Court File No. 08-CL-7878

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF UNIVERSAL SETTLEMENTS INTERNATIONAL INC.

SECOND REPORT OF THE MONITOR
December 22, 2008

INTRODUCTION

1. On December 2, 2008, Universal Settlements International Inc. ("**USI**" or the "**Applicant**") filed for and obtained protection from its creditors under the *Companies' Creditors Arrangement Act* R.S.C. 1985 c. C-36, *as amended* (the "**CCAA**") pursuant to provisions of an Order of this Honourable Court (the "**Initial Order**"). Pursuant to the Initial Order, Ernst & Young Inc. was appointed as monitor (the "**Monitor**") of the Applicant during these CCAA proceedings ("**CCAA Proceedings**").

2. The purpose of this report (the "**Report**") is to provide this Honourable Court with the Monitor's observations on the Applicant's proposed sale of certain corporately owned policies that USI purchased out of the receivership of Trade Partners, Inc. (the "**TPI AIDS Portfolio**") to SDM Holdings, LLC (the "**Purchaser**").

TERMS OF REFERENCE

3. In preparing this Report, the Monitor has relied upon unaudited financial information, the Applicant's books and records, financial information prepared by the Applicant, and discussions with the management, legal counsel and advisors of USI. The Monitor has not audited, reviewed, or otherwise attempted to verify the accuracy or completeness of the information and, accordingly, the Monitor expresses no opinion or other form of assurance on the information contained in this Report. An examination

of the financial forecast or any other future-oriented financial information as outlined in the Canadian Institute of Chartered Accountants Handbook has not been performed. Future-oriented financial information relied upon in this Report is based on management's assumptions regarding future events. Actual results achieved will vary from this information and the variations may be material.

4. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars. For ease of reference, the Monitor has provided certain Canadian dollar equivalents throughout this Report, using the C$1.18/US$1.00 exchange rate utilized in the Applicant's Motion Record.

5. Capitalized terms not defined in this Report are as defined in the Applicant's Initial Application and the Initial Order.

BACKGROUND

6. The affidavit of Christopher Halas dated December 22, 2008 filed in support of USI's motion seeking this Honourable Court's approval sets out the Applicant's information relating to the purchase, management and proposed sale of the TPI AIDS Portfolio. The Monitor has not been involved in any aspect of USI's activities with respect to the TPI AIDS Portfolio, including USI's efforts to sell it, and as a result is not in a position to provide any first-hand information concerning the TPI AIDS Portfolio or the proposed sale transaction.

7. The Monitor has reviewed the Applicant's materials filed in connection with the pending motion and has discussed the proposed transaction with the Applicant.

ACQUISITION AND VALUATION OF THE PORTFOLIO

8. The Monitor has been advised by the Applicant that it acquired the TPI AIDS Portfolio along with a substantial value of Non-AIDS policies out of the receivership of Trade Partners, Inc. pursuant to a January 14, 2005 Purchase and Sale Agreement for an aggregate purchase price of US$43 million.

9. The purchase price was not formally allocated between the AIDS and non-AIDS components; however, a valuation report prepared by Fasano Associates for the Receiver of TPI as at January 1, 2004 estimated the value of the AIDS component to be

US$4.65 million of a total estimated value of the portfolio of US$59.47 million. Using these relative values indicates a purchase price for the TPI AIDS Portfolio of US$3.36 million.

10. The Applicant has advised the Monitor that USI is the sole beneficial owner of the TPI AIDS Portfolio and that no interests in the portfolio were sold to investors.

11. The Fasano Valuation estimates the value as at January 1, 2004 of the TPI AIDS Portfolio to be approximately US$ 4.65 million. The notes to the Fasano Valuation indicate that the valuation was prepared on a policy by policy basis using then current general population actuarial and mortality tables, adjusted to reflect the mortality experience of the AIDS insureds in the portfolio during the period from 1996 to 2003, to estimate the maturity date for each policy and the individual policy premium details and arrangements to estimate the premium loads. The notes also indicate that the resulting cash flows were then present-valued using a discount rate of 20%. It does not appear that any provision was made for non-premium administration costs that the owner would incur over the life of the portfolio.

12. The Fasano Valuation includes detailed schedules providing the assumed maturities and premium payments by year over the projected life of the portfolio to 2083. The Monitor notes that the Fasano Valuation projects the death benefits to be received over a long period of time, with the receipts in each of 2004 through 2031 projected to range between approximately US$1 million and US$1.7 million. The largest annual maturities are projected to occur in 2023 (US$1.728 million). The projected maturities then decline after 2031 and are projected to fall below US$100,000 per year starting in 2045.

13. The Fasano Valuation projected the premium load for the TPI AIDS Portfolio to remain above US$300,000 per year through 2015, then tapering and dropping below US$100,000 starting in 2029.

14. The information provided by the Applicant concerning the death benefits realized since USI purchased the portfolio and the premium load and administrative cost burden incurred by USI during this period indicates that USI has received a net cash recovery over the four year period of approximately US$30,000. This supports the Applicant's contention that the actual mortality experience has varied from the projections

incorporated in the Fasano Valuation and that the ownership of the TPI AIDS Portfolio has not provided any significant net cash flow return to USI in the four years it has owned it.

15. There does not appear to be any certainty that the cash flow and return on this investment will improve in the coming years. The only fixed component of the investment is the premium load and administrative expense, which the Monitor agrees USI can ill-afford at present.

SALE PROCESS

16. Except for observing an initial telephone call between the Applicant and Silver Point Capital Fund, L.P. expressing preliminary interest in the TPI AIDS Portfolio, the Monitor has not had any direct involvement in the Applicant's efforts to market the TPI AIDS Portfolio for sale before and after the commencement of these CCAA Proceedings. As a result, the Monitor is not in a position to provide any commentary on the efficacy of the efforts and process undertaken by the Applicant to maximize the value to its stakeholders of these assets. The disposition of the Silver Point contact is described by the Applicant in their Motion Record.

17. The Monitor notes that the relevant considerations in assessing the proposed sale include:

   i) Whether the Applicant has made a sufficient effort to get the best price and has not acted improvidently;

   ii) The interests of all parties;

   iii) The efficacy and integrity of the process by which offers were obtained; and

   iv) Whether there has been unfairness in the working out of the process.

18. The Applicant's materials speak to its activities and the extent to which it believes it has canvassed the market of potential purchasers and has encouraged bona fide bidders to submit expressions of interest.

19. The transaction will generate much-needed liquidity in the near term, supporting the Applicant's primary objective which is to preserve and maximize the value of the

investor-owned policies. In this regard, the transaction is in the best interests of USI's stakeholders generally.

20. The Monitor notes that the Applicant engaged B3 Capital ("B3") to assist it in the sale process. B3 was engaged initially for several months on a small monthly retainer to canvas the market. That arrangement was terminated and B3 continued its efforts on a speculative basis and will be paid a portion of the commission being paid to the agent described in the following paragraph.

21. The Purchase Agreement provides that The Heritage Group Agency, Inc. ("**Heritage**") is to receive a broker's commission of US$270,000 (C$318,600). The Monitor understands from the Applicant that there is no brokerage or other agreement between Heritage and USI other than as is reflected in the Purchase Agreement. USI considers the commission reasonable in the circumstances because the proposed transaction represents in management's view a satisfactory result in the circumstances and the market rate of commission in this industry, according to USI, is typically three percent of face value or higher whereas the Heritage commission represents less than one percent of the face value of the policies being sold.

PROPOSED SALE TRANSACTION

22. The Purchase Agreement calls for a purchase price of US$2,470,000 (C$2,914,600). After payment of the broker's commission of US$270,000, US$2,200,000 (C$2,596,000) will be payable to USI and will be paid into escrow (held by Investrust, N.A.) upon closing. In addition, the Purchaser will assume and reimburse all premium payments made by USI or to be incurred by USI since October 15, 2008. The Applicant estimates this to represent a further recovery of approximately US$100,000 (C$118,000).

23. The Purchase Agreement provides that the Policies are purchased on an "as is" basis, except as otherwise provided for in the Purchase Agreement. Under the agreement, USI represents and warrants, among other things, that it (a) has ownership of the policies and that title is free of all encumbrances, (b) has no notice that the policies do not comply with applicable law; (c) is not subject to any legal proceedings in respect of the policies, nor has knowledge of any contemplated proceedings; (d) all contracts and documents provided to the Purchaser are true and correct; (e) all policies are in full

force and effect and the respective insurers are not in default of their obligations thereunder; (f) all existing indebtedness against the policies is paid off or shall be paid off by USI before the closing date; (g) USI has not granted any security interest or lien over its interest in any policy; and (h) the execution of the Purchase Agreement does not violate any law or order. USI has advised the Monitor that it does not anticipate any difficulty in complying with these representations and warranties.

24. The Purchase Agreement calls for the delivery of due diligence documentation to the Purchaser, and a due diligence period of 30 days. If the Purchaser is not satisfied with the due diligence, it may notify USI before the end of the due diligence period of its intention not to close the transaction. Because the Purchase Agreement is dated as of October 15, 2008, the Monitor is advised by USI that the due diligence period has already passed, and the due diligence of the Purchaser has been completed to its satisfaction, and that the Purchaser has advised USI of its intention to close it.

25. The conditions precedent to closing are (a) the delivery of the due diligence documents and the completion of due diligence (already completed), (b) that any required consents of any insured are obtained (the Monitor is advised by USI that no such consents are required) and (c) that the Purchase Agreement be approved by this Court, as evidenced by a final and non-appealable Order.

26. The Purchase Agreement contemplates a closing date of December 31, 2008, assuming that all closing conditions above are satisfied or waived.

27. US$550,000 (C$649,000) of the purchase price will be paid by the Purchaser upon receipt by the Purchaser of the ownership and beneficiary change forms executed by USI. USI has advised the Monitor that it believes it can get these executed forms to the Purchaser within the first two weeks of January. If that can be accomplished by USI, then US$550,000 will be available to it as of that time. However, the Purchase Agreement does give 60 days to USI to provide the executed forms to the Purchaser.

28. The balance of the purchase price is to be released to USI on a pro rata basis per face value of each policy, as the Purchaser receives confirmation that the ownership and the beneficiary changes to name the Purchaser or its nominee to the policy have been completed with the relevant insurer.

29. If the Purchaser fails to close without otherwise being excused from the transaction, USI shall be entitled to claim US$50,000 (C$59,000) from the Purchaser as liquidated damages for the breach. The Purchaser has the right to seek specific performance of the Purchase Agreement if USI breaches its obligations under the Purchase Agreement.

30. The Applicant estimates that, once fully completed, the transaction will generate net cash proceeds to USI totalling US$2.6 million (C$3.1 million) as follows:

    i) Purchase price, net of commission – US$2.2 million (C$2.56 million);

    ii) Reimbursement of premiums paid by USI – US$100,000 (C$118,000); and

    iii) Recovery of cash surrender value – US$312,000 (C$368,160).

31. The Monitor notes that the proposed transaction will provide partial relief for the Applicant's short-term liquidity issues assuming the US$550,000 initial release from escrow and the recovery of the cash surrender value on the retained policies can be achieved by mid-January as contemplated by the Applicant.

ALL OF WHICH is respectfully submitted this 22nd day of December, 2008.

ERNST & YOUNG INC.,
Court-appointed Monitor of Universal Settlements International Inc.

Name: Brian Denega
Title: Senior Vice-President