Key employee protection: Preserving your business.

Plan today for the future.
As a business owner, you recognize the importance of insuring your building, inventory, and equipment. These assets are vital to the success of your company. But what would happen if a key employee died unexpectedly or became disabled?[1]

Key employees are the foundation of a successful business. They are business owners, sales directors, CFOs, or any other individuals who are sources of leadership and profitability, and who would be extremely difficult to replace. Unless the proper steps are taken, the death or disability of a key employee can be devastating to the financial well-being of your company.

The solution: Key employee protection.
Funding a plan to protect key employees may give your business the additional funds it needs to:

- Hire and train replacements.
- Replace an employee's contribution to profits.
- Maintain the confidence of clients and creditors.
- Meet possible loan obligations if the key employee was also a guarantor on business loans.

There are three basic options for funding the costs associated with the sudden loss of a key employee: cash accumulation or a sinking fund, borrowing from a bank, or life insurance.

1. Cash or sinking fund.
In this option, a business establishes a savings plan, much like a bank account, to protect itself from the death or disability of its key employees. At death, the cash in the savings plan is used as a source of funding. Unfortunately, this method has several drawbacks:

- A savings plan accumulates funds over time. What if funds are needed tomorrow?
- Accumulated cash could cause an accumulated earnings problem.
- Any growth on the accumulated funds may be income taxable.
- A savings plan may be depleted to pay for other expenses.
- The business owner will pay dollar for dollar, thus depleting the amount of cash that could be used elsewhere.

2. Borrowing funds.
In this option, funds are borrowed, usually through a bank loan, to replace the financial loss caused by a key employee's death or disability.

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Drawbacks of this option include:

- A potential slowdown in business growth due to additional loan repayments.
- A reduction in future profits may occur because of the loan repayment.
- The business owner will pay dollar for dollar plus interest.
- The company's credit may be adversely affected due to greater debt.

3. Insurance.

Purchasing life and/or disability insurance on your key employees can be a cost-effective way to safeguard your business and minimize the impact of a key employee's death or disability. Life insurance and/or disability insurance can provide your business with the following advantages:

- Funding with insurance is easy to administer.
- Funds are available even if death or disability occurs the day after coverage begins.
- Although the premiums are not deductible, the life insurance proceeds at death are generally received income tax-free to the business.

Funding the future plan.

The business applies for a life insurance policy on the life of a key employee. The business is the owner and beneficiary of the policy. As policyholder, the business pays premiums to an insurance company for the policy as long as the key employee is alive and an employee. Should an insured key employee die, the death benefit proceeds from the insurance policy would pass generally income tax-free to the business,[2] providing an immediate cash source for debt repayment, liquidity, or other related concerns.

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[1]Disability insurance is available through one or more carriers not affiliated with New York Life, dependent on carrier authorization and product availability in your state or locality.

[2]The Pension Protection Act of 2006 established that the death benefit of an employer-owned life insurance policy will be income taxable to the extent that the benefit exceeds premiums paid unless the parties fit into one of the specified exception categories, a specified form of notice is provided to the employee, and the employee consents to be insured.