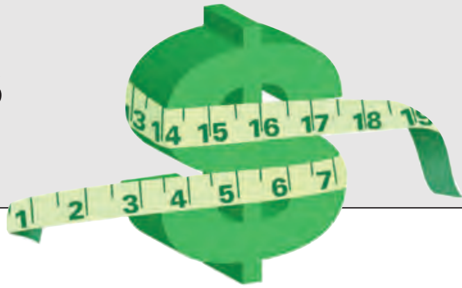

How to Get the Best Returns from Your Preneed Trust Fund Investment

By Jim Atwood, CEO of Infinity Management Advisors and FSI board member

The death-care industry has a number of available options for preneed funding; one of the most popular methods is a trust-funded preneed program.

Trusts offer a great potential for higher returns. While there may appear to be an increased risk compared to other options, due to market volatility, a death-care professional can mitigate risk by increasing transparency of trust activities with a proper investment policy statement, administration and appropriate record keeping. Plus, a trust-funded preneed program can avoid risks associated with other options. Selection of the right trust for your funeral home can be made easier by having a clear understanding of the trust and its effect on your business as a whole.

There is a symbiotic relationship between the investment strategy of your preneed trust, performance and cash flow that is oftentimes overlooked when utilizing a trust. Interaction between the three can result in either a positive or negative outcome for your funeral home.

For one Florida funeral home, delaying distributions resulted in a negative impact on its cash flow. The business waited up to two weeks for payment. Our company, Infinity Management Advisors, worked with the funeral director and key stakeholders to outline the funeral home's preneed trust goals, its internal processes and developed an investment policy statement outlining an investment strategy. As a result, the funeral director chose to move the funeral home's funds to a new trust to improve cash flow. The funeral home now receives distributions within 24 hours.

As shown in the above scenario, the investment strategy of your preneed trust, along with other factors, can significantly impact your business. Negative or delayed cash flow can result in stressful day-to-day business workings, while issues in cash flow can be linked to poor investment performance. All of which can be identified and addressed, if you understand the relationship between the three – investment strategy, cash flow and performance – and are aware of performance warning signs.

In this article we will examine preneed trust investment strategies, their impact on cash flow, key indicators of investment performance and important questions to ask your financial adviser regarding your preneed trust.

Investment Strategies

Three general investment types a trust will use are:

- Equity investments: the use of stocks.
- Fixed income investments: government or corporate bonds, mortgage-backed investments and securities.
- Liquid investments: readily available funds left to pay fees and distributions from the trust.

The balanced approach is a typical combination of the three investment types:

- Equity investments: 50 percent.
- Fixed-income investments: 47 to 48 percent.
- Liquid investments: 2 to 3 percent.

Appropriately named, this approach closely balances the funds distributed to equity investments and fixed-income investments, balancing the risk and the return of the preneed trust. The funeral home director and key stakeholder, based on a number of factors, determine the percentage of cash necessary in the trust to pay fees and disbursements. The size of the trust will impact the percentage of cash required – larger trusts will require less where smaller trusts will require more.

Cash Flow and Performance

A funeral home's preneed trust

will see an influx and outlay of cash as the business sells preneed contracts, and as contracts become at-need and services are provided. Proper management of this flow directly impacts overall cash flow and trust performance.

Like any business, a funeral home requires a certain amount of cash on-hand for daily operations, vendor payments and employee salaries.

Timely distributions of contract services provided are key to positive cash flow for a funeral home. Untimely distributions not only adversely impact cash flow, but could also be a warning sign of a performance issue. The selling of investments to make distributions may also be a warning sign your trust is underperforming.

The performance of the trust, or the rate of return on the investment, can have a direct impact on the funeral home's cash flow. A higher percentage of liquid investments may result in overall lower return on investment, therefore stunting the growth of the trust. Liquid investments have the lowest rate of growth. Managed appropriately, the percentage deposited or maintained in this investment type should be kept at the minimum level required by the investment policy statement.

On the flipside of the coin, if there is insufficient funds for distribution fulfillment, the trustee/investment manager may be required to sell equity or fixed investments. The trust may be required to liquidate a larger sum than needed for the disbursement – pulling cash out of the trust, again lowering the overall return on investment.

Funeral home directors may see records of sold assets on their monthly reports or they may be notified at the time of the sale.

Understanding the relationship allows funeral home directors and key stakeholders to be more cognizant of the health of their trusts and overall business.

Questions for Your Trustee

Whether in the beginning stages of selecting a preneed trust or in the midst of a trust experiencing warning signs, there are a few key questions to ask your trustee/financial adviser. Along with the questions are explanations of how the answers to these questions can help you understand your trust's performance:

Q. What does the cash flow analysis of the trust look like?

A. Your trustee should provide a cash flow analysis of the trust. In addition to the cash flow analysis, you will want to know if there have been any needs in the previous 12 months where the trustee had to raise cash for distributions.

Q. Is the trust maintaining enough cash to pay disbursement requests?

A. As with the first question, you want to understand how the trust is performing. The key to this question is being aware of any situations where the trustee has had to sell investments at any time to make disbursements.

Q. Has the trust needed to sell assets to raise cash for distributions?

A. If the trustee's response to this question is 'yes,' you should follow-up by asking how often this occurs and request an explanation as to why this is required. If the trust is performing according to the investment policy statement's goals and objectives, selling investments to raise cash should not be required. However, there are situations that arise that may justify this practice. For instance, it may be necessary if there is a larger than normal distribution request. If your funeral home's average monthly distribution is $20,000, but then you have a very busy month where you make a much larger distribution request, such as $75,000, the trust may be required to sell investments to fund the distribution.

Q. What is the current market value of the trust?

A. Your trustee should not only provide the market value of your trust but also give an indication of how the market value is trending. How the trust is trending – whether up or down – is an indicator of the investment performance and will allow you to understand if the trust is meeting the objectives outlined in the investment policy statement.

Keeping an open dialogue with your trustee is important to the health of your trust and ultimately your business. Staying actively engaged in the performance of your trust allows you to be educated about your business and spot any warning signs with time to make the necessary adjustments to prevent a crisis.

The right preneed trust for your business is one that uses an investment strategy, which promotes positive cash flow and performance. As our friends in Florida experienced, working with knowledgeable professionals, like those at Infinity Management Advisors, can assist your business in creating and following a road map that leads to a healthy investment that will sustain your business for years to come. •