

Charitable Gifts of Life Insurance Shared Benefits For The Donor And The Charity

Making a gift of life insurance to a favorite charity is an appealing planning strategy as it is flexible, cost-effective, and in many cases a tax-efficient way of leaving a legacy that will benefit the charity after your death. For a comparatively small premium contribution, the ultimate gift (the death benefit) is generally many times larger than the total payments. Life insurance can allow you the donor to make a significant gift without reducing your estate and depriving your surviving spouse or family of an inheritance. What better way to touch the future of a favorite charity?

A gift of life insurance can provide substantial benefits to both you the donor and your favorite charities.

Benefits to you ...

- Through the leverage of life insurance, you have the ability to make a substantial, long-term contribution that may exceed the amount donated through normal periodic contributions.
- It enables you to make a large endowment to charity without depleting your current capital.
- It avoids the costs, delays, publicity or other complications of estate settlement, since the gift is “self completing.”
- Life insurance can serve as a wealth replacement tool.
- The charitable gift of life insurance structured properly results in deductible income for income and/or estate tax purposes.

Benefits for the Charity ...

- Provides substantial deferred endowment funds helping to ensure the charity’s future.
- Provides security, as the amount of the gift can be set in advance

- Helps guarantee prompt payment and needed funds at a major donor’s death.
- Can be used to create an ongoing build-up of cash value that can be accessed for the charity’s immediate cash needs.¹

Four ways to support a charity using life insurance

One: Make a gift of an existing policy

You may choose to make an outright gift of an existing policy to charity. To gain a current income tax charitable deduction, you must be certain to transfer all rights of ownership in the policy to the charity i.e. the charity is made the owner and policy beneficiary.

In general the value of the deductible gift (subject to the general limitations placed on charitable contributions) you make is equal to the fair market value of the policy at the time of transfer.

As a general rule, if the value of the policy exceeds the premiums paid to the date of transfer, a donor may only deduct their cost basis in the policy.

More specifically, where a policy does not contractually require additional premiums to remain in-force at the time of the gift, the charitable deduction is the lesser of the policy replacement cost or your cost basis.

If the policy still requires additional premiums at the time of the gift, the charitable deduction is the lesser of the policy’s adjusted interpolated terminal reserve value (which is generally fairly close to the policy’s cash surrender value) or your cost basis in the policy.

¹ Donors and charitable organizations should be aware that loans and withdrawal from cash value life insurance policies may reduce death benefits, affect guarantees against policy lapse, and may have tax consequences.

Your advisors working with your insurance company can help you obtain the proper values.

For estate tax purposes once a completed gift of an existing policy is made to a charity, the policy proceeds will not be included in your estate at your death unless you die within three years of the transfer. However, should death occur during this three year period, although the policy proceeds will be included in your estate, this inclusion is offset by an estate tax charitable deduction for the amount of the death benefit going to the charity.

The pros and cons of this approach ... as the donor you lose control of the policy but you gain a current charitable deduction. In addition, where future premiums are required, payments made by you the donor can be structured to qualify as charitable deductions for income tax purposes.

In turn, the charity gains ... as it now has control of cash values, dividend rights etc., and receives death benefit free of federal income, gift and estate taxes, probate and other administrative costs and delays.

Two: Make the charity the beneficiary of an existing policy

As a donor you can maintain ownership of an existing policy and simply change the beneficiary designation to favor a charity. The charity can be named a sole beneficiary or only receive part of the policy proceeds; or simply be listed as a contingent beneficiary.

The pros and cons of this approach ... while a beneficiary designation is simple, private and requires little documentation, it is important to understand that because you retain control of the policy you will not be able to take any income tax deductions during your life. However, the policy proceeds, while includible in your estate at your death, will qualify for the estate tax charitable deduction for the policy proceeds paid to charity.

Three: Help the charity purchase a new policy

Alternatively, the charity could purchase a new policy on your life — subject to state insurable interest laws. The majority of states now have laws in place that give charitable organizations an insurable interest in your life as a donor, however the laws vary according to the applicable state statutes. As a donor, you should consult your personal tax and legal counsel as to the particular statutes that apply in your planning situation.

Under this approach, the charity purchases the policy, naming itself as owner and beneficiary and is responsible for making the premium payments. Of course, you can assist them in the process by making cash contributions equal to or greater to the needed premium dollars on an annual basis.

Pros and cons of this approach ...

Structured properly an annual charitable deduction should be available (subject to the general limitations placed on charitable contributions). However, it is important to understand that the charity is not obligated to maintain the policy nor are you obligated to continue premium contributions. Of course, where the policy is intended to serve as a future endowment, careful consideration should be given to both parties understanding of their roles, if the plan is to be successfully brought to completion.

Four: Gift assets to the charity and replace family wealth through a wealth replacement trust.

Sometimes life insurance is not the gift, but becomes the solution.

As a potential donor you may be inclined to make a substantial gift to your favorite charity, but you are hesitating wondering if you will deprive family members of assets they might need in the future. However, by directing your tax savings generated by your charitable gift to the purchase of a life insurance policy, you can donate your assets to charity and still send a benefit to your heirs.

The life insurance should be owned by your children or by an irrevocable life insurance trust (an ILIT) to ensure that upon your death the policy proceeds will not be included in your estate and your heirs will receive full benefit from the policy proceeds.

In Summary

Charitable giving using life insurance can work for you and for your favored charities.

A licensed financial professional can help guide you in choosing the right life insurance strategy — one that allows you to achieve your personal goals while helping you to support your favorite charity.



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conduct for individual life insurance,
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This material is designed to provide general information in regard to the subject matter covered. It contains references to concepts that have legal, accounting and tax implications. It is not intended as legal, accounting or tax advice. Consult your own attorney and/or tax advisor for advice regarding your particular situation.

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