Charitable Gift of a Life Insurance Policy

The Rationale...

- Life insurance can be a substantial, cost-effective gift to charity.
- A life insurance gift allows the donor's family to retain other assets.
- Life insurance proceeds are paid to the charity without probate delays.
- A life insurance gift is private; a bequest in a will is a matter of public record.
- An outright gift of a policy to a charity will create a current income tax charitable deduction (if the donor itemizes deductions) equal to the lesser of the policy's fair market value or the donor's basis in the policy.
- Death proceeds paid to a charity from an estate are deductible for federal estate tax purposes.
- Remaining premiums paid by a donor are deductible if the charity owns the policy, or the donor could donate the premium amounts directly to the charity.

The Choices...

- One, the donor gives an existing policy to charity, assigns all incidents of ownership to the charity and names the charity as beneficiary.
- Two, the donor applies for a new policy on the donor's life with the charity as the original policyowner and beneficiary (subject to state insurable interest laws).
- Three, the donor names a charity as a beneficiary of a policy that the donor continues to own.

The Tax Impact...

- The gift of an **existing life insurance policy** to charity qualifies for an income tax charitable deduction, provided the donor itemizes deductions and assigns all rights to the charity by naming the charity owner and beneficiary.
- The donor's deduction is the lesser of the fair market value of the policy or the donor's tax basis in the policy.
- The deduction is reduced if the policy is subject to a loan, or if a sale of the policy on the date of the gift would have produced ordinary income.
- The donor receives an income tax charitable deduction for premium payments the donor makes after a policy is transferred. If they're paid directly to the insurance company, the deduction that year is limited to 30% of the donor's adjusted gross income. But if the donor makes annual cash gifts to a public charity, which uses them to pay the premiums, the donor may deduct an amount up to 50% of adjusted gross income that year. Stricter limits apply in the case of gifts to a private foundation.
- If a donor wants to retain ownership and control of an **existing policy**, he or she can simply add the charity as beneficiary. This won't produce an income tax charitable deduction, but it will create an estate tax charitable deduction for the death proceeds that go to the charity at the insured donor's death.
- If the gift is a **new life insurance policy**, the donor should transfer funds for the purchase to the charity. The charity then becomes applicant, owner and beneficiary of the new policy on the

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donor's life. The initial premium transferred to the charity is generally deductible, and the policy's death proceeds won't be included in the donor's gross estate at death because the donor never held any incidents of ownership.

Other Considerations...

- The laws in most states make it clear that a charitable organization has an insurable interest in a donor. However, the donor's legal counsel should check the laws of a particular state before the donor chooses to give a new policy to charity.

The Bottom Line...

Life insurance helps create a charitable gift that is much larger than what otherwise might be given by the donor. Death benefits paid to the charity at the owner's death invariably far exceed the premiums paid for the gift, and the donor can retain other assets for other uses or planning solutions.

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1 The donor transfers ownership of a life insurance policy on the donor's life to a charity which changes the beneficiary designation to itself.

2 The donor may also pay the premiums on the policy, either by paying them directly to the insurance company...

3 ...or by making annual cash transfers to the charity, which then pays the premiums. More favorable deduction limits apply to the latter scenario.

4 At the insured's death, the life insurance company pays the policy proceeds to the charity as beneficiary.

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