Cancer Research Society

100% research since 1945

GIVING WITH LIFE INSURANCE

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Research Society

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In 1945, several Montreal women were deeply concerned about the lack of cancer research in Canada. Under the leadership of Mrs. Betty Caplan, these enterprising ladies founded the Cancer Research Society.

Through fundraising activities such as teas, bazaars, and bake sales, they collected $2,400 in donations for cancer research during their first year of activity. Since then, the Society has developed into a national organization that annually raises millions of dollars to support approximately 100 research projects each year in respected Canadian institutions.
The members of the Board of Directors serve on a voluntary basis, as do the renowned scientists who comprise the Scientific Advisory Board. Many dedicated volunteers assist with administrative work and fundraising activities.

The Society is a major national organization that exclusively funds cancer research, awarding grants to innovative scientists working in Canadian hospitals and universities. In the last 20 years, the Cancer Research Society has funded a total of over 110 million dollars of cancer research across Canada, including over 40 million in the past five years.

Please note:

This brochure was created for donors and friends of the Cancer Research Society. Although the information contained herein comes from reliable sources, it is not a substitute for professional advice. We recommend that you consult legal, financial, and estate planning specialists before making a decision involving planned giving. The Cancer Research Society, its employees, its advisors, and its representatives cannot accept responsibility for errors, omissions, or damages, which could be related to the publication of this material.

Throughout the text, when necessary, the masculine singular pronoun is gender-neutral, designating both men and women.

Ce document est également disponible en français.

GIVING WITH LIFE INSURANCE

INTRODUCTION

Most people have some type of life insurance, but few understand what a flexible tool it can be for financial planning. Insurance is not just protection for emergencies: It can allow you to accumulate funds on a tax-sheltered basis to supplement your retirement income, provide replacement income for your dependents if something should happen to you, or help you and your family pay for anticipated future expenses such as children's education.

This brochure gives an overview of various types of life insurance. Like other financial instruments, different types of insurance are appropriate to different stages of life. What is best for parents of a young family will change once the children are grown. Later in life, insurance can be an important tool for estate planning or for use in charitable giving.

TYPES OF LIFE INSURANCE

Life insurance takes many forms, all serving the same basic purpose: *to provide cash to meet the needs of survivors at the insured person's death*. Depending on the policy, life insurance may have a cash value that can be drawn upon before death. Anyone buying insurance can choose among policies intended primarily for protection through death benefits, or policies designed for investment purposes, with emphasis on increasing cash value. There are three general types of life insurance policies:

Term life insurance maximizes the death benefit payable if the insured person dies within a specified time, and is popular with those who need maximum protection at the lowest cost. It is often purchased by young parents primarily concerned about financial security for their family. If you purchase term insurance, you are paying for the risk of your death year by year, and coverage will continue as long as you pay the premiums. The cost of premiums normally increases with age. Term life insurance does not accumulate cash value.

Whole life insurance combines a death benefit with predictable growth in cash value. The premium and death benefit usually are fixed, and the cash value grows according to a predetermined schedule, though some policies also pay dividends, which may be used to purchase additional paid-up insurance. Depending on the policy, the premiums may be payable for life or for a term of years, with the policy being fully paid-up at the end of that term. You may surrender the policy for cash value, or borrow all or a portion of the cash value while keeping the policy in force. If you purchase a whole life policy when you are young, you will pay a higher premium than for term insurance because you are investing in a cash value account as well as covering the risk of dying.

Universal or variable life insurance policies place greater emphasis on growth. The premium and/or the death benefit may change, and growth in the cash value will depend on investment performance. Premiums may continue throughout the insured person's life or end when sufficient reserves are accumulated to sustain the policy. Large initial premium deposits may make future premium payments unnecessary.

Group insurance policies normally are offered by an employer, or through an individual's affiliation with an organization. Policies that are provided by an employer have no cash value to the employee, but are designed to provide at least a minimal level of life insurance in the unlikely event of the employee's death.

Any of these policies can have an important role in a person's financial plan. As time passes, however, the original reason for the policy may become less important. Policies with a face amount that once seemed large can become insignificant with inflation. As young children get older, and their parents accumulate other resources, the need for family financial protection may decrease. Policies purchased in the past to provide cash for estate settlement may have become less necessary since the repeal of the Succession Duty and Estate Tax.

TAXATION OF LIFE INSURANCE

Life insurance proceeds received on the death of the insured person generally are not taxable. This is one reason life insurance is so valuable: it provides tax-free cash at a time when funeral expenses must be paid, and when family members are distracted from their normal activities. The proceeds of a life insurance policy can provide a financial cushion at such a stressful time.

Policies that accumulate a cash value can be surrendered for cash, but this will have tax consequences: any excess of the cash surrender value over the adjusted cost base (ACB) of the policy is taxable to the policyholder. "Adjusted cost base" is determined as follows:

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or policies acquired before 12/2/82, "adjusted cost base" refers to total premiums paid with certain adjustments.

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or policies acquired after 12/1/82, "adjusted cost base" refers to total premiums paid less the net cost of pure insurance for all years the policy has been in force, again with certain adjustments.

These rules mean that policies acquired after 12/1/82 are likely to have more taxable gain upon surrender. If you plan to cash in a policy, your insurance company should be able to provide the "adjusted cost base" for you. But remember, these rules apply only if a policy is surrendered for cash. If proceeds are received because of the death of the insured, they are not taxed, no matter what the adjusted cost base.

OWNERSHIP RIGHTS

Ownership rights in an insurance policy consist of a bundle of contractual rights over the policy and its benefits. These include the right to surrender or cancel the policy, to change the beneficiary, to assign the policy, to borrow against the cash value of the policy, and to choose a settlement option. Collectively, these are called the "incidents of ownership."

The incidents of ownership can be assigned to another person, or to an organization. (Insurance can be an excellent way to make a charitable gift at a modest cost.) Once ownership is assigned to another, however, the decision is irrevocable so it should be considered carefully.

POSSIBLE BENEFICIARIES

While most people think of family members as beneficiaries of an insurance policy, it also is possible to name your estate or a charitable organization as beneficiary, or even to create a trust with life insurance proceeds. These options are briefly described below.

Estate: Naming your estate as beneficiary of a life insurance policy provides liquidity that can be very helpful, particularly if significant taxes will be due for the year of death. (A disadvantage, however, is that the proceeds of the policy become part of probate for the estate, and therefore are subject to probate fees.)

Family members: Spouses and children are most frequently named as beneficiaries of insurance policies which are, after all, usually purchased as a means of providing for their financial security. For most policies, it is possible to name a primary beneficiary, such as a spouse, and contingent beneficiaries—other family members--in the event the spouse named as beneficiary does not survive the insured person.

Organizations: Naming an organization as beneficiary of an insurance policy can allow you to make a substantial charitable gift at a modest cost. This can be done either by changing the beneficiary designation of an existing policy or by purchasing a new policy. Because beneficiary designations can be changed—unlike assigning ownership of a policy, which is irrevocable—naming a charitable organization as beneficiary does not qualify you for a donation receipt, whether the policy is old or new. However, if the charity remains the beneficiary, it will issue a donation receipt to your estate when it receives the death proceeds. This can reduce the taxes payable at the end of your life.

Life insurance trust: It is possible to name a trust as the beneficiary of your life insurance policy, and this may have advantages. For one thing, a trust can disburse funds over time rather than all at once—which may be better for your beneficiaries. Also, you can give a trustee latitude on investment decisions, or restrict decision-making, according to your goals for the trust. Life insurance trusts can satisfy a variety of objectives, and they have different tax consequences depending on how they are structured.

CHARITABLE GIFTS OF LIFE INSURANCE

Using life insurance policies to make charitable gifts has many advantages: You can make a large gift while paying for it in installments (the annual premiums on the policy). If the charity is named as beneficiary or owner of the policy (or both), as long as the premiums are paid, the charity will receive the amount stated in the policy. The insurance proceeds also are guaranteed to be paid promptly. Finally, life insurance can allow you to make a substantial gift without reducing assets intended for other family members. Some of the ways to make a gift of life insurance are described below:

1. **Give a paid-up policy:** If you have a policy you bought years ago to meet a family or business need that no longer exists, you can give the paid-up policy to charity and receive a donation receipt for the cash value. (If the cash value exceeds your adjusted cost base, you will have taxable income equal to the difference as a result of the gift.)

   ***Example**: At age 75, Jennie Stevenson was thinking about making an endowment gift to charity and wanted to do something during her lifetime. She depends on income from her investments, but she remembered that she had a paid-up $50,000 life insurance policy she no longer needed. By making the charity both the beneficiary and the **owner** of the policy, she received a donation receipt for the policy's cash value. Her gift was irrevocable, and was creditable up to 75 percent of her income (the excess could be carried forward up to five years).*

2. **Give an existing policy on which premiums are still owing:** Jennie's policy was paid up, but if she still owed premiums and continued to pay them, she would receive donation receipts for those payments as well as for the cash value of the policy. She could make the premium payments directly to the insurance company, or make annual gifts to the charity, which would use her gifts to pay the premiums. In either case the charity would send her a donation receipt.

3. **Purchase a new policy and transfer ownership to the charity you want to benefit:** If you do not have an existing policy you no longer need, and if you want to assure a major future gift but cannot afford to do so with your present assets, you can purchase a new life insurance policy and transfer ownership to the charity of your choice. If insurability laws in your province allow, you and the charity may even be co-applicants on the policy. You would receive a donation receipt for the premiums you pay, since a new policy normally will not have any cash value to transfer.

   ***Example**: Anthony Clark, in his mid-40's, would like to make a substantial gift to a charity. He has no existing insurance policy to contribute, nor does he have sufficient assets for a major outright gift, but he does have discretionary income. He purchases a new $40,000 policy, naming the charity as both owner and beneficiary. He makes five annual payments of $1,200 each, receiving a donation receipt for each payment. Assuming a combined federal/provincial tax credit equal to 50 percent of the donation receipts, his annual tax savings are $600. Thus his "net cost" for each premium is only $600, and he makes a future gift of $40,000 for a total net cost of only $3,000.*

4. **Name the charity as beneficiary:** If you want to retain ownership of a life insurance policy in order to have access to its cash value, you can still use it to make a future gift to charity. By naming the charity as beneficiary of a policy, you provide a future gift (so long as the policy is kept in force). It is possible to name an organization as primary beneficiary (to receive all proceeds of the policy), as co-beneficiary (proceeds will be divided, perhaps benefiting a family member and the charity), or as a contingent beneficiary (proceeds will go to a family member or other individual, unless that person predeceases the insured person, in which case proceeds will go to the charity.)

   ***Example**: Ted Stanley and his wife no longer need the $50,000 death benefit from a policy he bought to insure his life when their children were young, but they want to retain ownership of the policy in case their circumstances change. They decide to have Ted name two charities on whose boards they serve as equal beneficiaries of the policy's proceeds. When he dies, his estate will receive donation receipts of $25,000 from each charity ($50,000 total), resulting in a significant tax savings on his final return. If the donation receipts exceed 100 percent of his income in the year of death, the excess can be carried back to the previous year, again subject to the 100 percent-of-income limitation.*

5. **Name your estate as beneficiary and provide a bequest to the charity.** Another course of action is to name your estate as beneficiary and provide in your will for charitable bequests equal to the death proceeds from the policy. Prior to the 2000 Federal Budget, this was the only way your estate would receive a donation receipt. However, charities can now issue receipts when proceeds are paid to them directly as beneficiaries.

LIFE INSURANCE AS WEALTH REPLACEMENT

Some individuals who are considering a major gift to charity—whether in the form of cash, securities, real estate, or artwork—are concerned about diminishing the legacy intended for their heirs. One possible way to resolve this dilemma is to purchase life insurance having a face value equal to the donated asset and to name children or other heirs as the beneficiaries. If the asset is given to charity outright, the tax credit for the gift often is large enough to pay the premium needed to purchase the insurance policy.

> ***Example**: Antoine and Michelle Lobre want to contribute a piece of art appraised at $100,000 to their favorite museum, but don't want to reduce their children's inheritance. The tax credit from the gift amounts to $50,000 over several years. They use a portion of the savings to purchase a "second-to-die" policy that will pay $100,000 to the children when the surviving spouse dies.*

If Antoine and Michelle decided not to make an outright gift, they could contribute assets to a charitable remainder trust and receive both income for life and a donation receipt for the present value of the trust principal that will eventually be distributed to charity. Part of their trust income, as well as the tax credit from the donation receipt, could then be used to pay premiums on a life insurance policy that would replace the value of the donated asset for their heirs.

> ***Example**: At ages 68 and 67, Antoine and Michelle contribute bonds valued at $200,000 to a charitable remainder trust. They receive the net income from the bonds, which in this case is $14,000 per year. Moreover, they are entitled to a donation receipt for $48,247. Assuming the combined federal/provincial tax credit is 50 percent of the gift, this receipt results in a tax credit of $24,123. They then purchase a $200,000 life insurance policy, naming their children as beneficiaries, and they use the dollars saved through the tax credit plus some of the trust income to pay the premiums. Through this arrangement they make a future gift to charity, protect heirs, and preserve adequate cash flow for themselves.*

CONCLUSION

Life insurance can play many roles in financial and estate planning. It can provide financial security for young families, and a more comfortable retirement as parents grow older. It can pay funeral expenses or fund capital gain tax liability that arises in an estate. It can be transferred as a gift to a family member or a charitable organization.

Your need for insurance will change as your income, assets, and even your children grow. By thinking of insurance as a flexible, rather than a fixed, asset, you can use it to meet your family's needs and accomplish other goals that are important to you, during your lifetime and beyond.

If you would like to explore the options available for making a gift through life insurance, please call, write or e-mail us:

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The Cancer Research Society's charitable registration number with Canada Revenues Agency is **11915 3229 RR0001**.

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