AN OVERVIEW OF KEY PERSON BUSINESS PROTECTION PLANS

Over the years, you and your team have worked tirelessly to grow the value of your business. Along the way, you have made important decisions that have defined the success you experience today. As you think about your current team and the future of your business, have you considered the following questions:

According to a survey of small businesses by the National Association of Insurance Commissioners, **71%** of the firms surveyed said they were very dependent on one or two key people for their success. However, only **22%** of respondents had key person life insurance in place.

1. HOW WOULD THE LOSS OF A KEY SALES, BUSINESS DEVELOPMENT, OR OPERATIONS EMPLOYEE IMPACT YOUR ORGANIZATION?

2. HOW ARE YOU PROTECTING YOUR BUSINESS FROM AN EARLY DISABILITY, DEPARTURE, OR DEATH?

For many businesses, especially small to medium sized growing businesses, the loss of a key employee could be detrimental to continuing success. A properly funded business protection plan can provide the needed immediate funds when an event occurs. Some additional reasons for key person coverage would include:

- Your business needs to secure a loan or is currently carrying debt
- An indispensable employee that:
    - a) is highly productive in the areas of sales or business development, or
    - b) has a unique talent that would be very difficult to replace
- A larger company acquires a smaller successful business

Key Solutions

- Employer-Owned Life Insurance
- Individual Disability Coverage

Key Considerations

1. HOW MUCH LIFE INSURANCE COVERAGE DO I NEED ON MY EMPLOYEES?

It depends on how valuable the employee is to your organization. A good rule of thumb is to provide 5x-10x the total compensation of the employee. Key employees that are difficult to near impossible to replace should lean towards the higher amount of coverage to account for the delay in finding a replacement. Life insurance companies will consider between 10x and 20x income for ages up to age 69 for established businesses.

2. BE SURE TO OBTAIN NOTICE AND CONSENT FROM YOUR KEY EMPLOYEE TO COMPLY WITH IRC 101(J)

If the notice and consent requirements of IRC 101(j) are not met, death proceeds from employer-owned life insurance contracts may be taxable as ordinary income in excess of cost basis.

The Value of Permanent Life Insurance:

Permanent life insurance builds cash value inside the policy on a tax-deferred basis, which can be accessed via tax-favored distributions. Imagine the opportunity of utilizing this cash value as a mechanism for funding your business needs such as employee bonuses, a payout for separation of service or retirement, unexpected expenses, or any other business need. All while sheltering the earnings of the policy from taxation and providing a tax-free death benefit to protect your business.

Since you are insuring an indispensable employee, it would also make sense to implement a plan to reward and retain this key employee. The tax-deferred cash value accumulation of life insurance can be carried as an asset on the balance sheet of the business. In many times reducing or eliminating the long-term cost of the insurance itself. The life insurance policy could be used to fund executive benefit plans such as:

- Deferred Compensation
- Supplemental Executive Retirement Plan (SERP)
- Executive Family Protection
- Personal Estate Planning

The Value of Disability Insurance:

Individual disability coverage as a part of the business protection plan provides the business funds to overcome the financial challenge of the loss of a key employee if they become too sick or hurt to work. This is a risk that may be overlooked, but when individual disability and life insurance coverage are coupled together, the business protection plan is even better equipped to handle unexpected events.

The continued success of a business depends on its key people. Key person life insurance as well as key person disability insurance are important risk management tools. An annual premium paid to fund related policies is a small price to pay to manage a potential loss to a company.