

Plan for your business's future with confidence

Business continuation with life insurance

EQUITABLE

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A good financial strategy is designed to change as your business evolves

Your business is likely the cornerstone of your family's financial security. Now you need a plan to keep your business going, on your terms, no matter what. Equitable can help.

We commit to your future as if it were our own, with advice designed for you and products built to meet the changing needs of your business. By developing next-generation products and offering industry-leading insights, we're constantly offering new ways to help you make smart choices for your most important business decisions.

Protect your business and your family

Whether your business is a one-person operation, a partnership or a closely held corporation, a business continuation plan should be a component of your overall strategy. Together, we'll work to turn today's goals into tomorrow's accomplishments, to ensure your business lives on as you want it to.

When it comes to a business plan, it's important to answer these two questions

- What would happen to my business if I (or my partner) were to die today?
- Would my family's need for income and funding for their future plans be met if something happened to me today?



Your business continuation plan will also depend on whether you are the individual owner, or if there are multiple owners.

For individual owners

If you're a sole proprietor, you'll want to decide whether the business continues with a family member or someone else at the helm, or if it closes its doors. Determining whether the business continues requires the consideration of a number of factors. For example:

- Is your spouse involved in or interested in your company?
- How old are your children? If they are years away from adulthood, who will carry on the business?
- Are there any grown children in the business?

It's important for you to discuss these issues with your family and review these plans periodically as circumstances change, for both your family and your business.

Having a plan in place now will help you make a potential transition for your business easier for everyone involved — your family, your employees and your clients.

All in the family. Life insurance can also be used to equalize bequests in a situation where one sibling is taking the helm of a family business and another, with different talents and interests, has other career plans.



For co-owners

For closely held businesses of all kinds, preparing for the orderly transfer of ownership interests when one of the owners dies can provide assurance the business will continue as the current owners see fit. Such an agreement, known as a buy-sell agreement, describes the terms for the co-owners (or the business itself) to buy out the deceased's interest or redeem stock. It states how the value of the business is to be determined, the circumstances in which a buyout is to occur and how the agreement is to be funded.

A buy-sell agreement has several benefits to the business:

- You, individually, or as part of the current management, can to retain control.
- You actively choose the successors of your business.
- You won't have to worry about the family selling their interest in the company to an outsider not of your choosing.
- You can ensure a reasonable buyout price — either one predetermined or by using a set valuation method to arrive at one.

A buy-sell agreement also carries benefits for your family:

- Your family and remaining business partners have a clear understanding of terms and a more straightforward way to proceed.
- Your family has a ready buyer for your interest in the company offering fair compensation.
- Your family receives timely payment of their share of the business, helping to support their financial needs.
- Your family is financially provided for, regardless of future success of the business.

A well-crafted buy-sell agreement can potentially serve all your interests as a business owner, and as a family provider, by ensuring the continuation of the business and providing your family with the financial compensation they are due in the event of your death. There are several different types of buy-sell agreements. You should enlist professional legal help to create the best agreement for your particular business situation.

Tying a dollar amount to your business

Many business owners don't know the true market value of their business. For this reason, it's a good idea to engage a professional valuation specialist to determine an accurate going-concern value of your business today. These specialists are trained to use different methods and metrics, including comparable recent sales and discounted cash flow analysis, to arrive at a reasonable fair market value. The value they establish can be useful in creating business continuation agreements, such as a buy-sell agreement.

For companies of all types and sizes, hiring a certified valuation firm may be a sound investment, whether or not you are considering an exit event in the near future. The firm's fee normally is tax-deductible for your company. In addition to supporting your strategic planning, the appraisal can be useful for your personal planning.

To provide additional guidance, the IRS issued Revenue Ruling 59-60, itemizing eight factors to be considered in determining fair market value:

1. **The nature of the business and its history**
2. **The economic outlook in general and for the specific industry**
3. **Book value of the business and its general financial condition**
4. **Earnings capacity**
5. **Dividend-paying capacity**
6. **Goodwill**
7. **Recent sale of an interest in the business and the size of the interest to be valued**
8. **Market price of similar publicly held businesses**

Only one-third of family-owned businesses survive the transition to the second generation. A primary reason for this dismal survival rate lies in poor succession planning.

- *Money Management*, New York State Society of CPAs

How life insurance can help

Life insurance isn't only about protecting the financial security of you and your family. It's also about setting your business up now and in the future. Life insurance benefits are generally income tax-free and payments are immediate. It's a smart addition to many business plans.

For individual owners

Having a source of funds on hand for your family to implement your plans makes the transition easier, not just financially, but emotionally as well. In the absence of a family member capable of stepping in and willing to take on your role, there are generally three options:

Liquidate the business	A financial professional will help complete all the necessary documents once a plan selection has been made and it has been discussed with any appropriate tax, legal or business advisors.
Sell the business	In this scenario, life insurance proceeds can make up income lost by your business in your absence and help ensure financial obligations to creditors and employees are met. Both are important factors in maintaining the company's value and credit rating while your family finds a suitable buyer. Your family can also receive money to replace your income, particularly important if you were a breadwinner or vital financial contributor to the family.
Maintain ownership and hire someone to manage the company for the family	This might be a permanent strategy or a temporary measure for a younger family, perhaps to allow time for children to grow up. Here, life insurance proceeds can keep the business and your family on an even keel while a suitable person is found. Money will be available to pay for the costs of the search and make up for income lost during the transition period. If the new manager comes from within the company, there will be money on hand to search for and train a replacement to fill his or her previous position.

For co-owners

In order to execute a buy-sell agreement, a source of funds must be identified for the buyout. In many respects, choosing this source of funds is as important as the agreement itself. Arranging the specifics of who buys what, when and at what price is meaningless if money is difficult to obtain, or simply not available. Without proper funding, the buy-sell agreement may be relatively worthless. There are several different possible sources of funds for a buy-sell agreement:

Use cash or a fund	The owners could use cash, or set aside a fund to save for the buyout. This is generally not the preferred method for many businesses because of the large cash flow required, which could be used for reinvestment into the business.
Scheduled installment payout	An installment payout may be another option, where the surviving owners work out a schedule of payments to the family. The drawback to this method is that the family must wait to receive full payment, with no guarantee the company will be able to pay off the entire sum.
Borrow funds	The surviving owners could borrow funds from a lender. This is often difficult to obtain because the business may be struggling from the loss of a key owner, or the surviving owners may pay a steep interest rate. In contrast to an installment payout, which is the likely scenario without planning, your family receives their payment in the short term, when they likely need it most, without the company taking on a sizeable debt. Further, your family's payment isn't tied to the future success of the company.

Using life insurance for a buy-sell agreement

Life insurance as a funding tool

Life insurance as a funding tool can give flexibility to meet the arrangements of the buy-sell agreement. The policies can be purchased to cover all the owners, either by the principals to cover each other, or by the company to cover all. At the death of one of the owners, the life insurance benefits paid on the policy (or policies) are used to buy the deceased owner's interest from his or her family. Life insurance is unique in that it can guarantee[1] the amount of money for the buyout will be available precisely when it is needed[2] — whether the agreement has been in effect for a few months, a few years or a few decades.

Premiums

Premiums are regular and therefore budgeted. The life insurance benefit is generally income tax-free, although premiums are not tax-deductible. Your tax professional can advise you regarding your company's particular tax situation. At the death of an owner, life insurance proceeds can expedite a full and timely payment to the surviving family. The business continues with the surviving owners in control. The face value of the policy can cover only the buyout or a larger face amount can be purchased — to cover the company's lost income, extra expenses related to losing an owner or to retire debt.

Permanent life insurance policy

A permanent life insurance policy has some added advantages over a term insurance policy. It allows for the tax-deferred buildup of cash value. This asset can help enhance the company's credit rating, and can be used in an emergency to pay for unforeseen expenses. If a partner chooses to leave the company (within the terms of the buy-sell agreement) or retire, the cash value can be used, at least, to provide the down payment on a buyout.[3]

Buy-sell agreement

It's a good idea to draw up a buy-sell agreement right at the outset of your venture. If you choose life insurance to fund the agreement, the earlier the policies are obtained, the better, since premiums increase with the age of the person to be insured and your health may deteriorate. However, if you don't have a buy-sell agreement in place, think about drafting one now. A buy-sell agreement should be reviewed regularly, and the face amounts of any policies funding it should be increased as the value of the company increases. A policy used to fund a buy-sell for a startup business would be totally inadequate for a company that has grown into a multimillion-dollar operation.

Use a buy-sell agreement to ensure the shares of your business go to your loved ones — or business partners — after you're gone.

1 All guarantees are based on the claims-paying ability of the issuer.

2 Provided insurance contract remains inforce.

3 Accessing a policy's cash value through withdrawals or loans will reduce that cash value and the death benefit, and increase the chance the policy may lapse.

The value of a multidisciplinary team

You may need several types of professionals, working together, to plan for a full-value exit. They include:

- Legal advice, including help in drafting a buy-sell agreement
- Accounting services and tax advice from a qualified CPA
- Business valuation expertise
- Estate planning guidance
- Investment and insurance planning and services
- Business consulting

A coordinated planning process can help you turn the hope of a full-value exit event into a realistic plan with clearly defined action steps. It also will motivate you to communicate clearly with your team of advisors about how to convert your business equity into personal wealth, tax-efficiently.

Finally, this process can help you work toward other goals, such as increasing access to capital, protecting against the loss of key people, and meeting IRS requirements for valuing gifts and estate transfers.

How to take the next step

The next step may be a fact-finding session in which we can help you define business and personal goals and full-value exit strategy options, on a schedule that feels comfortable.

Together, we'll develop a plan allowing you to face the future with courage, strength and wisdom.



For more information, contact your financial professional or visit equitable.com.

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