

Uniform Prudent Investors Act (UPIA)

The purpose of this “white paper” is to help trustees better understand their fiduciary duties when accepting the position of Trustee. It is meant as an educational tool for our advisory community to use with their clients. Trusteeship itself is a serious matter that I believe, based on discovery and 25 years of experience, within the context of Irrevocable Insurance Trusts (ILIT), is not fully comprehended.

The UPI Act: The Dilemma for Trustees

As trustee you are ultimately responsible to the trust beneficiaries for the performance and management of the assets that reside in the trust under your care. So let me ask:

- How will you substantiate to your beneficiaries a standard of care in managing the life insurance property in your care?
- What process will you employ to demonstrate your duty to exercise reasonable care, skill and caution in managing the life insurance property?
- Who will you delegate this too? Who will you turn to for an objective opinion?
- What will happen if the life insurance asset “dies” before the Grantor?
- How will you fulfill your duty to monitor the suitability of such an asset of life insurance over the next 10, 20 or even 30 years?
- What process do you employ to fulfill your duty to investigate the components of life insurance that will likely bear importantly on the success of such an investment of capital?
- How will you go about optimizing return on the capital invested in the life insurance property?

In fulfilling these and other duties (appendix A) ¹ let me just say that ***prudence is a process not a result.***

1. Upon request Appendix A may be forwarded to you. This document explains all the duties of a trustee; Investing and Managing Trusts, John Train and Tom Melfe

The Problem

It’s getting more difficult for trustees to exercise prudent fiduciary responsibility in the life insurance arena. They must contend with developments affecting the policy’s performance such as: a premium continuing beyond illustrative assumptions, new product developments, expense analysis, mortality changes and changes in the law pertaining to their duties and what is expected of them.

For many trustees, life insurance is a “black box” - something they do not understand. The trustee usually does not have the knowledge, experience, or skill set to do a proper analysis. Trustees’ failure to adequately manage or administer life insurance can have a major, adverse impact on the death benefit they are supposed to be safe guarding for the beneficiaries.

According to surveys conducted, it has been shown that a glaring percentage of trustees do not have any stated guidelines, procedures, or processes in place to manage this valuable property. Those that do, I would contend, are frustrated with the lack of analytic tools that have some actuarial basis that can be utilized to document their attempted management of the life insurance property. Over 95% of trustees do not have a stated life insurance property management statement or, as it is more commonly referred to, an investment policy statement, that sets the parameters by which to judge the life insurance in the trust.

As stated above, prudence is a process, not a result. In your fiduciary capacity as trustee let me suggest that we at **The Efficient Edge** can help you fulfill your duties with our Life Insurance Property Management (LIPM) System based on proprietary, actuarially certified, insurance analytic processes that will allow you to optimize return on capital invested.

Who is The Efficient Edge?

- We are an actuarial based firm that is built on a fee-based platform that helps advisors and their clients optimize return on capital invested in life insurance.
- We bring a level of objectivity into a very product-centric environment only possible if the life insurance advisor assumes a fiduciary role and provides full transparency and full disclosure with the sole purpose of optimizing return, what we call looking through an “optimization lens”.
- We have built an insurance company outside the purview of the insurance industry
 - Former life insurance staffers who have designed product and thus are equipped to construct, reconstruct, or deconstruct product when necessary
 - Underwriting advocates, who have the experience to re-position medical files and conduct extensive pre-underwriting reviews. The benefit? This gives us the ability to negotiate as an advocate for the client whether we need to rehab the current coverage, consider new coverage, or explore the life settlement market
 - Life expectancy experts who give us the ability to meld together the probability of death and the probability of success of the actual policy
 - Expert witness and support litigation services
 - Advance market design expertise to better understand suitability

Reputation and litigation risk is usually the critical due diligence consideration in selecting a more robust firm with deeper capability. Professional fiduciaries and advisors are delegating an expertise and/or capability they do not have; hence, their priority is to select a firm that allows them to look at the right information in the right way that results in doing the right thing. Given the history of the commission-motivated life insurance sales and replacement schemes since the late 1970’s coupled with today’s lapsing policy environment, professionals are duty-bound to undertake a credible policy evaluation process that can withstand second opinion scrutiny. Therefore, to safeguard against litigation risk and its resulting reputation risk, you have to be able to have a firm or a process that can objectively with full disclosure and transparency, allowing the trustee to fulfill their duty of loyalty, not only identify risk components but also have the capability to build out a “decision option matrix” for remediation purposes, employ more sophisticated optimization strategies when necessary, and be hands-on.

To fully appreciate this safeguarding issue, it is important for you to differentiate factual risk-based evaluation from subjective illustration-based analysis. Illustration credibility issues for non-guaranteed policies were resolved in the early 1990's and subsequently integrated into the carrier illustrations. It is knowable by any licensed agent and policy administrator that illustrations for non-guaranteed policies are neither credible nor appropriate for predictive performance determinations or policy comparisons. Despite this fact, it is not uncommon for illustration-based administrators to market proprietary risk ratings that are not explainable much less credible (harsh but I am afraid true to the best of my knowledge).

As a practical matter, such ratings and policy comparisons are commonly used by life insurance agents to justify a replacement recommendation. This analysis, frequently referred to as a policy suitability analysis, must be differentiated from the product suitability determination expected of a professional fiduciary and based on trust objectives, Investment Policy Statement information, trustee risk management principles and policy evaluation criteria. A professional fiduciary is expected to undertake an annual investment review that identifies appropriate corrective action for review with the trust client. Hence, it is essential for a professional with fiduciary liability to select a firm that offers credible policy evaluation so that defensible product suitability determinations can be documented and reviewed with the client.