of Training and Marketing left the Company in May of 2006 and the Sales Director left in March of 2007. In addition, there has been a complete turnover of the Company's Field Sales Representatives. In March of 2007, a new Director of Marketing was hired and in May 2007 the CEO assumed management of the sales force.

The turnover in the Company's sales Department so far does not appeared to have had a severe detrimental effect on the Company as its monthly premium and annuity considerations have only slightly decreased over the examination period. However, there is some concern in that both the former Sales Director and Director of Training and Marketing had significant experience in the insurance and funeral home industries, whereas the new Sales Director and CEO had no such experience prior to working for CRL. In addition, according to the Company's business plans, in order for the Company to return to a profitable status, there will need to be a dramatic increase in sales volume. For example, it was noted annuity sales were projected to increase by 141% from the third to fourth quarter of 2007.

Although the CEO offered several means by which the Company could increase sales, he was unable to offer specifics as to how the Company would be able to increase its sales by the amounts shown in the business plan. In addition, differing opinions were offered by the Company's President and Vice President as to which types of products the Company should emphasize and whether the Company should attempt to renter certain lines of business or contract with independent agents.

A significant problem underlying the Company's ability to develop a comprehensive and effective marketing or business plan is that the Company was unable to provide a profitability analysis for its different lines of business. Although it was stated to the examiner that an analysis had been requested by the Company of its former actuary, there was no written documentation of this request, and the analysis was not provided to the Company. As a result, the Company is unsure which, if any, of its products are actually profitable. The Company has also not prepared an analysis to determine the effects of different commission or pricing structures for its products or of different interest rates for its annuity products. Absent such analysis, it is not possible for the Company to develop an effective marketing plan or strategy and determine where it should concentrate its marketing efforts. The Company should work with its actuary to obtain a profitability analysis of its various products. Once this analysis is obtained, the Company should reevaluate its business plan to reflect the findings of the analysis. In addition, the business plan should be adjusted to reflect realistic increases in sales for the various product lines.

It was noted that the Company has made some significant reductions to expenses since the dismissal of its former President in 2005. However, many of these reductions are simply the result of the elimination of the misappropriations and mismanagement of the former President. The Company's largest expense category has historically been salaries and this continues to be the case. The prior examination had noted that salaries paid to certain officers and employees appeared excessive given their job tasks and responsibilities. The Company has made significant reductions in salary expenses partly through cutbacks in employees and also through salary reductions for the officers. However, officer salaries and the salaries of some employees continue to appear to be excessive given the Company's continued poor operating performance and surplus declines. The Company should perform a thorough review of all expense line items to determine any areas where further reductions can be made. In addition, consideration should be given to further reducing officer salaries until such time as the Company returns to a profitable status.

REVIEW OF CURRENT LEGAL ACTIONS

The objective of the review of the current status of legal actions was to determine the likelihood that the Company would receive any significant amounts from the legal actions that it has taken and the potential exposures to the Company from pending legal actions. Procedures included reviewing legal judgments the Company has obtained and claims which have been filed against the Company, interviewing Company management and legal counsel and discussing the Company's pending legal issues with DIFP legal counsel.

The Company had filed a lawsuit against its former President, Joseph Warden and his wife Linda Warden seeking reimbursement for amounts that had been misappropriated from the Company. A judgment in the amount of $551,343 was rendered in favor of the Company on May 30, 2007. However, due to the fact that Joseph and Linda Warden do not have any known substantial assets and have significant outstanding mortgage and credit debts, the ability of the Company to collect on any amounts rendered in the judgment are highly questionable.

Varying opinions were offered as to whether the judgment would impact the ability of the Company to collect on claims it has filed under its fidelity bond coverages. While Company legal counsel was of the opinion that the judgment could have a favorable impact on the Company's efforts to collect on the fidelity bonds, it was noted that the total amount of the Company's fidelity bonds is only $200,000 with deductibles totaling $7,500. Therefore, the maximum amount the Company would be able to collect on the fidelity bonds would be limited to $192,500, which would not have a significant effect on the Company's overall surplus.

During examination fieldwork, the Company was served with a lawsuit from its former Sales Director. In the lawsuit the Sales Director alleges that there was an agreement between herself and the Company's former President under which she was to receive certain production bonuses which CRL failed to pay. The lawsuit is seeking $1.486 million in damages representing the bonuses that would have been paid under her interpretation of the alleged agreement. Varying opinions were provided by Company management and legal counsel as to the validity of the lawsuit.

The Company has turned the lawsuit over to new outside legal counsel. As a result, it appears that the legal fees incurred by the Company to defend against the lawsuit could be substantially higher that those originally represented by the Company's prior legal counsel. In addition, the lawsuit has the potential to affect any efforts the Company may make to attract additional capital contributions or the possible sale of the Company. The Company should work with its outside legal counsel to resolve the lawsuit as quickly and reasonable as possible.

REVIEW OF CPA MANAGEMENT LETTER COMMENTS AND WORKPAPERS

The objective of the review of the management letter comments and workpapers of the Company's independent CPA was to obtain some assurance regarding the amounts reported in the Company's financial statements, obtain a better understanding of the Company's operations and the implementation of internal controls subsequent to the prior examination and to document any significant problems or concerns noted by the independent CPA. Due to the limited scope, of the current examination, substantive or other testing to verify the amounts reported by the Company in its statement filings or extensive review of internal controls was not performed. However, due to the numerous problems noted in these areas in the prior examination and due to the concerns regarding the Company's operating results since the prior examination, it was determined that it would be beneficial to review the work performed by the independent CPA relating to their 2006 year end audit. Procedures performed were to obtain and review the independent CPA audit report, management letter and workpapers relating to the year end 2006 audit, to interview the independent CPA regarding the audit and any concerns he might have and to interview Company management regarding the CPA findings and concerns.

No significant problems or concerns were noted in review of the 2006 audit report. It appeared in review of the CPA workpapers, that the CPA had performed adequate procedures to verify the amounts reported per the Annual Statement.

The CPA did issue a management letter related to the 2006 audit noting several issues including some discrepancies in amounts reported per the Annual Statement and supporting schedules, inadequate documentation for some expenses and that investment transactions were not consistently reported on the trade or settlement date. These issues and the other comments in the management representation letter were discussed with Company management by the examiner. It appears that the Company has improved on its Annual Statement reporting since the prior examination, and no concerns were noted that would warrant further examination procedures.

The CPA indicated in his conversation with the examiner, that he was concerned about the Company's continuing poor operating performance. However, a going concern comment was not included in the audit report, as he had determined that the Company would most likely not become financially impaired within one year which would be the requirement for a making a going concern comment.

GENERAL COMMENTS AND/OR RECOMMENDATIONS

Capital and Surplus **Page 4**

The Company's current weak surplus position limits the actions the Company can take in order to grow its business and threatens possible action from the DIFP should the capital and surplus continue to deteriorate. The Company should take immediate steps to stabilize and increase its capital and surplus levels such actions could include obtaining additional capital contributions from current shareholders, obtaining additional capital contributions from outside investors, sale of part of the Company's real estate assets or a sale of the Company itself.

Business Plan **Page 5**

A significant problem underlying the Company's ability to develop a comprehensive and effective marketing or business plan is that the Company was unable to provide a profitability analysis for its different lines of business. As a result, the Company is unsure which if any of its products are actually profitable. The Company has also not prepared an analysis to determine the effects of different commission or pricing structures for its products or of different interest rates for its annuity products. Absent such analysis, it is not possible for the Company to develop an effective marketing plan or strategy and determine where it should concentrate its marketing efforts. The Company should work with its actuary to obtain a profitability analysis of its various products. Once this analysis is obtained, the Company should reevaluate its business plan to reflect the findings of the analysis. In addition, the business plan should be adjusted to reflect realistic increases in sales for the various product lines.

The Company has made significant reductions in salary expenses partly through cutbacks in employees and also through salary reductions for the officers. However, officer salaries and the salaries of some employees continue to appear to be excessive given the Company's continued poor operating performance and surplus declines. The Company should perform a thorough review of all expense line items to determine any areas where further reductions can be made. In addition, consideration should be given to further reducing officer salaries until such time as the Company returns to a profitable status.

Legal Actions

During examination fieldwork, the Company was served with a lawsuit from its former Sales Director. In the lawsuit the Sales Director alleges that there was an agreement between herself and the Company's former President under which she was to receive certain production bonuses which CRL failed to pay. The lawsuit is seeking $1.486 million in damages representing the bonuses that would have been paid under her interpretation of the alleged agreement. The Company has turned the lawsuit over to outside legal counsel and it appears that the legal fees incurred by the Company to defend against the lawsuit could be substantially higher that those originally anticipated. In addition, the lawsuit has the potential to affect any efforts the Company may make to attract additional capital contributions or the possible sale of the Company. The Company should work with its outside legal counsel to resolve the lawsuit as quickly and reasonable as possible.

ACKNOWLEDGMENT

The assistance and cooperation extended by the management and employees of Capital Reserve Life Insurance Company during the course of this examination is hereby acknowledged and appreciated.

VERIFICATION

State of Missouri)
) ss
County of)

I, Mark A. Nance, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of the Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

Mark A. Nance

Mark A. Nance, CFE, CPA
Examiner-in-Charge
Missouri Department of Insurance, Financial Regulation and Professional Registration

Sworn to and subscribed before me this 31st day of July 2007.
My commission expires:

04/24/08

Pamela L. Watson
Notary Public

NOTARY PUBLIC - State of Kansas
PAMELA L. WATSON
My Appt. Exp. 04/24/08

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with the National Association of Insurance Commissioners procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

Frederick G. Heese, CFE, CPA
Audit Manager
Missouri Department of Insurance, Financial Regulation and Professional Registration