The Business Owner's Guide to a Buy-Sell Agreement Review

The death, disability, severe illness or retirement of a controlling owner of a business can wreak havoc on the entity that the owner may have spent a lifetime building. If not adequately planned for, such events can lead to a forced sale of the business that is out of the family's control.

Buy-Sell Agreements can provide one of the most orderly means of transferring a business interest upon the death, disability, withdrawal or retirement of an owner. However, Buy-Sell Agreements must be funded to be of use. An agreement without a means to pay for the stock does not help anyone. Life insurance is one of the most cost efficient and tax efficient means to fund a Buy-Sell Agreement. All concepts, strategies and products discussed in this literature may not be suitable for every client.

Advantages of a Buy-Sell Agreement Funded with Life Insurance

- Helps create a market for a closely held business.
- Assures continuation of business that owners worked hard to create.
- Establishes a purchase price for each owner's interest in the business and, if the agreement is between non-family members, may be used to establish the value of the business for estate planning purposes.
- Restricts outsiders from obtaining an interest in the business or control of the business.
- Allows co-owners the ability to purchase the exiting owner's interest.
- Insurance death benefit provides estate liquidity and cash to beneficiaries not involved in the business.
- The potential for Accumulation Value in an insurance policy provides means of paying for interest if owner becomes disabled, retires or leaves the business.
- Helps to avoid family disputes.
- Avoids disruption of the business after an owner's death.

Key Considerations of a Buy-Sell Agreement

- The agreement must be funded to be effective.
- If insurance is used as the funding vehicle, premium payments must be made to keep the life insurance policy in force, otherwise the life insurance policy will lapse.

Why Should a Buy-Sell Agreement be Reviewed?

1. The value of every company changes yearly. In order to reflect an accurate transition if the Buy-Sell is implemented, an accurate valuation is needed to avoid challenges to the Buy-Sell Agreement's legitimacy.

2. Goals may have changed since the initial implementation of the Buy-Sell Agreement.

3. Life insurance product features have changed dramatically over the past several years offering benefits which were previously unavailable such as coverage for terminal, critical and chronic illness.

Is a Buy-Sell Review Needed?

Does the funding of your current Buy-Sell Life Insurance Plan...	Yes	No
...offer accelerated benefit options for terminal illness?	____	____
...offer accelerated benefit options for critical illness?	____	____
...offer accelerated benefit options for chronic illness?	____	____
...increase in value as your business value increases?	____	____
...pay an income tax free lump sum at the death of an owner?	____	____
...offer to continue paying premiums automatically during a disability?	____	____
...offer a stream of income that may supplement retirement income of an owner?	____	____
...offer a stream of income to buy out an owner?	____	____

If any of these questions were answered "no", talk to your agent about obtaining a no cost Buy-Sell Review.

Accelerated Benefit Riders

From ANICO®

Access policy's death benefit while insured is still living...

Three great living benefits for No Additional Premium[1]...

Critical – provides for the payment of an accelerated benefit if an eligible insured experiences a critical illness. Covered critical illness includes ***16 Different Illnesses***.[2]

Chronic – provides for the payment of an accelerated benefit if an eligible insured is unable to perform two out of six activities of daily living (***2 of 6 ADLs*** [2]) or is cognitively impaired.

Terminal – provides for the payment of an accelerated benefit if an eligible insured has an illness or chronic condition that is expected to result in ***Death Within 24 Months***.[2]

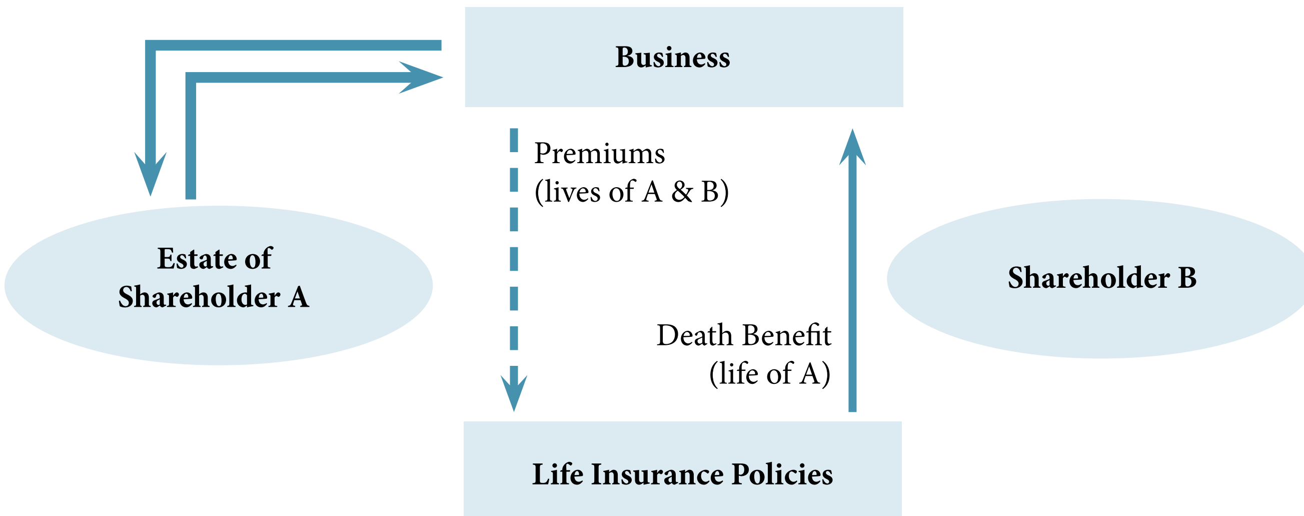
Receipt of Accelerated Benefits may effect eligibility for state or federal benefits such as disability and medicaid.

1 *The Accelerated Benefit Riders are offered for no additional premium; however, the accelerated benefit payment will be less than the death benefit because it is reduced by an actuarial discount which is based on the insured's future expected mortality at the time the benefit is exercised as well as an administrative fee of up to $500 that is assessed when accelerated benefits are elected.*

2 *Refer to Rider forms for a complete list of illnesses and definitions. Some states may limit the definition of terminal illness to conditions that are expected to result in death within 12 months. All riders may not be available in all states. Policy Form Series ABR14-TM, ABR14-CH, ABR14-CT (Forms will vary by state).*

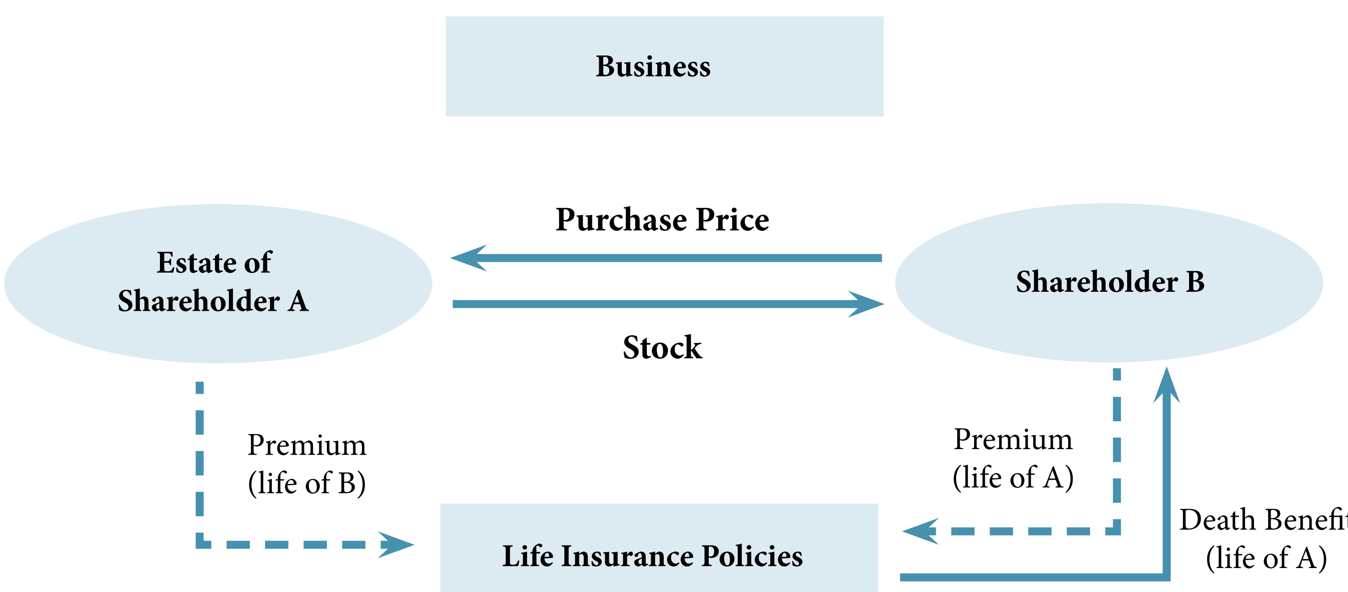
Types of Buy-Sell Agreements Funded with Life Insurance

Entity Purchase Buy-Sell Agreements



An **Entity Purchase Buy-Sell Arrangement** (or "stock redemption arrangement") funded with life insurance on the lifes of the shareholders is an arrangement among the owners and the entity. The entity agrees to purchase (or redeem) all of the interest of a deceased owner and the owners agree to sell their interests to the entity.

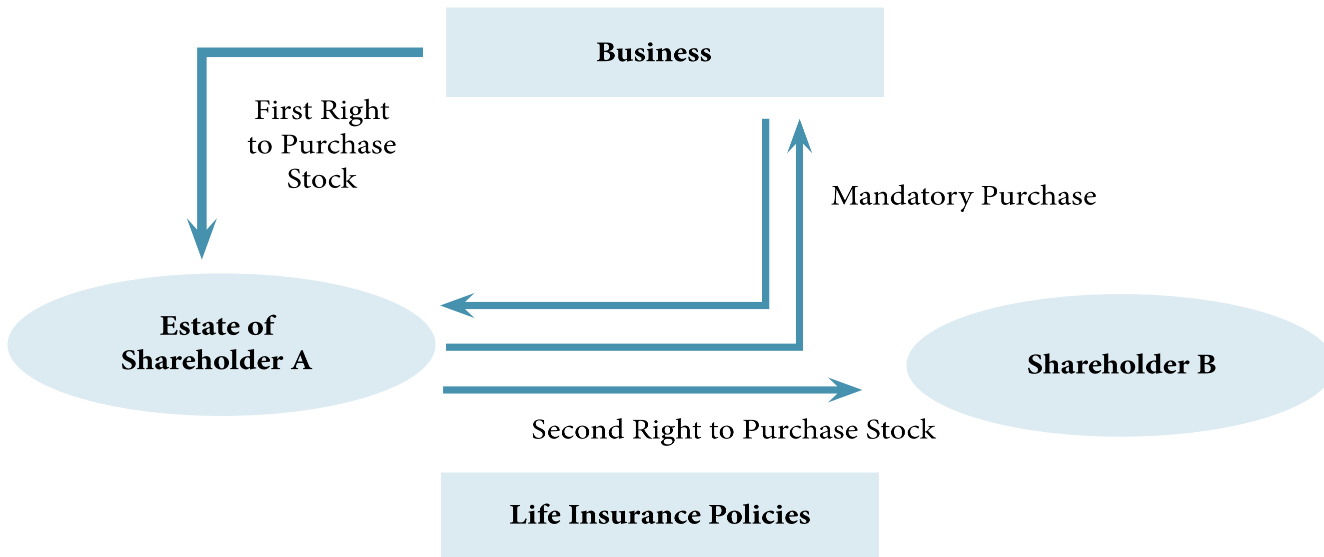
Cross Purchase Buy-Sell Agreements



In a **Cross-Purchase Buy-Sell Arrangement** funded by life insurance the owners (or their estates) are obligated to sell their interests to each other. The entity is not a party to the arrangement.

Types of Buy-Sell Agreements

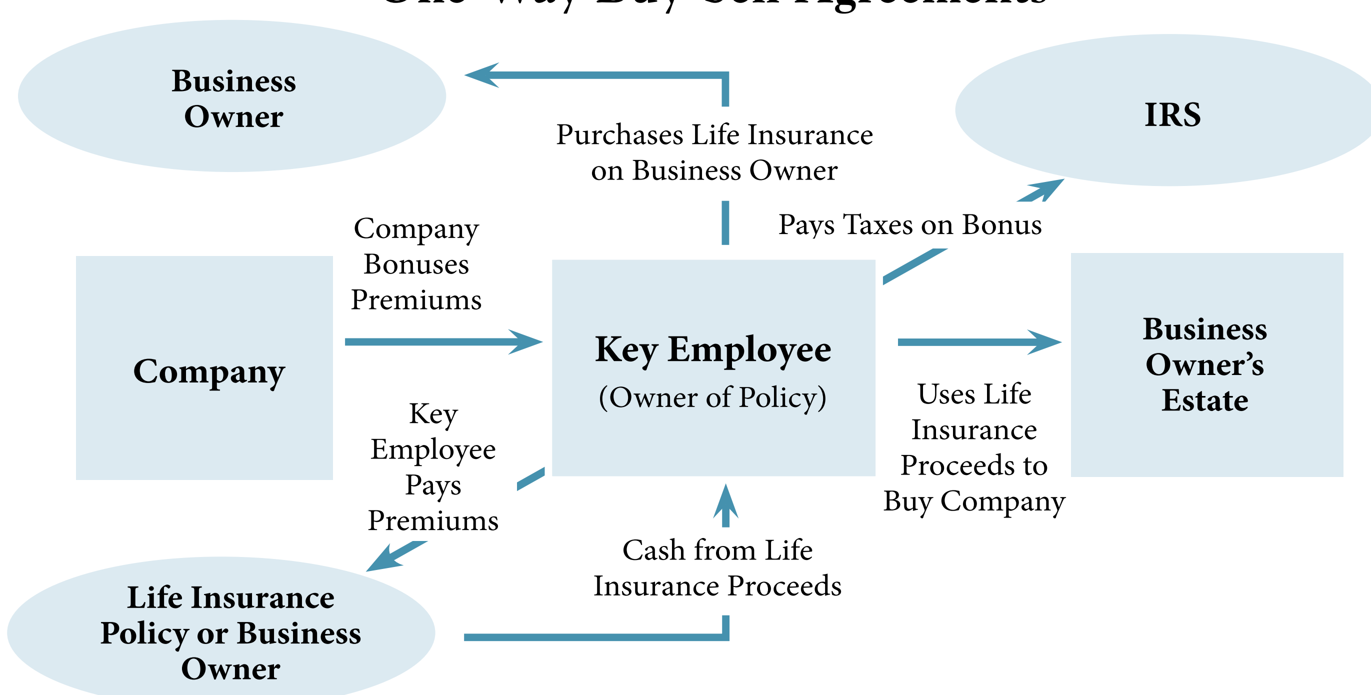
Wait and See Buy-Sell Agreements



(Policies owned by either the Business or the Shareholders.)

A **Wait and See Buy-Sell Arrangement** is a hybrid arrangement combining the features of both the entity purchase Buy-Sell Arrangement and the cross-purchase Buy-Sell Arrangement. With a wait and see Buy-Sell, either or both parties may own insurance. A wait and see Buy-Sell Arrangement generally gives the entity the option (or"right of refusal") to buy any portion of the deceased owner's interest within a certain time period after the owner's death. If the entity does not fully exercise the option, the remaining owner's have the second right of refusal. Finally, if the remaining owners do not exercise their right of refusal, then the entity must redeem the balance of the deceased owner's interest. Depending upon how the arrangement is funded and whether the entity or the surviving owner's acquire the deceased owner's interest, the arrangement will function as either an entity redemption or a cross-purchase arrangement.

One-Way Buy-Sell Agreements



A **One-Way Buy-Sell Arrangement** is a type of a Buy-Sell Arrangement in which a valued employee, who may be a family member or a key person in the business, will purchase and own a life insurance policy on the life of the business owner. In this situation, because there is generally only one business owner and one designated successor, only one life insurance policy is required to fund the arrangement. The valued employee, who may be a family member or a colleague, will also be the beneficiary of the life insurance policy. The company will pay a bonus to the valued employee in the amount of the premium payments annually to minimize the out-of-pocket expense of the arrangement. The bonus payments may be tax-deductible to the corporation when they are paid, but the payment will also be taxable to the recipient.

What Type of Coverage Should Be Purchased?

Term Life Insurance

Term life insurance is pure insurance protection that pays a predetermined sum if the insured dies during a specified period of time. On the death of the insured, term insurance pays the face value of the policy to the named beneficiary. All premiums paid are used to cover the cost of insurance protection.

The term may be one, five, 10, 20 years or longer and most expire at 60 or 65. But, unless renewed, the insurance coverage ends when the term of the policy expires. Since this is temporary insurance coverage it is the least expensive to acquire. Here are the main characteristics of term life insurance:

- Temporary insurance protection.
- Low cost.
- No cash value.
- Generally level death benefit.
- Usually renewable.
- Sometimes convertible to permanent life insurance.

Permanent Life Insurance

Permanent life insurance provides lifetime insurance protection (does not expire), as long as the premiums are paid. Most permanent policies offer a savings component combined with the insurance coverage. This component, in turn, causes premiums to be higher than those of term insurance. The savings component may offer a fixed interest rate or may be in the form of an indexed rate that is related to the performance of an exchange such as the S&P 500®.[3] This savings portion of the policy allows the policy owner to build cash value within the policy which can be distributed at some time in the future.

Here are the main characteristics of permanent life insurance:

- Permanent insurance protection.
- More expensive to own.
- Builds accumulation value.
- May have increasing death benefit.
- Tax free loans are permitted against the policy.[4]
- Favorable tax treatment of policy earnings.[5]
- Level or flexible premiums.

For a comprehensive Buy-Sell solution, Permanent Life should be selected to enable the policy owner to utilize the cash value during retirement years as a buy out distribution to the retiring business owner.

[3] *"Standard & Poor's®", "S&P®", "S&P 500®", and "Standard & Poor's 500™" are trademarks of Standard & Poor's Financial Services LLC ("Standard & Poor's") and have been licensed for use by American National Insurance Company. Signature Indexed Universal Life Insurance is not sponsored, endorsed, sold or promoted by Standard & Poor's and Standard & Poor's makes no representation regarding the advisability of purchasing Signature Indexed Universal Life Insurance.*

[4] *Loans are subject to interest charges and can reduce the death benefit paid to beneficiaries. Outstanding loans may affect the policy's death benefit, the value of the policy and possibly the length of time the policy remains in force. A loan's tax free status is subject to the policy remaining in force. If the policy lapses a taxable event is triggered.*

[5] *Neither American National nor its agents give legal or tax advice. Please contact your tax advisor or attorney regarding your specific situation.*

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