



## STEWARDSHIP OF TRUST-OWNED LIFE INSURANCE

The commonly held wisdom of most advisors is that anyone who has achieved a certain level of net worth (see appendix for thresholds) should place life insurance *inside* an irrevocable trust, thus increasing its value by removing it from the taxable estate.

Even though Trust-Owned Life Insurance (“TOLI”) offers clients a number of long-term planning benefits, very few of these policies ever meet their projections. Like every other asset, the ultimate disposition of these transfers is not guaranteed, and a positive outcome depends on how well the capital represented by the trust-owned policies is managed.

Ironically, most clients and many trust officers give little thought to the performance and actual value of life insurance held inside a trust. These assets are often left to languish in the portfolio when they could be actively managed for the benefit of the clients and their heirs.

### DANGERS AND RISKS

Although many trustees have experience managing trust-owned investment capital, few institutional trustees — and virtually no private trustees (wives, brothers, friends) — feel qualified to navigate the fiduciary territory of managing all the “moving parts” involved in the risk of policy and carrier performance.

### INDUSTRY STATISTICS

*Can trust-owned life insurance be trusted?*

- A 2004 industry study estimated more than 75% of cash value policies will not perform as originally illustrated and require some form of restorative action.
- Other studies estimate that 85% of existing TOLI policies could be restructured to provide 20% – 40% greater value.
- 43 states have a Uniform Prudent Investor Act setting standards for managing trust investments including life insurance.
- Yet more than 80 percent of trustees in one survey report they have no procedures for review, nor an exit strategy for underperforming policies.
- Roughly three quarters of trust-owned policies do not have active agents, and in nearly all cases, carriers do not support or compensate agents for audit, valuation or review.

The risk is in fact doubled. First for the client, if the policy does not support the estate plan (causing an erosion of the values the trust was intended to protect); and second, the fiduciary risk of the trustee if he or she does not initiate corrective action.

## A NEW PROFESSIONAL RESOURCE

Due to the availability of new products that offer lower costs, enhanced guarantees and greater flexibility, virtually all policies should be reevaluated. Even cash rich contracts that do not appear to be in jeopardy should be reviewed for policy structure and the utilization of capital (net amount at risk).

## APPENDIX

### The Dynamic Estate And Gift Tax Exemption

Year	Estate Tax Exemption	GST Tax Exemption	Max. Estate and GST Tax Rate	Gift Tax Exemption	Max. Gift Tax Rate
2003	\$1,000,000	\$1,120,000	49%	\$1,000,000	49%
2004	\$1,500,000	\$1,500,000	48%	\$1,000,000	48%
2005	\$1,500,000	\$1,500,000	47%	\$1,000,000	47%
2006	\$2,000,000	\$2,000,000	46%	\$1,000,000	46%
2007	\$2,000,000	\$2,000,000	45%	\$1,000,000	45%
2008	\$2,000,000	\$2,000,000	45%	\$1,000,000	45%
2009	\$3,500,000	\$3,500,000	45%	\$1,000,000	45%
2010	Unlimited	Unlimited	None	\$1,000,000	(35% <sup>1</sup> )
2011 <sup>2</sup>	\$1,000,000	\$1,000,000 <sup>3</sup>	50%	\$1,000,000	50%

<sup>1</sup> Highest individual income tax rate

<sup>2</sup> If no intervening congressional action

<sup>3</sup> Adjusted for inflation

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## TOLI CAPITAL MANAGEMENT STANDARD™

A trustee's responsibility for life insurance capital management, as a "Prudent Investor," has three components:

### *Policy valuation as an objective discipline*

- Utilizing in-depth knowledge of life insurance design.
- Company performance measures.
- Full review of contract value and marketability.

### *Plan review*

- Policies are placed in trust in the context of family philosophies, expectations and circumstances.
- This context shifts continuously, requiring not only a review of the policies relative to the family framework, but also in light of the array of planning options that have come available in the last few years.

### *Recommendations*

- Should policies be modified through re-negotiation with insurance companies?
- Should new policies be purchased to take advantage of today's more favorable actuarial and underwriting environment?
- Should capital be recovered and reapplied through a life settlement, an annuity arbitrage, or both?
- What are the structure and funding options available to most effectively manage the life insurance capital?



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