

in sights

The Need for Life Insurance in Business Succession

February 2020

Prepared by:

Executive Benefits Network
833 East Michigan Street | Suite 1480
Milwaukee, WI 53202
Phone 414.431.3999
Fax 414.431.9689
ebn-design.com

Business Succession and Life Insurance Go Hand in Hand

Life insurance plays a significant part in an individual's future and financial plan. Personal life insurance planning protects a family from the unknowns in life. Along with personal planning, insurance can be critical in business succession to ensure a business' financial security and longevity. As a business owner, you not only have to worry about your family, but you also have to take into consideration other individuals that depend on you including business partners and employees. As business owners spend a majority of their careers building the success of their business, the future needs to be considered. Maintaining the future and maximizing the value of the business should be a priority to the business owner.

There are many individuals that play a part in helping a business initiate a business succession plan including insurance advisors, accountants, attorneys and other financial advisors of the business. These individuals should all be linked together to ensure an effective plan is implemented. This whitepaper will go through how business succession and life insurance go hand in hand.

The Why for Business Life Insurance

1) Buy-Sell Agreements

In the event of a death or departure of a business owner, a buy-sell agreement allows the other business owner to have the possibility of purchasing the owner's interest in the business. Life insurance allows the partner in the business to have the cash to buy-out the other's interest. This type of agreement can eliminate conflict between all parties involved (e.g. family and key executives) and ensure the business continues to run smoothly. A permanent life insurance policy with cash value in the policy can assist with lifetime buy-outs.

2) Retirement

If a permanent life insurance policy with cash value is purchased on the business owner, the cash value could be used as a source of funding at the owner's retirement. Owners of the policy are able to take out policy withdrawals of premium basis and policy loans on a tax-free basis (subject to limitations). Having accessible cash allows the owner retiring to have more flexibility and less reliance on the business.

3) Estate Equalization

In a business, some of the owner's family members may be involved in the business, while others are not. To avoid conflict in an event of a death, life insurance plays a role in determining how the business is split up between family members. The beneficiary on the life insurance can be separated by listing those who are active members of the business and inactive members, so they may get the same amount of funds. It can also be written for the active business family members to have a fund to buy out the inactive family members. By using life insurance, it allows for equal treatment without conflict.

4) Key-Person Insurance

Buying a life insurance policy on the owner or a key employee can reduce the financial impact a business may incur in an event of a death. In the event of a death of a key employee, a loss of revenue and knowledge may be detrimental to the business. As the business takes time to recover, having additional funds to cover the loss, allows the business to have necessary liquidity to weather the turbulent times.

5) **Nonqualified Deferred Compensation Plans**

Life insurance policies can be used to informally finance a deferred compensation plan to recruit, retain and reward key employees. A nonqualified plan provides the key employee with an extra financial incentive from the business. The business owns this policy on the key employee, if the employee dies before the benefit is paid out, the business receives the funds. If the key employee retires or is employed in accordance to the terms of the nonqualified deferred compensation plan agreement, the company uses the policy's cash value to provide supplemental retirement income to the employee.

6) **Creditworthiness**

Lending institutions typically look for and require a business life insurance policy on an owner to give a business loan. It allows the lender to ensure that that borrower has assets to fall back on if something were to happen. The life insurance serves as an additional security for the business and business loans.

7) **Access to Accumulated Cash Value**

The cash value on a permanent life insurance product allows the owner of the policy to have access to immediate cash at needed times, including paying overhead expenses, uncertainty due to the economy, and supplemental cash flow. Any businesses may run into unseen circumstances, such as a recall, late-paying clients, a loss of a key-client, large business expense, etc. The cash value serves as a tax-advantaged saving vehicle for the business.

8) **Liquidity**

In the result of a death of a owner, life insurance provides the business immediate liquidity to avoid a forced sale of a business due to taxes, liabilities and expenses needed at the time of death.

Next Steps

As stated there are many benefits to including life insurance into your business succession plan for not only the owner, but for business partners, employees, family, and others that are involved. It is important to determine a plan with a life insurance/benefit specialist, attorney, accountants and financial advisor.

Product Selection: The life insurance/benefits specialist will be able to structure a plan based on the need of the coverage of the business and the budget. Different products and plan ideas will be suggested to ensure all aspects are being thoroughly considered to make the best plan for the business.

Buy-Sell Agreement: Ensure a buy-sell agreement in place for the owners of the business that if an owner dies, becomes disabled or leaves the business, the other owners, would be able to buy that individual's part of the business.

Post-Planning: Once a plan is implemented, it is important to monitor and review each year. Business and the economy does not stay the same from year to year, changes in the business' value and/or ownership could change the agreements or the amount of insurance needed. Review the product performance each year to ensure the cash value is meeting the objectives it was purchased for.

About Executive Benefits Network (EBN):

As the leading industry advisor, EBN specializes in the customized design, administration, and informal financing of Nonqualified Executive Compensation and Benefit Plans (Deferred Compensation Plans), as well as the procurement of Bank Owned Life Insurance (BOLI) programs to attract, retain, and reward key executive talent. We emphasize the importance of education and build long-lasting relationships with clients in all 50 states, and we have access to the highest rated insurance companies in the nation. Lastly, we believe that no two companies are alike in their needs; therefore, customization of executive benefit and compensation plans is paramount to a successful program.

ABOUT THE AUTHORS



R. David Fritz Jr., CLU®
Managing Partner
dfritz@ebn-design.com
Office: (414) 431-9688

David is the Co-Founder of Executive Benefits Network and a 34-year veteran of the financial services industry. David is a frequent speaker and author across the banking industry as an expert in the area of Nonqualified executive benefit plans and Bank Owned Life Insurance programs. David is the Past Chairman of The American College of Financial Services Foundation, Director of the Association for Advanced Life Underwriting (AALU) where he Chairs the BOLI/COLI/Nonqualified Plan Committee, Trustee of the Village of River Hills and President of the Milwaukee Country Club. He is a member of the Illinois Bankers Association, Wisconsin Bankers Association, Indiana Bankers Association, Bank Holding Company Association, the Society of Financial Service Professionals and the MDRT Association's Top of the Table.



Patrick J. Marget, JD, CPA, CFP®, CLU®
Managing Director
pmarget@ebn-design.com
Office: (414) 431-9681

Pat is a Co-Owner and Managing Director of Executive Benefits Network and a 20-year veteran of the financial services industry. Prior to entering the financial services industry, Pat worked as a senior accountant in audit for KPMG in the bank service area and as an attorney for Michael Best & Friedrich LLP where he concentrated on general corporate and securities law. Pat's career focus is in the BOLI/COLI marketplace, as well designing creative strategies for executive compensation planning, business succession planning and estate planning. Pat is a shareholder and Director of a bank in Iowa and is an active member in the State Bar of Wisconsin. He is a frequent speaker in industry meetings and seminars. He is a member of the Community Bankers of Iowa, Iowa Bankers Association and Wisconsin Bankers Association.