



Help business owners protect their most valuable asset

With key person insurance



Designed for you

This guide is designed to give you the tools you need to help you sell key person insurance.

From prospecting tips, to the questions to ask your business owner clients who are candidates for this coverage, to the tax considerations your clients may want to keep in mind, this guide contains valuable information that can help you successfully navigate the key person insurance marketplace.

What is key person insurance?

Key person insurance is life insurance on a key employee in a business. Small or large, most businesses have several “key employees,” including the owner or partners, the founders, and/or one or two employees who are top performers. Key person insurance provides the business with a source of funds when needed most — at the death of a key employee.



The tools you'll need:

- Learn how one Guardian FR has achieved success in the key person insurance market. FR Spotlight: Onofrio Cirianni ([Pub10468](#))
- Discover what you need to know about key person insurance — and the clients who can benefit from it. Key Person Client Portrait ([Pub8950](#))

What you need to know

Before you start prospecting for Key Person Insurance clients

The clients that can benefit most

- Small business owners face the greatest risk of financial problems due to the loss of a top performer.
- Medium-size businesses are great prospects, too.

Where can you find these clients? Your own client book of business is a great place to start. Additional ideas include:

- Business owners in your community — where you live, work and do business with merchants and service providers
- Employers of executives who are already your clients
- Business associates of those business owners you already work with

What your clients need to know

About key person insurance

- It's the **one way business owners can produce the desired amount of cash** at the precise moment it is needed — upon the death of the company's top performer.
- It **provides funds that can be used for any reason** — including paying off loans, hiring and training a replacement, meeting expense obligations, and redeeming the business interest of a deceased owner.
- It can help **assure banks, creditors and valued partners** that the business has the potential to continue operating in the event of the insured's death.
- It can **be structured with flexible options** that provide benefits for both key employees and business owners.
- It can **help business owners avoid a "key person discount"** in a business valuation situation (where the value of a business may be reduced due to the loss of a key person if no life insurance is in place to hire and train a replacement in a timely fashion).

The prospecting tools you'll need:

- Introduce your clients and prospects to key person insurance with MarketEDGE360 prospecting letters: ([Pub8954](#)) and ([Pub8953](#))
- Introduce your clients to the benefits of key person insurance. Key Person Client Flyer ([Pub8956](#))
- Give your clients an in-depth look at key person insurance. Key Person Client Guide ([Pub8955](#))



Key person insurance in action

- **Client:** John Roberts, owner of Monaco Manufacturing, a small medical device manufacturer.
- **Concern:** If John's chief engineer, Frank Stevenson, were to die, the business could suffer greatly.
- **Impact of key employee's death on business:** It would take time to find a new engineer as talented and experienced as Frank; in the meantime, the business would be unable to fulfill customized orders.

To protect the business:

- With Frank's permission, John purchases a \$1,500,000 Whole Life 99 key person policy on Frank's life.
- The policy has an annual premium of nearly \$22,500.
- The death benefit will protect Monaco Manufacturing should anything happen to Frank.

Year	Premium*	Cumulative Premium	Cash Value**	Death Benefit**
1	\$22,377	\$22,377	\$121	\$1,500,577
5	\$22,377	\$111,886	\$50,370	\$1,530,127
10	\$22,377	\$223,771	\$171,866	\$1,605,917
15	\$22,377	\$335,656	\$338,869	\$1,740,186
20	\$0	\$358,033	\$459,278	\$1,682,915
25	\$0	\$358,033	\$569,607	\$1,611,066

The example shown here is based on a hypothetical policy not available for sale, using Guardian's Ten Pay Whole Life policy, 2020 dividend scale, preferred risk class, and averaging male and female values for issue age 40. A full illustration, showing both guaranteed and non-guaranteed values, must be provided by a Guardian representative to an individual applying for a Guardian whole life insurance policy.

* The premium offset year is not guaranteed and relies on the payment of non-guaranteed dividends and the amount of paid-up additions in the policy in order to pay for the policy's required premium.

** Dividends are not guaranteed. They are declared annually by Guardian's Board of Directors.

Additional options

A key person plan can be as flexible as your client's needs dictate. Additional variations include:

- Providing a pre-retirement Split-Dollar death benefit for the protection of the key employee's family. (For more information, refer to [Pub9246](#))
- Bonusing the policy to the key employee at retirement, as an added employee benefit to provide post-retirement insurance and/or supplemental retirement income.¹



Working with key person insurance candidates

Some questions to ask

Asking certain questions — such as the following — may help your clients discover their need for key person insurance:

- Who is the most important person that helps make your business a success?
- Which other individuals — such as your partner or partners, executives, managers, or sales people — also make substantial contributions to your business's bottom line?
- What would happen to your business should any of these key people (including you) die?
- If one of your top performers should die, what steps would you have to take to replace that person — and how long do you think that would take?
- What kind of productivity and revenue losses could your business suffer in the meantime?

Once your client recognizes the need for this coverage, it's important that you both take certain factors into consideration, such as:

- How much coverage may be needed to adequately protect the business; and
- The effects that key person insurance could have on the business owner's tax situation.²

Real-life key person insurance stories

To share with your clients

Companies of any size can benefit from key person life insurance, as the following two examples illustrate:

How the sudden death of a key employee impacted “the golden arches”

No business is immune from the loss of a key employee. Case in point: McDonald’s. The day former Chairman and CEO of McDonald’s, Jim Cantalupo (age 60), died suddenly of a heart attack, McDonald’s stock lost nearly 3% of its value — despite the stock being in the midst of an upswing in price.⁴

The effect disability can have on a business

When Apple co-founder Steve Jobs announced his resignation in August 2011 due to his battle with cancer, Apple’s stock dropped 5% that same day. Prior to his resignation, the mere mention of Jobs’s health status routinely influenced Apple’s stock price, positively or negatively.⁵

Small businesses today face a wide array of risks. Fortunately, you can offer them the tools they need to help protect against the death, disability or resignation of a key employee.



Other ways you can help business owners retain key employees

The death of a key employee is not the *only* risk your business owner clients face — the potential that their top performers could become disabled or leave the business can also be great.

Two valuable tools you can offer

In addition to key person insurance, you can provide business owners with two valuable retention tools:

- An Executive Bonus (Section 162) Plan, and
- A Qualified Sick Pay Plan Funded with Disability Insurance.

Executive bonus (Section 162) plans

Executive Bonus Plans are another employee retention tool. These plans can be both low cost and easy to implement.

How Executive Bonus Plans work

- The business subsidizes the cost of a whole life insurance policy for the key employee through the form of bonus payments, which are used to make the premium payments.
- The bonus payments are taxed as ordinary income to the employee and are deductible to the business as a business expense, as long as the bonus amount is reasonable.
- The key employee owns the life insurance policy and names his or her own beneficiary/ies.
- The employee has full access to the policy's cash value and can use it as a source of retirement income if so desired.

Qualified Sick Pay Plans funded with disability insurance

Like Executive Bonus Plans, Qualified Sick Pay Plans are another way to reward and retain top performers so that they continue to work in your business and support a healthy business valuation.

Instead of making payments to disabled employees out of cash flow, consider funding your Qualified Sick Pay Plans with individual disability income insurance contracts. Even a temporary loss of a key person can reduce profitability. And your desire to make disability payments out of cash flow represents an unfunded liability on your balance sheet. This one-two combination will likely hurt your business' value.



A QSPP:

- can shift the burden of paying a disabled employee's wages from your client's business to the insurance company
- can preserve your business' value by stabilizing cash flows and expenses
- can be provided as an executive perk for your client's best employees

How a Qualified Sick Pay Plan funded with disability insurance works

- When a QSPP is funded by disability insurance:
 - The insurer will continue paying a portion (typically 60%–80%) of a disabled employee's wages.
 - The liability (wages payable) on your client's balance sheet is reduced — and those funds remain within the business.
 - The contributions your client's business makes towards the QSPP are tax deductible.
 - The business will not be responsible for making any premium payments during an employee's disability if a waiver of premium benefit rider is added to the plan at the time of purchase.
- The business owner controls which employees may participate in the plan and the level of coverage those participants will receive.

Let's talk about how
you can help your small
business clients protect
their most valuable asset
— their top performers.

Please give us a call at 800 871 7780,
Option 3, so we can help you explore
various options for your clients.

¹ Care should be taken not to create a promise, formal or informal, to give the policy to the executive at retirement. Doing so could inadvertently create a Non-Qualified Deferred Compensation plan, which would then be subject to IRC 409A. Consult your tax professional for more information. Policy benefits are reduced by any outstanding loan or loan interest and/or withdrawals. Dividends, if any, are affected by policy loans and loan interest. Withdrawals above the cost basis may result in taxable ordinary income. If the policy lapses, or is surrendered, any loans considered gain in the policy may be subject to ordinary income taxes. If the policy is a Modified Endowment Contract (MEC), loans are treated like withdrawals, but as gain first, subject to ordinary income taxes. If the policy owner is under age 59½, any taxable withdrawal may also be subject to a 10% tax penalty.

² Guardian, its subsidiaries, agents, and employees do not provide tax, legal, or accounting advice. Consult your tax, legal, or accounting professional regarding your individual situation.

³ Employer owned life insurance is received income tax free by the business only if IRC 101(j) is complied with.

⁴ Source: Kiplinger's, July 2004, p.66

⁵ Source: http://www.huffingtonpost.com/2011/08/24/jobs-apple-stock-market-after-hours_n_935899.html

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