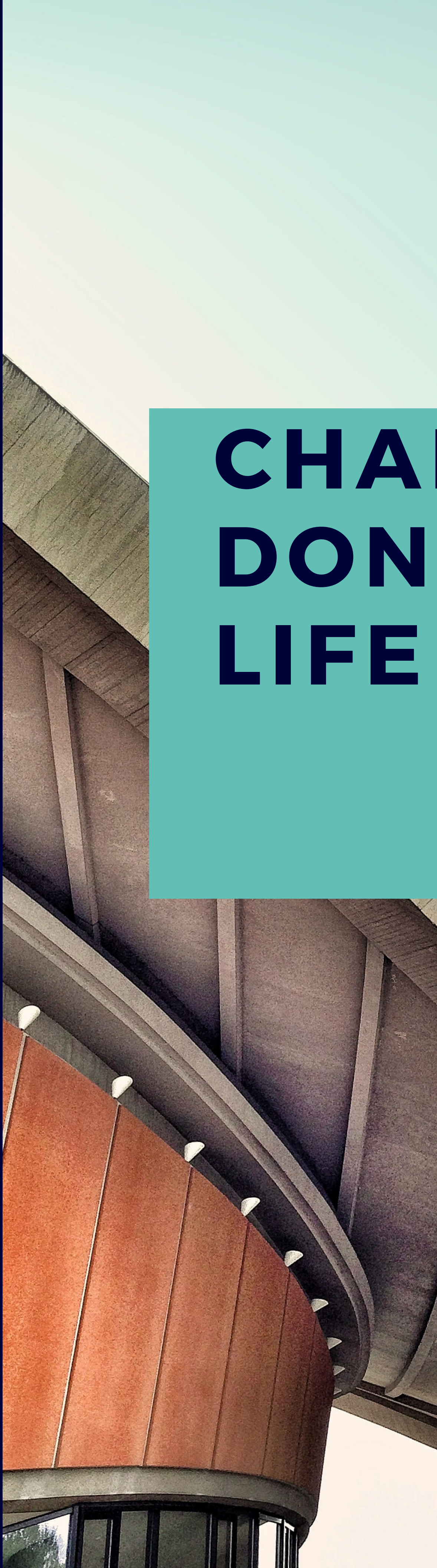

CHARITABLE DONATIONS OF LIFE INSURANCE

Guidelines for Canadian Insurers

MARCH 2021

CAGP

ACKNOWLEDGEMENTS

These best practices materials have been developed to provide guidance and support for donors, charities, advisors and insurers wishing to make charitable gifts of life insurance.

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We also wish to acknowledge the CAGP Government Relations Committee and National Education Committee, as well as a number of gift planners with a variety of Canadian charities who supported this work by reviewing draft materials and providing input and feedback.

OVERVIEW

This set of documents has been designed to assist donors, charities, insurance advisors and life insurers with the donation of life insurance policies to Canadian charities. It has been developed by the Canadian Association of Gift Planners in conjunction with the life insurance industry to help all parties mitigate risks, better protect consumers, and ensure that high-quality gifts of insurance are made to charities.

This Charitable Donations of Life Insurance Package consists of four Guides :

- *A Guide for Canadian Donors*
- *A Guide for Canadian Advisors*
- *A Guide for Canadian Charities*
- *A Guide for Canadian Insurers*

As best practices guides, all materials are optional, however **CAGP encourages each party to ask the other parties to follow their respective guides throughout the process.**

The first three guides listed above contain optional signature forms that will allow each party to document for their compliance records that best practices have been followed, should they wish.

These guidelines are applicable to both transfers of policies and the setup of new charitably-owned policies.

Additionally, other guideline resources available include:

- Understanding Tax Receipting for Charitable Gifts of Life Insurance
- How to use Life Insurance as a Charitable Gift
- What is Insurance Trafficking?

GUIDELINES FOR CANADIAN INSURERS

This information package is designed to assist you in making informed decisions when evaluating the transfer of an insurance policy to a Canadian charity, or in the setup of a new policy which is to be owned by a Canadian charity. It has been jointly developed by the Canadian Association of Gift Planners (www.cagp-acpdp.org), and representatives from the insurance industry.

In addition to this document, there are information documents available for charities, advisors and donors at www.cagp-acpdp.org. We encourage insurers to ask advisors to consider these best-practices documents when a charity is involved in the ownership of a new or existing policy that is being used for the purposes of making a charitable donation.

GUIDELINES FOR CANADIAN INSURERS

Steering clear of regulatory concerns and reducing risk

One of the driving factors in the creation of this toolkit was provincial insurance regulatory concerns around the trafficking of life insurance policies, in particular Stranger-Owned Life Insurance (STOLI) and viatical settlements. Both of these are prohibited in almost all Canadian provinces, with the exception of Quebec and Saskatchewan at the time of publishing these guidelines.

Provincial regulators are concerned that entities whose business is focused on the trafficking of life insurance policies (STOLIs and viatical settlements) may use their charitable status to try and bypass life insurance trafficking prohibitions. If an advisor or insurer were to participate in such a transfer – knowingly or unknowingly – it might result in compliance risks to their practice.

These guidelines are designed to help insurers and advisors to keep a compliant practice, and to ensure that there is a public set of standards and guidelines to help you interact in a positive way with charities.

IMPORTANT

These guidelines will help you minimize the risks (including regulatory risk) of acceptance of a life insurance policy donation. Adhering to these best practices cannot, however, guarantee that a transfer or donation of insurance will be free of regulatory concern.

Establishing a valid relationship between donor and charity

For either a new policy donation, or the transfer of an existing life insurance policy from a donor to a charity, to be appropriate there should be a clear relationship between the donor and the charity prior to the gift being made. One or more of the following may be used as evidence:

1. *The donor has a history of giving to the charity over multiple years.*
2. *The donor has a history of volunteering or working for the charity.*
3. *The donor or a close family member has been a past recipient of the charity's programs or services.*
4. *The donor has a clear interest in the mission and/or mandate of the organization.*
5. *The donor is making a gift to a community or other foundation, where the intention is to have the death benefit flow to its general funds for the betterment of the community it serves or to another charity that meets the above criteria.*

The absence of an existing relationship does not *automatically* mean a gift of insurance is illegitimate, however both advisor and charity should proceed with caution when engaging a donor offering a gift of insurance where there is no relationship. The advisor should take time to ensure that there is a clear and legitimate philanthropic intent on behalf of the donor that extends beyond a simple desire to obtain a tax receipt, especially for situations where ongoing premiums will be required for a long period of time.

EVALUATING THE LEGITIMACY OF A CHARITY

In Canada, charities are required to file annual reports with CRA. These reports are publicly available on the CRA Charities Directorate website, and contain a significant amount of information on a charity's activities. Any Canadian charity can be searched for by name or registration number at: https://apps.cra-arc.gc.ca/ebci/hacc/srch/pub/dsplyBscSrch?request_locale=en

Every registered charity in Canada is required to file an annual T3010 report. This report may be used as a quick and easy initial resource to help assess the legitimacy of a charitable organization. It should not be the sole tool used in making an assessment, but can be a "litmus test" to determine basic details about the charitable organization.

EVALUATING THE LEGITIMACY OF A CHARITY (CONT'D)

If there is concern about a charity being a legitimate organization, as opposed to a "front" for a STOLI or viatical settlement company, the "long form T3010" charity reporting form can be quickly evaluated.

Useful information to review includes:

Section B
- List of Directors/Trustees and Like Officials

Section C
- Provides descriptions of the charity's programs and services.

Schedule 5
- Information on acceptance of non-cash gifts (including donations of life insurance)

Schedule 6
- Detailed information on assets, income and expenditures.

Together, the information contained in the T3010 can help paint a basic picture of the charity and its operations as an initial first step. Without going into excessive detail, a legitimate charity should normally have a majority of arms-length directors and clearly defined programs and services. The financial details reported in Schedules 5 and 6 should give an indication as to the size and scope of the charity.

EVALUATING THE LEGITIMACY OF A CHARITY (CONT'D)

“Red flags” on donated policies

There are a number of possible “red flag” scenarios with donated policies:

1. The donor has no relationship with the charity and no clear philanthropic intent.
2. The size of the death benefit of the policy is very large relative to the donor’s and/or charity’s financial situation. It is important to evaluate the donor’s financial situation in relationship to the current and projected net worth of the donor and their estate, not their ongoing income.

“Yellow flags” on donated policies

“Yellow flags” may require some investigation but may not be cause for concern.

1. The charity takes over as payor.
   a) Legitimate – the donor is making gifts of publicly-listed securities to the charity to take advantage of preferential tax treatment. The charity then liquidates the securities and uses the funds to pay the premium.
   b) *Likely l*egitimate – the charity has determined that they wish to cash out the policy after donation, or the ROI is sufficiently high that they have made a business decision to pay for the policy on their own.
   c) Potentially problematic – there is no relationship between the donor and the charity AND the charity will become payor.
2. The policy is a term policy, other than term to 100. Generally, term policies are limited in nature and it would be unusual for a charity to accept one as a gift, unless the plan was to exercise a conversion option. There may be legitimate reasons for the gift and/or conversion, however, it may be wise to ask for documentation as to the reasons the gift is being made.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY

Underwriting a policy for charitable ownership can have some different considerations to take into account as compared to underwriting a for-profit, corporately-owned policy. Charities do not have a shareholder structure and the considerations and evidence to support insurable interest will be different. This document is intended to highlight some of these differences and provide a general overview of the considerations insurers may want to take into account when underwriting a policy to be owned by a charity.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Personal needs should be met first

The donor should demonstrate they already have an appropriate amount of insurance in place to fund their own personal needs prior to applying for a new charitably-owned insurance policy.

Insurable interest

Insurers will look to establish the charity has an insurable interest in the life to be insured. This will require the applicant to provide sufficient evidence of both a connection to the proposed insured, and that the charity has a pecuniary interest in the life of the insured. Assuming the insurable interest is established, the amount of insurance to be applied for must then be reasonable. Each of these factors is discussed below.

> It is important to realize that each insurer will have its own criteria on each of these issues, and that each policy application will be assessed on its individual merits and the supporting evidence submitted.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Establishing a legitimate connection to the charity

The following factors may support that a legitimate interest exists in a charity:

1. The donor has a history of giving to the charity over multiple years.
2. The donor has a history of volunteering or working for the charity.
3. The donor or a close family member has been a past recipient of the charity's programs or services.
4. The donor has a clear interest in the mission and/or mandate of the organization. While individual circumstances may vary widely, the insured should be able to clearly describe why they are interested in supporting this particular charity.

   As an example, someone who grew up in an abusive household may wish to support a women's shelter. In this case the donor would not qualify under (3) above but there would be a very clear connection between the mandate of the charity in question and the donor's background.

5. The donor is making a gift to a community or other foundation, where the intention is to have the death benefit flow to its general funds for the betterment of the community it serves or to another charity that meets the above criteria.

Evidence to support this connection will be required and each insurer will assess the case on its own merits, and will have its own standards as to what is acceptable.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Establishing the pecuniary interest of the charity

Establishing the pecuniary interest of a charity may be done through a variety or combination of methods within the insurer's comfort level:

1. Risk of loss through death established from a history of past donations.

2. Risk of loss through death from a pledge made by the donor for future gifts.

3. A clear commitment to make a gift to the charity as part of the donor's estate plan.

Any of the following may be helpful as evidence:

- An existing bequest made in a will.
- An existing bequest via a beneficiary designation on an asset. (RRSP, Insurance, including Segregated Funds, Annuities, etc).
- A pledge or gift agreement signed by the donor to provide the charity a gift from their estate which establishes the terms of the gift.
- An existing financial and estate planning document outlining an estate gift to the charity.

The insurer will need to review the specific situation and all the facts in totality on a case-by-case basis to determine if the pecuniary interest is established and if the need for the insurance, the estate planning considerations, and any other relevant considerations are acceptable to the insurer. **A simple stated desire to make a donation will not likely be enough.**

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Assessing the reasonableness of the amount of insurance

Once the insurable interest is established, the reasonableness of the amount of insurance will be an important factor. There is a connection between the amount of insurance and the extent of the pecuniary interest.

Charitably-owned insurance should not be creating an estate. The donor’s past pattern of giving to the charity, and/or their evidenced future charitable intentions will be the most important factor to be taken into account in most situations and the evidence to support the amount will be important (see also discussion under the next section '**Understanding how donors give from their Estate**').

In assessing the reasonableness of the amount of insurance being applied for, the insurance should also have a death benefit and premium that is reasonable in light of:

- the donor’s net worth,
- the donor’s ability to pay the premium,
- the donor’s estate and family situation, and
- the donor’s other personal or corporate insurance coverage.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

As noted previously, the insurance should not be creating an estate to gift. Furthermore, most donors would not normally be giving away the majority of their estate when they have other family to consider (although, in the case of estrangement or a very high net worth, this may not hold true), whereas a donor with no family or other interests to consider may give a higher percentage of their worth to a charity.

The amount of the donation should therefore be considered in the context of the donor’s net worth and other estate assets. A donor with a $2,000,000 net worth in their estate who wishes to leave a $100,000 policy to charity would be reasonable. In the opposite scenario, a donor with a projected $100,000 estate value wishing to leave $2,000,000 as an insurance gift should clearly be cause for concern and should generally not be acceptable.

Each insurer may have their own internal underwriting guidelines and will need to review the specific situation and all the facts in totality on a case-by-case basis to determine if the life insurance need and amount are justified.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Understanding how donors give from their estate

Charities rely on estate gifts as a major source of stable long-term funding, and hence protecting a planned estate gift is of major financial importance to the charity.

For the donor, insurance can be a way to ensure a charitable bequest is guaranteed to be funded upon their passing. Other assets, such as investments or cash could be given, but there is always a risk that such gifts could fail due to market fluctuations, unexpected heath care costs, or even litigation around the estate, which may delay or reduce available funds to gift from the estate.

In Canada, research by CAGP and other organizations has shown that the amount given at death by estate donors is often 100 to 1000 times higher than their annual contributions.

Often donors limit the amount given to a charity in their lifetime to ensure they have sufficient personal resources while alive but intend to leave a significantly higher amount at their death (while still being reasonable in light of the size of their estate). While monthly and annual donors are the most likely of all donors to make estate gifts, there are often gifts made from estates from individuals who did not give to the charity in their lifetime.

When applying this thinking to charity owned life insurance, it is important to note that insurers need to assess the reasonableness of any policy amount when underwriting, and most insurers commonly look to the loss that is being insured. Common examples in other life insurance contexts are to plan for estate taxes, income replacement of a spouse, key-man insurance, and buy-sell business arrangements. While these losses do not necessarily have a direct analogue to a donor/charity arrangement, there are a number of proxies that may be used to help assess the value of the donor to the charity.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Past giving is one relatively easy proxy to use in assessing the amount, and some lesser multiple of the prior annual giving may be easier to accept as a reasonable amount by many insurers. Larger multiples, and any sizeable amount where there is no prior history of giving will require additional consideration and may be challenging to justify if excessive.

Other complementary evaluations of the donor's worth to the charity may include pledges made by the donor, existing estate gifts and other evidence as outlined earlier in this document.

To help illustrate that the long-term value of a donor to a charity is often not fully reflected in past annual giving, one of the largest Canadian hospital foundations provided CAGP with data from nearly three decades of research. 59% of their estate donors who were also annual donors left estates to the foundation that were more than 300% higher than their cumulative lifetime giving. 9% gave between 200% and 300% of their cumulative giving, and 8% gave an estate gift that was between 100% and 200% of their cumulative lifetime gifts. Ongoing research in this area by CAGP and other organizations supports that this is a consistent finding across the entire sector.

UNDERWRITING GUIDELINES FOR ISSUING A NEW POLICY TO BE OWNED BY A CHARITY (CONT'D)

Structure of new policies intended for charitable ownership

A new policy owned by a charity should almost always be a limited-pay policy of some kind. The persistency and potential lapsing of the policy will be a concern for the charity, the donor, and the insurer.

While a pay-for-life policy may be viable in certain circumstances, as a general rule the younger the donor, the more likely a policy should be limited pay, in order to mitigate risk to the charity.

There are circumstances where a pay-for-life policy would be appropriate. However, as a reasonable guideline, product suitability should be questioned if a pay-for-life policy was chosen instead of a limited pay if the insured is under age 65. The younger the donor, the more concerning a pay-for-life policy is from a suitability and persistence standpoint.

A term policy, other than Term-100 proposed to be owned by a charity at onset should always be strongly questioned during the underwriting process.

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