Funding Buy-Sell Agreements with Life Insurance

AS A BUSINESS OWNER, IT IS IMPORTANT TO PLAN FOR SIGNIFICANT LIFE EVENTS AND HOW THEY CAN AFFECT YOUR BUSINESS.

The death or permanent disability of a shareholder or partner can have a significant impact on the long-term viability of your business, so it is crucial to factor this into your company's financial planning. If your business loses an owner, the remaining owner(s) must decide how to continue operations, minimize disruption and maintain control of the business if ownership of shares changes hands.

RUBACH WEALTH
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There are three main approaches to funding a buy-sell agreement using life insurance:

CROSS-PURCHASE METHOD

Each shareholder purchases a life insurance policy on the life of the other shareholder(s), naming themselves as the beneficiary. If a shareholder dies, the buy-sell agreement requires the surviving shareholder(s) to purchase the shares of the deceased shareholder at fair market value. The life insurance benefit is used to fund this purchase.

PROMISSORY NOTE METHOD

The company purchases a life insurance policy on the life of each shareholder, with the corporation as the beneficiary. If a shareholder dies, the buy/sell agreement requires the surviving shareholder(s) to purchase the shares of the deceased shareholder at fair market value. The life insurance benefit is paid into the company's capital dividend account, which is then distributed to the surviving shareholder(s) and used by them to fund the purchase of shares.

CORPORATE REDEMPTION

The company purchases a life insurance policy on the life of each shareholder, with the corporation as the beneficiary. If a shareholder dies, the buy-sell agreement requires the company to purchase and absorb the shares of the deceased shareholder at fair market value. The life insurance benefit is used by the company to fund the purchase of shares.

Funding buy-sell agreement with life insurance policy offers the best solution given the potential tax advantages.

Which of these three approaches is best for your business will depend on a variety of factors, but ultimately the outcome will be same: less uncertainty for your business, strengthened control of ownership following the death of an owner, and a tax-efficient approach to funding the purchase of the deceased owner's shares.

The advisors at Rubach Wealth have experience structuring the optimal life insurance solutions for funding buy-sell agreements. So let's start a conversation about how we can help you safeguard your business interests in the face of uncertainty.

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