

ILIT's and the Uniform Prudent Investor Act Trust Owned Life Insurance (“TOLI”) Under The “UPIA”

Trustees are facing increased scrutiny of their investment performance in these difficult economic times. For those Trustees of trusts owning life insurance (“TOLI”) they face additional challenges in their management of this “special asset”. *The Uniform Prudent Investor Act (“UPIA”) and similar statutes require as rigorous a management model for life insurance as for all other types of assets.*

A Trustee might monitor the investment assets in a trust to ensure their performance is meeting expectations, *but a trustee should also be monitoring and reviewing the life insurance assets in a trust for which they are responsible.* It is important to note that the UPIA sets a basic standard which may vary from state to state, although the specific trust documents may be drafted whereby the trustees are held to even a higher standard than set forth by the UPIA.

Acting in a fiduciary capacity, trustees bear the burden of carrying out the trust's objectives for all beneficiaries. The UPIA is very specific in noting that when acting in such a fiduciary capacity, the trustee must “consider the purpose, terms distribution requirements and other circumstances of the trust”. *The Act holds all trust assets to the same standards and requires trustees not only to monitor performance, but to also assess the risks and quality of assets in the trust.*

TOLI requires that the Trustee determine the need and quantification of the life insurance death benefit amount in conjunction with clients counsel, and other financial advisors as supported by the overall estate plan. This further requires that the Trustee be actively engaged in the review and selection of the appropriate types of life insurance, product selection and diversification, including carrier diversification and selection. These requirements extend well beyond the monitoring process for policy

performance, although it is policy performance that often leads to issues concerning the life insurance asset.

The practical standards a trustee should follow for ongoing monitoring of the policy would include, although may not be limited to, policy performance, policy design taking into consideration whether it is a MEC, or may become a MEC, the funding schedule, cost of insurance, and the in-force illustration to confirm that the projected policy performance is consistent with the intended purpose and results as originally planned. It is also important to evaluate the carrier, the health of the insured and life expectancy, and a comparative cost study in light of the facts and circumstances to alternative products.

Past legal issues that have given rise to a Trustee being sued have included the failure to pay the premium, even though the trust received the funding required; poor investment decisions related to variable life contracts which adversely affected policy performance; failure to follow the originally proposed premium funding schedule; failure to detect poor policy performance due to overly optimistic assumptions at time of issue, which now risk the policy lapsing prior to the insured life expectancy; policy loans to fund premium payments that reduced the death benefit even though the original illustration projected a “vanishing premium”.

Trustees must establish a formal procedure for managing the life insurance asset to comply with their fiduciary responsibilities. Our service provide Trustees with a formal written due diligence report that can satisfy their fiduciary responsibility in providing monitoring of the life insurance asset, including comparative product performance and cost results, along with any issues requiring corrective action to meet the originally intended objectives and trust provisions. This service does not give notice to the original servicing agent of the policy.