



Business Use of Life Insurance

What is it?

Businesses use life insurance in a variety of important ways. For example, life insurance is the preferred method of funding buy-sell agreements. It is also a major component of many employee benefit programs, both group plans and special carve-out plans for highly compensated employees. Life insurance taken on the life of a key employee can provide cash to finance any losses and expenses that result from the individual's sudden death. Also, life insurance provides a secure source of funding for a company's qualified and nonqualified retirement plans. Life insurance can also be used to guarantee repayment of a business loan, allowing an owner to obtain financing for a new or expanding business.

Using life insurance for business purposes can have significant tax consequences. It's important to understand the issues up front and to structure the arrangements so as to minimize or eliminate the tax impact.

Funding your buy-sell agreement with life insurance

If you're a party to a buy-sell agreement that obligates you to purchase your partner's business interest if he or she dies, will you have the funds to pay for your partner's share? You'll need to set aside a sizable cash reserve if you expect to fully fund the purchase. If you think you can simply take out a loan if needed, you

may find yourself unable to obtain one if your partner's death results in a disruption of business with an accompanying loss of revenue. Life insurance provides an alternate method of funding a buy-sell agreement. If you and your partner are insurable, it offers relatively low-cost coverage. And its use is not limited to your partner's death. If you purchase permanent cash value insurance, you can use the accumulated cash value to purchase your partner's share if he or she retires or becomes disabled. For more information, refer to *Funding Your Buy-Sell Agreement with Life Insurance*.

Use business life insurance for tax planning

Life insurance is an important feature of many business arrangements. Its most important uses include the following:

- Funding buy-sell agreements
- Providing an employee benefit
- Insuring a key employee
- Guaranteeing a business loan

Using business life insurance for these purposes presents many tax-planning opportunities. It's important to plan carefully because the tax consequences can be significant enough to spell the difference between a business's success and failure. For more information on the issues you should consider in tax planning, refer to *Use Business Life Insurance for Tax Planning*.

See disclosures on final page.

Life insurance as an employee benefit

Life insurance is a basic component of many employee benefit packages. As an employer, you may want to consider offering most employees some form of group plan. For highly compensated employees, you can offer individualized coverage through a carve-out plan, such as a split dollar plan, a reverse split dollar plan, a death benefit only plan, or an executive bonus plan. Life insurance provides advantages to both you and your employees. Your employees can receive death benefit coverage at minimal or no cost since you pay some or all of the premiums, and, if your company is a C corporation, you may be able to claim the premiums as a deductible business expense. For more information on the variety of life insurance plans you can offer your employees, see Life Insurance as an Employee Benefit.

Split dollar life insurance, including nonqualified deferred compensation plans

Are you seeking a low-cost method to attract, motivate, and retain key employees? Are you also interested in finding a way to fund nonqualified deferred compensation plans for them? A split dollar plan allows you to carve out key employees from your group plan and offer them life insurance while fully securing your cash outlay. For more information, refer to Split Dollar Life Insurance, Including Nonqualified Deferred Compensation Plans.

See disclosures on final page.



Group life insurance

Many employees have come to expect group life insurance as part of their benefits package. As an employee, group life functions somewhat differently from your individual life insurance plan. It offers a number of important advantages. For a detailed explanation of some of the unique characteristics of group life insurance and for tips on whether to accept group life if your employer offers it, see Group Life Insurance.

Life insurance coverage on a key employee

As a business owner, the death of a key executive, manager or shareholder can leave you facing a number of cash needs. A replacement must be recruited and trained, inexperienced subordinates may cause mistakes or delays that result in losses, loans may come due, and customers must be assured the business will continue to operate. How will you finance these expenses without jeopardizing your business operations and cash flow? Key employee life insurance can protect your

business against financial loss if a key person dies. For more information, refer to Life Insurance Coverage on a Key Employee.

Death benefit only plans

A death benefit only plan is another form of group carve-out arrangement. As an employer, it allows you to offer key employees an attractive benefit at a reasonable cost. These plans are specifically designed to provide an estate tax advantage by keeping the death benefit out of the employee's estate at death. For more information, see Death Benefit Only Plans.

Life insurance in qualified plans

In addition to using life insurance to provide a death benefit for your employees, you can also use it to fund your company's qualified retirement plan. Certain legal limits apply in general and according to the type of plan (defined contribution or defined benefit). Using life insurance together with a qualified plan combines the benefits of both while also offering unique advantages to you and your employees. For more information, refer to Life Insurance in Qualified Plans.

Corporate-owned life insurance (COLI)

How can you assure employees that you'll be able to meet your obligations under a nonqualified deferred compensation plan? You can use corporate-owned life insurance (COLI) to fund your nonqualified deferred compensation plan. COLI provides a source of cash to meet your obligations and assures employees that their benefits will be protected from the demands on your cash flow. For more information, see Corporate-Owned Life Insurance (COLI).

Business credit life insurance

As the owner of a new or expanding business, you may have difficulty obtaining a loan to finance your business needs. Lenders want assurances that loans will be repaid, even if you die unexpectedly. Business credit life insurance can make it possible--or easier--for you to obtain a business loan by guaranteeing its repayment through a life insurance policy taken on your life. For more information, refer to Business Credit Life Insurance.

Disclosures – Important – Please Review

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