



You've Been Named the Trustee of an ILIT – Now What?

Over the years, many individuals set up Irrevocable Life Insurance Trusts (ILITs) as a way to own life insurance for estate planning purposes. ILITs were particularly widespread in the 1990s and 2000s as more individuals were subject to estate taxes due to lower estate tax exemption amounts and higher estate tax rates. Especially when compared to today.

In addition, ILITs are popular for those who live in one of the 12 states, and the District of Columbia, that have a state estate or inheritance tax. ILITs are also regaining popularity because of a political desire to expose more individuals and families to the estate tax. Also, the federal estate tax exemption amount is scheduled to decrease in 2026, by half, according to current law.

Many, if not most, of these ILITs in existence have trustees who are either family members or friends, rather than professionals or financial institutions. A family member or friend is often chosen because of the belief that an ILIT is relatively uncomplicated. It typically only owns life insurance. There is also the belief that the individual has a greater knowledge and understanding of the trust creator's (the grantor's) wishes and intent, and that they are willing to act as trustee for little or no compensation,

unlike a financial institution. Unfortunately, most family members and friends are not accustomed to the duties and responsibilities required of a trustee and are not familiar with the complexities of life insurance.

If you're a trustee of an ILIT, let's review some of the basics about your role and responsibilities. This is only a brief description. You should seek further advice and instruction from an estate planning attorney.

- 1. Fiduciary Duty** – A trustee is a fiduciary and fiduciaries are held to a high standard of conduct and care. The fiduciary duties are imposed by state law as well as the terms of the trust document. The trustee has a duty of loyalty to act solely in the best interests of the ILIT's beneficiaries and not to the grantor. That's often a point of conflict. Other duties include following the terms of

the trust; dealing with multiple beneficiaries impartially; and avoiding self-dealing or using trust assets for the trustee's personal gain. The trustee can be personally liable to the beneficiaries for a breach of fiduciary duty.

2. Asset and Investment Management –

Nearly all states have adopted the Uniform Prudent Investor Act (UPIA) which requires a trustee to “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.” Unfortunately, these standards may be easier to understand and apply with investments such as mutual funds, stocks, bonds, and other possible investments but the UPIA does not provide specific guidance on life insurance. Life insurance is much more complex than most people believe. For example, there is term insurance that expires after a certain term unless renewed, and there are permanent policies that continue in force so long as sufficient premiums are paid. There are also many different variations of permanent policies, each with different objectives in mind, such as maximization of death benefits, or a healthy mix of death benefits and cash value accumulation, or premium flexibility, or access to living benefits. Some permanent policies may be subject to interest rate fluctuations and/or market volatility. Some may insure one life while others may insure two. Some provide guarantees while others do not.

The ILIT trustee must not only ensure that premiums are paid on a timely basis but have a good understanding of the type of policy or policies in the trust. Each policy should be regularly reviewed to ensure that it is still the best product for the situation, and that it is performing adequately and as intended. That review may also include a review of the insurance carrier's financial strength; consideration of new product innovations; and consideration of the need for additional life insurance to achieve the grantor's intended goals. If there are issues, the trustee has a duty

to take steps to remedy the situation, which may include converting a term policy to a permanent policy, replacing the policy, directing more premium into the policy, and more.

- 3. Administration –** The trustee has a duty to understand the provisions of the trust document, and to understand any additional rights and responsibilities imposed by the trust, or authority granted by the trust. Poorly drafted trusts may need to be reviewed by qualified legal counsel prior to acceptance of the trustee position.

A few of the administrative duties required are:

- a. Tax returns and financial statements may need to be prepared with the help of a qualified accountant.
- b. Legal notices, known as Crummey Notices, may be required to be given to beneficiaries if money was gifted into the trust by the grantor.
- c. Distributions from the trust may need to be made if required by the trust document.
- d. Life insurance proceeds or other trust assets may need to be used to acquire assets from the decedent's estate.
- e. Trust bank accounts need to be set up and managed.
- f. Engaging attorneys, accountants, life insurance experts and other professionals may be required.
- g. Accurate books and records must be kept.
- h. Conducting policy reviews and filing for insurance claims may be required.

Conclusion

As you can tell, an ILIT trustee is a fiduciary subject to many responsibilities and duties, many of which may not be familiar to the family member or friend who has taken on the role. Violating that fiduciary duty may result in personal liability. The job of trustee may, therefore, not be as easy or worry-free as originally envisioned. Almost certainly, potential personal liability may not have crossed your mind. Regularly dealing with attorneys, accountants and other professionals or consultants may not be a responsibility you want. Therefore, it is important that you carefully consider all of the factors that go into the role of an ILIT trustee.

For More Information Contact:



To obtain more information, you can start with your Security Mutual Life insurance advisor but ultimately, you should consult with a knowledgeable estate planning attorney. Contact your Security Mutual Life insurance advisor today to get the process started. Your advisor will assist in assembling your team and coordinate activities aimed at achieving your desired outcome.

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