

## **Life Insurance as a Wealth Replacement Strategy**

Individuals who would like to donate assets to charity without affecting the value of the estate left to their heirs, wealth replacement insurance is becoming a popular option.

How it works:

- The donor wants to donate an asset to a charity without affecting the value of the estate left to their heirs
- To help offset the gift to charity, the donor purchases a life insurance policy based on their life; the donor's heirs are named as beneficiaries
- Upon the death of the donor, the heirs receive the proceeds of the policy in cash, replacing the asset donated to charity.

### **Advantages**

Wealth replacement insurance provides a number of benefits when completed to leaving other tangible assets to heirs. The beneficiaries receive the proceeds of the insurance policy tax-free and in cash. This can be a considerable benefit when compared to leaving tangible assets that may have to be sold in order to pay capital gains tax or real estate, where the asset cannot be easily divided or sold. The transition of assets is simplified by avoiding probate and estate administration fees. Last of all, the heirs will receive the proceeds in a timely manner – a significant benefit to consider during their special time of need.

### **Drawbacks to consider**

Due to fluctuations in the market value of an asset, the value of the policy may be less than the value of the asset donated to charity.

### **Tips**

- Purchase a life insurance policy with an increasing death benefit, the value of the policy can increase over time. This could help compensate the heirs for the increasing value of an asset that is donated to charity.
- If the donor has a spouse, they can reduce the cost of the insurance premiums by purchasing a joint second to die policy.

## The Benefits of Donating the Proceeds of Insurance

### **Donating a contract during life**

If you are looking for alternative ways to give, leveraging the benefits of insurance can be a very effective way to donate. The gift of a permanent life insurance policy during life, for example, provides donors with an affordable means to make a large contribution. Here's how it works:

- The donor arranges with a charity to purchase a life insurance policy based on the donor's life
- The charity is named as the owner of the contract, and the beneficiary of the proceeds upon the donor's death
- The donor then makes regular payments to the charity or to the life insurance company to make the premium payments.
- Upon the donor's death, the proceeds of the policy pass directly to the charity.

There is also the option of transferring an existing policy to a charity. The donor transfers ownership of the existing policy to the charity while naming it as the beneficiary of the contract. In return, the donor receives a tax credit based on the cash surrender value of the policy. The donor may have some income to include as the policy is treated as having been disposed of.

### **Advantages**

The advantages of giving the proceeds of an insurance contract to a charity makes this option stand out when compared to other alternatives. Firstly, it can provide individuals with an affordable means to leave a very substantial gift to charity. Secondly, because the insurance contract is owned by the charity, it is not considered part of the donor's estate. This means that the proceeds will pass directly to the charity upon the donor's death, without the possibility of the transaction being contested by creditors or heirs. And finally, because the charity is deemed to be both the owner and beneficiary of the policy, the donor can receive donation receipts for the premiums paid on the insurance contract during their lifetime.

### **Issues to Consider**

Once the ownership is transferred to the charity, it cannot be revoked. Another important consideration is the long-term commitment that is required on the part of the donor. The policy premium must either be "paid-up" front or premiums must continue to be paid.

### **Donating proceeds upon death**

Donating the proceeds of life insurance upon death is another planned giving option accomplished by naming the charity as the beneficiary of the policy. But unlike donating the proceeds from an insurance policy during life, this option provides donors with the ability to remain control over the eventual proceeds until death.

### **Advantages**

The donor will retain control over the policy – during their lifetime. The donor can access the surrender value of the contract, or designate a new beneficiary at any time. When the donor dies, the proceeds of the policy will be paid directly to the charity, bypassing probate and estate administration fees. A charitable tax receipt equal to 100% of the policy's value will be issued to the donor. The executor can either claim this on the deceased's final tax return or, if necessary, carry back any unused portion to the previous year.

### **Issues to consider**

Because the donor retains control over the policy, they will not receive any tax relief during their lifetime.