

Life

Business solutions

Key person

Case study



MEET THE CLIENT

An established company listed as an S-Corporation provides IT services to small- and medium-sized businesses. The owner founded the company 15 years ago and has grown the original staff of three employees to over 40, spanning across four states. As the company has grown over the years, additional leadership has emerged to meet the demands of its customers. One employee has been the lead on a number of initiatives that play a big role in the company's future success. Not only has this employee proven their ability to get new offices running smoothly, but they are also responsible for maintaining employee training programs.



Aware of the value this employee adds to the company, the owner considers how the business would survive without them. The owner consults an insurance agent about protecting the business by purchasing a key person life insurance policy on this star employee's life.

Part of the employee's job entails launching new store locations. In the event of the employee's death, a delayed store launch could cost the company \$200,000 - \$400,000. A key person coverage amount of \$400,000 would help mitigate this loss. After weighing the product options with help from a life insurance agent, the owner decides to purchase an indexed universal life policy with the Waiver of Surrender Charge Option,¹ providing \$400,000 in death benefit protection and access to accumulated cash value.

Note that the company purchases the policy on the employee's life, pays the premiums, and is the beneficiary of the policy. However, the employee still has to apply for the coverage, sign the application, and qualify for coverage before it can be issued.

Hypothetical scenario 1 – **Death trigger**

The employee is leading the way toward opening the company's sixth store when tragedy strikes and they are killed in a car accident. The opening of the new store is now pushed back three months and ends up costing the company over \$300,000. However, the company owner can use the death benefit proceeds from the indexed universal life policy on the employee's life to help offset recent costs to the business caused by the accident.

Hypothetical scenario 2 – **The employee leaves the company**

The employee schedules an important meeting to notify the company's owner that their spouse has accepted a new opportunity. The position requires them to relocate, and the owner is losing one of the company's best employees. The employee's skill set is very specialized, and the company loses money every day the employee isn't there to help launch the new store. The owner decides to use a staffing firm to assist in the hunt for a replacement. To help with these expenses, the company cashes in the policy. Because the policy had a waiver of surrender charge option, the company didn't have to pay a surrender charge, and therefore had access to the full cash value to help cover the cost of the recruiting firm and other losses the business may face.

Hypothetical scenario 3 – **Policy provides incentive for the employee**

The company's owner is appreciative of all that their star employee has done for them. The owner explains that they are setting up a bonus program through which they will be funding a life insurance policy with significant cash value growth potential. The policy will act as a non-qualified deferred compensation plan, so at retirement, the company can take withdrawals and loans² from the policy's cash value for the employee to use for retirement planning purposes, legacy building, or other needs. The employee will receive income as a taxable compensation benefit. This scenario can give the employee more incentive to stay with the company for the long term and shows appreciation for the value the employee adds to their company.





1. Must be applied for at time of application. Available for an additional charge per \$1,000 per month, depending on issue age and underwriting class. Surrender charges will be waived upon a full surrender or partial surrender. Surrender charges will not be waived if the policy is surrendered under a 1035 Exchange (except in Florida). A decrease charge will be assessed if a reduction in the policy face amount is requested during the Waiver of Surrender Charge Period. However, if a partial withdrawal results in a reduction of the face amount, the withdrawal charge is waived.

2. In some situations loans and withdrawals may be subject to federal taxes. North American Company does not give tax or legal advice. Clients should be instructed to consult with and rely on their own tax advisor or attorney for advice on their specific situation. Income and growth on accumulated cash values is generally taxable only upon withdrawal. Adverse tax consequences may result if withdrawals exceed premiums paid into the policy. Withdrawals or surrenders made during a Surrender Charge period will be subject to surrender charges and may reduce the ultimate death benefit and cash value. Surrender charges vary by product, issue age, sex, underwriting class, and policy year.

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