Trusts are often considered “the most useful single estate planning device.” They are useful because they are flexible, and they are flexible because there are only six essential elements necessary to establish a trust. First, one needs the intent to create the trust with some form of property. Second, there needs to be property with which to establish the trust, sometimes referred to as the res. Third, there must be a trustee—someone to hold and keep safe the property within the trust. Fourth, the trust needs a beneficiary—someone who benefits from the trust. Fifth, there must be a valid trust purpose—a reason for establishing the trust that is not contrary to law or public policy. Finally, the trust must comply with formalities, such as the Statute of Frauds. These relatively basic requirements result in a death transfer method that can be used for numerous purposes, both complex and simple.

The benefits associated with a trust are what make it a popular and effective method of passing property at death outside of probate. Significantly, a trust provides for asset management via the trustee. This is especially attractive to parents looking to protect young children by appointing someone to handle financial affairs should the parents die. The trustee aspect of the trust is also valuable for elderly individuals whose children or spouse are mentally or physically incapable of making financial decisions, but are still healthy enough to potentially outlive the capable elder. The existence and

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2. Id.
3. Id.
4. Id.
5. Id.
6. Id.
7. Id. at 83.
8. Id. at 83 n.3.
9. Id. at 83.
10. Id. at 81.
11. Id.
continuance of a trust is unaffected by the creator’s later incompetency, incapacity, physical disability or similar misfortune. 13 Another benefit associated with trusts is that because trust property is not considered a probate asset, time and cost savings result from probate avoidance. 14 And last, the transfer of estate property through a trust can result in substantial tax savings. 15

Life insurance is an agreement between an individual policy holder and an insurance company essentially declaring that, subject to the payment of premiums, the insurance company will pay a specified amount to a designated beneficiary upon the death of the insured. 16 In fact, life insurance has been termed “the most important asset of middle-class Americans.” 17 This is because insurance indemnifies the policy holder against loss, damage, or liability resulting from unknown or contingent events. 18

Many individuals have combined the benefits of life insurance with the benefits of a trust. 19 They do so by establishing a trust, purchasing a life insurance policy, and requesting that the insurance company issue a policy naming the trustee as owner and/or beneficiary of the policy. 20 Thus, the life insurance proceeds will be distributed according to the trust. A potential problem once existed because the res of the trust is technically a future claim to insurance money, meaning that at the time of the trust’s formation there was no property with which to establish that trust. Trust law, however, has subsequently been found to be “flexible enough to allow future profits to be a sufficient ‘interest’ to sustain a trust.” 21

In theory, the combination of the life insurance policy and the trust added another necessary element to the trust’s original six—an element that emanates from the requirements of an insurance policy. For an insurance policy—either in life or in property—to be valid, “[t]he person taking out the policy must have an insurable interest in the subject matter of the insurance.” 22 Thus, for a trust to be the valid policy holder of life insurance and thereafter receive life insurance benefits, the trust must have an insurable interest in the individual insured.

2008).

14. ANDERSEN, supra note 1, at 82-83.
15. Id. at 82.
17. ANDERSEN, supra note 1, at 125.
18. 43 AM. JUR. 2D Insurance § 3 (2005).
19. ANDERSEN, supra note 1.
20. BOGERT ET AL., supra note 13, § 236.
21. ANDERSEN, supra note 1, at 87.
An insurable interest is defined as “[a] legal interest in another person’s life or health or in the protection of property from injury, loss, destruction, or pecuniary damage.” 23 An individual possesses an insurable interest in an insured subject matter when the individual is so related to or concerned with the subject matter as to “derive a pecuniary benefit or advantage from its preservation, or [] suffer a pecuniary loss or damage from its destruction, termination, or injury by the happening of the event insured against.” 24 For example, a wife has an insurable interest in her husband because she is so related to her husband that she derives a pecuniary benefit from his survival, such as his financial contribution to the household. The wife would also suffer a pecuniary loss from her husband’s death—i.e. the loss of any such financial support.

In general, the issuance of an insurance policy is void unless the person taking out the policy has an insurable interest in the subject matter of the policy. 25 Thus, an insurance company cannot issue a life insurance policy to an entity lacking the required insurable interest in the insured’s life or health. The purpose is to prevent individuals from intentionally destroying property or killing another to receive insurance benefits, as well as “to prevent the use of insurance contracts for gambling or wagering.” 26 Each state dictates what qualifies as an “insurable interest,” either through common law or, more frequently, state statute.

The United States District Court for the Eastern District of Virginia, in Chawla ex rel. Giesinger v. Transamerica Occidental Life Insurance Co., helped expose an issue common to many state insurable interest statutes. 27 In analyzing Maryland’s insurable interest provisions, the court noted how Maryland’s statute, by restricting the scope of an insurable interest to (a) those related by blood or law, (b) those holding an interest in the continuation of the life of the individual, and (c) those involved in a contract or option for specified business purchases and sales, effectively eliminated the potential for any trustee to be a holder of a valid insurable interest in the insured of a life insurance policy. 28

This discovery could have startling effects for all individuals involved in the numerous trusts established as owners of life insurance policies. The statutory problem exposes trustees to causes of action on behalf of the estate.
of the decedent and potentially subjects that trustee to fiduciary liability resulting from the purchase and payment of premiums on an invalid policy.\textsuperscript{29} Moreover, an estate representative may be subject to personal liability if he or she declines to pursue an action on behalf of the estate against the trustee of the trust.\textsuperscript{30}

This note analyzes the court’s decision in \textit{Chawla}, explores the repercussions of the problem exposed by the decision, and proposes a legislative solution involving a statutory amendment for those states that either lack statutes addressing the issue or whose current statutes contain the flaw. Part II of this note examines the circumstances involved in the formation of the \textit{Chawla} dispute. Part III discusses the holding of the district court and how the court exposed the flaw in Maryland’s insurable interest statute. Part IV analyzes the implications of the \textit{Chawla} decision and discusses the status of insurable interest statutes across the United States. Part IV examines why the restriction on the scope of insurable interest is a problem, discusses the issues raised by it, and surveys possible solutions. This note concludes in Part V.

\textit{II. Chawla ex rel. Giesinger v. Transamerica Occidental Life Insurance Company: The Problem Unveiled}

\textit{A. The Facts}

Harald E. Giesinger applied for a one million dollar life insurance policy with Transamerica Occidental Life Insurance Co. (Transamerica) in May of 2000.\textsuperscript{31} Harald named Vera Chawla the owner and beneficiary of the policy, but Transamerica stated that Chawla lacked an insurable interest in Harald’s life.\textsuperscript{32} Subsequently, Harald changed the name of the owner and beneficiary of the life insurance policy to the “Harald Giesinger Special Trust,” for which Harald and Chawla served as co-trustees.\textsuperscript{33} Transamerica issued the policy based on the information provided in the application.\textsuperscript{34} In his application, Harald falsified his medical history and failed to disclose numerous medical procedures undergone and diagnoses given between the end of 1999 and the beginning of 2000.\textsuperscript{35} Harald Giesinger died in September of 2001.\textsuperscript{36}
Chawla entered a claim for benefits under the life insurance policy as trustee of the “Harald Giesinger Special Trust.” Transamerica rescinded the policy, refunded the premiums, and denied Chawla’s claim, stating that the policy was invalid because of the misrepresentations made by Harald in the application. Chawla filed suit against Transamerica for breach of contract, and Transamerica asserted a counterclaim for fraud. Both Chawla and Transamerica filed for summary judgment.

The question posed before the district court was whether the life insurance policy issued to the “Harald Giesinger Special Trust” was enforceable. The court ultimately decided the life insurance policy was void and, therefore, validly rescinded by Transamerica.

III. The Integral Question of Chawla: Why Did the Court Hold the Life Insurance Policy Issued to the “Harald Giesinger Special Trust” Void?

The court found Transamerica’s rescission of the life insurance policy appropriate for two reasons. First, the rescission was valid because of the material misrepresentations made by Harald in the life insurance application. Those misrepresentations, in and of themselves, were enough to render the policy void. It is the district court’s second line of reasoning, however, that fuels the discussion at hand. The court declared the life insurance policy void because, under Maryland law, the “Harald Giesinger Special Trust” lacked an insurable interest in Giesinger’s life.

Maryland law stated that “[b]efore a person can validly procure insurance upon the life of another, he must have an insurable interest in that life.” Further, the Maryland Code dictated that a life insurance policy may not be procured by a person “unless the benefits . . . are payable to: (i) the individual insured; (ii) the individual insured’s personal representative; or (iii) a person with an insurable interest in the individual insured at the time the insurance policy is issued.”

37. Id.
38. Id.
39. Id.
40. Id.
41. Id. at *3.
42. Id. at *5-7.
43. Id. at *4.
44. Id. at *3-5.
45. Id.
46. Id. at *6-7.
contract was made.” A “person” under Maryland law is “an individual, receiver, trustee, guardian, personal representative, fiduciary, representative of any kind, partnership, firm, association, corporation, or other entity.” In this case, the “Harald Giesinger Special Trust” is deemed the “person” procuring the life insurance policy. The trust is not the individual insured nor is the trust the personal representative of the individual insured. Therefore, Chawla needed to show that the “Harald Giesinger Special Trust” held a valid insurable interest in Giesinger’s life.

Maryland law provided three means to establish an insurable interest. First, in those “related closely by blood or law, a substantial interest engendered by love and affection is an insurable interest.” Second, an insurable interest exists in one who has “a lawful and substantial economic interest in the continuation of the life, health, [and] bodily safety of the individual,” with the additional clarification that “an interest that arises only by, or would be enhanced in value by, the death, disablement, or injury of the individual is not an insurable interest.” Third, an insurable interest can be found in parties involved in limited business settings; essentially, the contract or option for sale or purchase of interest in a business partnership or stock shares in a closed corporation.

The “Harald Giesinger Special Trust” failed to meet any of the three avenues provided by the statute. First, the trust could not establish an insurable interest under the first prong via a close relationship by blood or law to Harald. Second, the trust could not establish an insurable interest under the second prong because it stood to gain more from Harald’s death, due to the death benefits under the policy, than it would if Harald remained alive. The trust “suffered no detriment, pecuniary or otherwise, upon the death of the decedent.” Finally, the trust could not establish an insurable interest under the third prong because the trust was not a business, trade, or partnership, and

49. Id. § 1-101(dd).
51. Id.
52. Id.
54. Id. § 12-201(b)(2)(i).
55. Id. § 12-201(b)(3).
56. Id. § 12-201(b)(5)(i)-(iii).
58. Id.
59. Id. at *7.
60. Id.
no contract for the sale or purchase of a business was involved.\textsuperscript{61} As a result of the trustee’s failure to establish the possession of an insurable interest in the life of Harald, the court held that the insurance policy naming the “Harald Giesinger Special Trust” as beneficiary was void and validly rescinded by Transamerica.\textsuperscript{62}

Chawla appealed the summary judgment granted by the district court.\textsuperscript{63} The Fourth Circuit affirmed the district court’s ruling upholding Transamerica’s rescission of the policy based on the misrepresentations made in the life insurance application, but vacated the district court’s ruling that the policy could also be rescinded because the trust lacked an insurable interest in the individual insured.\textsuperscript{64} The Fourth Circuit stated that after appropriately awarding summary judgment based on the misrepresentation issue, the district court should have exercised judicial restraint and refrained from unnecessarily addressing the insurable interest issue.\textsuperscript{65}

Despite the Fourth Circuit vacating any law established by the district court relating to the insurable interest issue, the problem with the statute’s insurable interest provisions now stands in a spotlight.

\textit{IV. The Questions that Count: Analysis of the Chawla Decision}

To understand why the \textit{Chawla} decision is noteworthy, it is important to understand who is affected by the ruling and what exactly that effect comprises. After understanding the problem \textit{Chawla} exposes, a means for developing a solution needs to be addressed.

\textit{A. The First Relevant Question . . . Who Cares?}

The \textit{Chawla} decision cannot and should not be viewed as an isolated incident. Unfortunately, many states insurable interest provisions are analogous, if not identical, to Maryland’s statute in \textit{Chawla}.\textsuperscript{66} These states follow the same basic pattern of recognizing insurable interests in a limited number of situations, none of which include trustee status under a trust due to receive benefits from a life insurance policy.\textsuperscript{67} For example, in Alaska, an individual cannot procure life insurance “unless the benefits under the contract are payable to the individual insured, the personal representatives of the

\begin{itemize}
  \item \textsuperscript{61} \textit{Id.}
  \item \textsuperscript{62} \textit{Id.}
  \item \textsuperscript{63} Chawla v. Transamerica Occidental Life Ins. Co., 440 F.3d 639, 641 (4th Cir. 2006).
  \item \textsuperscript{64} \textit{Id.} at 648.
  \item \textsuperscript{65} \textit{Id.}
  \item \textsuperscript{66} \textit{See} sources cited infra note 73.
  \item \textsuperscript{67} \textit{See} sources cited infra note 73.
\end{itemize}
individual insured, or to a person having, at the time the contract was made, an insurable interest in the individual insured.”

There are three methods under Alaska law to establish an insurable interest. First, an individual can hold an insurable interest if the individual is “related closely by blood or by law, a substantial interest engendered by love and affection.” Second, an insurable interest exists in one who holds “a lawful and substantial economic interest in having the life, health, or bodily safety of the person insured continue, as distinguished from an interest that would arise only by, or would be enhanced in value by, the death, disablement, or injury of the individual insured.” Third, individuals who are party to a contract for the purchase or sale of a business or stock hold an insurable interest.

If an Alaska court were forced to analyze the validity of an insurance policy issued to a trust in Alaska, the result should technically be the same as that reached in Chawla. That trust would be found to lack an insurable interest in the insured and the policy would, therefore, be held void.

There are currently twenty states that do not contain a provision within their insurable interest statutes that establishes such an interest in the trustee of a trust. Eleven states, including Delaware and Virginia, do contain a provision within their statutes that establishes an insurable interest in the trustee of a trust.

Two of those eleven, Alabama and Oklahoma, just

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68. ALASKA STAT. § 21.42.020(a) (2002).
69. Id. § 21.42.020(d).
70. Id. § 21.42.020(d)(1).
71. Id. § 21.42.020(d)(2).
72. Id. § 21.42.020(d)(3).
74. ALA. CODE § 27-14-3 (2008); DEL. CODE ANN. Tit. 18, § 2704(c) (2002); FLA. STAT. ANN. § 627.404 (West 2008); GA. CODE ANN. § 33-24-3 (West 2006); ME. REV. STAT. ANN.
recently amended their insurable interest statute, likely in response to the concerns raised by the Chawla decision.\textsuperscript{75}

Many states lack specific statutes defining what constitutes an insurable interest.\textsuperscript{76} In these states, common law dictates whether an insurance policy with a trust as holder should be held void for absence of an insurable interest in the insured.

B. The Follow Up Questions . . . Why Do We Care? What Does This Mean?: The Effects of Chawla’s Revelation

The Chawla decision potentially influences trust law in at least twenty states, and the effects can be significant. Chawla directly impacts the validity of irrevocable life insurance trusts, the use of which are pervasive throughout estate planning.\textsuperscript{77} This impact means that the beneficiary of an irrevocable life insurance trust could be subject to liability, the trustee of an irrevocable life insurance trust could be subject to liability, and the decedent’s estate representative may incur personal liability. Most importantly, Chawla could mean the subversion of a testator’s intent, resulting in potentially great losses to those the testator particularly cared about and actively sought to protect.

1. The Irrevocable Life Insurance Trust

An irrevocable trust is a trust that cannot be terminated by the settlor, the person requesting to establish the trust for the benefit of the third party,\textsuperscript{78} post creation.\textsuperscript{79} A life insurance trust is simply a trust containing one or more life

\textsuperscript{75} Ala. Code § 27-14-3 ("After satisfaction of the requirements of Section 27-17A-32(d)(1), the trustee of a trust established by a certificate holder which complies with the requirements of Chapter 17A has an insurable interest in the life of a preneed contract purchaser or a preneed contract beneficiary."); 36 Okla. Stat. § 3604(C) ("A trustee of a trust, whenever established, shall be deemed to have an insurable interest in: a. the individual insured who established the trust, b. each individual in whose life the owner of the trust for federal income tax purposes has an insurable interest, and c. each individual in whose life a beneficiary of the trust has an insurable interest; and the proceeds of the life insurance policy are primarily for the benefit of the trust beneficiaries having an insurable interest in the life of the individual insured.").


\textsuperscript{78} Black’s Law Dictionary, supra note 16, at 1546.

\textsuperscript{79} Id. at 1549.
insurance policies payable to the trust when the insured dies.\textsuperscript{80} An irrevocable life insurance trust (ILIT) is a combination of the two: a trust containing a life insurance policy payable to the trust upon the death of the insured that cannot be terminated by the settlor.\textsuperscript{81} ILITs are frequently used by estate planners as a method of transferring property at death\textsuperscript{82} because the ILIT has all the benefits of life insurance combined with the advantages of a trust.\textsuperscript{83} The life insurance helps establish an estate, stimulates pecuniary saving, and safeguards loved ones and friends from the potentially crippling financial burden resulting from the early death of a provider.\textsuperscript{84} The trust provides the ability to plan for future contingencies.\textsuperscript{85} The ILIT also delivers certain bonuses in regards to tax breaks and creditors’ rights.\textsuperscript{86} In fact, ILITs are so popular that many “how to” guides are printed to aid estate planners in establishing ILITs for their clients.\textsuperscript{87}

One reason ILITs may be favored is because their use allows for the non-probate transfer of the subject property, thereby avoiding the often tedious accompaniments that probate confers.\textsuperscript{88} Also, with an ILIT, the death benefits paid out of the policy are neither subject to income tax\textsuperscript{89} nor included in the decedent’s estate for potential federal estate tax purposes.\textsuperscript{90} ILITs can be advantageous for numerous individuals. They are frequently established as the beneficiary for life insurance policies on behalf of family members.\textsuperscript{91} They may be purchased during divorce proceedings to ensure readily available cash for alimony and child support payments.\textsuperscript{92} Further, ILITs may be

\begin{itemize}
\item \textsuperscript{80} Id.
\item \textsuperscript{81} See id.
\item \textsuperscript{82} See, e.g., Lawrence Brody, The Insurance Counselor: Irrevocable Life Insurance Trust: Forms and Drafting Notes (Roger D. Winston et al. eds., Am. Bar Ass'n 2d ed. 1999); Sebastian V. Grassi, Jr., A Practical Guide to Drafting Irrevocable Life Insurance Trusts (with Sample Forms and Checklists) (2003); Georgiana J. Slade, Planning and Administration Issues After Execution of an Insurance Trust, in 39th Annual Estate Planning Institute 717 (PLI Estates & Trusts, Course Handbook, 2008). These practitioner manuals as well as numerous texts and articles both acknowledge and treat as valid the irrevocable life insurance trust.
\item \textsuperscript{83} Bogert et al., supra note 13, § 235.
\item \textsuperscript{84} Id.
\item \textsuperscript{85} Id.
\item \textsuperscript{86} Id.
\item \textsuperscript{87} E.g., Brody, supra note 82; Grassi, supra note 82; Slade, supra note 82.
\item \textsuperscript{88} Bogert et al., supra note 13, § 231.
\item \textsuperscript{89} Id. § 264.15.
\item \textsuperscript{90} Id.
\item \textsuperscript{91} Id. § 235.
\item \textsuperscript{92} See id. § 234; J. F. Rydstrom, Annotation, Court’s Establishment of Trust to Secure Alimony or Child Support in Divorce Proceedings, 3 A.L.R. 3d 1170, § 7 (1965).
\end{itemize}
established for individuals who are not related by blood to the individual, such as long-time friends or employees, and they can also be used to care for individuals with special needs.\textsuperscript{93}

The flaw in many irrevocable interest statutes, as revealed in \textit{Chawla}, is that the trust, the entity to whom the death benefits of the life insurance policy comprising the ILIT are to be paid, does not have an insurable interest in the life of the individual insured. Subsequently, these trusts could be held void, giving rise to several problematic repercussions.

2. The Potentially Extreme Problem with the Statute “As Is”: The Impact on Irrevocable Life Insurance Trusts

Keeping in mind the extensive use of ILITs by estate planners, holding these numerous ILITs void for lack of an insurable interest triggers the possibility of several adverse consequences. In several states, if the beneficiary or other payee of a life insurance policy issued in violation of the insurable interest statute receives any benefits accrued upon the death, disability, or injury of the individual insured, either the insured, an executor, or an administrator may maintain an action to recover such benefits from the person receiving them.\textsuperscript{94} Thus, in the situation of an ILIT held void for lack of an insurable interest, the estate of the decedent has an action against the beneficiary of the ILIT for the benefits from the trust.\textsuperscript{95} The creation of this cause of action will often be moot because the beneficiaries of the estate of the decedent and the beneficiaries under the ILIT are frequently the same individuals: the decedent’s family members. However, in those instances where the beneficiary of the ILIT is not a beneficiary of the estate, such as in the case of a close friend, the action may be aggressively pursued.\textsuperscript{96} Further, one can deduce that those cases in which the decedent chooses to leave property to a non-family member are also those situations where a trust is most likely to be used so that the property will pass outside of probate.\textsuperscript{97}

Additionally, by purchasing and paying premiums on a life insurance policy that lacks an insurable interest, the trustee of the ILIT may be subject to

\textsuperscript{93} Bogert et al., supra note 13, § 234.


\textsuperscript{95} See supra note 94.

\textsuperscript{96} For example, one partner of a same sex couple leaves their estate to a child and also establishes an ILIT for the benefit of their partner. If the child never approved of their parent’s lifestyle choice, that child may harbor personal reasons to contentiously pursue a claim against the parent’s partner.

\textsuperscript{97} See, e.g., supra note 96.
liability. 98 One of the primary responsibilities of a trustee is to “preserve and maintain trust assets.” 99 This duty requires the trustee to ensure that the trust property is not subject to waste or diminution in value, and it also requires the trustee to ensure the trust property is productive. 100 Paying the premiums on an invalid life insurance policy is, in essence, a loss for the trust. For example, after the purchase of a life insurance policy, premiums are paid over a number of years to maintain the policy and keep it active. 101 If a policy is held void due to a lack of an insurable interest, those premiums are returned, assuming the policy was not procured by fraud. 102 Although the premiums are returned, the profit that could have been earned, such as interest on alternative investment methods, is foregone. These lost profits constitute a loss to the trust. Thus, by establishing and maintaining the invalid life insurance policy with the resulting loss to the beneficiaries, the trustee of the ILIT has failed his or her duty to make the trust property productive. 103 Trustees are “liable for losses if there is a breach of trust or breach of duty [and] the beneficiaries of a trust may sue a trustee to recover profits or recoup losses resulting from the trustee’s breach of any of its duties.” 104 The end result: the trustee of the ILIT is exposed to liability.

If a trust is found to be invalid, there is the further possibility that the trustee could be held liable for payments or conveyances made as directed under that invalid trust. 105 Some courts have concluded that holding the trustee accountable for payments made as directed is unfair because the trustee is simply complying with the settlor’s intentions. 106 To mitigate this liability, these courts have adopted the view of the Restatement (Second) of Trusts, 107 which states that the trustee should be liable “if, but only if, when he made such payment or conveyance he knew that the trust was invalid or had or should have had reasonable doubt as to its validity.” 108

In the case of the ILIT, in connection with the trustee’s knowledge or doubt as to the trust’s validity, the possibility that an ILIT trustee will be held liable for payments or conveyances made under the invalid trust likely depends on

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98. See 76 A.M. Jur. 2d Trusts § 404 (2005).
99. Id.
100. Id.
103. See 76 A.M. Jur. 2d Trusts § 432.
104. Id. § 333.
106. Id. § 2.
107. Id. § 4.
his or her individual representation of skill.\textsuperscript{109} The fact that a trustee is under a duty to exercise due care, diligence, and skill in administering the trust, or else be held liable for resulting losses to the trust estate, is ubiquitous in trust law.\textsuperscript{110} The standard measure of care required of a trustee in administering the trust is to "exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property . . . ."\textsuperscript{111} There is an exception, however, if the trustee has special or professional knowledge or skill,\textsuperscript{112} "or procures his appointment as trustee by representing that he has greater skill than that of a man of ordinary prudence . . . ."\textsuperscript{113} Under such circumstances, the trustee assumes a duty to administer the trust according to this higher level of skill.\textsuperscript{114} Thus, if the trustee of the ILIT possesses greater knowledge regarding trust administration and law, such as that of an attorney, then it is very possible that the court will take into account his or her expertise and find that the trustee should have been aware of the problem regarding insurable interests and its effect on ILITs, and subsequently had reasonable doubt as to the validity of the ILIT.

Trustees have been held responsible for payments or conveyances made under an invalid trust regardless of lack of knowledge of invalidity or lack of reasonable doubt as to validity.\textsuperscript{115} This liability is based on the theory that, because the trustee can always request from a court both a determination of a trust’s validity and a determination of the trustee’s duties under the trust, the trustee likewise has the ability to ensure that any payments he or she makes in accordance with the trust are valid.\textsuperscript{116} Therefore, it is possible that a failure of the trustee to ensure the validity of a trust before making any trust conveyances could be found tantamount to a failure of the trustee to act within his or her duty to preserve and maintain trust assets. A breach of a trustee’s duties results in the imposition of just liability.\textsuperscript{117}

In the case of ILITs, it is likely the court would only hold liable those trustees who either were appointed trustee post-revelation of the insurable interest problem or who, for some reason or another, should have been aware of the exposure of the problem. These trustees, before initiating or making

\textsuperscript{109} See James L. Rigelhaupt, Jr., Annotation, Standard of Care Required of Trustee Representing Itself to Have Expert Knowledge or Skill, 91 A.L.R. 3d 904, § 2(a) (1979).
\textsuperscript{110} Id.
\textsuperscript{111} Restatement (Second) of Trusts § 174.
\textsuperscript{112} Rigelhaupt, supra note 109.
\textsuperscript{113} Restatement (Second) of Trusts § 174.
\textsuperscript{114} Id.; Zitter, supra note 105.
\textsuperscript{115} Zitter, supra note 105, § 3.
\textsuperscript{116} Id.
\textsuperscript{117} 76 Am. Jur. 2d Trusts § 333 (2005).
any further distributions under the trust, could have petitioned the court for a validity determination. Courts, hopefully now aware of the issue, can properly inform trustees whether the trusts are invalid. For those trustees whose ILITs were established before the revelation of the issue, courts will likely waive liability if the trustee previously requested that the court verify the validity of the trust’s insurable interest and was informed that the trust was sound.

Liability may also be incurred by the decedent’s estate representative if he or she chooses to forego a claim against the trustee of an ILIT. The personal representative of an estate owes a fiduciary duty to each beneficiary of the estate to bargain for their rights and allocate to them their share of the estate. AccOMPANYING this fiduciary duty is “a mandatory duty to seek out and collect every asset” of the estate. If the personal representative “fails to recover estate assets,” he or she is personally accountable. Often, and likely having been chosen by the testator in part for this very reason, the personal representative will seek to enforce the testator’s intent. For example, if the personal representative knows that the testator intended for the proceeds of a life insurance policy to go to someone other than the beneficiaries of the estate, the personal representative may opt not to pursue a claim against the trustee of an invalid ILIT. This action may subsequently expose the personal representative to personal liability. Again, this is most likely a claim that will only be pursued when the beneficiaries of the estate are not those who will receive the benefits of the life insurance policy under the ILIT.

The drafting attorney of the ILIT may also be held liable for negligence associated with the trust creation. Attorneys must exercise care in writing a will or inter vivos trust to protect the rights and interests of those who could foreseeably be injured by an improper drafting. Some courts find that the attorney owes this fiduciary duty to both the client and the intended beneficiaries under the instrument. If the client or intended beneficiary suffers “deprivation as a result of a mistake in the drafting of the will or trust,” the drafting attorney could be held liable in tort. A client could maintain an

118. 31 AM. JUR. 2d Executors and Administrators § 391 (2008).
119. Id.
120. Id.
122. 31 AM. JUR. 2d Executors and Administrators § 391.
124. Id.
125. Id.
action based on tort theories of negligence, breach of contract, and breach of fiduciary duty. An intended beneficiary, despite a lack of privity with the drafting attorney, may have a cause of action based on “the contractual theory of third-party beneficiary, or the tort theories of negligence or quasi-offense.” If unaware that the potential problem in the insurable interest statute might invalidate the trust, an attorney currently drafting an ILIT could be held liable to both the client or the client’s estate and any intended beneficiaries under the ILIT.

Finally, philosophically, the invalidation of these types of trusts thoroughly trounces the testator’s wishes associated with the creation of the trust. An individual who establishes a trust in an effort to make a testamentary disposition of property has likely invested considerable time, thought, and money into a legally and realistically effective estate plan. Within the law of wills and trusts, the testator’s intent is of paramount import. Why in this instance— that of an ILIT—should courts ignore that intent? In the most benign case, one where the beneficiary of the trust and the beneficiary of the estate are the same, all that is lost is income that could have been earned from the money had it been kept in a different form, such as an interest-bearing account. But in the most harmful cases, where the positions of the beneficiary under the trust and the beneficiary of the estate are in direct opposition, an individual for whom the testator truly cared could lose the support the testator intentionally provided. It would seem that the rejection of the testator’s intent in these cases imposes too great a loss.

C. The Biggest Question . . . What Is the Solution?

Admitting there is a problem is the first step, and by far the easiest portion of this analysis. Determining and implementing a solution is certainly the more time-consuming and challenging step.

In those states that lack statutes establishing what constitutes an insurable interest, the definition is derived from common law. Common law is law of necessity and exists only in the absence of statutory law. While fundamentally immutable, common law should and must change when change is necessary. Change in common law states can be effectuated by either the legislature through the adoption of a statute, or through courts via rulings that

126. 7A C.J.S. Attorney & Client § 321.
127. Id.
129. 7A C.J.S. Attorney & Client § 159.
132. Id. § 15.
subsequently create and change the law.\textsuperscript{133} Change through the court system can be a long process, not only because a court must wait for an appropriate case through which to effectuate the change, but also because courts are always reluctant to modify precedent.\textsuperscript{134} Legislation would be the more effective and efficient route in those states that do not already have established statutory definitions of insurable interests. To sufficiently amend the situation and overwrite the common law, legislatures must remember to expressly state that the statute is repealing the common law rule, must be sufficiently broad and specific to cover every aspect of that common law rule, and must provide an adequate substitute remedy.\textsuperscript{135}

In the case of the ILIT lacking a necessary insurable interest compliant with statutory provisions, a request to the court to solve the issue presents two possible outcomes. On one hand, the court could find, as the Chawla court did, that the ILIT lacks an insurable interest in the insured, and therefore, the insurance policy is invalid.\textsuperscript{136} As stated, the detrimental repercussions of this decision would be numerous.\textsuperscript{137} At the very least, there would be an increase in litigation given the causes of action that could arise after determining invalidity. Further, there would be a flurry of different opinions on how to impose “liability” on those individuals potentially held responsible. The court could either provide leniency due to the prior common and frequent use of the ILIT without any indication of doubt as to validity, or the court could strictly follow the law, and under that law, find those individuals liable.

On the other hand, the court could determine that the trust does, in fact, hold an insurable interest in the insured. To do this, however, the court could not merely interpret the current insurable interest statutory provision, at least not through strict construction. The court would have to be judicially active and in essence create a new insurable interest in the trust. This is a “separation of powers” 101 issue: it is the province of the legislature to write the law and the province of the judiciary to interpret that law.\textsuperscript{138} As the problem arises out of the insurable interest provisions of state statutes,\textsuperscript{139} the appropriate solution lies with the creators of those statutes: the legislatures.

\begin{itemize}
  \item[133.] \textit{Id.}
  \item[135.] 15A C.J.S. \textit{Common Law} § 16.
  \item[137.] See supra Part IV.B.2.
  \item[138.] 16A AM. JUR. 2D \textit{Constitutional Law} § 246 (2008).
  \item[139.] See supra note 73.
\end{itemize}
Because of both the frequency of and the benefits to using ILITs, legislatures should develop language to validate a life insurance policy held by a trust otherwise lacking an insurable interest. This could be accomplished by extending the list of valid insurable interests to include one established in the trustee of a trust.

Delaware law, via three methods, instills an insurable interest in the trustee of a trust. Simplified, Delaware’s statute states first, for federal income tax purposes, the trustee of a trust has an insurable interest in the life of the individual who established the trust. Second, for a trust with a receiving life insurance proceeds, the trustee of the trust has an insurable interest in the life of the individual who established the trust. Third, for a trust with multiple beneficiaries funded by life insurance proceeds, the trustee of the trust has an insurable interest in the life of the individual equivalent to the aggregate of those beneficiaries. Although the Delaware legislature addressed the issue, the statute is wordy and difficult to understand. Because a change in the law should provide clarity through understandable and concise language, patterning a statutory revision upon the Delaware statute is not advisable.

A different option for correcting the problem exposed in Chawla would be to model legislative change after Virginia’s law, which instills in the trustee of a trust an insurable interest in “(i) the individual insured who established the trust, (ii) each individual in whose life the owner of the trust for federal income tax purposes has an insurable interest, and (iii) each individual in

141. See, e.g., id.

The trustee of a trust established by an individual has an insurable interest in the life of that individual and the same insurable interest in the life of any other individual as does any person who is treated as the owner of such trust for federal income tax purposes. The trustee of a trust has the same insurable interest in the life of any individual as does any person with respect to proceeds of insurance on the life of such individual (or any portion of such proceeds) that are allocable to such person’s interest in such trust. If multiple beneficiaries of a trust have an insurable interest in the life of the same individual, the trustee of such trust has the same aggregate insurable interest in such life as such beneficiaries with respect to proceeds of insurance on the life of such individual (or any portion of such proceeds) that are allocable in the aggregate to such beneficiaries’ interest in the trust.

Id.
143. Id.
144. Id.
145. Id.
146. See supra note 142.
whose life a beneficiary of the trust has an insurable interest.”\textsuperscript{147} This clear, precise wording covers the issue exposed by \textit{Chawla} by providing specifically that the trustee of the trust has an insurable interest in the individual insured.\textsuperscript{148}

A third possibility is to follow the straightforward approach of Utah.\textsuperscript{149} Utah law provides a “nonexhaustive list of insurable interests.”\textsuperscript{150} Included on the list is the statement that “[a] trust has an insurable interest in the subject of the insurance to the extent that a beneficiary of the trust has the insurable interest.”\textsuperscript{151} This is by far the most succinct and yet still effective state statutory revision of the insurable interest provisions. Depending on the level of specificity with which state legislatures might wish to approach amending current statutes, following the example of either Virginia or Utah would be sufficient to validate the ILIT.

Along with the adoption of new statutory language, state legislatures adopting such changes should deem the amendment to have retroactive effect. It is true that \textit{ex post facto} law is typically prohibited and often correctly so.\textsuperscript{152} This prohibition is appropriate because it often involves instances where the retroactive effect would criminalize conduct that was legal when performed.\textsuperscript{153} Criminalizing conduct that was legal when performed is a violation of an individual’s right to due process, specifically, notification prior to action that his or her conduct might result in unfavorable legal consequences.\textsuperscript{154} Trust law, however, is not a situation of criminal conduct, but rather one of civil technicalities. Retroactive law is sometimes allowed in civil contexts.\textsuperscript{155}

Presently, there are numerous trusts established as the taker under a life insurance policy. These trusts were created without any associated fraud or peccant intent, and under the assumption that they were a valid testamentary act. The legislature should seek to protect those trusts and give effect to the intent of settlors by according any amended statute retroactive status.

\textit{V: The Bottom Line: Address the Problem}

The problem exposed in \textit{Chawla} is that every existing ILIT could be void in those states lacking statutory recognition of an insurable interest in the

\begin{thebibliography}{9}
\bibitem{147} Va. Code Ann. § 38.2-301(B)(5) (West 2007).
\bibitem{148} Id.
\bibitem{149} Utah Code Ann. § 31A-21-104(3) (2007).
\bibitem{150} Id.
\bibitem{151} Id.
\bibitem{152} 82 C.J.S. Statutes § 415 (2007).
\bibitem{155} Id.
\end{thebibliography}
trustee of a trust named as the beneficiary of a life insurance policy. This problem is pervasive in United States statutes and, due to the resulting harmful consequences, will soon need to be addressed in state legislatures. Some states may prefer to allow the issue to be determined through judicial means, but the most effective solution lies in legislative amendment. This solution would be best obtained by adopting language patterned after the current Utah law which, as one in a nonexhaustive list of insurable interests, vests an insurable interest in the trustee of a trust listed as the beneficiary of a life insurance policy.156

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