Fast Facts About Donating and Receiving Gifted Life Insurance Policies

WRITTEN BY
Mike Pepe, Founder & Chief Strategy Officer, Proformex

According to one LIMRA study, more than 1 in 4 Americans who own life insurance policies say they purchased the policy with the intention of donating it to a charitable cause such as a non-profit or a college or university endowment fund. This statistic begs a few questions:

- How does donating a life insurance policy work?
- What makes this method of giving a favorable choice for policyowners looking for ways to donate?
- What should organizations receiving gifted life insurance policies know about this type of donation?

This educational guide answers these questions for policyowners considering donating a life insurance policy and for those charitable organizations receiving policies as donations.

Why might a policyowner consider donating their life insurance policy?

There are a few reasons why a policyowner might consider donating a life insurance policy rather than writing a check to their charitable cause of choice. Perhaps the most obvious is the unique tax benefits it provides. Not only does the owner receive a charitable contribution tax deduction (in most cases) when donating a policy, but the policy is also no longer counted toward their estate for estate tax purposes.

Beyond the favorable tax treatment, donating a life insurance policy is also a great way to get rid of an unwanted policy an owner no longer needs. **So much can change between the time an owner purchases coverage and when they expect to need it. It's critical owners are educated on the options they have besides simply surrendering the policy back to the insurance company or letting it lapse.**

Lastly, for owners who wish to leave a legacy for a cause they believe in, donating a life insurance policy is an excellent way to boost their giving. Because the death benefit of a life insurance policy greatly exceeds the premium paid into it, the donor's generosity is multiplied. Though the organization or foundation won't receive the gift immediately, they do end up with a larger donation in the long run.

How can a policyowner donate their policy to a charitable organization?

If an owner decides to donate a life insurance policy, they have at least four different options: name the charitable cause as the beneficiary of a new or existing policy, transfer ownership of the policy, donate gift dividends from their policy, or add charitable giving riders on the policy. Each method of donating has unique advantages and disadvantages, so it's important the owner understands the implications before committing as some of these decisions are irrevocable.

1) Designating a charitable organization, non-profit, or academic institution as the beneficiary

Donor Advantages

- Policyowner still gets cash value accumulation on the policy for the entire coverage period
- Ensures privacy of the transaction, which can be important for policyowners who prefer their family members and heirs aren't aware of their donations
- The beneficiary designation can be changed at will – whether removing a beneficiary or adjusting the division of proceeds across multiple beneficiaries, the policyowner retains the right to make any revisions for the duration of the contract

Donor Disadvantages

- Since the policyowner maintains full control of the policy, they cannot receive a charitable contribution tax deduction
- The policyowner must continue paying premiums to keep the policy inforce

Recipient Advantages

- Recipient gets a lump sum payment that's much larger than the amount of premium paid into a policy
- The recipient's operational budget remains unaffected since they do not have to assume responsibility for premium payments

Recipient Disadvantages

- The policyowner can change their mind at any time

2) Transferring ownership from the policyowner to the charitable organization, non-profit, or academic institution

Donor Advantages

- Policyowner will receive a charitable contribution tax deduction
- The policy will no longer be counted toward the estate for estate tax purposes
- Policyowner may receive additional tax deductions if they choose to maintain responsibility for premium payments even after the ownership is transferred
- Charitable donations have no ceiling, so there's no limit on the amount donated through a gifted life insurance policy

Donor Disadvantages

- This decision is irrevocable

Recipient Advantages

- Gives recipient full control of the policy
- Organization can name itself beneficiary of the policy and then get a tax-free payout
- For permanent policies with cash value, recipients can surrender the policy and get immediate value

Recipient Disadvantages

- Unless the policyowner specifies otherwise, the organization receiving the gifted policy will likely have to assume responsibility for premium payments until the policy is paid up (depending on the organization's operational budget, this may not be a feasible way to accept a gift)

3) Giving earned dividends from a policy

This method only applies to permanent policies that explicitly earn dividends from the insurance company they're written through each year.

Donor Advantages

- Policyowner can get a charitable contribution tax deduction on any dividends donated
- Owner maintains full control of the policy

Donor Disadvantages

- Dividend pools are typically tied to a policy's death benefit, so donating dividends may reduce their death benefit

Recipient Advantages

- Organization receives an immediate cash payment – they do not have to wait for the policy to pay out to receive the value of the gift

Recipient Disadvantages

- Dividends are not guaranteed year over year, so organizations will not be able to rely on receiving a gift of the same value every year

4) Including charitable giving riders on a policy

Donor Advantages

- These riders typically come at no additional cost
- Charitable giving riders often do not reduce either the cash value or death benefit of the policy

Donor Disadvantages

- Limitations may apply on the maximum allowable gift amount, so their donation could be reduced or constricted

Recipient Advantages

- Receive a specific percentage of the policy's face value
- Eliminate the need to create, fund, and administrate separate gift trusts until the policy pays out

Recipient Disadvantages

- Limitations may be placed on the maximum allowable gift amount, reducing or constricting the size of the donation

What should an organization know about receiving a life insurance policy as a donation?

Like with anything else, it's important to assess both the upside and the downside before proceeding. Life insurance can be complex, and not all insurance companies operate the same. A little education goes a long way.

First, it's important to clarify the method by which the donor will give their policy to you. Then, assess the pros and cons as listed in the previous section. For example, if the option chosen requires that you assume responsibility for premium payments, is that something your organization can handle?

Once you decide to accept the gifted life insurance policy, it's important to keep track of that policy for the coverage period. Unless it's a permanent policy that you choose to surrender for immediate value, you'll want to make sure the policy premium payments stay current – whether your organization covers the cost or not – and you'll also want to make sure to track up-to-date policy values to make sure no material changes occur with the coverage.

If any of this sounds daunting to you, you should know there are plenty of people and technologies who can help ease the burden of monitoring a gifted policy. Whether you decide to work with an advisor who will manage your gifted policies for you, or you leverage a system like Proformex to securely store and manage your gifted policies, you don't have to do it alone.

Conclusion

Donating life insurance policies will continue to be a trend that grows more popular over time due to the unique tax benefits this method of giving offers both donors and recipients. It's important policyowners are empowered with information about this option so they can take advantage while supporting a cause or organization meaningful to them.

Charities, non-profits, or academic institutions that receive these gifted policies need to know how to manage those policies over time and should also know that managing those gifts doesn't have to be overly complex and difficult. Industry experts – whether individual financial professionals or technologies built by industry innovators – are more than willing to help ensure you're getting the value you need from those gifted policies.

To learn more about how charitable foundations, non-profits, and academic institutions with endowment funds are using Proformex to manage their gifted life insurance policies, visit our website.

Disclaimer: This article is intended for educational purposes only. Neither Proformex nor any of its representatives offer tax or financial advice. You should always consult an estate or tax attorney for specific advice for your unique circumstances.

About the Author - Mike Pepe

Mike Pepe capitalized on his nearly 20 years of life insurance policy expertise by launching Proformex, an inforce policy management platform that helps fiduciaries, financial planners, insurance brokerages and agents monitor, manage and govern their life insurance policies. Its SaaS (Software as a Service) solutions are designed to proactively alert customers of potential problems with their life insurance policies and protect against degradation and asset erosion.

Prior to founding Proformex and serving as its Chief Strategy Officer, Mike started in the life insurance business with Mass Mutual and quickly became a leading agent. Soon after, he cofounded River Financial Group, a full service financial advisory firm. His focus was on building a highly successful financial planning practice which took into account the various parts of a holistic financial plan. As he focused on estate planning, he started The TOLI Group, a life insurance firm which was designed to fill the gap in the market for insurance consulting and the need for ongoing policy monitoring and management support, especially as it relates to trust owned life insurance.

About Proformex

At Proformex, we're reimagining how the industry thinks about protection assets. Your life insurance and annuities data is valuable. We connect you to it. The result is an end-to-end, digital solution to manage life and annuities. We help you maximize potential from your existing business—increasing the lifetime value of your client relationships, mitigating policy and reputational risk, and creating new opportunities for revenue growth.

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