

SPRING NEWS

Charitable Gifts of Life Insurance

Many Americans decide to make a difference by donating money to local religious, educational, social, or cultural organizations, and this type of charitable giving can also provide tax benefits for the donor and his or her heirs.

A charitable donation does not have to be cash. Gifts of life insurance have some unique advantages:

- Because life insurance is a contract that passes outside the will, it cannot be contested in probate proceedings.
- The payment of a life insurance policy death benefit is private-not a matter of public record.
- Although payment of the life insurance death benefit is deferred, the charity may be able to use the cash values immediately.
- The charity does not pay income or estate tax on the benefit.
- There are no probate delays.
- Assets are preserved for the donor's family.

Life insurance can be donated to charity in two ways:

The first arrangement is used when the insured/donor wants to retain control over the insurance policy. Under this system, the insured is the owner of the policy, the charity is the beneficiary, and the premiums are not income-tax-deductible. Since the insured owns the policy at death, the death benefit will be included in his or her estate, but it will be 100% deductible from the estate, since it is payable to a charity.

In the second arrangement, the charity is both owner and beneficiary of the policy. Here, the premiums may be income-tax-deductible within IRS guidelines.

If the donor gives an existing policy to charity, the value of the policy (generally, it's cash surrender value plus any unearned premiums) or the policyholder's basis (normally the premiums paid), whichever is less, is allowable as an itemized income tax deduction. The tax consequences of future premium payments would work as described above where the charity is both owner and beneficiary.

Charitable Remainder Trusts (CRTs) and Irrevocable Life Insurance Trusts

A charitable remainder trust (CRT) allows an individual to give an asset to charity while retaining an interest in the asset during his or her lifetime. This can help the donor increase income, reduce estate and income taxes, avoid taxes on gains, and make a significant charitable contribution without reducing his or her family's inheritance.

It is generally best to fund a CRT with an asset that would produce substantial long-term capital gains tax if sold outside the trust. After the trust is executed, the donor transfers the appreciated asset to the CRT, which sells the asset and gives the donor an income for life, for a term of years, or for joint lives. At the death of the donor or other named beneficiary, the remaining trust assets pass to the charity. Here are some benefits of using this strategy:

- When the trust is created, the donor gets a current income tax deduction based on the future amount passing to the charity.
- The trust pays no capital gains tax when it sells the asset.
- The trust can invest in assets paying a higher rate of return than the donated asset was producing, and the trust has more to invest, since it doesn't pay tax on the gain. This can result in increased income for the donor.
- Estate taxes are reduced, since the asset placed in the trust has been removed from the estate.

Upon the donor's death, assets remaining in the CRT pass to the charity.