



# INDEPENDENT INVESTOR

Timely Insights for Your Financial Future

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## Enhancing Charitable Gifts With Life Insurance

If you are a regular donor to charity, life insurance could help you to make a much larger gift to your cause of choice.<sup>1</sup> Instead of making periodic cash contributions to a charity, you could use the same amount to pay the premium on a life insurance policy to benefit the charity. Upon your death, the charity would receive the full face value of your policy—which would likely amount to considerably more than you could afford to donate during your lifetime.

### Donors Benefit, Too

In addition to enhancing charitable gifts, life insurance offers potential income, estate and gift tax benefits to donors as well. The actual benefits you realize would depend on the type of life insurance used and how the donation is structured.

Term life insurance policies are the least expensive to purchase but involve risks that may jeopardize achieving your charitable-giving goal. For instance, if the policy were to expire before your death, the charity wouldn't receive any proceeds. Similarly, because term insurance premiums can rise dramatically over time, premiums can eventually become prohibitively expensive.

Further, if you were to become uninsurable or no longer able to afford the monthly premiums, your charity could end up with nothing. For this reason, so-called permanent policies, such as whole life, are generally more attractive for charitable-giving purposes because they typically have level premiums for the life of the contract and generally do not expire if you've made all of your premium obligations.

In addition, a permanent policy has a cash value component, which can increase the range of gifting strategies.

## Structuring Life Insurance Gifts

There are two basic ways of using life insurance to make charitable gifts. One is to donate an existing life insurance policy. To do so, you must transfer ownership of the policy to the charity, giving up all control of the policy. Because the transfer is irrevocable, you obtain the full tax advantages of charitable giving. You may be able to take an income tax deduction equal to your basis or the policy's fair market value, as well as a charitable deduction for the premiums you pay. The policy will not be included in your gross estate unless you die within three years of the transfer (in which case, your estate would receive an offsetting charitable deduction).

The other way to use life insurance for charitable giving is to donate a new policy. With this strategy, you purchase a policy and pay the premiums but immediately assign ownership of the policy to the charity. In this case, you would be entitled to take a charitable deduction for the premiums.

Alternatively, you may want to consider naming a charity as beneficiary of your policy. While this approach is simple and would still give you access to any cash value of the policy during your lifetime, its tax advantages are limited because you retain control over the policy until you die. Upon your death, the proceeds would be included in your gross estate, although the full amount of the proceeds payable to the charity would be deducted from your estate.

Another easy-to-execute approach is to gift a policy's dividends to a charity. This method may be appealing if your goal is to pass the policy's death benefit on to your heirs. You can designate a charity to receive any of a permanent policy's dividends when you apply for a policy or at any time while you own it. While you retain control over the policy and its cash value, you also receive an income tax deduction for dividends paid to the charity. However, death benefit proceeds are included in your gross estate.

Finally, if complexity is not a concern and you are planning a substantial gift, you may want to consider using life insurance to fund a charitable remainder trust. To do this, you would want to work with an attorney to create a charitable remainder trust and then purchase life insurance to fund the trust. During your lifetime, the trust would provide you with a specified amount of income. Upon your death, the principal of the trust would pass to the designated charity. In conjunction with the charitable remainder trust, you could also purchase another life insurance policy to benefit non-charitable beneficiaries, such as your spouse and children.

## Communicating the Benefits

As good as your intentions may be, don't be surprised if your charity is not enthusiastic about receiving a gift of life insurance. It may prefer to receive a cash donation, which it can put to use right away. Indeed, if your recipient is a large charity with an investment management arm, it may decide to cash in your policy donation and invest the proceeds on the assumption that it could earn a higher rate of return than by waiting to collect the death benefit.

On the other hand, if you are donating to a smaller charity, you could point out that a life insurance gift can be preferable to alternatives, such as donating stock.<sup>2</sup> Unlike stocks, whose value is subject to market changes, the amount the charity will eventually receive from life insurance is guaranteed as long as you continue paying the premiums.

Because state and federal tax laws are complex, it is best to discuss your situation with qualified tax and insurance professionals before deciding on the structure of a life-insurance-based giving plan.

<sup>1</sup>Life insurance policies are subject to substantial fees and charges. Death benefit guarantees are subject to the claims-paying ability of the issuing life insurance company. Loans will reduce the policy's death benefit and cash surrender value, and have tax consequences if the policy lapses.

<sup>2</sup>Investing in stocks involves risks, including loss of principal.

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