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Life Insurance as a Charitable Giving Tool Is More Attractive than Ever

By Vernon W. Holleman, III

Vernon W. Holleman, III,
Vernon W. Holleman, III, is president of The Holleman Companies in Chevy Chase, Md., which focuses on business-succession, executive-benefit and financial-security planning. He can be reached vernon@hollemanco.com.
www.hollemanco.com

In light of last year's financial meltdown, it is a good time to talk to the (still) wealthy about using life insurance as a financial tool for giving to charity.

For those with a private foundation, help them think about using life insurance as "asset replenishment" after the recent market storm. The idea is simple—to replenish recent asset losses of the foundation using life insurance on the donor as an asset that, created with the stroke of a pen, creates dollars not there today for real leverage tomorrow.

Life insurance can potentially afford the donor the ability to think about new opportunities for gifts, as today most are simply thinking of how to complete gifts already made and are making few new commitments. Uniquely, you can help them ensure that assets that have been lost are recovered or guarantee a nice return.

Charities love planned gifts—and today they are looking for good planned giving stories to tell. Help them tell by exciting your clients about the power of giving life insurance. After many of the exotic and hyped investments failed or proved a fraud, demonstrating the tax-free growth and returns of life insurance, a known commodity, is cool again.

Using life insurance is a great way for a donor to make a real impact—for example, at his or her alma mater. The school would apply for a $1 million life insurance policy that the school would own and be the beneficiary of. The donor would make annual gifts of the premium to the school and take charitable deductions for doing so.

In a recent example of this, my firm helped a 55-year-old man who wanted to create a gift using life insurance because making a notable current gift was not an option, but he wanted to leave an impact on the school he adored. We suggested he go through some preliminary underwriting to test the market for his insurability—with no obligation. After collecting medical records, the underwriter at the carrier with the most competitive product deemed he looked to be in "preferred" health. The donor had a number in his mind (they always do) and a preferred health rating would mean he could accomplish his goal of a $1 million policy with his budget.

After full underwriting, it turned out he was "super preferred," all the better. This created a roughly $9,500 annual premium for the policy. He examined several funding alternatives—pay forever and abbreviated scenarios, and determined the pay forever was the best bet because it provided the best return on his investment.

He also wanted to make sure the policy made it to his age 100 and that there was cash value in the contract, but did not want to fund the policy to have it endow (equal cash value to death benefit at age 100). The internal rate of return (IRR), if the donor lives to be 100, of the contract he chose will be no less than 7%—a handsome long-term net return. Both

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the donor and the school were pleased – the proverbial win-win.

Issues to consider

Insurable interest is the first planning aspect that must be confirmed. In my example above, the donor had not only gone to the school, he had two children who had gone there, had served on the school's board, and most important, he had a long track record of giving, both annually and during campaigns. Truth is, the school would suffer a financial loss at his death.

It is very important you understand the relationship of your client (the donor) with the charity so you are able to justify the insurable interest to the underwriter(s) at the carrier(s). Please do this *first*—don't just assume anyone with a charitable intent can acquire life insurance because they want to; insurable interest laws were established for a good reason. Also, you don't want to have gotten your client excited by the idea, only to find that they just started working with a charity and there is not enough history to justify insuring them.

It would be easy to assume that your client can take a full tax deduction for this planned gift of life insurance, but don't assume—confirm it with a tax professional, so that there are no surprises.

Insurability is important too. The specific rating classification is also important, as it makes a real difference in the planning. Today, most carriers have as many as five different standard or better ratings. Each improvement in underwriting class means savings for the donor and/or a greater gift to the charitable organization. Here it is key to shop multiple carriers, as those with standard and preferred "plus" ratings can create real savings over a carrier with only standard and preferred rating classes. However, this theory must be tested as costs will differ and a true market analysis is the only way to find the best product choice for the client.

You must help your client both budget for this acquisition—both short and long term. Don't assume that because someone of means is making a planned charitable gift that they will want to pay that premium forever, or that they won't ever have cash-flow issues. Therefore, be wary of using a no-lapse guarantee product that may have little premium paying flexibility downstream if a donor ceases payments. Also, remember the charity is going to own the policy and may need to cash the policy in before it matures—so having cash buildup is key.

On the other side, a whole life product may not give enough flexibility either, and a variable product that sees down markets may affect the expectations of the donor and the charity too much. Our best success using life insurance for charitable purposes has been with the traditional universal life product with good cash accumulation until late in life, but not funding it to endow, to keep the premium reasonable.

This strikes what we have found to be a reasonable balance between keeping the premium down, but building a cushion of cash value for periods of need, or years that accidentally may be missed or a decision by the institution to cash out early. Talk through with the donor and the charity these issues and their importance so proper planning can be implemented.

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