Life Insurance and Charitable Giving
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Life insurance can be an excellent tool for charitable giving. Not only does life insurance allow you to make a substantial gift to charity at relatively little cost to you, but you may also benefit from tax rules that apply to gifts of life insurance.

**Why use life insurance for charitable giving?**

Life insurance allows you to make a much larger gift to charity than you might otherwise be able to afford. Although the cost to you (your premiums) is relatively small, the amount the charity will receive (the death benefit) can be quite substantial. As long as you continue to pay the premiums on the life insurance policy, the charity is guaranteed to receive the proceeds of the policy when you die. (Guarantees are subject to the claims-paying ability of the issuing insurance company.) Since life insurance proceeds paid to a charity are not subject to income and estate taxes, probate costs, and other expenses, the charity can count on receiving 100 percent of your gift.

Giving life insurance to charity also has certain income tax benefits. Depending on how you structure your gift, you may be able to take an income tax deduction equal to your basis in the policy or its fair market value (FMV), and you may be able to deduct the premiums you pay for the policy on your annual income tax return. When an insurance contract is transferred to a charity, the donor's income tax charitable deduction is based on the lesser of FMV or adjusted cost basis.

**What are the disadvantages of using life insurance for charitable giving?**

Donating a life insurance policy to charity (or naming the charity as beneficiary on the policy) means that you have less wealth to distribute among your heirs when you die. This may discourage you from making gifts to charity. However, this problem is relatively simple to solve. Buy another life insurance policy that will benefit your heirs instead of a charity.

**Ways to give life insurance to charity**

The simplest way to use life insurance to give to a charity is to name a charity to receive the benefits of your life insurance policy. You, as owner of the policy, simply designate the charity as beneficiary. Designating the charity as beneficiary may allow you to make a larger gift than you could otherwise afford. If the policy is a form of cash value life insurance, you still have access to the cash value of the policy during your lifetime. However, this type of charitable gift does not provide many of the income tax benefits of charitable giving, because you retain control of the policy during your life. When you die, the proceeds are included in your gross estate, although the full amount of the proceeds payable to the charity can be deducted from your gross estate.

Another alternative is to donate an existing life insurance policy to charity. To do this, you must assign all rights in the policy to the charity. You must also deliver the policy itself to the charity. By doing this, you give up all control of the life insurance policy forever. This strategy provides the full tax advantages of charitable giving because the transfer of ownership is irrevocable. You may be able to take an income tax deduction equal to the lesser of your adjusted cost basis or FMV. The policy is not included in your gross estate when you die, unless you die within three years of the transfer. In this case, your estate would get an offsetting charitable deduction.

A creative way to use life insurance to donate to a charity is simply for the charity to insure you. To use this strategy, you would allow the charity to purchase an insurance policy on your life. You would make annual tax-deductible gifts to the charity in an amount equal to the premium, and the charity would pay the premium to the insurance company.

One final method is to use a life insurance policy in conjunction with a charitable remainder trust. This strategy is relatively complex (it will require an attorney to set up), but it provides greater advantages than other, simpler methods. You set up a charitable remainder trust and transfer ownership of other, income-producing assets to the trust. The income beneficiary of the trust (you or whomever you designate) will get the income from the assets in the trust. At the end of the trust term (which might be a certain number of years or upon the occurrence of a certain event, such as your death), the property in the trust would pass to the charity. You'll receive a current tax deduction when you establish the trust for the FMV of the gifted assets, reduced according to a formula determined by the IRS. Life insurance can then be purchased (usually inside an irrevocable life insurance trust to keep the proceeds out of your estate) to replace the assets that went to the charity instead of to your heirs.