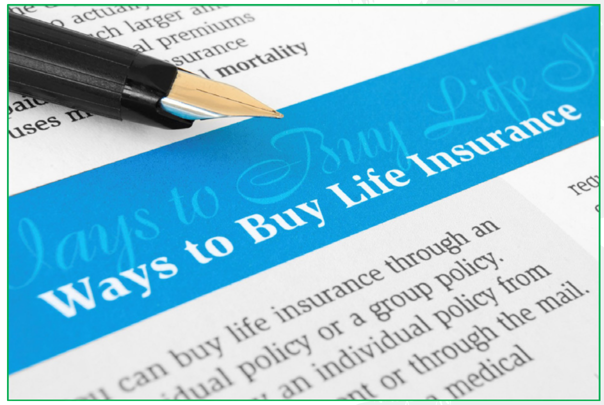
American Endowment Foundation

Leveraging Life Insurance for Charitable Good



Purchasing life insurance for estate liquidity reasons has been a standard practice for many years. However, with the proper structure, life insurance can help create a zero-tax estate plan by gifting the policy into a donor advised fund. This helps a donor achieve charitable good greater than the more common method of gifting either cash or marketable securities. Four ways to gift life insurance are:

1. Direct Donation of Existing Policy:
Donors who have old policies once acquired for other reasons (mortgage/debt risks, education for children, survivor income, etc.) may no longer need the coverage and can gift the policy directly into a donor advised fund (DAF). According to IRS regulations, the DAF administrator must become the owner and sole beneficiary of the life insurance policy.

However, determining the accurate value of that deduction requires an appraisal. Cash-value policies (i.e. whole life) are valued at fair market value (FMV), limited by their cost basis. The fair market value of a policy that is not fully paid up is the lesser of premiums paid or its interpolated terminal reserve amount. The FMV of a paid-up policy is valued at its replacement cost. How are these determined exactly? This is where a qualified appraiser is required to determine an accurate value.

2. Direct Donation of Dividends:
The annual dividends of the policy can be assigned into a DAF. This eliminates out-of-pocket contributions while still creating a deduction as dividends are paid. This process can be amplified by using the dividends to purchase a new policy of which the DAF administrator becomes the irrevocable owner and beneficiary.

3. Primary/Contingent Beneficiary of Life Insurance Policy:
Although this route will not create a current income tax deduction, it does create a federal estate tax deduction for the full amount of the proceeds payable into the DAF, regardless of policy size.

4. Charitable Rider:
A charitable rider is an addition to a life insurance policy that would pay a specific percentage of the face value of a policy to a specific qualified charity. There is usually no additional cost and it does not reduce the cash value/death benefit of the policy nor add a premium increase. For illustration, if a life insurance policy had a value of $1 million with a charitable rider of 1%, then at death, the heirs of the decedent would receive the $1 million proceeds of the policy and a specifically named charity would receive $10,000 (1% of the $1 million policy value).

Does it make sense to purchase a new policy for the purpose of charitable gifting?
If the individual is healthy and can pass an insurance physical, it may make sense to purchase new life insurance for the purpose of donating to charity. The death benefit could fund a special project or endow a donor's lifetime gifts forever through their DAF.

The DAF administrator must become the owner and sole beneficiary of the life insurance policy. The donor (and possibly their spouse) would be the insured. The donor would make the premium payment directly to the DAF administrator, and then that organization pays the premium to the insurer. The donor is able to deduct the premium amount as an income tax charitable deduction.