A Report on the Financial Aspects
of the Rahabilitation Plan For
National Investors Life Insurance Company
National Investors Pension Insurance Company
Mt. Hood Pension Insurance Company
National Equity Life Insurance Company, Inc.
S&H Life Insurance Company
University Life Insurance Company of America

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I. INTRODUCTION

Engagement

This report is a result of work completed by Milliman & Robertson (M&R) at the request of the Rehabilitators of National Investors Pension Insurance Company (NIPIC), National Investors Life Insurance Company (NILIC), Mt. Hood Pension Insurance Company (Mt. Hood), National Equity Life Insurance Company, Inc. (NEL), S&H Life Insurance Company (S&H), and University Life Insurance Company of America (UL), referred to collectively hereafter as the "Companies." Since the entry of rehabilitation orders relating to these companies on July 13, 1983, M&R has been retained to provide technical support to the Rehabilitators.

This support has been provided through participation in many of the meetings which led to the development of the Rehabilitation Plan and by the development of projections which illustrate the potential financial impact of various aspects of the Rehabilitation Plan. Our role has been to respond to requests from the Rehabilitators to interpret the financial implications of alternative courses of action being considered by the Rehabilitators. This report presents a summary of the financial results that may emerge if the Rehabilitation Plan developed by the Rehabilitators and submitted to the Rehabilitation Courts on October 13, 1983, as subsequently supplemented, is adopted in its present form.

Purpose of Report

The major purpose of this report is to present a projection of the future financial results expected to emerge if the Rehabilitation Plan is adopted. Our projections are based upon certain assumptions regarding the future. As stated above, the Rehabilitation Plan itself has been developed by the Rehabilitators; the assumptions that underly the financial projections have been developed in discussions with the Rehabilitators. The actual financial results that emerge in the future will reflect the actual experience rather than the assumptions which have been made, and it is important to recognize there can be significant variations in the future financial results, if the assumptions are not realized.

Limitations on Scope of Report

As stated above, M&R developed the projections. We did not, however, generate the data used to develop the September 30, 1983 starting balance sheets on which the projections are based. We have performed no audit or independent verification of the assets or liabilities that appear in these balance sheets. We have not independently confirmed that the reserves, which comprise the major portion of the liabilities, are as shown, but rather have accepted all the September 30, 1983 starting values supplied to us. In other words, our role has been to accept the starting financial statements as provided by the sources described in Appendix B and then to develop projected financial statements based on these opening balance sheets and the terms of the Rehabilitation Plan. An analysis of these assets and liabilities was accomplished by the accounting firms of Ernst & Whinney and Arthur Andersen.

II. ASSUMPTIONS: GENERAL

Developing a financial projection for an entity as complex as this group of companies requires a great many assumptions. In a practical sense it is difficult to convey the complete rationale underlying each assumption; however, this section of our report describes certain structural, financial, and tax assumptions underlying our projections. Certain critical financial and actuarial assumptions are set forth in Section V.

Appendix A contains a comprehensive description of the many detailed assumptions used to develop the financial projections. These assumptions were arrived at through our discussions with the Rehabilitators and members of various regulatory working groups. In most cases, the assumptions reflect consensus judgments of the group. Probably no one would find each and every one of these assumptions to be the precise assumption he or she would have selected. On the other hand, all of the assumptions represent reasonable estimates based on the collective judgment of the group working on the project.

It is important to remember assumptions are estimates of what will happen in the future. It is clear that the future experience under the Rehabilitation Plan will not follow these assumptions exactly -- in some cases, experience will be more favorable and, in other cases, less favorable. These assumptions are intended to represent a best estimate of future events; for some of the important assumptions, we have provided projections under alternative assumptions to show

the sensitivity of the projections to changes in assumptions. Our projections assume an April 1, 1984 effective date of the Plan of Rehabilitation.

Restructuring of Companies

The Rehabilitation Plan calls for the ultimate survival of two or three insurance companies to continue as separate entities. National Investors Life Insurance Company (NILIC), University Life (UL) and National Investors Pension Insurance Company (NIPIC) are the three projected surviving entities. The legal and re-insurance arrangements to reach this corporate structure are complex and, at the point of this report, not yet complete. For purposes of our projections we have assumed that all of the assets and liabilities will be "pooled" into one company. It is our understanding that the ultimate structure will achieve the same actu-arial results as a pooling.

Financial Condition as of Beginning Date

Appendix B contains detailed balance sheets for each of the six insurance com-panies as of September 30, 1983. Also shown there are balance sheets for the six companies combined.

As described in Appendix B, these balance sheets have been developed based on information supplied to us by personnel of the various companies, as well as the public accounting firms of Ernst & Whinney and Arthur Andersen who have been reviewing the financial statements of the Arkansas and Indiana companies, respec-tively. It is important to note that they do not reflect any potential adjustment

to surplus required on account of any taxes that may be payable in the future due to operations conducted through September 30, 1983.

Rehabilitation Plan Effective Date

The Rehabilitation Plan is to be in effect for a forty-two month period. The effective date has not been decided at this time. In our projections, we have assumed that the plan would become effective April 1, 1984 and continue for forty-two months through the end of September, 1987.

Federal Income Tax Consequences of Restructuring

Our projections have been completed on the assumption no federal income tax will be incurred during the rehabilitation. This follows from the assumption that all amounts credited to policyholders' accumulation accounts will be deductible, a position we believe to be correct. It is important to note we are not tax experts and this assumption should be verified with tax counsel.

Value of Affiliate Securities

The Rehabilitation Plan is based on a "worst case" assumption with respect to the value of affiliate securities, and for purposes of our projections, these securites have been displayed at their September 30, 1983 carrying values in Appendix A. Although shown at their carrying values in Appendix A, the projections assume, for the purpose of determining the assured rates described in the

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effect,

Rehabilitation Plan, that these assets generate no income in the future, i.e., in effect, they assume the assets have zero value.

III. RESTRUCTURING OF POLICY LIABILITIES

The six insurance companies have hundreds of policy forms, issued to approximately 400,000 policyholders, that will be affected by the Rehabilitation Plan. However, for purposes of analysis, we have grouped the policies into four types: Single Premium Deferred Annuities (SPDA), Group Pension Products, Traditional Life Insurance, and Single Premium Whole Life. We believe this allocation of policies to be appropriate since it recognizes product variations which influence the financial aspects of the plan without creating unnecessary complexity in the model. Also, this process allows for treating policyholders of generally similar policies in a consistent and equitable manner. It should be noted that there is a fifth category of policyholders — those receiving periodic annuity payments as of September 30, 1983 -- but these policyholders are unaffected by the plan (see Appendix A). The largest and financially most significant are the SPDA policies but the plan addresses all of these contracts.

This section of our report describes our understanding of how the Rehabilitiation Plan will affect each group of policyholders.

SPDA Policies

SPDA policyholders will be offered a series of five options as follows:

A.

B.

C.

A. Continued SPDA with moratorium on surrenders for the duration of the rehabilitation period. Policyholders will be credited with a rate based upon the average of the top ten companies active in the SPDA market, plus 1/2%. In the event the Companies' assets at the end of the rehabilitation period are inadequate to fund this liability, the liability will be adjusted downward but in no event will it result in a credit less than a 5.5% rate for the period. The Plan defines the 5.5% minimum as the "assured" rate.

B. SPDA with 10% free withdrawal annually. Policyholders will be entitled to withdraw up to 10% of their minimum guaranteed account balances per year. The credited rate will be the same as described in Option A. In the event that the Companies have inadequate assets at the end of the rehabilitation period to fund the liability, the liability will be adjusted downward but in no event to less than it would have been at a minimum credited rate of 3.6%. The Plan defines the 3.6% rate as the "assured" rate for this option.

C. Annuitization. Policyholders will be offered a variety of annuity options on a life, joint life and certain basis. The options will be priced based on an implicit interest assumption equal to the market rate for annuitization of ten carriers active in the SPDA market place, increased by 1/2 percent. However, the annuitants will receive a different level of payments during the rehabilitation period. During the rehabilitation period annuitants will receive payments based upon the following rates:

D.

E.

Life Annuity (C-1)	9.0%
Life Annuity with 5 Years Certain (C-2)	9.0
Life Annuity with 10 Year Certain (C-3)	9.0
5-1/2 Year Certain (C-4)	3.8
10 Year Certain (C-5)	7.0

If the assets of the companies are inadequate to fund the liabilities at the end of the rehabilitation period, then the liabilities will be adjusted downward but in no event will the future monthly payments be less than the level of those received during the rehabilitation period.

D. SPDA with policy loan. Policyholders can borrow up to 75% of their current account value, with a loan interest rate of 8.0%. The loaned amount will be credited a rate of 5.5% and the unloaned portion will be credited with the average rate of ten companies active in the SPDA market increased by 1/2 percent. In the event that the assets of the company are inadequate to fund its liabilities, the liability will be adjusted downward but in no event will the policyholder be credited less than 1% on borrowed funds and 4% on unborrowed funds. Upon repayment of outstanding indebtedness a policyholder could elect any of the other SPDA options. The Plan defines the 1% on borrowed funds and 4% on unborrowed funds as the respective "assured" rates.

E. Present Value Option. Policyholders will receive 40% of their account values on the date the Rehabilitation Plan becomes effective and the remaining 60% at the end of forty-two (42) months.

Options A through D all provide for policyholders to participate in Phase 2 of the Plan. Option E does not provide such participation.

Group Pension Products

This category includes contracts where contributions are or were made by the policyholder and the contract calls for interest to be credited to some date in the future, at which point funds are to be returned to the policyholder either in a lump sum or on an annuitization basis. The actual contracts represent some of the variations currently found in pension funding vehicles and cover ten policy forms with varying contractual provisions as to surrender and 10% free withdrawal provisions. We have assumed the Rehabilitation Plan will offer all of these plans the same or similar options offered to the SPDA policyholders because of the similarity of the basic contracts.

Two of the contract forms are Investment Only contracts with guaranteed contractual rates for a five year period. We assumed that under the Rehabilitation Plan this guaranteed rate will be credited only until the end of the current contract year at which point the plan assured rates will apply. For all other group pension forms we assume the Rehabilitation Plan will provide the same or similar options offered the SPDA policyholders.

Single Premium Whole Life

Single Premium Whole Life involves payment of one premium at the inception of the contract for which the policyholder receives on annually increasing death benefit. No further premiums apply to this policy form. In addition, the contract provides for a guaranteed cash value in the event of surrender. The death benefit each year consists of the cash value in that year plus an additional death benefit. As the contract approaches maturity, the cash value becomes the dominant component of the total death benefit until the cash value equals the total death benefit at maturity.

The Company can and currently does provide larger cash value accumulations than those guaranteed in the contract. Since the Single Premium Whole Life contract is basically an accumulation contract, we have assumed holders of these policies will be offered the same options as the SPDA policyholders.

Traditional Life Policies

We understand the Rehabilitation Plan will offer policies with cash values, in a premium paying mode, a loan provision during the rehabilitation period. This will replace their existing loan provision and allow for a loan for up to 75% of the cash value, at the policy loan rate in the existing contract. All other contractual provisions will be continued except that, for the most part, policyholders may not surrender for cash during the rehabilitation period. (Policyholders with cash values of $2,000 or less will be allowed to surrender for cash — or in the case

of certain types of contracts, will receive cash automatically.) Extended Term Insurance and Reduced Paid Up options will be continued. In addition the automatic premium loan provisions will be continued as stated in the existing contract. Death benefits will be paid as incurred.

The policy loan option for policies with cash values not in a premium paying mode, is to be the same as for the premium paying policies. Death claims will be paid as incurred. No other changes will be made to these policies.

Policies with no cash values are largely term insurance coverages in a premium paying mode. All premium notices will continue to be sent out (as they will for premium paying policies with cash values); if premiums are paid, all contractual provisions are to be honored. If a premium is not paid, the policy will lapse for no value.

All options such as waiver, accidental death benefits and other ancillary coverage will continue to be covered, provided the contract remains in force and premiums are paid as appropriate (subject, in the case of ancillary coverages with cash values, to the previously noted provision re cash value of $2,000 or less).

IV. PROJECTIONS

Projection Overview

The projection system is based on a model of the assets and liabilities of the six companies in rehabilitation. The companies' insurance liabilities reflect hundreds of different policy forms at many different issue ages. Since it is impractical to project financial results for each policy form/issue age combination, we have developed a liability model which allocates each policy liability to a model "cell" based on various plan characteristics and issue age groupings. This allocation is performed in a manner that recognizes significant variations in liability characteristics but combines similar liabilities where such a grouping does not distort financial results. Using such a modelling process results in a model involving less than one hundred cells in place of thousands of individual policy liabilities.

Also, in order to project assets and asset cash flow, we developed an asset model which is manageable for projection purposes but which retains the characteristics of the detailed asset portfolio. A thorough description of these models, including the plans and ages used as model cells, and other details is included in Appendix A.

The model we constructed for the six insurance companies has insurance liabilities of $4,408.5 million at September 30, 1983, which equals the actual insurance liabilities of the six Companies on that date after adjustment as described in Appendix B. In fact, the model is company distinct — carrying the liabilities and