

## **BUSINESS LIFE INSURANCE**

### *What is Business Life Insurance?*

Business Life Insurance provides protection from the danger of financial loss caused by disability or loss of a business owner, partner or key employee. Business Life Insurance can ultimately provide:

- *Income* to owners', partners' or employees' families
- *Benefits* to owners, partners or stockholders
- *Coverage for debts* of a business
- *Assurance* the business can continue to operate as usual

### *The Need for Business Life Insurance*

If a business is a sole proprietor or a partnership, when the owner dies, by law, that business or partnership ceases to exist. The family of that sole proprietor or other business partners must be assured that income will still be provided so the business can continue.

The needs of the owner of a corporation are similar to those of a partnership. In addition, business owners look for ways to protect themselves in case they lose a key employee to death or because that employee leaves the company. They also look for a way to provide a life insurance incentive program that would provide benefits to the employee's spouse should the employee die.

### *Business Succession*

The owners of closely held businesses may have strong emotional ties to their companies. They are justifiably proud of the company and want their families to continue to benefit from this success. However, few business owners have given much thought to what will happen to the business when they die.

### *Critical Questions for Business Owners*

- Who will purchase the business interest?
- What is a fair price?
- When will the sale be made?
- Where will the funds come from?

Business planning, especially for the succession of a business, is a very complex discipline and will generally require the efforts of more than one professional. A business planning team may consist of the client, the agent, the attorney and the accountant.

## *Buy-Sell Agreements*

A buy-sell agreement is a legal document drawn up by an attorney stipulating what happens to the business owner's share in a business upon death, disability or retirement. The buy-sell agreement provides:

- Specified parties will purchase a deceased owner's interest at an agreed- upon price.
- The deceased owner's estate is obligated to sell the interest at that price.
- There are no options; both the sale and purchase are mandatory.

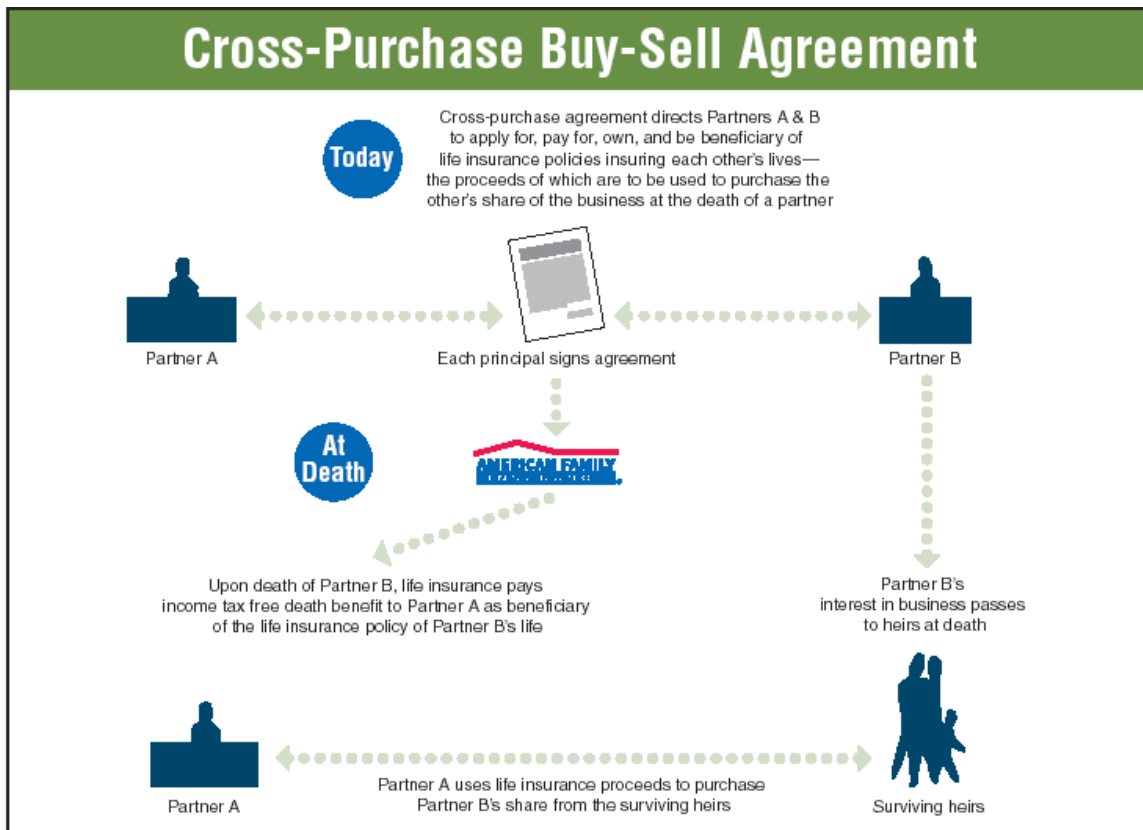
Life insurance can be used to fund the buy-sell agreement. Term, whole life or universal life can be written to cover a pre-established price. For a sole-proprietor, this buy-out is called a one-way buy-out. For partnerships and corporations, the most common types of buy-sell agreements are cross-purchase and entity purchase agreements.

### *The One-Way Buy-Out Plan*

Under a one-way buy-out plan, a key employee agrees to purchase a deceased business owner's interest. To fund the plan, the key employee purchases a life insurance policy on the life of the business owner. The key employee owns the policy, is the beneficiary and pays the non-deductible premiums. The face amount of the policy is equal to the purchase price of the business. Upon the business owner's death, the key employee usually receives the proceeds free of income taxes. Pursuant to the one-way buy-out agreement, the funds are then transferred to the deceased owner's family or estate in return for his or her ownership interest.

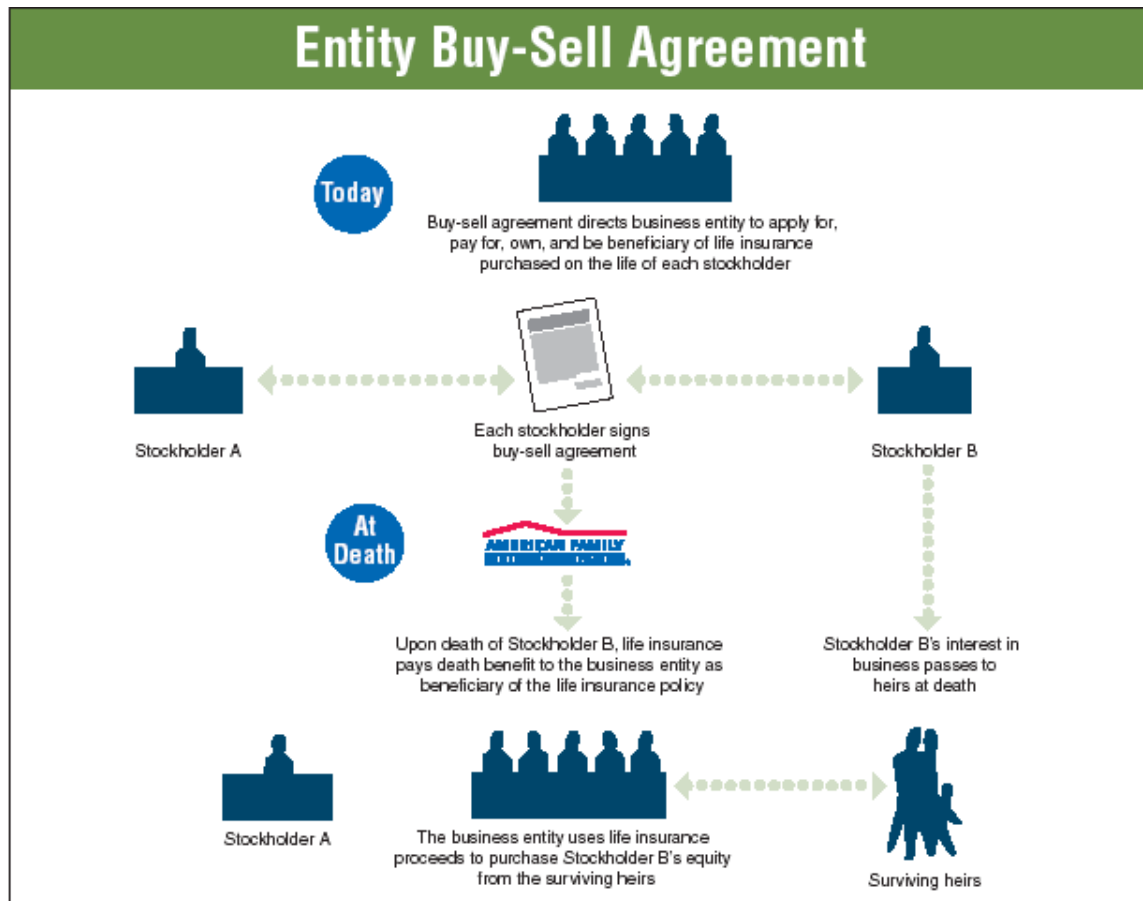
### *The Cross- Purchase Plan*

The cross-purchase plan is an agreement between the owners individually. If life insurance is used to fund the cross-purchase plan, each business owner is the applicant, premium payer, beneficiary and owner of insurance on the life of each of the other owners, in an amount equal to his/her share of the purchase price.



### *The Entity Purchase Plan*

The entity purchase agreement (stock redemption in the case of a corporation) is an agreement between the business and its owners. The event triggering the entity purchase can be death, disability or termination of employment of the owner. If life insurance is used to fund the entity purchase plan, the business is the applicant, premium payer, beneficiary and owner of insurance on the life of each of the owners. The amount is equal to the value of each business owner's interest in the company.



### *Key Employee Life Insurance*

Nearly every business has key employees who are critical to the overall success and profitability of the business. Key employee insurance is self-explanatory - insurance on the life of a key employee, purchased to reimburse an employer for the economic loss caused by the death of that employee.

Not everyone, obviously, is a key employee. Smaller businesses tend to have a great need for key employee insurance since they do not have a large pool of employees from which to select a replacement if a key employee dies. A key employee can be anyone who is responsible for management decisions, who is highly compensated, who has a significant impact on sales, or who has a special rapport with customers.

Key employee insurance is one of the simplest of the business life insurance plans to implement. The business applies for, owns and is the beneficiary of insurance on the key employee's life. If the employee dies, policy proceeds are paid income tax-free to the employer.

### *Executive Bonus Plan*

Executive bonus is a life insurance incentive plan designed to help attract and maintain valuable employees. It allows an employer to provide valuable life insurance protection for a selected employee on a tax-deductible basis. The employer has total discretion to select the employee, or employees, to be covered by the agreement, as well as the amounts of insurance to be provided.

The employee usually applies for and owns the policy, naming someone other than the employer as beneficiary. The premium is declared as additional compensation on the employee's W-2. Since premiums are taxed as additional compensation to the employee, it is deductible in the year paid by the employer. As with other life insurance, the death proceeds will be received income tax-free by the employee's personal beneficiary.

