FUNDING A BUY-SELL AGREEMENT WITH LIFE INSURANCE

HEFFERNAN INSURANCE BROKERS

Because You're Different

As a partner or co-owner (private shareholder) of a business, you've spent years building a valuable financial interest in your company. You may have considered setting up a buy-sell agreement to ensure your surviving family a smooth sale of your business interest and are looking into funding methods. One of the first methods you should consider is life insurance. The life insurance that funds your buy-sell agreement will create a sum of money at your death that will be used to pay your family or your estate the full value of your ownership interest.

How funding with life insurance works

When using life insurance with a buy-sell agreement, either the company or the individual co-owners buy life insurance policies on the lives of each co-owner (but not on themselves). If you were to die, the policy owners (the company or co-owners) receive the death benefits from the policies on your life. That money is paid to your surviving family members as payment for your interest in the business. If all goes well, your family gets a sum of cash they can use to help sustain them after your death, and the company has ensured its continuity.

Advantages of using life insurance

- Life insurance creates a lump sum of cash to fund the buy-sell agreement at death
- Life insurance proceeds are usually paid quickly after your death, ensuring that the buy-sell transaction can be settled quickly
- Life insurance proceeds are generally income tax free; a C corporation may be subject to the alternative minimum tax (AMT)
- If sufficient cash values have built up within the policies, the funds can be accessed to purchase your business interest following your retirement or disability

The buy-sell agreement should be fully funded

The amount of insurance coverage on your life should equal the value of your ownership interest. Then, when you die, there will be enough cash from the policy proceeds to pay your family or estate in full for your share of the business. But if all that is affordable is insurance coverage for a portion of your interest, you might want to go ahead and fund that amount. Later, the company may be able to increase the amount of insurance or use additional funding methods. In the meantime, the agreement should specify how your family or estate will be paid.

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