Trustee Administration of Life Insurance
(Part 1 of 4)

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This is the first of a four part series on the administration of life insurance as an asset of trust. This first part discusses the duties of trustees under different models for administering an irrevocable life insurance trust. The second part will examine the impact of the Prudent Investor Rule on holding life insurance in a trust. The third part will describe one approach that trustees may take in evaluating the appropriateness on insurance as an asset in a particular trust. The final part deals with decisions that will be faced by trustees when life insurance is held in a trust.

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"What usually is done may be evidence of what ought to be done, but what ought to be done is fixed by a standard of reasonable prudence, whether it usually is complied with or not."

—Justice Oliver Wendell Holmes (1903)

PREFACE

Life insurance proceeds play an integral part in the financial well being and wealth of many Americans. Traditionally, life insurance has been an important source of funds for family support in the event of the death of the major breadwinner; for the payment of federal and state death taxes; for bequest objectives; and, more recently, for asset diversification and tax-favored investment.

The need to promote a discussion regarding best practice standards for ILIT trustees increases as the propensity for litigation rises in the general society. The law surrounding many of the issues discussed in this article is thin; and there is little in the way of statutory or judicial guidance with respect to many critical elections faced by the ILIT trustee. What does it mean, for example, to state that a trust beneficiary has a beneficial interest in an asset that represents merely a state-contingent

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claim? Most insurance policies do not stay in force long enough to pay a death benefit. If the state-contingent claim (i.e. the contract must be in force at the time of the insured's death) shares some of the characteristics of a lottery ticket, does the beneficiary have cause to sue if it does not pay off? Can the trustee be surcharged for purchasing such an asset in the first place? What are prudent standards of management for such an asset?

Part One discusses trustee duties under three models of ILIT management. Its primary objective is to shape an understanding of the legal context in which the trustee makes important asset management elections. It commences with a discussion of the statutory framework which defines an ILIT trustee's management duties and responsibilities. The statutory framework will assist in identifying the similarities and differences in the management duties of the different trustee models. The statutory framework further authorizes a trustee to delegate its management responsibilities. Such delegation will become the most important management tool for many ILIT trustees. Restatement Third's repeal of the anti-delegation rule is especially important in that it allows the trustee and the trustee's legal advisors to draft and implement a series of delegation agreement documents that clarify and codify trustee responsibilities.

Part Two reviews the advice offered to ILIT trustees following the promulgation of the Restatement (Third) of the Law of Trusts: The Prudent Investor Rule. It provides a critical evaluation of both the details of the advice as well as the assumptions upon which recommendations regarding policy management are based. A central theme of this section is that, either through design or happenstance, the life insurance industry has co-opted much of the vocabulary informing the Prudent Investor Rule to advance sales objectives that often bear an uneasy relationship with the underlying principles of modern trust management. Furthermore, to a great extent, trustees following such advice assume a difficult burden. Rather than creating an ILIT-owned insurance portfolio that is adequately diversified according to carrier and product type, the advice forthcoming from the insurance practitioner community often encourages a form of extreme concentration risk (often, all coverage is provided by one policy on the life of the insured/grantor). Additionally, it may require the trustee, in the event of litigation, to defend its abilities as a forecaster of policy performance as well as future carrier solvency. For most trustees, this may prove to be a difficult burden of proof. Trustees can more profitably direct their efforts towards establishing reasonable portfolio design, implementation and management guidelines than towards picking the "winning" insurance companies and contracts.

Part Three introduces a tool that trustees may use to facilitate and demonstrate competent administration of the insurance portfolio. It begins with a brief discussion of the "quandary" of the trustee who, when faced with the duty of prudent asset management, is bombarded with unsubstantiated sales claims and marketing pressures. This section argues that ILIT trustees face many of the same type of hard-to-evaluate-and-verify assertions that were once endemic in the U.S. money management industry. Contradictory and irreconcilable claims made by competing money managers were the bane of trustees charged with the prudent management of financial assets. The development of tools and techniques based on accepted standards of quantitative performance analysis was pioneered by organizations like the CFA Institute (formerly, the Association for Investment Management and Research). The objective is to level the playing field and make it more difficult for sales organizations to game their investment track records or to present misleading performance results. The central theme of this section is that a comparable standard of evaluation is required to prevent the gamesmanship currently rampant within insurance sales and marketing; and, it presents an example of such an evaluative tool in the form of an objective comparative benchmark model. The model presented in the article serves as a basis for demonstrating the prudence of the initial acquisition of the insurance contract(s) as well as for ongoing annual fiduciary reporting for the ILIT's insurance portfolio.

Part Four introduces an asset management tool that may be adapted for use by ILIT trustees at all skill levels. The article discusses a variety of issues underlying the need for a written Investment (or, Insurance) Policy Statement [IPS], and advances a rationale for particular approaches to some critically important asset management elections faced by ILIT trustees. When delegating certain fiduciary functions to qualified agents, the IPS assists the trustee to set the terms of the delegation prudently. Finally, the article concludes with a sample IPS. IPS language may be wordsmithed by the document draftsperson to achieve desired objectives; and, the sample IPS offers commentaries designed to facilitate drafting flexibility. A central theme in this section is that the trustee is on more firm footing by assuming the role of manager of policy rather than forecaster of insurance carrier solvency or insurance policy results. The single greatest step towards implementing prudent asset management is to diversify the ILIT portfolio. Diversification, in the context of ILIT administration, does not refer to the purchase of financial assets such as stocks, bonds and real estate. Rather, it refers to the avoidance of asset concentration risk by placing all coverage with a single carrier under a single policy form (Whole Life, Universal Life, Variable Life, etc.). Although the trustee must still keep an eye on each policy and each underwriting company, prudent asset management becomes a function of portfolio composition and implementation

rather than accurate forecasting of future policy performance or carrier solvency. Depending on the resources and skill level of ILIT trustees, there exists a spectrum of prudent asset management approaches from which the trustee may choose.

The authors intentionally have restricted the topics that this article addresses. Except as to a trustee's investment management duties vis-à-vis a life insurance policy, this article is not intended to be a comprehensive analysis of an ILIT or other trustee's fiduciary duties arising either under the law or a declaration of trust. This article does not discuss income, gift and estate tax issues concerning ILITs or other trusts which hold life insurance except in summary fashion. Notwithstanding the premise advanced in this article, the authors do not intend to establish new or different standards against, or by which, to evaluate the investment management performance of an ILIT or other trustee which is responsible for trust-held insurance.

PART 1: TRUSTEE MANAGEMENT OF AN ILIT-HELD LIFE INSURANCE POLICY— AN AFFIRMATIVE DUTY

Inherent in the concept of trusts is the trustee's responsibility to manage the assets of a trust in a prudent manner.[1] Although the specifics of a trustee's continuing investment management duties may vary, fundamental criteria are set forth in The Uniform Prudent Investor Act of 1994 ("UPIA")[2] which incorporated principles enunciated in The Restatement (Third) of the Law of Trusts.[3] If a life insurance policy constitutes the corpus of a trust, the trust form most likely will be that of an irrevocable life insurance trust ("ILIT"). ILIT trustees and their advisors (*e.g.,* estate planning attorneys, accountants, financial planners and insurance agents) usually consider an ILIT trustee's "management" responsibilities to consist primarily of sending Crummey notices[4] and paying policy premiums. However, a life insurance policy also may be held as the, or part of the, corpus of other types of irrevocable or revocable trusts. Regardless of the type of trust, a safe generalization of current trustee practices is that, although trustees may provide certain administrative services to ILITs, many trustees do not render investment management services for trust-held life insurance policies.[5]

§ 1.1 TRUSTEE INVESTMENT MANAGEMENT UNDER PRUDENT INVESTOR ACT

Contrary to the existing norm, the authors contend that a life insurance policy held in trust is subject to the same investment management standards as is any other asset held in trust and that the UPIA applies to ILIT

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[1] California Probate Code section 16040(a) (California Uniform Prudent Investor Act) Thompson*West 2005. Both the California Uniform Prudent Investor Act and the Uniform Prudent Investor Act use the terms "assets"; "portfolio" and "investments." Under the Uniform Prudent Investor Act, the "term 'portfolio' embraces all of the trust's assets." UPIA section 2(b). To avoid confusion with the commonly used term "portfolio" in reference to a portfolio of stocks, this article most frequently employs the terms "assets" or "investments" in reference to all of the assets held in a trust. *See,* California Probate Code sections 10645 *et. seq.,* Teitelbaum, Mark A., "Trust-Owned Life Insurance: Issues Trustees Face; Decisions Trustees Need to Make," *Journal of Financial Service Professionals,* (July, 2005), pp. 38-49; and, Teitelbaum, Mark A., "Trust-Owned Life Insurance: Is It An Accident Waiting to Happen?" *National Underwriter* (May 17, 2004), pp. 38-43.

[2] Uniform Prudent Investor Act, drafted by the National Conference of Commissioners on Uniform State Laws, Annual Conference, Chicago, IL, July 29 - August 5, 1994. For an extensive discussion of the Prudent Investor Rule and Modern Portfolio Theory *see* Moses, E., Singleton, J. and Marshall, S., "Modern Portfolio Theory and the Prudent Investor Act," *ACTEC Journal,* Vol. 30, No. 3 (2004); "Using a Trust's Investment Policy Statement to Develop the Portfolio's Appropriate Risk Level," *ACTEC Journal,* Vol. 30, No. 4 (2005); "Computing Market Adjusted Damages in Fiduciary Surcharge Cases Using Modern Portfolio Theory, *ACTEC Journal,* Vol. 31, No. 1 (2005); "The Appropriate Withdrawal Rate: Comparing a Total Return Trust to a Principal and Income Trust, *ACTEC Journal,* Vol. 31, No. 2 (2005).

[3] Restatement (Third) of Trusts; Prudent Investor Rule, American Law Institute (1992).

[4] *Crummey v. Commissioner,* 397 F.2d 82 (9th Cir. 1968), 22 AFTR2d 6023, 68-2 USTC 12,541), *aff'g* and *rev'g* TC Memo 1966-144; accepted by Internal Revenue Service, Rev. Rul. 73-405; Grassi, Sebastian V., "Key Issues to Consider When Drafting Life Insurance Trusts," *A Practical Guide to Drafting Irrevocable Life insurance Trusts* 2004 (discussion of drafting and implementation considerations).

[5] Harris, R.L. and Prince, R. A., "The Problem with Trusts Owning Life Insurance," *Trusts and Estates* pp. 62-64 (May 2003); Teitelbaum, *supra* (example of increased recognition of ILIT trustee responsibility; the authors contend that the duty is mandatory rather than discretionary); "How the Irrevocable Life Insurance Trust Works" (Chart) www.givingto.msu.edu/pgaol/html/how; Barney, Austin D., "The Hazards of Unmanaged Life Insurance Policies," Planned Giving Design Center, www.pgdc.com (6/8/04); Whitelaw, C. Markham and Ries, William C., "Managing Trust-Owned Life Insurance Revisited," *Trusts & Estates* pp. 38-45 (April 1999).

[6] Collins, Patrick J. and Jurkat, Dieter, "The Decision to Replace Trust Owned Life Insurance Policies," *The Banking Law Journal* (November/December 2005) pp. 975-1005; Teitelbaum, *supra* (arguing that UPIA terminology of "portfolio" applies to all trust assets, and accordingly applies to trust-held life insurance); UPIA, Section 2(b); Weidenfeld, Edward L., "Professional Liability Issues for Estate Planning Attorneys Working With Life Insurance Products," *Tax Management Estates Gifts and Trusts Journal,* (November 11, 1999) ("ILITs by definition cannot diversify the type of asset involved....." at 9); Esperti, Robert A. and Peterson, Renno L., *Irrevocable Trusts: Analysis,* RIA Checkpoint (2004).

trustees.[6] Investment management of a life insurance trust requires a trustee to evaluate a life insurance policy prior to its inclusion as part of the trust corpus and thereafter, on a periodic basis, to assess the policy vis-à-vis the trust's purposes and objectives.[7] After a policy becomes a trust asset, the trustee should manage the policy in accordance with its fiduciary duties. A trustee's management of a life insurance policy should reflect and incorporate the principle of diversification as articulated in the UPIA. Since an ILIT by definition usually has only one type of asset, diversification in an ILIT could be accomplished through "vertical" diversification. Thus the ideal ILIT corpus might consist of several types of life insurance policies issued by different carriers.

§ 1.2 NEW OPERATING MODELS NECESSARY

In recent years, surcharge actions by disgruntled beneficiaries against trustees have increased.[8] Among the contributing causes are the fragmentation of the traditional family, the creation of subsequent families with their various and divided loyalties, the passage of wealth from the World War II generation to members of their often-conflicted families, and increases in life expectancies. Although not an exclusive list, the existence of any one of the above factors in a family unit could result in fewer remaining assets being available to pass onto the succeeding generations. The purpose of this article is not to discuss such factors, but rather to acknowledge their existence as a contributing cause to increases in fiduciary litigation. ILIT trustees are not immune from the surge in fiduciary litigation even though the increase has been relatively minor in comparison with the exponential growth seen in other types of fiduciary litigation.[9]

Although some ILIT trustees are professionals, most are family members or friends of the settlor. Regardless of the identity of an ILIT trustee, a common (although most frequently tacit and implied) understanding between a settlor and an ILIT trustee seems to be that an ILIT trustee's administrative duties are to be minimal during the lifetime of the insured settlor. The norm of a "quiet" ILIT trust administration during the settlor's lifetime enables a settlor to establish an ILIT and to achieve family and tax objectives with reasonable fiscal economy.

With the increased risk of a legal challenge based upon a trustee's failure to satisfy investment management criteria for trust-held life insurance policies, the status quo of a "passive" ILIT administration during the settlor's lifetime may no longer function as an adequate shield against beneficiary dissatisfaction. The search should be for new ILIT operating models which would enable a trustee to comply with the UPIA investment management requirements. Notwithstanding attempts to minimize administrative expenses during a settlor's lifetime, under almost any new operating construct, the insured settlor's out-of-pocket costs probably will increase. The settlor and the settlor's advisors should engage in a risk analysis with both good management practices and trustee surcharge protection balanced against additional settlor costs and beneficiary-instigated litigation either prior to or following the settlor's death.

§ 1.3 INTERACTION BETWEEN THE SETTLOR AND THE TRUSTEE OF AN IRREVOCABLE LIFE INSURANCE TRUST

Life insurance proceeds constitute an integral part of the financial planning and well being of many Americans.[10] Traditionally, Americans have regarded life insurance proceeds as a secure reservoir of cash otherwise unobtainable through savings or investments. For a young family, life insurance proceeds can furnish a source of support in the event of the family breadwinner's untimely death.[11] For substantial estates, insurance proceeds can provide a readily available source for the payment of federal or state estate taxes. Insurance proceeds can facilitate other personal, estate planning and financial objectives such as: 1) continuance of a prior standard of living; 2) avoidance of a forced sale of assets; 3) funding for a business buyout or succession planning; 4) transfer of wealth to succeeding generations; and 5) funding of charitable bequests. With or without an investment component, life insurance may function as an asset-diversification alternative.[12]

§1.3.1 Common Life Insurance Ownership Forms

The most common model of life insurance ownership is for the owner of a life insurance policy also to be the insured upon whose life the policy is written. Although the owner typically pays the policy premiums, and although the policy is an asset which (even-

[7] UPIA, Section 4; Weidenfeld, supra at 5-6.

[8] Teitelbaum, supra at 41; "Trust Laws Get a Makeover," *Wall Street Journal,* Part D, p.1, July 29, 2004; "As Financial Services Consolidate, Trust Managers Come Under Fire," *Wall Street Journal,* Part 1, p. 1, July 20, 2004.

[9] Collins, Patrick J., "Diversification, Due Care and the Duties of an ILIT Trustee," *California Trusts and Estates Quarterly,* Vol. 7, Issue 2 (Summer 2001).

[10] Grassi, *supra.* Warner, Norcross and Judd, LLP, "Irrevocable Life Insurance Trust," (2004) at www.wnj.com/estateplanning/ilits.pdf.

[11] *See*, for example, Chen, P., Ibbotson, R., Milevsky, M. and Zhu, K., "Human Capital, Asset Allocation, and Life Insurance," *Financial Analysts Journal* (forthcoming).

[12] *Id.:* Life insurance is a perfect hedge for human capital in the event of death; *i.e.,* term life insurance and human capital have a negative 100% correlation with each other in the live vs. dead states. If one pays-off at the end of the year, the other does not and vice versa. Thus, the combination of the two provides great diversification to an investor's total portfolio.

tually) should increase the value of the owner's estate, the owner typically does not derive lifetime economic benefits from policy ownership. For this reason, an owner of a life insurance policy usually wants to manage and to control the policy during the owner's lifetime and to minimize administrative and other expenses that might arise in connection with policy ownership. Concurrently, for a policy owner whose estate may be subject to federal estate taxes, the owner will want the policy proceeds to be exempt from those taxes. Commentators have labeled these conflicting desires as "the pipe" dream that, by its very appellation, means that the desired results are concomitantly unattainable.[13] However, many current stratagems involving life insurance planning represent attempts to facilitate such mutually exclusive "pipe dream" objectives. These approaches often depend, though indirectly, upon "owner-managed" trust arrangements.

If, as of the date of a decedent's death, the decedent owns a policy of life insurance, the policy's date of death value will be included in the decedent's estate for federal estate purposes and will be subject to federal estate taxes unless the decedent's gross estate is not of sufficient value to be subject to such taxes.[14] Under the 1954 Internal Revenue Code as amended ("IRC"), the term "ownership" as used in conjunction with life insurance is defined broadly and includes incidents of ownership as well as outright ownership.[15] A decedent may be deemed to possess an incident of ownership through indirect control or management of a life insurance policy and regardless of the manner in which title to the policy is vested.[16]

If the policy owner transfers ownership of the policy to an independent third party, the policy proceeds still will be included in the deceased owner's estate unless, as of the decedent's date of death, three years have elapsed from the date of the transfer.[17] As a result of taxpayer efforts to exclude policy proceeds from a decedent's estate, countless battles have arisen between the Internal Revenue Service and taxpayers about the elements of policy ownership, the efficacy of policy transfers and retained incidents of ownership.[18] Transfer formalities, including acknowledgment by the issuer of a new policy owner, require strict adherence and thorough documentation.[19] For an ILIT trustee (or the trustee of any other type of irrevocable trust which owns a policy of life insurance), the three-year rule creates additional complexity respecting the type of policy which will be used in funding the ILIT. Specifically, a trustee must determine whether to accept a settlor's proposed transfer of an existing policy or to purchase a new, perhaps more economically favorable policy. The uncertainty of a settlor's survival may make a trustee's decision even more difficult.

Third party ownership from the date of a policy's issuance (which may or may not involve a trust) should not result in the inclusion of the policy proceeds in the insured's estate, regardless of whether the insured dies within the three-year period commencing with the policy's issue date.[20] Ownership will not be attributed to the insured/settlor even though the insured may have participated in the application process or may have assisted in the policy purchase. From the perspective of federal estate taxation and except for prohibited insured/settlor's participation in the acquisition process, an independent third party who purchases a life insurance policy is regarded as both the purchaser and the owner of the policy.[21]

§1.3.2 Techniques for Preventing the Inclusion of Policy Proceeds in a Decedent's Estate

Common methods of preventing the inclusion of policy proceeds in a decedent's estate are cross-ownership of life insurance policies by husband and wife, ownership of life insurance policies by adult children and establishment of an ILIT. The cross-ownership and outright ownership techniques are appealing. These techniques not only function to remove the insurance proceeds from the insured/owner's estate, but in addition, they are simple and inexpensive to implement. Further, unlike a trust, cross-ownership and outright ownership do not require continuing administration or monitoring except perhaps to the extent that the insured/owner continues to finance premium payments through gifts.

For the insured/owner, the major disadvantage of either the cross or outright ownership techniques is that a purportedly independent third person owns the policy, and as such possesses sole legal power over the

[13] Grassi, *supra.*

[14] 1954 Internal Revenue Code sections 2041(1), 2042(2); in 2005, the applicable exclusion amount is $1,500.000; for 2006-2008, the exclusion amount increases to $2,000,000; in 2009, the exclusion amount is $3,500,000. The current estate tax is scheduled to be repealed in full in 2010, but it to be fully reinstated in 2011, including an exemption reduced to $1,000,000.

[15] Treasury Regulation section 20.2042-1(c)(2); *Commissioner v. Estate of Karagheusion,* 56-1USTC 11,605, 233 F.2d 197 (2d Cir. 1956); Warner, Norcross and Judd, *supra.*

[16] *Id.; Estate of Noel v. Commissioner,* 380 US 678 (1965).

[17] 1954 Internal Revenue Code section 2035(d); Tech. Adv. Mem. 200432015, paragraph 35,410.

[18] *See, e.g., Estate of Karagheusion, supra; Estate of Noel v. Commissioner,* 380 US678 (1965); *Estate of Bloch, Jr. v. Commissioner,* 78 T.C. 850 (1982); Tech. Adv. Mem. 9323002.

[19] *Id.;* Reynolds, Katherine M., "Irrevocable Life Insurance Trusts" www.mbf-law.com 1999-2004.

[20] *Id.;* Lipoff, Lawrence M., "Irrevocable Life Insurance Trusts," Seminar Handout, aol.com/CRT Trust/ILIT.html 1996.

[21] Lipoff, *supra* at 5-6; Grassi, *supra.*

policy and its proceeds. Except for "informal" influence which the insured/owner still might exert over a family member or friend, the insured/owner cannot direct disposition of the proceeds, policy retention or investment decisions, nor can the owner/insured exercise any other privilege of ownership. As a consequence, once the insured/owner relinquishes policy ownership, the new owner's act(s) could be contrary to those which the insured/owner otherwise might want.

With substantial estates or complex family situations, an ILIT usually is preferable to either cross-ownership or an outright transfer. In the estate(s) of a surviving spouse or of adult child(ren) whose estate(s), even without the addition of the policy proceeds, would be subject to federal estate taxes, a properly created and implemented ILIT will prevent the inclusion of the policy proceeds in such individual's taxable estate. Although the insured must relinquish ownership upon the establishment of an ILIT, the ILIT, nevertheless, enables the insured/settlor to maintain control of the policy and the policy proceeds through the terms and conditions included in the declaration of trust. In an ILIT, for example, the insured/settlor can name specific and contingent beneficiaries, prescribe the conditions upon which receipt of policy proceeds are to be predicated, define terms and conditions of income and principle distribution, set forth investment guidelines and objectives and define management standards and operations. The ILIT may permit the insured/settlor to provide separately for potentially antagonistic beneficiaries. The settlor also can use the trust format to insure coordination between the disposition of the policy proceeds and the settlor's other assets.[22]

§1.3.3 Difficulties in Trustee Selection

Although the selection and designation of a trustworthy, honest and knowledgeable trustee is critical in the formation of any trust, the often thought-provoking process is especially difficult when the trust is an ILIT. Neither the ILIT settlor, nor if married, the settlor's spouse, should act as the ILIT trustee.[23] Practical considerations arising from unique ILIT characteristics complicate the ILIT trustee-designation process. ILITs typically are dry trusts—that is trusts that contain no (or very few) assets other than a life insurance policy and, perhaps, a small amount of cash. An ILIT normally does not produce any income nor does it contain assets that may generate funds through realized appreciation. As a consequence, an ILIT generally is not an economically self-sufficient entity.

Notwithstanding any legal obligation which an ILIT trustee may have to pay policy premiums, the insured settlor usually is the source of the cash by which such premiums are paid. Typically, the insured/settlor also pays for any legal advice required for establishing an ILIT, *e.g.,* advice concerning the federal estate and other tax consequences arising from the creation of an ILIT, alternative ownership forms and financing options. In most instances, the settlor will continue to pay for additional legal and accounting services, trustee fees or other administrative expenses. Although the above-items represent out-of-pocket expenses, it is postulated that few, if any, settlors fully understand the extent of their continuing financial responsibilities when they execute an ILIT. In light of the immediate and continuing financial obligations, most ILIT settlors would balk at a suggestion that additional out-of-pocket costs might be required in the form of trustee fees or other administrative expenses. The financial considerations complicate further the difficulties which a settlor confronts in securing an ILIT trustee.

Historically, many institutions which served as ILIT trustees were willing to characterize their ILIT administrations as "loss" leaders with relationship factors and the potential of fees upon the policy's maturity being given primary emphasis. Consistent with this approach, an institution would charge nominal trustee or administrative fees. Several factors are contributing to changes in this institutional practice. The attractiveness of special client relationships and deferred profitability are diminishing in view of increased pressures for greater profitability and required investment management of ILIT held life insurance policies.[24]

[22] *Id.;* USALAW—"What Does the Trustee Do?," A client's Guide to Irrevocable Life Insurance Trusts, www.usalaw.com.

[23] Grassi, *supra.*

[24] The Office of Thrift Supervision, for example, lists several procedures for ILIT implementation: (1) disclosure of conflicts of interest where the commercial fiduciary acts as life insurance agent; (2) consent of beneficiaries or court order in the event of conflicts of interest; (3) prudent selection and retention criteria for insurance policies; (4) full compensation disclosure; and (5) ILIT diversification: "A conflict of interest for a savings association occurs when the life insurance policy is sold or underwritten by an affiliate of the savings association. In most cases, specific language will be present in the trust instrument creating the ILIT that will allow a trustee to purchase and/or hold an insurance policy sold and/or underwritten by a savings association, its subsidiaries or affiliates. Such language in the trust instrument resolves the conflict of interest but state law, a court order or consent of all the beneficiaries may also be utilized to resolve any conflicts of interest. Savings associations performing trustee services for these ILITs must also meet their duties of prudence in regards to the selection and continued holding of the life insurance policy (ies) which represent a significant portion of the assets of the irrevocable life insurance trust. The savings association should document all of the benefits that it, its affiliates and its subsidiaries receive in connection with the purchase, holding or sale of the life insurance policy…. The subject of diversification of trust account investments must also be addressed under the applicable state's prudent man/prudent investor statute." *OTS Trust and Asset Management Handbook* (July 2001) §870.1.

Expanding surcharge risks are as much a concern for institutions as for individual trustees. Institutional trustees continue to confront mounting regulatory pressures and greater public awareness of their fiduciary and fiscal responsibilities.[25]

If an institution acts as an ILIT trustee, the institution should provide comparable investment management services for the ILIT as it would for any other trust. Further, institutions should receive reasonable compensation for rendering such services. The above dynamics mean that fewer settlors will find institutions willing to act as low-cost ILIT trustees in exchange for the traditional goodwill and prospective profit.

Notwithstanding the common institutional approach of charging minimal or no ILIT administration fees, many settlors prefer that a family member, friend or business associate serve as the ILIT trustee. Typically, such "friendly" trustees request no compensation whatsoever and settlors perceive them as being more amenable to settlor administrative "suggestions."[26] On the other hand, such friendly trustees also may fail to understand the duties and the risks associated with the office of ILIT trustee. Moreover, the friendly trustee's agreement to serve is commonly conditioned upon an (at least implied) understanding that the trustee's duties will be minimal, and any required duties will be performed by the settlor or the settlor's advisors. If a friendly trustee were to be aware of the ILIT duties imposed by the UPIA, then even a friendly trustee might be much less willing to accept the office of trustee without being reasonably compensated.

In light of the litigation risks, an informed trustee (professional or friendly) might seek some type of formal protection against individual financial liability from the settlor. The protection could be in the form of settlor indemnity, appropriate liability insurance or exculpatory provisions. Although liability insurance would afford the most protection, the costs would be substantial. Since an ILIT trustee might be subject to personal/individual liability, and since an ILIT trustee should be more than a mere caretaker of an ILIT-held life insurance policy, the settlor and his advisors should advise the designated trustee to seek independent legal counsel. Assuming that most potential trustees would not want to pay for such legal counsel, the settlor, by default, might have to assume financial responsibility for such advice. The settlor's payment of the trustee's legal fees could become still another complicating factor. Various state bar ethical rules preclude the payment for legal services by other than the attorney's client unless certain safeguards are satisfied.[27]

§1.3.4 ILIT Trustee Patterns

Three basic ILIT trustee patterns provide the point of departure for this article's discussion of investment management alternatives for ILIT trustees. The distinguishing characteristics of each pattern are the type of trustee and the services rendered by the trustee. For purposes of this article, the referenced ILIT will be a dry trust with a corpus consisting only of life insurance policy(ies).

In the first and most common pattern, the ILIT trustee is a family member, friend or sometimes business associate of the ILIT settlor. This type of ILIT trustee does not render investment management services. Both the settlor and the trustee regard the ILIT trustee as a mere caretaker. The settlor acts as the real manager of the ILIT and typically performs (or arranges for the performance of) the few minimally necessary ILIT ministerial duties.

Currently, the second pattern is more of a theoretical projection of a best practice rather than a form regularly implemented. It is this pattern, however, which the authors foresee as offering the most realistic alternative for satisfying an ILIT trustee's investment management duties. In this pattern, the ILIT trustee could be either a "friendly" trustee or an institution. The ILIT trustee would perform required ministerial duties such as sending Crummey notices or paying policy premiums. If the ILIT trustee did receive compensation, the same would be paid commensurate with the services rendered. Under this scenario, it is assumed that the ILIT trustee lacks the skill and knowledge necessary to satisfy UPIA investment management requirements, and therefore declines to undertake this traditional trustee responsibility. Instead, the trustee would delegate investment management duties to a qualified agent, and the trustee's investment management responsibilities would be reduced to monitoring the agent and its performance.

In the third pattern, the trustee usually would be an institution or other type of professional trustee.

[25] Weidenfeld, *supra.* Teitelbaum, *supra* at 41 ("Clearly, the trend is toward setting standards relative to the monitoring of life insurance and assuring that there is both a prepurchase and ongoing review of the policies"); OCC Bulletin 2000-23 (July 23, 2000); *see also, Meyer v. Berkshire Life Insurance Co.,* D. Md., No. CCB-99-1432, 3/31/03 (for analogous liability finding against institution for failure to diversify).

[26] Weidenfeld, *supra* at 2; Esperti, Robert A. and Peterson, Renno L., *Irrevocable Trusts: Analysis,* RIA Checkpoint (2004).

[27] *See, e.g,* Rule 3-310(E) "Avoiding the Representation of Adverse Interests," California Rules of Professional Conduct, The State Bar of California (2005).

The third pattern exists when the ILIT trustee agrees to provide investment management services for trust-held life insurance. The trustee would have a sophisticated knowledge of the insurance industry and its products, the means and techniques with which to evaluate a policy of life insurance, the terms of the trust and the needs of its beneficiaries. Whether an institution engages in such active investment management will depend in large part upon available in-house expertise, degree of perceived risk and economic ramifications. Regardless of which of the above-described trustee patterns a settlor selects, the current practice of an ILIT trustee (or other trustee whose trust holds a policy of life insurance) failing to adhere to UPIA-imposed investment management standards should cease.

§ 1.4 THE LEGAL CONTEXT FOR ILIT INVESTMENT MANAGEMENT

An ILIT trustee will find few formal guidelines about its investment management responsibilities.[28] In general, the Uniform Prudent Investor Act, as adopted and modified by the majority of states, provides a comprehensive structure for trustee investment management responsibilities. Additionally, the Office of the Comptroller, the Office of Thrift Supervision, state attorney generals and other governmental agencies may promulgate regulations and standards pertaining to a trustee's investment duties.

§1.4.1 Trustee Duty to Manage Prudently: Evolution of the Law

When a statute or the settlor does not relieve or modify an ILIT trustee's investment management duties, the Restatement (Third) of Trusts and its progeny, the Uniform Prudent Investor Act, will be the primary source as to the nature and extent of those duties. Notwithstanding modifications and revisions in the articulation of a trustee's investment management duties during the last several hundred years, the intent of the mandate has remained the same: those charged with the financial security of another person's assets must demonstrate care in the investment and management of those assets.

A widely accepted historic formulation of a trustee's investment management duties was embodied in the Prudent Man Rule. Although numerous courts have analyzed the proper application of the Prudent Man Rule, a Massachusetts' court[29] in 1830 articulated the classic definition:

> All that is required of a trustee to invest is that he shall conduct himself faithfully and exercise sound discretion. He is to observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested.[30]

In enunciating the Prudent Man Rule, the court couched its definition in qualified terms (*e.g.,* "probable"); used a conservative reference (*e.g.,* "permanent"); and rejected risk (*i.e.,* "not in regard to speculation") as an acceptable part of an investment strategy.

The thus-formulated Prudent Man Rule continued to be reiterated as the national investment standard for trustees and fiduciaries until the latter half of the twentieth century.[31] In 1972, Congress enacted The Uniform Institutional Management of Funds Act ("Funds Act"),[32] and in 1974, Congress enacted the Employee Retirement Income Security Act.[33] In part, each Act represented Congress' attempt to reconcile traditional investment management standards with contemporary fiduciary management responsibilities arising in a business or institutional context. The reform legisla-

[28] *But see,* Esperti and Peterson, *supra* at 12.02[6] (discussion of trustee liability). A more complete discussion on the topic of standards of practice for commercial and professional fiduciaries is found in §4.1 of this article.

[29] *Harvard College v. Amory,* 9 Pick (26 Mass.) 446 (1830).

[30] *Id.* at 461.

[31] The Restatement (Second) of Trusts section 228 (1959). For a history of investment management standards *see* Longstreth, Bevis, *Modern Investment Management And The Prudent Man Rule* (Oxford University Press 1986); and Simon, W. Scott, *The Prudent Investor Act: A Guide To Understanding* (Namborn Publishing 2002).

[32] The Uniform Institutional Management of Funds Act adopted by the National Conference of Commissioners on Uniform State Laws, 1972.

[33] Employment Retirement Income Security Act (ERISA), section 404(a)(1)(B), 29 U.S.C. section 1104(a) ("..."a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and…with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims….") ((1974).

tion set forth in the referenced Acts embraced and incorporated Modern Portfolio Theory.[34]

Notwithstanding the passage of the above Acts, the world of private trusts continued to rely upon the Prudent Man Rule for another twenty years, functioning in a vacuum which excluded modern academically-based investment principles. The 1992 Restatement (Third) introduced a contemporary formulation of the Prudent Person Rule.[35] The Restatement broadened the scope of a trustee's reference for decision-making. To comport with the more fluid financial and social contexts in which modern trusts existed, Restatement section 227 broadened the scope of a trustee's reference for purposes of the trustee's decision-making by providing:

> The trustee is under a duty to the beneficiaries to invest and manage the funds of a trust as a prudent investor would, in light of the purposes, terms, distribution requirements, and other circumstances of the trust.[36]

A trustee could not satisfy section 227's prescriptions by confining its inquiries to the four corners of the governing instrument.[37] Instead, the Restatement directed the trustee to investigate real world facts relevant to the pending investment decision. Section 227 emphasized the privity which existed between a trustee and its beneficiaries.[38] Yet, the section omitted provisions relating to the weight to be given to the stated indicia; to possibly conflicting beneficiary needs or objectives (*e.g.,* income versus remainder beneficiaries); and a methodology for resolving conflicts.

Established trust law required a separate and distinct fiscal and economic assessment of each trust asset. A trustee could be held accountable for the failure of one investment notwithstanding the profitability of the trust's investments viewed in their totality. In conformance with Modern Portfolio Theory, subsection (a) of section 227 demanded a radical change in a trustee's investment perspective. Under subsection (a), a trustee had to create a formal "overall investment strategy" which demonstrated the trustee's understanding of the purpose and effect of each investment "in the context of the trust portfolio and as part of an overall investment strategy."[39] Although the new investment criteria no longer held a trustee as a guarantor of each investment, the subsection, in fact, created a higher standard for trustee investment performance. Subsection (b) of section 227 required that diversification, a critical component of Modern Portfolio Theory, be incorporated into a trustee's "investment strategy."[40] With the exception of ILIT's which generally hold just one policy of life insurance, asset diversification has become an essential and mandatory component of contemporary trustee investment models.

The Restatement Commissioners seemed to recognize the conundrum caused by replacing the traditional "prudent man" rule with the sophisticated trustee investment performance standards required under Modern Portfolio Theory. The new "investment" requirements demanded more expertise in financial theory and practice than many trustees possessed or would be capable of acquiring. A foreseeable consequence of the new standards would be an inability to secure the services of individuals or institutions willing to serve as trustees of private trusts. To avoid such a result, the Commissioners introduced the concept of "trustee delegation."[41]

In 1994, the National Conference of Commissioners on Uniform State Laws ("Commissioners") incorporated the Restatement-revised trustee investment management rules into the Uniform Prudent Investor Act ("UPIA").[42] Following the Restatement, the Commissioners substituted the Prudent Investor Rule for the Prudent Man Rule. Like the Restatement, the UPIA emphasized pru-

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[34] Uniform Prudent Investor Act, *supra,* Prefatory Note ("... a large and broadly accepted body of empirical and theoretical knowledge about the behavior of capital markets, often described as 'modern portfolio theory' "); Espirti and Peterson, *supra* section 12.02[1] footnote 11 ("Modern portfolio theory is an investment approach developed by Professor Harry Markowitz of the University of Chicago for which he won the Nobel Prize in Economics in 1990. This theory, which is quite complex, essentially states that if two investment portfolios have the same expected return, the one with the lower volatility should actually realize the greater rate of return of the two portfolios over time.") This follows from the mathematical approximation of the growth of compound wealth (compound average = arithmetic average – 1/2 variance); and, as a consequence, the rational investor maximizes the utility of terminal wealth by selecting the portfolio with the most favorable risk/return tradeoff. Evaluation of this tradeoff (as opposed to evaluation of investments in isolation) is of central importance in modern trust management.) *See also* Ellis James, B., Hartog, John A., Wolf, Kenneth S. and Gifford, L. Andrew, "Issues in Trust Administration and Experiences of Professional Trustees: Applying Prudent Investor and Principal and Income Act Adjustment Powers," *Estate Planning* 2005 (Continuing Education of the Bar, California, 2005).

[35] Restatement (Third) of Trusts: Prudent Investor Rule section 227 (1992).

[36] *Id.*

[37] *See*, for example, *Hatleberg v. Norwest Bank Wisconsin,* 678 N.W.2d 302 (WI App. 2004) ("…the duties of a trustee go beyond the four corners of the trust instrument.").

[38] Restatement (Third) of Trusts: Prudent Investor Rule section 227.

[39] *Id.*

[40] *Id.*

[41] *Id.*

[42] UPIA, *supra;* Spalding, Albert D., "Put Your Trust in Trustees," *Journal of Accountancy,* Vol. 186, No. 5 (Nov. 1998).

dence as the all-embracing standard by which a trustee's investments were to be evaluated. UPIA subsection 2(a) provided:

> A trustee shall invest and manage trust assets as a prudent investor would by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill and caution.[43]

In UPIA subsection 2(a), the Commissioners significantly broadened the criteria by which investment decisions were to be judged. Again echoing the Restatement, the UPIA required a trustee to consider the terms and conditions set forth in the declaration of trust, the actual circumstances in which the trust was to operate and the needs of the beneficiaries.[44] The Commissioners formally extended a trustee's horizon beyond the four corners of the trust. Notwithstanding the expanded reference scope, the use of the word "caution" reinforced the traditional and necessary conservatism which a trustee had to display in its financial management of trust assets.[45]

The UPIA fully embraced Modern Portfolio Theory by incorporating "five fundamental alterations in the previously accepted standards for prudent investing." The "new" UPIA investment principles were: 1) trust assets should reflect sound diversification to minimize risk; 2) since risk and return were related, trustees should analyze risk in terms of contribution to portfolio performance; 3) fees and costs should be reasonable and minimized to the extent consistent with the trust's investment strategy; 4) the trustee should balance income production against principal maintenance and appreciation because of the trustee' duty of impartiality; and 5) the trustee should, and might have, a duty to delegate its investment management responsibilities.[46]

UPIA subsection 2(b) provided that a trustee's performance was to be assessed with reference to the "trust portfolio as a whole" rather than in relation to the profitability of each individual investment.[47] UPIA subsection 2(c) listed eight factors which a trustee had to consider in making investments. These factors included: 1) economic conditions; 2) the possible effects of inflation or deflation; 3) the tax consequences of any act; 4) the total return anticipated from the portfolio; and 5) the liquidity needs of the trust and its beneficiaries.[48]

While the UPIA released a trustee from the duty of guaranteeing the profitability of each investment, its articulated investment standards were complex and comprehensive. To succeed under the UPIA, a trustee had to possess a mastery of financial theory and its application(s) and access to the sophisticated financial tools necessary to support required financial and economic asset analysis. In the words of one author, in evaluating assets and asset performance under the UPIA, "Generally a trustee must: 1) employ the generally accepted standards of objective quantitative and statistical analysis; and (2) conduct analysis according to the financial evaluation principles embodied in modern portfolio theory.[49] Other commentators observed that "The fiduciary must exercise 'care, skill and caution' in order to assure that the advice is prudent and suitable. If 'care' can be defined as extensive consideration before committing trust assets to a particular course of action; if 'skill' can be defined as expertise in financial economics and the statistical and quantitative methods underlying Modern Portfolio Theory; and if 'caution' can be defined as an unbiased and critical examination of the likely monetary effects of asset management decision, then the fiduciary or the agents of the fiduciary must demonstrate competency in these areas."[50] Given the responsibility to act prudently, a trustee would have to evaluate potential investments against each of the UPIA subsection 2(c) factors, and then create a record reflecting both the evaluation and the action taken in accordance with such evaluation. Like the Restatement, the UPIA's authorization of trustee delegation of investment duties presented a reasonable alternative for trustees who, for whatever reason, declined to accept responsibility for managing a trust's investments.

§1.4.2 UPIA Governs ILIT Investment Management; State Legislative Exemptions: Settlor Intent and Other Attempted Trustee Exculpation

Legislative efforts to reconcile the disparity between accepted UPIA standards and existing ILIT trustee practices can be best characterized as ineffec-

[43] UPIA, Section 2(a)

[44] UPIA, *supra*, Section 2(a). Section 4.1 of this article discusses Office of Thrift Supervision regulations suggesting that certain savings association ILIT trustees may be responsible for determining the adequacy of insurance coverage with respect to the needs of the beneficiaries and the goals of the grantors. The OTS appears to extend a trustee's duty to obtain adequate property and casualty insurance coverages into the life insurance area as well.

[45] UPIA, *supra,* Section 2(c).

[46] *Id.*

[47] UPIA, Section 2.

[48] *Id.*

[49] Weidenfeld, *supra* at 5; *see also,* Teitelbaum, *supra* at 42-43.

[50] Avery, Luther J. and Collins, Patrick J., "Managing Investment Expenses: Trustee Duty to Avoid Unreasonable or Inappropriate Costs," *ACTEC Notes* (Fall 1999), p. 124.

tive. In large part, such attempts have relied upon Restatement section 22l which provides that section 227's requirements are expressly subject to "contrary investment provisions of a trust or statute."[51] For the most part, the state legislative approach has been to attempt to exempt an ILIT trustee from some or all of the UPIA requirements.

A Maryland statute excuses a trustee from evaluating insurance assets held as part of a trust corpus.[52] A Pennsylvania statute seeks to protect an ILIT trustee by providing that a trustee will not be held accountable for loss arising from the acquisition or retention of a life insurance policy as a result of a trustee's failure to: 1) determine whether the contract is, or remains, a proper investment; 2) investigate the financial strength of the insurance company; 3) exercise a non-forfeiture provision available under the contract; or 4) diversify the contract.[53] Since the Pennsylvania statute negated most of an ILIT trustee's investment management responsibilities, the risk of loss for inadequate or negligent investment management shifted to the beneficiaries. Under a Florida statute, an ILIT trustee which delegates its investment management responsibilities to an agent has no continuing monitoring duties for either the insurance held in the trust or the designated agent.[54]

In California, the state legislature appears to have sought a balance between the competing interests of an ILIT trustee and trust beneficiaries. Section 16048 of the California version of the UPIA ("California Act") provides:

> In making and implementing investment decisions, the trustee has a duty to diversify the investments of the trust unless under the circumstances it is prudent not to do so.[55]

If charged with a breach of trust for failing to perform its UPIA investment management responsibilities, a California ILIT trustee might advance the statutorily-sanctioned "prudence" defense emphasizing the circumstances existing as of the date(s) of the alleged breach.[56] Both the difficulty of establishing prudence and of excluding the influence of subsequent events undercuts efficacy of the defense.

Notwithstanding the statutory defense available to a California ILIT trustee, current ILIT operational practices weaken its effectiveness. Even if an ILIT trustee wanted to implement UPIA investment standards, the attempt probably would not be successful. Most settlors desire to maintain control over an ILIT-held insurance policy and correspondingly are reluctant to incur realistic administrative costs. The ILIT settlor's retention of de facto power over the ILIT creates an untenable situation for the trustee. In the event of beneficiary dissatisfaction with almost any aspect of the ILIT's investment management, (*e.g.,* insufficient proceeds upon the death of the insured settlor), the ILIT trustee could be charged with breach of trust. The "prudence" defense seemingly would have to incorporate continued settlor control and virtual management. In light of the express UPIA mandates and (presumably) the trustee fiduciary duties set forth in most declarations of trust, the prudence defense would seem difficult to establish.

One comment to section 227 elaborates upon a settlor's ability to alter prescribed statutory investment management provisions. The comment provides that the clause "terms of the trust" is to be "broadly defined to include intentions of the settlor manifested in any way that admits of proof in a judicial proceeding."[57] To further facilitate a settlor's efforts to communicate intent, the comment continues: "Thus, the trust terms, expressed and implied, may be derived from written or spoken words, circumstances surrounding the establishment of the trust, and sometimes, statutory language that is automatically imported into the trust or by which some trusts are established."[58]

The UPIA relying upon Restatement principles also authorizes a settlor to override investment management provisions by providing:

> The prudent investor rule, a default rule, may be expanded, restricted, eliminated, or otherwise altered by

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[51] UPIA, Section 1(b).

[52] Code section 15-114 (c), Maryland Annotated Code *(Estates & Trusts). See also* Collins, Patrick J., "Statutory Exemption From Fiduciary Liability for Trustees of Life Insurance Trusts," *Maryland Bar Journal* (January/February, 2000), pp. 54-58. The reader is cautioned that several printer errors change the meaning of certain sentences and paragraphs. The article points out that the statutory exemption is limited; and that, in the event of policy underperformance or lapse, it would be difficult to determine whether the cause flows from failure to perform an exempt duty or from a breach of a non-exempt duty (*i.e.,* payment of unjustifiably high commissions for product acquisition and maintenance).

[53] Pennsylvania Consolidated Statutes, Title 20, Chapter 72, Sections 7201-7214.

[54] Florida Statutes, Title XXXIII, Chapter 518.112.

[55] The Uniform Prudent Investor Act (California Probate Code, sections 16045-16054) Thompson*West, 2005, enacted in 1995 became effective on January 1, 1996.

[56] *Id.* at section 16051.

[57] Restatement (Third), *supra;* "Trustee Administration Powers: Drafting Considerations," fender.ceb.ucop.edu?Reporters/gateway.dll/.../001.

[58] Restatement (Third), *supra. See also* Restatement (Third) of Trusts: Prudent Investor Rule section 229, Reporter's Notes on Comments c and d (trustee held liable for failure to diversify despite express settlor authorization).

> the provisions of a trust. A trustee is not liable to a beneficiary to the extent that the trustee acted in reasonable reliance on the provisions of the trust.[59]

Like several other states which have enacted the UPIA, the California legislature acknowledged a settlor's power to alter the UPIA's investment criteria and requirements. In California Probate Code section 16046 (b), the legislature granted a settlor the right to expand or to restrict the provisions of the Prudent Investor Rule.[60] Foreseeing interpretation disputes in the event of such settlor action, the legislature also sought to protect a trustee which, in good faith, relied upon settlor-created deviations from standard investment rules.[61] A fair summary of the California legislature's intent would appear to be that maximum protection is to be afforded to both settlor and trustee when the settlor alters the basic investment rules and the trustee exhibits good faith in attempting to adhere to such settlor directives.

Given the current litigious environment, a state legislature's approval of the right of a settlor to change a trustee's statutorily-mandated investment duties may not afford sufficient trustee protection in the event that an ILIT beneficiary sustains economic loss for which the ILIT trustee may be held accountable. If a settlor attempts to vary the fundamental UPIA guidelines, caution dictates that the trustee seek prior court approval.

In addition to the "shield" afforded by any relevant state statute(s), a trustee may want or demand more specifically tailored protections. These might include special trust provisions or even a separate agreement that provides trustee protection through settlor indemnity, exculpation or insurance.[62] Settlor granted exculpation often is limited by case law or statute providing that a settlor cannot insulate a trustee from an intentional breach of trust or excuse a trustee's failure to perform an explicit duty or responsibility as set forth in the trust.[63] Given the express statutory provisions describing a trustee's investment management responsibilities, the efficacy of settlor exculpation may be limited. Perhaps, a more realistic assessment of the effect of an exculpatory clause is that it acts as cumulative or supplemental security for a trustee rather than as a firm shield or defense.[64]

Courts vary broadly in their interpretations of settlor exculpatory clauses excusing trustee compliance with a statutory prescription or mandatory fiduciary duty. While appearing to give token respect, courts and beneficiaries seem to ignore the latitude which statutes accord to settlor intent and good faith trustee reliance. Since a trustee is a fiduciary, courts tend to evaluate a trustee's performance strictly and to regard settlor exculpatory language as inconclusive.[65]

In the ILIT context, no authority has been found as to the weight which a court should accord to an exculpatory clause in determining whether a trustee should be surcharged for failure to comply with UPIA standards, including the diversity requirement.[66] Notwithstanding the difference which purportedly should be given to a settlor's express intent, the trustee still might be subject to surcharge if a court were to consider diversification as a non-delegable duty. Since the protection afforded by an exculpatory clause might be less than adequate, some commentators have suggested that the most effective protection would be prior court or beneficiary consent.

§1.4.3 Care and Skill Standards for Different Types of Trustee

Restatement section 227 prescribes the standards that a trustee's performance must satisfy. To implement the standards, the Restatement established a test in which a trustee's performance is compared against that of a hypothetical "prudent investor" who exercises "reasonable care, skill, and caution."[67] Section 227's comment expands upon the intangible and fluid nature of the performance standard. It juxtaposes distinct performance expectations for trustees with differing capacities, a non-professional trustee as exemplified by a settlor's family member or friend as compared with an institutional trustee. The comment provides in relevant part:

> The standards of trusteeship are neither excessively demanding nor mono-

[59] UPIA, *supra* at Section 1(b).

[60] California Probate Code, section 16046 (b), Thompson* West, 2005.

[61] *Id.*

[62] Fedner, *supra.*

[63] Esperti and Peterson, *supra* 12.02 [3]; Trusteeship of Williams, 591 NW 2d, 743 (Minn. App. 1999); Weidenfeld, *supra* at 10; *see also* California Probate Code section 16202.

[64] *See also* Collins, Patrick J., "The Lawyer As Trustee: Do Exculpatory Provisions Mitigate Liability Under Prudent Investor Standards," *Maryland Bar Journal* (January/February 2003), pp. 48-50.

[65] Esperti and Peterson, *supra.*

[66] Restatement (Third), section 227, comment g. *See* Collins, *supra* at 9, for a discussion of possible defenses based upon section 227 g comment. *See also* Collins, Patrick J., "Observations On Life Insurance Trusts and The Prudent Investor Rule," *Insurance Law* (Spring 1999), p. 7; and, Collins, Patrick J., "Diversification: Recent Legal and Academic Perspectives," *California Trusts and Estates Quarterly* (Fall 2003).

[67] Restatement (Third) section 227.

> lithic. They should neither effectively preclude service by conscientious family members and friends nor permit casual, inattentive behavior by trustees who can, because of their expertise, meet a higher than ordinary standard of conduct and competence. Thus, the applicable requirements of care and skill allow responsible individuals of ordinary intelligence to serve as trustees and to adopt reasonable investment strategies of types that are appropriate to their skills. Yet the standards require fiduciaries possessing special facilities and skills to make those advantages available to the trust and its beneficiaries.[68]

The Restatement Commissioners envisioned a two tiered investment management system. In contrast with the lenient standard acceptable for the non-professional trustee, the Restatement required that an institutional trustee had to "possesses a degree of skill greater than that of an individual of ordinary intelligence" and was to be liable for loss that resulted from a failure to make diligent use of that skill.[69] The higher standards may be applicable to certified financial planners and lawyers who act as trustees.[70] A lawyer who not only prepares an ILIT, but who also advises a client about insurance products may be deemed to have abandoned the counselor's role for one which subjects the attorney to a higher performance standard.[71]

Although the UPIA requires a trustee with special skills or expertise to use such attributes for the benefit of its trust and beneficiaries, the UPIA does not distinguish between professional and non-professional trustees as to the standards under which performance is to be evaluated. The difference between performance expectations and standards by which to evaluate such performance is subtle but important. Under Modern Portfolio Theory, all trustees are to be evaluated by one objective investment management standard.[72] The application of consistent criteria to all trustees represents a major departure from traditional trust law and would have created a patent unfairness for non-professional trustees, but for the delegation option which became an equalizer for the various performance skill levels of professional and non-professional trustees.[73]

Although this article's major focus is upon ILITs, the authors' broader concern is with the investment management of life insurance policies held in any type of trust. Regardless of whether a family/friend or professional acts as trustee of an ILIT or other trust holding life insurance, the UPIA standard means that a trustee is expected to possess a sophisticated knowledge of the insurance industry, issuers, policy types and finance in general. More specifically, an ILIT trustee is expected to have the ability to evaluate the policy issuer; the current and prospective economic viability of the life insurance policy; the likelihood of the policy proceeds satisfying the objectives and needs of the trust and its beneficiaries, and competing insurance products.[74]

As part of its investment management duties, an ILIT trustee should diversify trust assets. If an inter vivos trust contains a life insurance policy and other assets, the trustee should be capable of assessing the life insurance policy with evaluative tools comparable to those employed for other trust held assets. If an individual or institution serves as trustee of several different settlor-created trusts, *e.g.,* an ILIT and a revocable inter vivos trust, a trustee might be justified in regarding the ILIT-held policy as a composite part of an asset pool, each asset of which contributed to proper asset diversification.[75]

When an ILIT is funded with the usual one life insurance policy, the diversification requirement presents an implementation issue. Standard diversification usually contemplates allocation of assets within a wide spectrum of possible investments. One approach to satisfying the diversification requirement for ILITs would be for the trustee to strive for vertical diversification within the single asset class of life insurance

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68 *Supra,* Comments & Illustrations.

69 *Id.*

70 UPIA, Section 2(f); Spalding, *supra*; Teitelbaum, *supra* at 41 argues that the UPIA by implication suggests that a different evaluative standard may apply to a professional versus a non-professional trustee; Schultz Collins Lawson Chambers, Inc., "The Lawyer As Trustee: Duties With Respect to the Inception Assets," Fiduciary Forum Vol. 8, Issue 1, March 2004 at www.schultz-collins.com.

71 Weidenfeld, *supra;* Esperti and Peterson, *supra* at paragraph 12.02[3]. *See* §4.1 of this article for a discussion of standards for ACTEC fellows acting as trustees.

72 *But see* Schultz Collins, *supra* (difference in ability levels of professional/institutional trustees versus friend-type trustee continue to influence evaluation of trustee performance). Neither Restatement (Third) nor this essay suggests that there is only a single "path to prudence" which demands that all trustees use the same portfolio optimization algorithms, risk measures, comparative benchmarks, etc.

73 Rief, Frank, J. III, "Life Insurance Planning Techniques," *ALI-ABA Course of Study Materials* (1999).

74 Harris and Prince, *supra;* Teitelbaum, *supra.* Part II of this article discusses the reasonableness of such expectations and the likelihood that a trustee can successfully discharge the tasks of policy evaluation and carrier solvency forecasting.

75 Collins, Patrick J., *supra* at 9; Weidenfeld, *supra;* Esperti and Peterson, *supra.*

policies. Instead of relying upon different assets mixes a ILIT trustee could diversify within the asset class by purchasing several different types of policies from various issuers.[76]

A practical limitation inherent within the proposed ILIT diversification model would be the likely increase in administrative costs, particularly premium costs. Under Restatement section 227 and the UPIA, a trustee can incur only reasonable costs in its trust administration.[77] The consideration, particularly in light of current practices, is whether the additional costs, which ILIT diversification almost certainly would necessitate, would be justified. Although an ILIT's administrative costs may increase as a result of purchasing or maintaining several life insurance policies, the long-term economic protection achieved through such diversification should justify the additional costs. If potential litigation expenses are also considered, increases in administrative expenses may prove to be much less than would appear at first.[78]

§ 1.5 A TRUSTEE'S DELEGATION OPTION

Under the original formulation of The Prudent Person Rule, a trustee could not delegate its investment management responsibilities.[79] The Restatement changed the historic norm.[80] In section 227 (c) (2), the Commissioners authorized a trustee to delegate its investment management duties to a qualified agent. Yet the Commissioners also insured that the change did not mean that a trustee could abandon total responsibility for trust investments nor ignore its fiduciary duties to beneficiaries. Section 227 extracted a quid pro quo for permitting a trustee to delegate. The subsection required a trustee: 1) to adhere to certain formalities in making a delegation; and 2) then throughout the term of the delegation, to monitor the performance of the agent.[81] As a result of the Commissioners' adoption of new investment management standards, a trustee had a clear choice: either possess the requisite investment skill and knowledge for investment management as required by Modern Portfolio Theory or delegate such investment responsibilities to a qualified agent.

The Restatement comment to §227 explained the prudence that a trustee must exercise in delegating its investment management responsibilities:

> Prudence thus requires the exercise of care, skill and caution in the selection of agents and in negotiating and establishing the terms of delegation. Significant terms of delegation include those involving the compensation of the agent, the duration and conditions of the delegation and arrangements for monitoring or supervising the activities of agents.[82]

The UPIA incorporated the Restatement concept of permissible trustee delegation and by so doing, formally signaled the demise of the non-delegation rule of investment management responsibilities. After authorizing trustee delegation of investment management duties, UPIA §9 further provided:

> The trustee shall exercise reasonable care and skill, and caution in: (1) selecting an agent; (2) establishing the scope and terms of the delegation, consistent with the purposes and terms of the trust; and (3) periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the terms of the delegation.[83]

By embracing the "delegation" concept, both the Restatement and the UPIA seemingly sought to forestall a readily foreseeable consequence of the more exacting investment management performance standards. Investment standards that were both difficult to accomplish and that portended increased risk for failure to do so might deter otherwise qualified individuals and institutions from serving as trustees. By permitting a trustee to delegate its investment management duties, the 1992 Restatement sought to insure that the pool of trustees remained undiminished. To emphasize the importance of the new investment management alternatives (either possessing the necessary investment management skills or delegating the

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[76] *Id.;* Zaritsky, Howard M. and Leimberg, Stephen F., *Tax Planning With Life Insurance* 2nd. edition (Warren Gorham & Lamont, 1999/2000); *see also,* Henkel, Kathryn G., "Life Insurance in a Qualified Plan," *Estate Planning and Wealth Preservation: Strategies and Solutions* (Thomson RIA, 2005) at www.Thomson.com.

[77] Restatement (Second) of Trusts, Section 171 (1959).

[78] *See* §4.3 of this essay (Diversification and Investment Policy) for further discussion. *See also* Collins, Patrick J., "Diversification: Recent Legal and Academic Perspectives," *California Trusts and Estates Quarterly* (Fall 2003).

[79] UPIA, *supra* Section 9, Comment ("The former nondelegation rule survived into the 1959 Restatement....").

[80] Restatement (Third) of Trusts; Prudent Investor Rule, Section 227 (c).

[81] *Id.*

[82] *Supra* at Section 171, Comment a (1992).

[83] UPIA, *supra* at section 9.

responsibility), the Commissioners did more than just authorize trustee delegation. They imposed a duty upon trustees to delegate investment management duties in those situations where it was prudent to do so.[84] If investment management services were to be delegated, the Commissioners required a trustee to exercise prudence in its delegation.

In codifying the UPIA delegation option, the various state legislatures confirmed trustee delegation as a mainstay of modern fiduciary investment law. The California Prudent Investor Act[85] ("California Act") exemplified the manner in which states incorporated the UPIA delegation option. The California statute authorized trustee delegation while retaining the "prudence" safeguard originally set forth in the Restatement. California Act section16052 (a) provided, "A trustee may delegate investment and management functions as prudent under the circumstances."[86] The California statute further mandated that a trustee exercise prudence in the selection of the agent, memorialization of the trustee/agent agreement and continued monitoring of the agent's performance.[87] In exchange for strict observance of the delegation formalities, the California Act granted a trustee immunity from beneficiary complaints about an agent's acts.[88]

§ 1.6 DELEGATION MECHANICS

As part of the process of designating an ILIT trustee, the settlor and the trustee should determine whether the proposed ILIT trustee possesses the investment management skills required by the UPIA. If a proposed trustee does not possess such skills, the settlor and the trustee should agree that the trustee is not to perform investment management services, but rather that the trustee will appoint a qualified agent to manage the life insurance policy(ies) to be held in the ILIT. In light of the delegation, the settlor and trustee should specify the remaining duties of the trustee; trustee compensation; and the reporting responsibilities of the trustee. Trustee compensation should be commensurate with the trustee's decreased duties.[89] The settlor should not directly compensate the agent. The UPIA requires that the trustee designate the agent and be in privity with the agent.[90]

Once the ILIT has been prepared, but preferably prior to its implementation, a trustee intending to delegate its investment management duties should identify an agent and conclude formal arrangements with that agent. To illustrate due diligence in the selection of the agent, the trustee should 1) interview several agents; 2) obtain information about the agent's education and experience; and 3) contact and interview the agent's references. The trustee should document thoroughly the investigative and other efforts that it made in identifying the agent. [See Exhibit 1]. A trustee also should consider other steps to demonstrate its due diligence in the appointment process such as ascertaining the agent's ability to respond to damages. Since prudence is a subjective standard, the trustee should seek court instructions if uncertain about any aspect of the delegation (*e.g.,* the memorialization of the delegation, the allocation of compensation between the trustee and the agent, or the respective post delegation duties of the trustee and the agent).

By the act of delegation, the trustee shifts the risks inherent in the investment management of any trust-held asset to the agent.[91] From a beneficiary's perspective, one result of such delegation might be that accountability for proper investment management would be more difficult to assess and possible recovery for malfeasance in the performance of managing trust assets more difficult to achieve. Substantial agent compliance requirements incorporated into a delegation agreement might facilitate several objectives including bolstering trustee defenses and greater protection of beneficiary interests.

The trustee should insure that the agent understands the nature and scope of its duties and its obligations under local state law. For example, the California Act imposed specific duties upon the agent, including "the duty to exercise reasonable care to comply with the terms of the delegation."[92] The California Act incorporated, almost verbatim, the UPIA provision governing the investment management responsibilities of an agent. Another duty that the California Act imposed upon the agent was the requirement that the agent submit to the jurisdiction of the California courts.[93] Although the California Act reiterated the

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[84] Weidenfeld, *supra.*

[85] California Probate Code, Section 16045 (Thompson* West 2005).

[86] California Probate Code, Section 16052.

[87] *Id.*

[88] *Id.; but see* Office of the Attorney General of the State of California, Opinion, 1996 Cal, AG Lexis 13; 79 Op. Atty Gen. Cal. 88 (June 19, 1996).

[89] UPIA, *supra* at Section 9, Comment (Costs). *See also* Anderson, R.L. and Hoisington, W.L., "Practical Applications of the Prudent Investor Standard," *Proceedings of the New York University 56th Institute on Federal Taxation* (New York University 1998) §29-18.

[90] *Id.*

[91] *Id.*

[92] California Probate Code, Section 16052.

[93] *Id.*

jurisdictional provision set forth in the UPIA, the consequence of that provision might be to preclude agents which are part of major national firms or which reside in states other than California from serving as agents of California trustees.

Concurrently with the execution of the ILIT or other declaration of trust, the trustee and the agent should execute an agreement. Their written agreement should contain the standard terms and conditions found in most performance contracts such as: 1) performance expectations and goals; 2) periodic review and evaluation of the agent's performance; 3) agent compensation; 4) the frequency and type of agent reporting; 5) records the agent should maintain; 6) the consent of the agent's employer, if any; 7) the term of the agreement; 8) termination causes and procedures; and 9) remedies and procedures in the event of the agent's breach. The agreement also should set forth the agent's statutorily-imposed duties and the agent's acceptance of the same; the agent's acknowledgment of the privity which exists between the trustee and the agent and the agent's consent to submit to the jurisdiction of the state courts. If the agent is to maintain performance insurance, the agreement should provide that proof of such coverage should be submitted to the trustee not less frequently than annually.[94] [See Exhibit 2].

The trustee and the agent should discuss possible agent conflicts of interest; and, if any exist, they should be either waived or otherwise resolved. An insurance agent which sold a policy of insurance to the trustee or which received annual residuals as a result of a prior sale to the settlor should not act as the trustee's agent. The potential for a conflict of interest would be too substantial.[95] [See Exhibit 3]. The trustee should never agree to indemnify the agent. Although the direct relationship is between the trustee and the agent, the trustee should consider giving either or both the settlor and the beneficiaries the opportunity to interview the proposed agent and to voice any objection to the agent prior to the finalization of the agency agreement. In the event that the trustee believes that the settlor or one or more beneficiaries may be antagonistic to the proposed agent, the trustee should insist that such beneficiaries have independent counsel. If the objecting beneficiaries do not consent to the agent's service, then either a new agent should be retained or the trustee should seek instruction from the court.

Not less frequently than annually, the trustee should review the performance and acts of the agent.[96] The agent should provide an annual written report in which any trust-held life insurance policies are evaluated in terms of UPIA investment management criteria.[97] The trustee should determine whether the agent's reports and the trustee's evaluation of the agent should be distributed to the settlor, to the beneficiaries or to both. If the trustee does distribute the agent's report or the trustee's evaluation, the trustee should provide a reasonable period for comment or objection and state that if none is received within the stated period, that the distributed materials are deemed approved. If any objection were received, the trustee would have to determine whether court instruction should be sought.

§ 1.7 CONCLUSION

In the authors' opinion, the UPIA requires investment management of a life insurance policy held in an ILIT. A trustee who is charged with responsibility for a life insurance policy must manage that policy just as it would any other trust investment. Since the UPIA only endorses one investment standard against which to evaluate a trustee's investment management, the objective investment evaluative criteria apply regardless of whether a trustee is a family member or friend of the settlor or a professional or institutional trustee. An ILIT trustee either should possess the requisite investment management skills or should delegate its investment management duties.

In accordance with Modern Portfolio Theory, the usual single ILIT asset, a policy of life insurance, should, in general, be diversified. Diversification could be accomplished through vertical integration, that is, with the purchase of more than one life insurance policy from more than one carrier and with each policy displaying varying characteristics.[98] If an ILIT trustee lacks the requisite investment management skills, the trustee should appoint an agent. The ILIT trustee should observe the UPIA standards in both the original retention of the agent and during the continued term of the agent's service. With respect to the three basic ILIT trustee scenarios, it is postulated that the form in which the trustee retains standard trust powers except for those relating to or concerning

[94] *See* §4.4.2 of this essay for a discussion of an agent "service contract."

[95] *See* the discussion regarding conflict of interest in § 2.5.2 of this article.

[96] *Id.* For a discussion of prudent delegation in the qualified retirement plan context, *see* Matta, Richard K., "Re-Thinking The Investment Consulting Model: Hiring A Co-Fiduciary 'Manager-of-Managers'" at www.groom.com. Matta argues that prudent delegation requires an ERISA plan consultant to acknowledge a "co-fiduciary" role.

[97] *See* Part Three of this article for an example of an insurance evaluation report.

[98] *See* the discussion of an asset allocation matrix in the sample Investment/Insurance Policy Statement presented in this article.

investment management of a life insurance trust will become standard.

The authors recognize that diversification more likely than not will result in an overall increase in the cost of establishing and maintaining an ILIT. ILIT settlors might be resistant to the increased administrative and operational expenses which UPIA compliance is likely to generate. Yet, UPIA compliance ultimately might prove to be the least expensive alternative for settlors and their trustees.

EXHIBIT 1

Annual ILIT Trustee Investment Management Checklist

Year__________

I. Life Insurance Polices Held in Trust.

1.1 The following policy(ies) of life insurance is/are held in trust:

1.1.1 ____
1.1.2 ____
1.1.3 ____

1.2 Other assets held in trust:
____
____
____

II. Basic Factors Considered by Trustee.

With respect to the/each life insurance policy(ies) identified in I above, the Trustee has considered each of the following factors:

2.1 The guidelines set forth in the Trust's Investment Policy Statement.

Date___________ Initials:_______________

2.2 The present and future needs of the Trust and its beneficiaries in terms of the Trust's purposes and objectives.

Date___________ Initials:_______________

2.3 The Trust's present and anticipated financial requirements.

Date___________ Initials:_______________

2.4 General economic conditions.

Date___________ Initials:_______________

2.5 The current ratings assigned to the insurance carrier(s).

Date___________ Initials:_______________

2.6 Diversification of the trust's assets.

Date___________ Initials:_______________

III. Other Factors Considered by the Trustee.

3.1 Various other factors that should be considered in evaluating a trust's investments, including without limitation the role of each investment; total expected return from the investment; the significance of a particular asset to the trust's purpose.

Date___________ Initials:_______________

3.2 Additional Trustee Notes and Comments.

____
____
____
____
____

IV. Confirmation of Decision-Making Procedures.

4.1 Each decision was made after a good faith determination, and based upon a reasonable belief, that such decision was in the best interest of the Trust.

Date___________ Initials:_______________

4.2 All inquiries were made that appeared reasonable in order to make an informed, good faith decision on the matter.

Date___________ Initials:_______________

4.3 All reasonable inquiries have been made that an ordinarily prudent person would have made under the circumstances.

Date___________ Initials:_______________

4.4 Before relying on information, opinions, reports, or statements prepared by another, a determination was made as to the reliability and competency of the preparer and reasonable inquiries were made that an ordinarily prudent person would make under similar circumstances.

Date___________ Initials:_______________

4.5 Before relying on information, opinions, reports, or statements prepared by another, the Trustee had no knowledge that would have caused such reliance to be unwarranted.

Date___________ Initials:_______________

4.6 Before relying on information, opinions, reports or statements, including financial statements and other financial data, prepared or presented by another person or entity as to the matters which the Trustee believed to be within such other person's professional or expert competence, all reasonable inquiries were made that an ordinarily prudent person would have made under similar circumstances.

Date___________ Initials:_______________

4.7 Before relying on information, opinions, reports or statements, including financial statements and other financial data, prepared or presented by another person as to matters which the Trustee believed to be within such other person's or entity's professional or expert competence, the Trustee had no knowledge that would cause such reliance to be unwarranted.

Date____________ Initials:________________

4.8 Notes:

____
____
____
____
____

Trustee Declaration.

The Trustee declares under the penalty of perjury under the laws of the State of ___________________ that the foregoing is true and correct.

Executed this ______ day of _________, 2_______ at ________________, _____________________.

____
Trustee

EXHIBIT 2

Annual Checklist of Fiduciary Duties for Trustee in Delegating Investment Responsibilities

Year_______________

1. The Trustee reviewed its decision with respect to the appointment of the agent and either: (a) confirmed that the agent continued to be competent and reliable and that the agent merited the Trustee's continued confidence with respect to the delegation; or (b) that the current agent no longer satisfied the above criteria and that the Trustee forthwith would terminate the services of the instant agent; assume permanent or interim investment management decisions and/or would identify, evaluate and appoint another agent.

   Date___________ Initials:_______________

2. Before relying on information, opinions, reports or statements prepared by the agent, the Trustee made such reasonable inquiries as would have been made by an ordinarily prudent person under similar circumstances.

   Date___________ Initials:_______________

3. Before relying on information, opinions, reports or statements prepared by the agent, the Trustee had no knowledge that would cause such reliance to be unwarranted.

   Date___________ Initials:_______________

4. The Trustee conducted its annual review of the general investment policies and working investment guidelines of the Trust, evaluated policy performance against appropriate benchmarks and made any adjustments or alternations to policies and guidelines that were deemed needed.

   Date___________ Initials:_______________

5. Additional Trustee Notes and Comments:
   ____
   ____
   ____
   ____
   ____

Trustee Declaration.

The Trustee declares under the penalty of perjury under the laws of the State of __________________ that the foregoing is true and correct.

Executed this ______ day of _________, 2_______ at ________________, _____________________.

____

Trustee.

EXHIBIT 3

Agent Information and Disclosure Checklist

1. Do you have a "W-2" employment relationship with any insurance carrier?
2. Does any insurance carrier impose minimum insurance production requirements (life only or life plus other lines) in order to keep your employment contract in force?
3. Is a copy of your contract available for inspection?
4. Other than cash compensation and customary employee health/pension benefits, does the company provide sales incentives such as trips and prizes for sales production?
5. Does your primary carrier require a "first right of refusal" for insurance applications?
6. If you do not have a "W-2" employment relationship with any insurance carrier, do you or the firm which employs you, receive income under a General Agent's contract or a "Personal Producer/Bonus" contract?
7. If yes, does the carrier(s) impose minimum insurance (life only or life plus other lines) production quotas in order to keep the contract in force?
8. Are you a member, affiliate or partner in a "Special Producers Group?"
9. In conducting an insurance analysis, will you receive compensation only if an insurance transaction occurs?
10. Will you charge a fee for your insurance/planning services?
11. Are you a Registered Investment Advisor?
12. Have you ever had any professional, securities, or insurance licenses suspended, restricted, or revoked in any state?
13. Has the California Department of Insurance received complaints regarding your work activities?
14. Has the California Department of Insurance held a hearing regarding consumer complaints?
15. Please describe briefly your rebate policy (if any) for California life insurance buyers.
16. Do you include in your insurance analysis policies which are "no-load / low-load"?
17. Do you include in your insurance analysis "variable life" policies?
18. Have you ever been the subject of SEC or NASD disciplinary actions?
19. Other than through a mutual fund or unit investment trust, do you own the securities of any life insurance or reinsurance company?
20. What is your educational background and what professional degrees & designations do you hold?
21. For all insurance products which you recommend, illustrate, compare, or discuss, please indicate the first-year and renewal commissions (if any) that you will receive if the product is put into force and the premiums are paid.