CHAPTER 1

The Loewen Group Inc.

Whatever you do, always save six for pallbearers.
—Max Shulman

On January 22, 1999, John Lacey, a renowned turnaround specialist, was appointed chairman of the Loewen Group Inc., the second largest death care company in North America. Headquartered in Burnaby, British Columbia, Loewen owned over 1,100 funeral homes and more than 400 cemeteries in the United States and Canada; it also owned 32 funeral homes in the United Kingdom. The company had come a long way since its modest beginnings in Canada, where Ray Loewen, the founder and, until recently, chairman and chief executive officer (CEO), started out helping his father run the family funeral business in the late 1950s. During the previous two decades Loewen Group had grown explosively, mainly by acquiring small independent funeral homes and cemeteries in densely populated urban markets; in recent years the company had also acquired several large established funeral chains. Over the prior five years alone, consolidated revenues had grown by nearly 30 percent a year on average, from $303 million to over $1.1 billion.

Despite its impressive growth, however, the company now faced a major financial crisis. For 1998 it would report a loss of $599 million, compared to earnings of $42 million the previous year. Loewen's ongoing acquisitions program had been aggressively financed with debt. At year-end 1998, total interest-bearing debt stood at more than $2.3 billion—more than *seven times* the amount outstanding five years earlier. Loewen's common stock, which was simultaneously traded on the New York, Toronto,

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and Montreal stock exchanges, had ended the year at around $8 in New York, down from roughly $40 at the end of 1996.

Confronted with the company's mounting difficulties, the board of directors decided in October 1998 to replace Ray Loewen as CEO; soon thereafter, with the appointment of John Lacey, he was also replaced as chairman. The company also took some steps to raise profitability and cash flows. It consolidated various administrative functions at corporate headquarters and cut management overhead; it reviewed its pricing policies; and it hired investment bankers to explore various financing options, including asset sales, strategic partnerships, and outside capital investments in the company. However, the company's situation continued to worsen, and in mid-February Standard & Poor's downgraded Loewen's public bonds to B–, causing the stock price to drop by 38 percent in a day. In addition, certain covenants in Loewen's bank debt would be violated as a result of the company's 1998 financial performance, making it necessary to restructure the debt.

Loewen had not yet missed any payments on its debt, and had approximately $30 million of cash on hand. However, this would not be sufficient to meet several large interest and principal payments that were due over the coming months. A payment default would only make negotiations with creditors more difficult and increase the likelihood of bankruptcy. This possibility would no doubt weigh heavily on the managers' minds as they turned to the important task of restructuring the company's debts.

THE DEATH CARE BUSINESS

The primary activities of death care firms include the provision of funeral, burial, and cremation services, and related products like cemetery plots, caskets, urns, and grave site markers. Funeral services and cemetery plots can be sold either on an at-need basis (i.e., at the time of death) or on a prearranged or "pre-need" basis. In the latter case, payment for a funeral service or cemetery plot is made in advance, and the proceeds are either held in trust or invested in an insurance policy (that names the death care firm as beneficiary).

While traditional burials account for the majority of funeral services performed in the United States, cremations have been increasing in popularity in recent years. In 1998, almost 24 percent of all dispositions took place through cremation, compared to only 6 percent in 1975; analysts ex-

[1]Industry statistics in this section are derived from firms' annual reports and the Merrill Lynch industry report, "Post Life Services," by Fran Blechman Bernstein and Yasmine C. Nainzadeh, April 26, 1999.

pect this figure to reach 33 percent by 2010.[1] In 1998, approximately 26 percent of Loewen's funeral services were cremations. Although cremations generate relatively higher profit margins (35–40%) than traditional burials (30–35%), they contribute less to gross revenue. Cremations are much more common outside the United States, representing, for example, roughly 60 percent of dispositions in the United Kingdom.[2]

In 1999 the death care industry was highly fragmented, with approximately 22,000 funeral homes and 9,600 commercial cemeteries in the United States. Most of these were small family-owned concerns that served their local communities, where reputation and personal relationships were critically important in generating future business. (In a given geographic market, families generally used the same funeral home to care for their entire funeral needs over time.)

The largest firms in the industry were, like Loewen, publicly traded, and had achieved this scale by acquiring hundreds of independent funeral homes and cemeteries. Exhibit 1.1 lists the twelve largest North American death care companies. The largest firm, Service Corporation International (SCI), owned 3,442 funeral homes, 433 cemeteries, and 191 crematoria, spread across 20 countries. Loewen's other major competitors were Stewart Enterprises and Carriage Services Inc. At the end of 1998, the four largest firms collectively owned 2,986 funeral homes and 1,083 cemetery properties in the United States, but this represented only 13.5 percent and 11.3 percent, respectively, of each market.

Exhibit 1.2 presents Loewen's financial statements. Exhibits 1.3 and 1.4 present comparative financial, operating, and stock market data for Loewen and its three main competitors. Exhibit 1.5 reports acquisition premiums paid by Loewen and its competitors.

Aggregate revenues in the death care industry were relatively predictable. One reason was that death rates were largely driven by demographic factors that did not vary significantly from year to year. Since 1960, the number of deaths in the United States had increased at an annually compounded rate of 0.8 percent a year. Occasional large deviations from this rate were possible, however.[3] Another stabilizing influence on revenues was the historical lack of price competition in the industry. New entry into the funeral home business was extremely difficult, given how

[2]See Craig F. Schreiber and Benjamin C. Esty, "Service Corporation International," HBS Case No. 296–080 (July 24, 1996).

[3]For example, the number of deaths in the United States actually declined in 1981 and 1982—by 0.6 percent and 0.2 percent, respectively—but then increased by 2.3 percent in 1983 due to the sudden onset of HIV-related illnesses.

much weight most people placed on tradition and reputation when selecting a funeral home. (Most family-owned funeral homes in the United States had been passed down through several generations.) New entry into the cemetery business was often limited by regulation or by scarcity of land. Further, in the case of at-need sales, bereaved family members were rarely in a frame of mind to haggle over price.

Such industry stability was manifested in an exceedingly low business failure rate among funeral homes. According to Dun & Bradstreet, the average annual failure rate for funeral homes and crematoria—8 out of every 10,000—was less than one-tenth the rate for all U.S. businesses.

Pre-Need Business

During the 1990s, pre-need sales of funeral services and cemetery plots had come to represent an increasing share of the death care business. The segment of the population that was most likely to buy on a pre-need basis—people who were now in their 50s and 60s—was rapidly expanding. From the companies' perspective, pre-need sales provided a way to lock in sales growth and market share. Companies also could earn an investment return on monies that were paid to them in advance, and held in an insurance policy or trust. As shown in Table 1.1, a large and increasing fraction of Loewen's revenues was derived from pre-need sales, particularly of cemetery plots.

Service Corporation International was especially aggressive in marketing its pre-need business. At the end of 1998, SCI had a pre-need funeral backlog of $3.7 billion, compared to $410 million for Loewen, $819 million for Stewart Enterprises, and $225 million for Carriage Services.[4] (The backlogs represented the total value of insurance policies outstanding that had been taken out to cover the costs of providing future services and products under pre-need sales contracts.) It was estimated that the total pre-need market in the United States was between $20 billion to $50 billion in size, measured by current backlogs.[5]

Accounting for Pre-Need Sales Accounting for pre-need sales was complicated.[6] For funerals, the company received cash when the pre-need con-

[4]See Bernstein and Nainzadeh, "Post Life Services."

[5]Data from the National Funeral Directors Association.

[6]A detailed discussion of corporate accounting for death care companies appears in David Gallo, Ian Reynolds, and Collin Roche, 2000, "The Loewen Group: An Autopsy of a Chapter 11 Death Care Company," Harvard Business School, and Bernstein and Nainzadeh, "Post Life Services."

TABLE 1.1 Loewen Group's Pre-Need Sales

	Funeral Services		Cemeteries	
	Pre-Need Sales ($millions)	Pre-Need as Percent of Total	Pre-Need Sales ($millions)	Pre-Need as Percent of Total
1995	$ 97	22%	$ 88	61%
1996	$190	35%	$189	66%
1997	$267	44%	$325	77%
1998	$258	41%	$306	75%

Source: Company annual reports.

tract was purchased, but the costs of providing the funeral were mostly incurred when the customer died. On average, it took about twelve years for the contract to convert to at-need. The standard industry practice was to defer the recognition of revenue from the contract to when the funeral was performed (and the associated costs were incurred).

In the interim period, the company had two options for dealing with the initial cash payment from the customer. One option was to invest the cash in an income-earning trust and report the amount held in the trust, including any accrued investment income, as deferred revenue (i.e., a liability). When the customer eventually died the revenue was fully recognized, and the cash was withdrawn from the trust to pay for the costs of providing the funeral.[7]

A second option was to use the cash to purchase a life insurance policy in the customer's name, with the company as beneficiary. When the customer died, proceeds from the policy would pay for the funeral. Prior to this event, the insurance policy was treated as an off–balance sheet asset.[8] Loewen funded 57 percent of its pre-need funeral sales with insurance poli-

[7]Some state laws allowed companies to keep a specified fraction of the initial cash payment outside of the trust to pay for administrative costs. Such "retainage" was typically 10 to 15 percent of the contract sales price. Loewen accounted for retainage as current revenue at the time the pre-need contract was signed. It was the policy of all other companies to defer recognizing retainage as revenue until the funeral services were actually delivered.

[8]Upon purchasing the insurance policy, the death care company would receive a cash sales commission back from the insurance company, which would be immediately recognized as income.

cies (as opposed to trusts). The company currently operated three insurance subsidiaries that specialized in selling these policies.

A different approach was used to account for pre-need sales of cemetery plots. Customers were generally expected to make a down payment (of up to 20 percent of the total price) and pay the balance in four or five annual installments. The practice followed by Loewen and the other death care companies was to book the entire purchase price as current period revenue, showing future installment payments as long-term receivables.[9] To ensure matching of revenues and expenses, all current and future costs that would be incurred as a result of the sale were immediately expensed.[10]

Sales commissions paid to Loewen staff at the time of pre-need sales—whether sales of funerals or cemetery plots—were capitalized, and written off over time. Most companies, including SCI, used a twenty-year amortization period; Loewen used ten years.

GROWTH THROUGH CONSOLIDATION

Loewen Group and the other large public death care companies employed a dramatically different business model than traditional family-owned funeral homes. Traditional businesses historically had to contend with high fixed operating costs, which limited profit margins. Fixed costs were high because a funeral home might typically perform only one or two services a week, yet have to employ an office receptionist and various back-office staff full time. Similarly, essential assets like hearses and embalming equipment would sit around most of the time unused, tying up capital.

In the 1960s, Robert Waltrip, founder of Service Corporation International, recognized the potential to realize enormous cost savings in the industry by buying up funeral properties in concentrated geographic areas and eliminating redundant assets and overhead expenses. A cluster of funeral homes formed this way would only have to employ a single receptionist, for example, and could share hearses and other fixed assets. A typical cluster might include ten to twenty properties, located within a thirty- to sixty-mile radius. It was estimated that in an SCI-owned funeral home, fixed costs represented 54 percent of revenues on average, compared

[9]A reserve was established for uncollectible accounts and cancellations.

[10]Typically some of the cash down payment was placed in a trust, to cover future expenditures on cemetery-related merchandise. Another small portion of the down payment would be placed in a separate "perpetual care" trust to fund future maintenance of the property.

to 65 percent for the rest of the industry (although SCI homes were typically somewhat larger than average).[11] Clearly the cluster strategy was more appropriate for concentrated urban markets, where the properties were closer to one another; the strategy worked less well in rural areas. To avoid alienating local communities, SCI tried as much as possible to avoid altering the appearance of the acquired businesses. Most of these businesses continued to operate under the same name; no "SCI" sign or logo was displayed.

SCI's consolidation strategy had two other potential benefits. First, through increased buying power, the company might be able to obtain price concessions from suppliers (e.g., for caskets and embalming chemicals). In addition, managers of the acquired businesses would gain access to SCI's considerable financial resources and professional management practices. Thus SCI-owned funeral homes were also able to lower their variable costs, which were estimated to be 15 percent of revenues, versus 23 percent for the average U.S. funeral home.[12]

The consolidation strategy had its critics, however. Over the years there had been recurring accusations in the news media that SCI and other funeral home consolidators eliminated competition and charged excessive prices.[13]

RAY LOEWEN'S WAY

In the late 1960s, SCI, which was based in Texas, began to acquire properties in Canada. Ray Loewen's entry into the funeral home consolidation business effectively began in 1969, when he purchased a funeral home in British Columbia after learning that the home's owner was thinking of selling out to SCI. At the time, Loewen owned a single funeral home in Ontario, having sold the family business to his brother several years before.

Loewen foresaw that increasing numbers of funeral home directors, many of them in their 20s or 30s who had inherited the business from their parents, would be receptive to selling out to pursue alternative careers for financial or lifestyle reasons. Others might decide to sell because a dispro-

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[11]See Schreiber and Esty (based on data reported by SCI).

[12]Ibid.

[13]For example, see Bruce Mohl, "Growth of Chains Has Led to Rise in Funeral Prices," *Boston Globe*, August 28, 1995, p. 1. In 1998, the CBS investigative news program *60 Minutes* ran a report investigating allegations of overcharging by SCI.

portionate fraction of their wealth was tied up in the business, even though they were satisfied in their current jobs.

As he expanded his holdings within Canada, Loewen approached the consolidation process differently from SCI. The few Canadian funeral directors who had sold their businesses to SCI thus far appeared to be unhappy with SCI's approach of managing "from afar."[14] Loewen's approach, in contrast, was to take a majority ownership stake in each acquired business, but to retain the same managers if possible and to give them relative autonomy. He would say:

> *You can't have a group of MBAs in a head office telling funeral directors how to work. They feel they know their craft and their community. So let's stress local management. If a man wants to retire—or do some estate planning—and he has a good operation, number one in his community, let's give him a good deal, allowing him to live well, ease up a bit, but remain with the firm that carries the family name.*[15]

The seller would often retain a small minority stake in the business. SCI, in contrast, had a policy of acquiring full ownership of acquired properties, although the previous owners might be kept on in management roles.

After acquiring a business, Loewen Group would often inject much needed new financing for capital improvements and increased merchandising. However, the company eschewed aggressive sales tactics, the use of telemarketing, and negative advertising that was critical of competitors. Loewen believed such tactics undermined the industry's credibility. About his main competitors at the time—SCI and Arbor Capital, a Canadian firm—he said: "Their aggressive approach hurts us all, because it reflects badly upon funeral service."[16] Loewen also was highly critical of Arbor Capital's practice of building funeral homes directly on cemetery properties; he believed each business required a distinct type of management.

As Loewen Group continued to grow through acquisitions during the 1970s and 1980s, its demand for capital increased, and in mid-1987 it listed its shares on the Toronto Stock Exchange. (Three years later it also acquired a U.S. listing on Nasdaq.) In August 1987, Loewen made its first acquisition in the United States, the Chapel of the Valley funeral home in

[14]Kenneth Bagnell, "A Profitable Undertaking," *Globe and Mail*, October 21, 1988, p. 128.
[15]Ibid.
[16]Ibid.

Sacramento, California. The owner was paid $1.8 million, and required to stay on as manager for three years. "It was made clear," the owner said, "that if I did not wish to work, they did not wish to buy."[17] At the time, SCI faced no meaningful competition in the United States. Shortly thereafter, Loewen acquired a small local chain of funeral homes in Fresno, California. The seller later commented: "In less than a year our calls are well up, so are our revenues. All because of Loewen. We thought we knew this business. But this Canadian makes us look like schoolboys. He's a genius in marketing."[18]

Having achieved a foothold in the giant U.S. market, Loewen Group's growth escalated. Dozens, later hundreds, of new properties were added every year. By 1998, the company had properties in forty eight U.S. states and eight Canadian provinces. (See Exhibit 1.6 for a ten-year summary of Loewen's financial position.) Ray Loewen apparently spared no expense in courting independent funeral home and cemetery owners. One cemetery owner from Indiana described his experience:

> *Mr. Esterline . . . says he and his wife were flown first-class to Vancouver, where they joined about 50 other owners of private cemeteries at the elegant Pan Pacific Hotel. The next day, they were all shuttled by seaplane to the Queen Charlotte Islands off the western coast of Canada. "Ray Loewen and his wife were greeting each of us as we got off," Mr. Esterline recalls. Nearby was Mr. Loewen's 110-foot yacht, the Alula Spirit, with a helicopter on deck.*
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> *The fishing was first-rate. Guides led them aboard smaller boats, and everyone got a wet suit. Another boat cruised nearby, serving hot coffee. Others took helicopter rides, hopping to different islands for eagle watching. At night, the prospects stepped aboard the Alula Spirit for cocktails with company officials, who laid out bold expansion plans.*
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> *The hospitality was soothing. "It made us feel good about" a sale to Loewen, remembers Ann Taylor, Mr. Esterline's sister and a co-owner of the cemetery.*[19]

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[17]Ibid.

[18]Ibid.

[19]Dan Morse and Mark Heinzl, "Laid Low: Funeral Home Operators Discover the Downside of Sale to Consolidator," *Wall Street Journal*, September 17, 1999, p. A1.

SCI'S HOSTILE TAKEOVER OFFER

Described in the news media as "fierce competitors" and "arch rivals," Loewen Group and SCI increasingly found themselves competing for properties in the same markets. In 1994, the two companies collided in the United Kingdom, where both sought to acquire the large British funeral company, Great Southern Group. SCI ultimately prevailed, paying almost $200 million.[20]

During 1996 SCI had made several informal acquisition proposals to Loewen, but all were declined. On September 17, 1996—the very day that Loewen's stock began trading on the New York Stock Exchange—SCI announced a formal offer to acquire all Loewen common stock for $43 a share. The offer was addressed to Ray Loewen personally, in a letter from SCI's president (Exhibit 1.7).[21]

Loewen's board of directors promptly rejected the offer. Ray Loewen believed the company's stock, which only two weeks earlier had traded around $30 a share, was significantly undervalued. He portrayed SCI's action as an attempt to eliminate an important, and more successful, competitor. In a letter to shareholders, he expressed his confidence in the company's long-run business plan, noting that "during the past five years, Loewen's revenue and earnings have experienced the highest growth rates of public companies in our industry, 41.5% and 36.8%, respectively."[22] Although within two weeks of its initial offer SCI increased its bid to $45 a share—and redirected its offer to Loewen's shareholders directly—Ray Loewen said the company's stock was worth at least $52 a share.

The stock price was depressed, he argued, because of a recent unfavorable jury verdict against the company in Mississippi. A funeral home operator had accused Loewen Group of reneging on an agreement to purchase two of his homes, plus certain insurance services. Although the properties were worth only a few million dollars, in November 1995 the jury found the company liable for damages of $500 million, including $400 million in punitive damages. Loewen's stock price fell by 15 percent on the day the verdict was announced, and its bonds were soon downgraded to specula-

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[20]Rachel Bridge, "SCI Set to Tie Up Southern Deal," *Evening Standard*, August 8, 1994, p. 1.
[21]SCI also jointly offered to acquire all of Loewen's Series C preferred stock outstanding for $29.51 per share, to be paid in SCI common stock.
[22]The Loewen Group Inc., Form 8-K, September 26, 1996.

tive, or "junk," status.[23] An expert witness for the company would later argue that the verdict resulted from the "ruthless and blatant working up of both racial and nationalistic prejudice, particularly against Canadians."[24] To appeal the verdict, under Mississippi law the company would have had to post a bond equal to 125 percent of the award, or $625 million. In early 1996, it settled the suit for $85 million.[25]

The company responded to SCI's offer in several ways. It filed an antitrust lawsuit in U.S. federal court against SCI; soon thereafter a number of states, as well as the Canadian government, started their own antitrust investigations of the proposed acquisition. It also adopted lucrative severance packages, or "golden parachutes," for more than seventy of its senior executives.[26] And, perhaps most significantly, it accelerated its acquisition program.

In late August, Loewen, in partnership with The Blackstone Group, had acquired the fourth-largest funeral service provider in the United States, Prime Succession Inc. (Blackstone was an investment bank in New York that specialized in advisory work, and also made proprietary private equity investments.) The total purchase price was $320 million, financed with $190 million of bank and public high-yield debt. A few months later, in a similar transaction, Loewen and Blackstone acquired Rose Hills cemetery, the largest cemetery in North America, for $285 million ($155 million of this deal was financed with debt as well). In each transaction, after four years Loewen would have the option to buy Blackstone's equity stake at a specified price; after six years, Blackstone would have the option to sell its stake to Loewen, also at a specified price. (Exhibit 1.8 summarizes the terms of the two acquisitions.)

During all of 1996, Loewen acquired 159 funeral homes, 136 cemeteries, and 2 insurance companies, for total consideration of $620 million. By the beginning of 1997, it had entered into agreements to purchase $222 million of additional properties.

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[23]Junk bonds, also known as *high-yield* or *below investment grade* bonds, are bonds that receive less than a BBB– credit rating by Standard & Poor's, or less than a Baa3 rating by Moody's Investors Service.

[24]Tamsin Carlisle, "Canada's Loewen Group, Founder Seek $725 Million from the U.S.," *Wall Street Journal*, January 13, 1999, p. B8.

[25]Loewen Group later hired the attorney who had represented the plaintiff in the case, to make sure he would not be retained in future lawsuits against the company. See John Schreiner, "Ray Loewen Looks Back from the Brink," *Financial Post*, February 17, 1993, p. 3.

[26]Loewen already had a "poison pill" shareholder rights plan in place before SCI made its offer.

A relatively high percentage of the financing for these acquisitions came from issuing debt. The company's stated policy on debt financing was to try to maintain its long-term debt/equity ratio in the range of 1.0:1 to 1.5:1.[27] It expected that this ratio would move towards the top of the target range when it made more acquisitions, but it would endeavor to bring the ratio back down eventually through equity issues. At the end of 1996 Loewen's debt/equity ratio was 1.4:1.

In the first week of 1997, SCI suddenly announced that it was dropping its bid for Loewen. In addition to concerns over the antitrust suit and Loewen's various takeover defenses, SCI cited Loewen's high debt financing costs as a major deterrent to proceeding with the offer. Special mention was made of the Prime Succession and Rose Hills transactions. Later, a Loewen spokesman would say that the company had taken on enough debt "to make it impossible for a sensible company to take it over."[28]

FINANCIAL DISTRESS

Loewen continued its aggressive growth strategy in 1997, acquiring 138 funeral homes, 171 cemeteries, and an insurance company, paying a total of $546 million. The year also marked the company's entry into the United Kingdom, where it acquired thirty two funeral homes. Debt again played an important role in financing this growth, and for the full year, interest expense on long-term debt was $132 million, up from $93 million in 1996.

Loewen's businesses, however, performed less well than expected. The company attributed this in part to a decline in death rates, which negatively impacted all death care companies. Although Loewen's total funeral revenues increased by 9.5 percent during the year, its established funeral homes (i.e., those not acquired during the year) performed 3.2 percent fewer services than in 1996, and the gross margin earned by these properties declined from 40.8 percent to 38.7 percent. The company attributed most of the margin decline to an increase in reserves for doubtful accounts. The gross margin earned by Loewen's cemetery business also declined in 1997, from 31 percent to 28.2 percent. The company said this decline occurred in part because it reversed $3.7 million of sales (and $1.2 million of related costs) that it had reported in 1996 for transactions that were supposed to take place in 1997, but were never consummated. In addition, it took a $2.1 million write-down for cemetery accounts receivable.

[27]The Loewen Group Inc., Form 10-K, December 31, 1996.
[28]Morse and Heinzl, "Laid Low."

These trends worsened in 1998. Revenues and profits for the company's established funeral services and cemetery businesses continued to fall. In August the company announced that second-quarter earnings were 56 percent lower than the previous year. And in early October, it announced that earnings for the third quarter would likely be more than 30 percent below what analysts had forecasted—causing Loewen's stock price to fall 15 percent in a single day. Management blamed the shortfall on declining death rates, difficulties in integrating newly acquired assets, and problems in the cemetery business. (In 1998 Loewen's cemetery business had a gross margin of 12.6 percent, compared to 28.2 percent the previous year.) By the end of 1998 Loewen's stock price had fallen to $8, from $26 at the start of the year.

New Management

In the second half of 1998, Loewen took a number of steps to address its problems. It severely cut back the pace of acquisitions. (During all of 1998 it acquired only 89 funeral homes and 65 cemeteries, paying $278 million.) It hired investment bankers to explore different options for raising cash and improving profitability. It sold one of its insurance subsidiaries for $24 million.

In October, following the company's third-quarter profit warning, Ray Loewen resigned as chief executive officer, and three months later he was also replaced as chairman. Loewen had recently owned more than 18 percent of the company's common stock, but he had been forced to surrender almost his entire stake to the Canadian Imperial Bank of Commerce to settle a personal loan. Now the company's largest shareholder, the bank nominated John Lacey as Loewen Group's new chairman.

A graduate of Harvard Business School, John Lacey had built a reputation as a successful turnaround specialist. On the day that his appointment was announced, Loewen's stock price increased by 20 percent on the Toronto Stock Exchange. In previous assignments, Lacey had shown an ability to raise large amounts of cash through asset sales. For example, while at Oshawa Group, a Canadian grocery store chain, he negotiated the sale of the entire company for $1.5 billion. Following his appointment to Loewen, however, Lacey said: "My role over the last five or six years has been one of maximizing shareholder value. . . . I think what I do is look for opportunities to deliver value to the shareholders."[29]

[29]Drew Hasselback, "Lacey Joins Loewen for Another Selloff," *Financial Post*, January 25, 1999, p. C2.

Company Debt

By the end of the year, Loewen Group's long-term debt was the highest it had ever been, at $2.3 billion (including debt due within a year). The debt structure was complicated (see Exhibit 1.9). It owed approximately $540 million to a consortium of 25 Canadian and U.S. banks, led by the Bank or Montreal. It also had over $1.5 billion of senior guaranteed notes outstanding, most of which were publicly traded ($300 million of this debt came due on October 1).

Almost all of the debt was secured, or collateralized, by various assets of the company. If Loewen were ever liquidated, secured creditors would be legally entitled to receive the cash generated from the sale of the assets that secured their debt. In 1996, the banks and the note holders had agreed to share most of their security on a pari passu basis (i.e., in the event of liquidation, the two groups of creditors would have equal claim to the resulting cash proceeds).[30]

Loewen also had large contingent and other liabilities outstanding. This amount included $87.8 million owed to former owners of certain funeral and cemetery properties that Loewen had acquired. For tax reasons, the sellers had chosen to be paid in installments over several years.[31] In return, they had signed contracts promising not to compete against Loewen during the life of the payments ("noncompetition agreements").

The company's bank and public debt contained numerous restrictive covenants. Among other things, the covenants specified precise limitations on the amount of debt that the company could have, the amount of dividends that it could pay, and the amount of new preferred stock that it could issue. Other covenants restricted the company's ability to sell assets, or required that when assets were sold the proceeds be used to retire debt. A covenant in Loewen's bonds stated that if ownership of the company's

[30]The security consisted of accounts receivable and any related rights to receive payment, the capital stock of substantially all of Loewen's majority-owned subsidiaries, and a guarantee by each subsidiary that had pledged its stock.

[31]As of December 31, 1998, the amounts owed over time were as follows (in $millions):

1999:	$13.8
2000:	$14.5
2001:	$11.6
2002:	$10.6
2003:	$8.9
Thereafter:	$28.4

stock changed significantly, it would have to offer to repurchase the bonds for 101 percent of their face value.

If Loewen was ever found to be not in compliance with a covenant, or it missed a scheduled interest or principal payment, an event of default would be declared. Creditors would then, after 30 days, have the right to accelerate their claims (i.e., all principal and accrued interest would become immediately due and payable). "Cross default" covenants in the debt ensured that if any one debt contract went into default, all other contracts would be considered in default as well.

In early 1999 Loewen was not in compliance with certain covenants in its bank debt. If it could not persuade its banks to waive the defaults or renegotiate the covenants, the company might have no choice but to file for bankruptcy.

Bankruptcy

Corporate bankruptcy in the United States is governed by the U.S. Bankruptcy Code. Chapter 11 of the Code deals with reorganizations. If a company files for Chapter 11, it is allowed to conduct its regular business and propose a financial restructuring plan without interference from creditors (e.g., secured creditors cannot seize its collateral). A central presumption of the Code is that the firm would be worth more as a going concern than if shut down.[32] The bankruptcy case is overseen by a judge, who can hear appeals from creditors if they believe they are being unfairly treated. Creditors are also allowed to form committees to represent their interests in the case. Such committees can hire their own legal and financial advisors and charge all professional fees to the company. The company also hires its own advisors.

To emerge from bankruptcy, management of the firm (the "debtor") proposes a plan of reorganization to the creditors. The plan divides the firm's creditors and other financial claimholders into classes, and each class is asked to exchange its claims for new claims. Each class votes separately on the proposed plan. If each class approves the plan by at least one-half in number and two-thirds in value, the judge would approve, or "confirm," the plan and the firm would exit from Chapter 11. Minority

[32]In some countries, such as the United Kingdom, bankruptcy generally means that the firm is liquidated or sold, and the proceeds are paid to creditors from most senior to most junior. In these countries, shareholders would receive anything only if there is enough value to make all creditors whole—which rarely happens.

creditors who voted against the plan would have to accept the will of the majority. The judge would in addition have to determine that the reorganization plan would leave the firm with a sensible new capital structure that is not overleveraged.

Management has the exclusive right to propose the first plan. The law states that a plan has to be proposed within 120 days of the bankruptcy filing and confirmed within an additional 60 days. After this date the judge can allow other interested persons to file alternative plans. Most judges are willing to grant management extensions to the deadline, however. In practice, multiple extensions are often granted, and large, complex cases might run for two or three years before an initial vote is taken.

In addition to being protected from creditors, firms benefit in other ways while they are in Chapter 11. They do not have to pay interest on their debt.[33] They can cancel leases and other so-called "executory contracts." (An executory contract is a contract where both parties to the contract are still obligated to perform future services.) And they can borrow on favorable terms from new lenders through "debtor-in-possession financing," based on a provision of Chapter 11 that gives any new lenders to a bankrupt firm higher priority than the firm's prebankruptcy lenders.

If Loewen were to file for Chapter 11, its situation could be complicated by the fact that roughly 10 percent of its business was conducted in Canada.[34] A U.S. bankruptcy filing would almost certainly trigger a simultaneous bankruptcy filing in Canada. Canadian bankruptcy law is governed by the Companies' Creditors Arrangement Act (CCAA), which differs in some important ways from Chapter 11. Like Chapter 11, CCAA initially gives operating control of the company to management; however, it is generally easier for creditors to remove management than in the United States. In addition, management has only one chance to present a reorganization plan. If the plan fails to pass, or was not submitted within the allotted time, under the "guillotine rule" the firm would be liquidated. There is no provision for debtor-in-possession financing as in the United

[33]A Chapter 11 debtor does not even have to *accrue* interest on its unsecured debt. At the end of a case the firm would owe unsecured creditors the same face value of debt that it had owed at the beginning of the case. Interest can continue to accrue on the firm's secured debt, but the amount is limited by the value of the underlying security.

[34]Loewen's U.S. assets were owned and operated by Loewen Group International Inc., which was a wholly owned subsidiary of the Canadian parent company.

States.[35] If Loewen filed for bankruptcy in both countries, some kind of administrative protocol would have to be established for resolving potential conflicts between the two courts.

THE COMPANY'S OPTIONS

John Lacey had relatively little time to develop a plan for dealing with the growing crisis. The company had $42 million of debt payments coming due in the first two weeks of April, and in early March it still had not reached an agreement with its banks on how to restructure their loans. Although a few months earlier the company had found a buyer for its insurance subsidiary, raising large amounts of cash through asset sales could be difficult. The death care industry in general was feeling the effects of lower death rates, so there might be limited demand for Loewen's properties. Further, piecemeal sales of assets could take a long time, given the company's organizational complexity (it had over 850 U.S. and 100 Canadian subsidiaries).

On a different front, the company had recently filed a lawsuit against the U.S. government seeking $725 million in damages related to the 1995 settlement in Mississippi. Alleging significant "anti-Canadian" bias by the Mississippi court, the company was arguing that the court's behavior violated a provision of the North American Free Trade Agreement (NAFTA), which bars discrimination against foreign investors. It was unclear whether Loewen would win the suit, however, and even if it did, years could pass before it received any payment.

Making a difficult situation even worse, regulators had recently suspended the licenses of sixteen of Loewen's funeral homes in Florida after discovering certain accounting violations. Whether the full extent of the problem had been discovered remained to be determined.

[35]Voting takes place similarly under CCAA as under Chapter 11. Under CCAA, three-quarters in value and one-half in number of the holders in each class of claims are required to approve the plan. In the United States, if one or more classes do not approve a plan, the judge can either order the parties to modify the plan and vote again, or "cram down" the plan over the objections of the dissenting classes. In Canada there is no equivalent of the cram-down.

EXHIBIT 1.1 Twelve Largest North American Death Care Companies by Revenues, 1998

Company	Country	Revenues (US$millions)	Number of Employees
Service Corporation International	U.S.	$2,875	27,266
Loewen Group Inc.	Canada	1,136	16,700
Stewart Enterprises	U.S.	756	11,200
Carriage Services Inc.	U.S.	117	940
Arbor Memorial Services	Canada	97	1,620
Federated Funeral Directors	U.S.	34	200
Gatlings Chapel	U.S.	21	125
Trillium Funeral Service Corp.	Canada	15	100
Forest Lawn–Ocean View	Canada	15	100
Woodlawn Memorial Funeral Home	U.S.	15	90
Doane Beal & Ames Inc.	U.S.	10	90
Fairlawn Mortuary	U.S.	9	50

Source: One Source Global Business Report.

EXHIBIT 1.2 Loewen Group's Financial Statements (Dollars in US$millions)

Loewen Group, Consolidated Income Statement

	1996	1997	1998
Revenue			
Funeral	$549.8	$ 602.1	$ 631.2
Cemetery	286.7	422.0	408.5
Insurance	71.9	90.0	96.5
	$908.4	$1,114.1	$1,136.2
Cost and expenses			
Funeral	326.9	374.2	407.3
Cemetery	197.8	303.0	357.2
Insurance	54.7	73.3	80.0
	$579.4	$ 750.5	$ 844.5
	$329.0	$ 363.6	$ 291.7
Expenses			
General and administrative	71.2	112.8	133.3
Depreciation and amortization	53.1	65.4	88.5
Asset impairment[a]	—	—	333.9
Restructuring costs	—	33.4	—
	$124.3	$ 211.5	$ 555.7
Earnings (loss) from operations	204.7	152.1	(264.0)
Interest on long-term debt	93.0	132.3	182.3
Investment impairment and contingent loss[b]	—	—	315.2
Loss on early extinguishment of debt	—	7.7	—
Gain on sale of investment	—	(24.1)	—
Finance and other costs related to hostile takeover proposal	18.7	—	—
Earnings (loss) before undernoted items	93.0	36.3	(761.5)
Dividends on preferred securities of subsidiary	7.1	7.1	7.1
Earnings (loss before income taxes and undernoted items	85.9	29.2	(768.6)
Income taxes			
Current	22.5	34.2	23.1
Future	0.9	(33.4)	(187.6)
	23.5	0.8	(164.5)
	62.4	28.4	(604.1)
Equity and other earnings of associated companies	3.6	13.4	5.1
Net earnings (loss) for the year	$ 66.0	$ 41.8	$(599.0)
Basic earnings (loss) per common share	$ 1.01	$ 0.48	($ 8.22)
Fully diluted earnings (loss) per common share	$ 1.00	$ 0.48	($ 8.22)

[a]Amount for 1998 represents a write-down of the book values of certain properties that the company is considering for possible sale, to reflect the properties' estimated current "fair value." The properties consist of 124 cemeteries, 3 funeral homes, and some other assets. Fair value is based upon the properties' estimated future operating cash flows, as well as anticipated proceeds from selling the properties.
[b]Amount for 1998 represents a write-down of the company's investment in Prime Succession and Rose Hills, reflecting the company's behalf that its option to purchase Blackstone's majority equity stake in each entity is significantly less likely to be exercised, while Blackstone's option to sell its stake to Loewen is significantly more likely to be exercised.

EXHIBIT 1.2 *(Continued)*

Loewen Group, Consolidated Balance Sheet

	December 31,	
	1997	**1998**
Assets		
Current assets		
Cash and term deposits	$ 36.8	$ 94.1
Receivables, net of allowances	251.0	221.7
Inventories	34.9	34.5
Prepaid expenses	11.1	8.9
	$ 333.8	$ 359.2
Long-term receivables, net of allowances	410.4	647.1
Cemetery property	553.7	1,235.8
Property and equipment	224.0	826.0
Names and reputations	305.6	748.7
Investments	957.8	3.4
Insurance invested assets	797.2	266.7
Future income tax assets	633.1	12.0
Prearranged funeral services	130.9	413.9
Other assets	156.6	161.1
	$4,503.2	$4,673.9
Liabilities and shareholders' equity		
Current liabilities		
Current indebtness	—	66.2
Accounts payable and accrued liabilities	160.2	170.1
Long-term debt, current portion	43.3	874.1
	$ 203.7	$1,110.5
Long-term debt, net of current portion	1,750.4	1,393.9
Other liabilities	308.9	399.3
Insurance policy liabilities	214.5	166.9
Future income tax liabilities	310.0	208.9
Deferred prearranged funeral services revenue	410.4	413.9
Preferred securities of subsidiary	75.0	75.0
Shareholders' equity		
Common shares	1,271.2	1,274.1
Preferred shares	157.1	157.1
Retained earnings (deficit)	98.4	(539.7)
Foreign exchange adjustment	13.6	13.9
	$1,540.2	$ 905.4
	$4,503.2	$4,673.9

EXHIBIT 1.2 *(Continued)*

Loewen Group, Consolidated Statement of Cash Flows

	1996	1997	1998
Cash flows from operating activities			
Net earnings (loss)	$ 66.0	$ 41.8	$(599.0)
Items not affecting cash			
Depreciation and amortization	53.2	65.4	88.5
Amortization of debt issue costs	4.1	6.8	26.6
Asset impairment	—	—	333.9
Investment impairment and contingent loss	—	—	315.2
Gain on sale of investments	—	(27.2)	(6.8)
Future income taxes	0.9	33.4	(187.6)
Equity and other earnings of associated companies	(3.6)	(13.4)	(5.1)
Restructuring costs	—	15.7	—
Other, including net changes in other noncash balances	(167.4)	(216.4)	(90.2)
	$ (46.9)	$(160.7)	$(124.5)
Cash flows from investing activities			
Business acquisitions	(556.9)	(481.6)	(252.6)
Construction of new facilities	(17.7)	(32.4)	(19.2)
Investments, net	(148.4)	14.5	(1.4)
Purchase of insurance invested assets	(85.2)	(262.0)	(224.1)
Proceeds on disposition and maturities of insurance invested assets	71.9	252.6	180.2
Purchase of property and equipment	(54.9)	(52.8)	(43.5)
Proceeds on disposition of investments and assets	3.7	70.1	56.3
	$(787.5)	$(491.6)	$(304.4)
Cash flows from financing activities			
Issue of common shares, before income tax recovery	216.9	439.4	1.8
Issue of preferred shares, before income tax recovery	154.1	—	—
Increase in long-term debt	1,037.4	1,343.6	1,105.4
Repayment of long-term debt	(514.5)	(1,083.0)	(645.7)
Common share dividends	(6.7)	(12.3)	(14.7)
Preferred share dividends	(6.5)	(9.5)	(8.9)
Current not payable	—	—	71.7
Repayment of current note payable	(38.6)	—	(5.4)
Debt issue costs	(29.2)	(7.1)	(17.9)
	$ 813.1	$ 671.0	$ 486.3
Increase (decrease) in cash and cash equivalents during year	(21.3)	18.7	57.4
Effect of foreign exchange adjustment	(0.1)	0.0	(0.0)
Cash and cash equivalents, beginning of year	39.5	18.1	36.8
Cash and cash equivalents, end of year	$ 18.1	$ 36.8	$ 94.1

Source: Loewen Group Inc., Form 10-K, December 31, 1998.

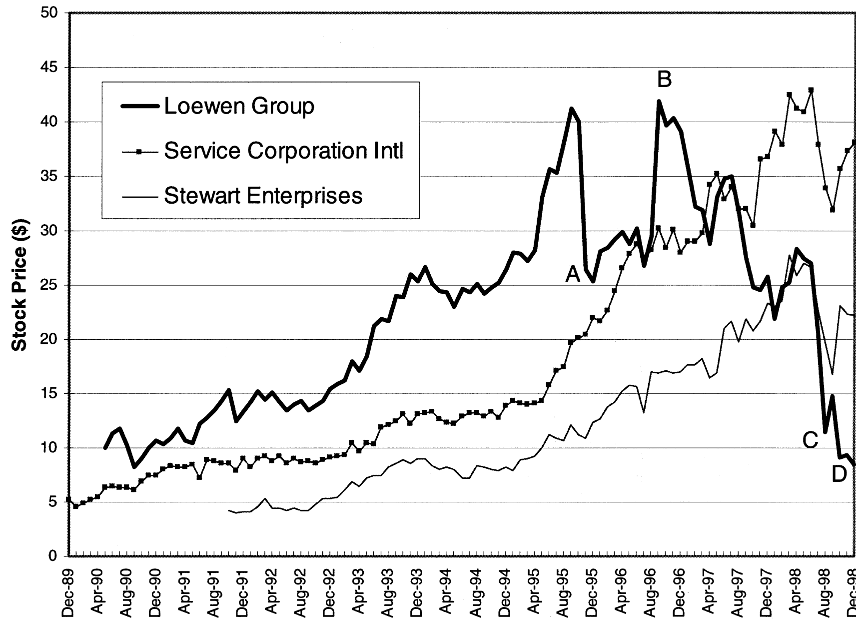
EXHIBIT 1.3 Selected Data on Loewen Group and Its Main Competitors (Dollars in US$millions, except Per Share Items)

	Loewen Group		Service Corp. International		Stewart Enterprises		Carriage Services	
	Dec 97	Dec 98	Apr 97	Apr 98	Dec 97	Dec 98	Mar 97	Mar 98
Sales	$1,114.1	$1,136.2	$ 2,468.4	$ 2,875.1	$ 532.6	$ 648.4	$ 77.4	$116.8
Gross profit	370.7	291.7	812.8	879.3	175.1	217.1	27.2	45.8
Selling, general, and administrative expense	99.5	125.2	66.8	66.8	15.4	16.6	5.3	7.6
Depreciation and amortization	71.4	88.5	125.2	160.5	18.0	21.1	7.8	11.4
Operating profit	199.8	78.0	620.8	651.9	141.8	179.4	14.1	26.7
Interest expense	127.5	182.3	141.1	177.1	38.0	43.8	6.2	10.2
Taxes	2.7	(164.5)	205.4	176.4	36.7	23.1	3.7	7.5
Net income	42.7	(599.0)	333.8	342.1	69.7	41.9	3.6	8.9
Earnings per share (reported)	$ 0.48	($ 8.22)	$ 1.36	$ 1.34	$ 0.76	$ 0.43	$ 0.33	$ 0.67
Assets	$4,503.2	$4,673.9	$10,514.9	$13,266.2	$1,637.2	$2,048.9	$277.9	$466.1
Short-term debt	43.5	940.3	64.6	96.1	34.0	11.2	2.3	6.4
Long-term debt	1,750.4	1,393.9	2,634.7	3,764.6	524.4	913.2	126.0	216.2
Preferred stockholders' equity	232.1	232.1	—	—	—	—	14.0	1.7
Common stockholders' equity	1,383.1	748.3	2,726.0	3,154.1	819.6	839.3	98.6	200.4
Number of funeral homes	1,070	1,151	3,127	3,442	419	575	120	166
Number of cemeteries	483	550	166	151	131	141	20	27
Common stock beta[a]		1.15		0.74		1.05		0.85

Source: Datastream and company annual reports.

[a]Beta is calculated using the most recent five years of monthly data, based on month-end closing prices (including dividends). The stock market index used is the Standard & Poor's 500.

EXHIBIT 1.4 Long-Run Stock Price History (stock prices in US$)



Selected key events:

A	Nov. 2, 1995	Loewen Group is hit with a $500 million civil damages award by a Mississippi jury in a breach of contract suit.
B	Sep. 17, 1996	Service Corporation International makes an unsolicited offer to acquire Loewen.
C	Aug. 6, 1998	Loewen discloses that second-quarter earnings were 56% lower than last year.
D	Oct. 8, 1998	Ray Loewen is removed as CEO of Loewen Group, following company's announcement on previous day that third-quarter earnings will be less than 13 cents a share, versus analysts' consensus estimate of 19 cents a share.

Casewriter note: Carriage Services first began trading publicly in August 1996, and is omitted from the figure for clarity.

Source: Datastream.

EXHIBIT 1.5 Acquisition Multiples

	(1) Revenues of Acquired Companies (US$millions)			(2) Amount Spent on Acquisitions (US$millions)			Acquisition Multiple: (2) ÷ (1)		
Acquirer	**1996**	**1997**	**1998**	**1996**	**1997**	**1998**	**1996**	**1997**	**1998**
Carriage Services	$ 28.6	$ 42.8	$ 51.9	$ 69.1	$ 118.3	$ 158.7	2.41x	2.77x	3.06x
Equity Corp.	30.9	49.0	56.8[a]	65.0	156.1	120.0[a]	2.11x	3.19x	2.12x
Loewen Group	251.5	187.6	29.1	620.0	546.0	278.0	2.47x	2.91x	9.55x
Service Corp. Intl.	180.0	260.0	296.0	363.0	643.0	784.0	2.02x	2.47x	2.65x
Stewart Enterprises	68.8	77.8	109.1	179.0	184.5	266.3	2.60x	2.37x	2.44x
Total	559.8	617.2	486.1[b]	1,296.2	1,647.9	1,487.0[b]	2.32x	2.67x	3.06x[b]

[a]For nine months ended September 30, 1998.

[b]Excludes Equity Corporation. Approximately 40% of Equity Corporation's stock is owned by Service Corporation International.

Source: Merrill Lynch industry report by Fran Blechman Bernstein and Yasmine C. Nainzadeh. "Post Life Services," April 26, 1999.

EXHIBIT 1.6 Loewen Group, Ten-Year Financial Summary (Dollars in US$millions, except Share Prices)

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
Sales	$ 63.8	$117.6	$188.5	$231.5	$300.1	$ 417.5	$ 598.5	$ 899.4	$1,114.1	$1,136.2
Gross profit	25.5	47.2	72.2	87.4	114.5	159.0	225.4	328.6	370.7	291.7
Operating profit	17.7	31.0	44.4	52.0	66.6	94.6	131.9	195.1	199.8	78.0
Net income	6.2	11.1	16.5	20.5	27.9	38.5	(76.7)	63.9	42.7	(599.0)
Total assets	$163.4	$341.3	$446.1	$547.0	$748.5	$1,115.7	$2,263.0	$3,496.9	$4,503.2	$4,673.9
Total liabilities	108.0	238.3	275.5	343.0	472.3	829.8	1,977.1	2,728.0	3,291.9	5,000.7
Long-term debt due in one year	5.1	7.2	6.9	7.9	6.6	45.5	69.7	79.6	43.5	874.1
Long-term debt	79.7	172.1	217.0	251.5	334.4	471.1	864.8	1,428.6	1,750.4	1,393.9
Capital expenditures	$ 3.1	$ 8.6	$ 14.0	$ 12.6	$ 22.2	$ 39.8	$ 36.1	$ 72.6	$ 85.3	$ 62.7
Acquisition expenditures	36.0	159.7	78.4	87.3	147.6	265.6	487.9	619.6	546.5	252.6
Proceeds from issuance of common and preferred stock	33.9	53.5	46.0	33.7	54.4	53.4	203.1	454.7	462.4	1.8
Proceeds from issuance of long-term debt	14.0	91.7	197.5	34.3	92.9	187.4	396.5	1,128.4	1,385.4	1,105.4
Market value of common stock[a]		$301.6	$438.1	$550.8	$980.7	$1,086.9	$1,219.2	$2,310.6	$1,903.2	$ 624.9
Book value of common stock		134.2	197.1	245.7	324.8	411.1	614.7	891.1	1,383.1	748.3
Year-end stock price		$ 10.88	$ 13.38	$ 15.50	$ 25.38	$ 27.00	$ 25.31	$ 39.13	$ 25.75	$ 8.44

[a]Loewen Group's common stock was first traded in a U.S. market in 1990.
Source: Datastream United States database.

EXHIBIT 1.7 Letter to Raymond Loewen from William Heiligbrodt, SCI's President and Chief Operating Officer

September 17, 1996

Mr. Raymond L. Loewen
Chairman of the Board and Chief Executive Officer
The Loewen Group Inc.

Dear Mr. Loewen:

As you know, I have tried to reach you several times since September 11. While your office has assured me that you received my messages, my calls have not been returned. In view of that, and in view of the importance of this matter, I am sending this letter.

I would like to discuss with you a combination of our two companies. The combination would involve a stock-for-stock exchange accounted for as a pooling which values Loewen Group at US$43 per share. We believe that this transaction can be structured in a manner that is tax-free to both companies. . . .

I think you and your Board and stockholders would agree that our proposal is a generous one, resulting in the following premiums for Loewen Group stockholders:

- 48.9% above the price at which Loewen Group stock traded 30 days ago;
- 39.3% above the price at which Loewen Group stock traded one week ago; and
- 27.4% above the price at which Loewen Group stock is currently trading.

This represents an opportunity for your stockholders to realize excellent value, by any measure, for their shares. In addition, and importantly, since your stockholders would be receiving stock, they would continue to participate in Loewen Group's business as well as share in the upside of our business.

Thus, in essence, your stockholders would:

- continue their investment in our industry;
- get an immediate, and very significant, increase in the market value of their investment;
- get that immediate and substantial increase on an essentially tax-free basis; and
- diversify their risk by participating in a much larger number of properties.

This is a "win-win" situation for you and your stockholders.

Finally, with respect to consideration, I would note also that our proposal is based on public information. After a due diligence review, we may be in a position to increase the consideration that your stockholders would receive. . . .

I would very much like to discuss any and all aspects of our proposal directly with you and your Board of Directors. We believe you and they will recognize the tremendous benefit to your stockholders of our proposal. Our proposal is conditioned upon approval of our Board and upon negotiation of mutually satisfactory agreements providing for a combination on a pooling basis.

We hope that after you meet with us, you will similarly determine that the transaction should be pursued. We look forward to hearing from you.

In view of the importance of this matter, we are simultaneously releasing this letter to the press.

Sincerely,

William Heiligbrodt
President and Chief Operating Officer
Service Corporation International

Source: "Service Corporation International Announces a Proposed Business Combination with the Loewen Group Inc.," PR Newswire, September 17, 1996.

EXHIBIT 1.8 Summary of Prime Succession and Rose Hills Acquisitions

Prime Succession

Under the transaction, all of the outstanding common stock of Prime Succession Inc. was acquired by a special-purpose entity, Prime Succession Holdings, Inc. (PSHI). The total purchase price, including transaction and financing costs, was $320 million. The excess of the purchase price above the fair value of the acquired assets (estimated at $230 million) would be reported as goodwill, and amortized over 40 years.

The purchase price was financed with $190 million of debt, $62 million of 10% payment-in-kind preferred stock, and $68 million of common stock—all issued by PSHI. The debt included a $90 million bank term loan from a group of institutions led by Goldman, Sachs & Co., and a $100 million public issue of 10.75% senior subordinated notes, with Smith Barney Inc. as lead manager of the offering. In addition, the Bank of Nova Scotia provided a $25 million revolving credit facility.

All of the preferred stock and $16 million of the common stock (23.5%) were purchased by Loewen Group. Blackstone Group purchased the remaining $52 million of common stock. Blackstone and Loewen would have the right to designate five and three nominees, respectively, to PSHI's board of directors. Two former executives of Loewen would manage PSHI, but Blackstone would control the strategic, operating, financial, and investment policies of the firm. Neither party would be allowed to sell its shares to an unaffiliated party without the consent of the other.

Loewen would account for its investment in PSHI using the equity method of accounting, reporting its proportional share of the net earnings (or losses) of PSHI, after deducting the payment-in-kind dividend.

Between the four- and six-year anniversary of the transaction, Loewen would have the option to "call" or purchase Blackstone's PSHI common stock at a specified price. This price was determined by a complicated formula. In general, the price paid to Blackstone increased as the estimated value of PSHI's common stock (V, defined below) passed certain thresholds. Regardless of what V was, however, Loewen could not exercise its option unless Blackstone received at least a 24.1% compound annual return on its initial investment of $52 million. If the option was exercised after four years, for example, Loewen would have to pay Blackstone at least $123.5 million.[a]

Between the six- and eight-year anniversary of the transaction, Blackstone would have the option to "put" or sell its PSHI common stock back to Loewen at a specified price. This price was also determined by a complicated formula. As with the call option,

(Continued)

[a]This calculation is based on analysis reported in Gallo, Reynolds, and Roche, "The Loewen Group" (unpublished student manuscript, 2000).

EXHIBIT 1.8 *(Continued)*

Blackstone's dollar return from exercising the put would in general increase with V. V was estimated as the difference between the estimated value of PSHI's assets and all debt and preferred stock outstanding (including accreted payment-in-kind dividends). The value of PSHI's assets was in turn estimated by multiplying PSHI's EBITDA (earnings before interest, taxes, depreciation, and amortization) for the latest twelve months by a multiple. This multiple was the ratio of the original transaction price ($320 million) to PSHI's average EBITDA for the first two years following the acquisition.

Rose Hills

This transaction was structured essentially the same way as the Prime Succession acquisition.

A special-purpose entity, Rose Hills Holding Corp. (RHHC), was formed to acquire the cemetery and mortuary operations of The Rose Hills Memorial Park Association, for total consideration of $285 million. This amount was financed with $155 million of debt from banks and other institutional investors, $86 million of 10% payment-in-kind preferred stock, and $44 million of common stock. Loewen purchased the entire issue of preferred stock. Blackstone purchased 79.5% of the common stock, and Loewen purchased 20.5%.

Blackstone would control the board of directors, and the strategic, operating, financial, and investment policies of the firm. Loewen would account for its investment in RHHC using the equity method of accounting.

The transaction terms also included a call/put agreement that was similar to the one in the Prime Succession deal.

Source: The Loewen Group Inc., Form 8-K dated August 29, 1996, and Form 10-K dated December 31, 1996.

EXHIBIT 1.9 Loewen Group's Long-Term Debt, Including Amounts Due within One Year, December 31, 1998 (Dollar Amounts in US$millions)

Bank credit agreement	$ 330.0
Management Equity Investment Plan bank term credit agreement due in 2000	97.3
9.62% Series D senior amortizing notes due in 2003	42.9
6.49% Series E senior amortizing notes due in 2004	42.9
7.50% Series 1 senior notes due in 2001	225.0
7.75% Series 3 senior notes due in 2001	125.0
8.25% Series 2 and 4 senior notes due in 2003	350.0
6.10% Series 5 senior notes due in 2002 (Canadian $200)	130.7
7.20% Series 6 senior notes due in 2003	200.0
7.60% Series 7 senior notes due in 2008	250.0
6.70% PATS senior notes[a]	300.0
Present value of notes issued for legal settlements discounted at an effective interest rate of 7.75%	38.2
Present value of contingent consideration payable on acquisitions discounted at an effective interest rate of 8.0%	19.8
Other, principally arising from vendor financing of acquired operations or long-term debt assumed on acquisitions, bearing interest at fixed and floating rates varying from 4.8% to 14.0%, certain of which are secured by assets of certain subsidiaries	116.4
Total	$2,268.0

[a]These notes are due in 2009, but are redeemable in full at the holder's option on October 1, 1999. If the option is not exercised by this date, the interest rate on the notes is reset at a fixed rate tied to then-current credit spreads.

Source: Loewen Group Inc. Form 10-K, December 31, 1998.

Note: Long-term debt matures as follows ($millions):

1999	$874.1
2000	23.3
2001	370.1
2002	144.1
2003	563.1
Thereafter	293.3

In addition to long-term debt listed above, $66,222,000 is outstanding under a revolving receivables finance facility with a bank. The facility is an obligation of a wholly owned company subsidiary, and is secured by cemetery receivables. No additional borrowings are permitted under the facility, based on the value of eligible receivables. The facility bears interest at a floating rate based on commercial paper rates (5.51% at December 31, 1998).