KEY PERSON BENEFITS TOOL-KIT

CPS ADVANCED MARKETS

CONTACT INFORMATION

CPS ADVANCED MARKETS

(805) 597-3636

Tom Virkler, JD, CLU
tom@cpsadvancedmarkets.com

www.CPSadvancedMarkets.com

Every Business Owner's Goal:

To conduct their business profitably until they can pass it

… to whom they want,

… when they want,

… for the amount they want.

SURVIVOR INCOME BENEFITS PLANS

"SIB" – An Agent's Primer

Marketing Note: If your intent is to introduce your business prospect to the concept of key person benefits by describing the SIB plan then it is important that you have a basic understanding of how the benefit is structured and how it works. The following is a summary of the plan's important features and is for your use, these are not for presentation to the prospect, these are the things you can talk about and need to know.

There are specimens in this tool-kit for any documents mentioned and annotated (*).

I. SIB DEFINED AND DESCRIBED

A. The plan is a legally binding and enforceable agreement between an ER and one or more chosen EE's

B. It provides (only) a death benefit to an EE's designated beneficiaries

C. The benefit pays only if the EE dies while in the employ of the ER as agreed

D. The plan pays to the beneficiary or contingent beneficiary in a designated class of beneficiaries – said class being broadly defined so as not to fail for lack of a beneficiary

II. THE PRACTICAL BENEFITS OF SIB

A. To the Employee
Assurance that if pre-mature death occurs during the working life of the EE that his or her family are financially able to continue in their current lifestyle.

B. To the Employer
  1. Reduction of possible EE anxiety over the financial well-being of his or her family in the event of early and unexpected death – resulting in better productivity

  2. Employee Retention - the plan acts as "Silver" Handcuffs on the EE because leaving the company would result in loss of the benefit

III. SIB IS A "NON–QUALIFIED" PLAN

Because the plan does not have all the tax advantages of a "qualified" plan under the law (e.g. a 401(k) or qualified pension plan) the ER has greater latitude in the design and operation of the benefit. For example:

A. Freedom to include only those EE's in the plan that he or she desires (certain legal requirements may require that the plan be offered only to EE's designated as "top hat" or "highly compensated" under the law – an explanation of this is not necessary here – usually any EE "key" enough to merit attention for this plan would qualify as being in one or both categories)

B. Freedom to vary the benefit design from plan participant to plan participant – the ER can award different benefit amounts based on EE value, length of service, etc.

C. Minimal Regulatory Reporting – Some attorneys will advise that a letter of plan implementation be sent to the Department of Labor and that each participating EE be given a Summary Plan Description – if so, we can assist with specimens

IV. SIB IS UNCOMPLICATED

A. To informally fund – The ER does not have to make any plans to fund the possibility of a payout and can choose to simple pay necessary death benefits out of current cash flow. However, you should suggest that they informally fund the plan with an "un- earmarked", business-owned life insurance policy on each participant, proceeds to be used should death occur.

B. To implement – At most the completion of the following at the advice and with the aid of counsel:

1. ER/EE agreement* and company resolution*

2. EE Summary Plan Description

3. Notice of plan implementation to Department of Labor

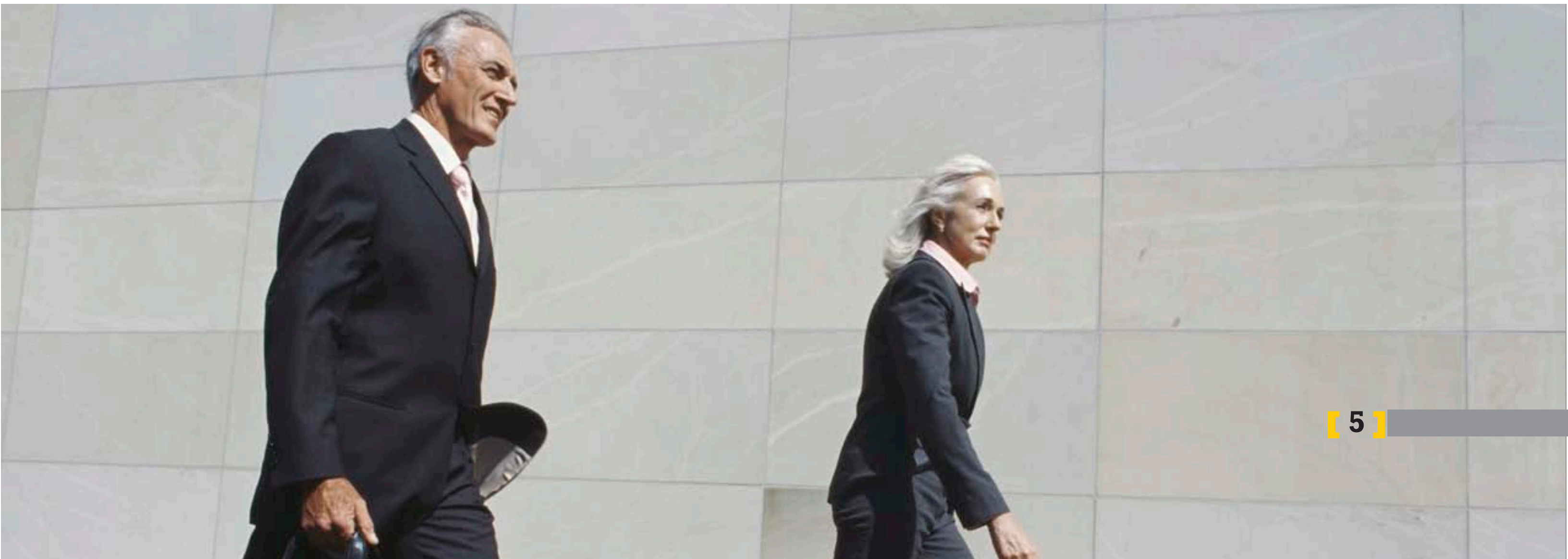
4. Completion of any notice and consent measures required for the fulfillment of the provisions of IRC 101(j)

Marketing Note: Always ask the carrier involved what they recommend when placing business or corporate owned life insurance ("BOLI" or "COLI") - most will have procedures.

C. Administration

1. During Employment – The Form 8925 required by IRC 101(j) – again the BOLI concerns – must be filed with the business tax return each year that the policy is in force

2. In The Event of Death – Benefits do not have to be paid in a lump sum. The plan can be designed to pay installments over a period of years. In this case it is the ongoing responsibility of the business to see that those payments are made. Most plans pay a lump sum benefit.



V. SIB IS ECONOMICAL

A. Because the period of risk is clearly determinable the plan can be funded with term insurance

B. Plus, potential cost of recovery using:

1. Purchase of extra death benefit, or

2. ROP riders, or

3. Payment of benefits in installments (ER has the use of the unpaid death benefits over the payout period)

VI. THE LIKELY TAX CONSEQUENCES OF SIB

Marketing Note: Always be careful when discussing taxes to make clear that you are not a tax professional, nor are you offering tax advice. It will be necessary for clients to talk to competent professionals in that area.

A. To the Employer

1. Because the business has an ownership interest in the policy, premiums paid are not income tax deductible

2. Death benefits are received by the business income-tax free (assuming that no disqualifying events, like a transfer-for-value of the policy, have occurred). This is true even if the proceeds are received when the EE is no longer with the ER, but the policy is still in force

3. Benefits to the EE's designated beneficiary are tax-deductible when paid

B. To the Employee

1. There is no current taxable economic benefit (unlike split dollar)

2. Benefits received by beneficiaries could be non-includible in the estate of the EE (unlike deferred compensation)

C. To the Beneficiaries - Benefits are received and taxable as income

FOR ANSWERS TO QUESTIONS OR NEED FOR ADDITIONAL INFORMATION
contact Tom Virkler, Director – CPS Advanced Markets, at 805-597-3636 or tom@cpsadvancedmarkets.com.

THE THREE-LEGGED BUSINESS PLANNING STOOL

Business Planning Concerns and Prospect Question Sheet

Marketing Note: A business owner may understand the goal of making arrangement for eventual disposition of the business in a manner desired, but may not have given though to the fact that, in order to reach that point successfully, the business must attract and keep and protect against the untimely loss of people key to the business' success. The following questions can help direct thinking in all three planning areas.

Planning Leg #1 - Questions concerning business transition

Planning who will own and/or manage the business next and ensuring it happens in a manner than makes everyone whole and satisfied ***(business transition arrangements)***

1. How long do you plan to own and/or manage the business?
2. Who do you want to own and/or manage it next?
3. How will that transition take place (sale, transfer, gift, inheritance)?
4. What arrangements have been made to assure all this takes place?

Planning Leg #2 - Questions concerning protection against loss of key employees

Planning to survive the untimely loss of critical employees (key person life and disability coverage)

1. Are there any employees whose untimely death or disability would jeopardize the immediate and/or long-term well-being of the business?
2. What would be the costs associated with that loss?
3. Have any steps been taken to protect against the possibility?

Planning Leg #3 - Questions concerning key person compensation

Planning to prevent losing critical employees to the competition (key person benefits)

1. You provide good benefits to your general workforce – is there a possibility that key employees might be hired away because they are attracted with additional benefits?
2. Do you think that additional benefits would make it attractive to stay here?
3. Would you consider benefits that are effective both in cost and in strengthening your hold on key employees?

SIB - STARTING THE CONVERSATION

Marketing note: Clients who have not done any key person benefit planning may not even know where to start in giving consideration to extra benefit compensation to selected employees. It is often helpful to briefly describe the SIB plan since it is the least complicated of the non-qualified plans. Below is a suggested dialogue. Before using this approach, be completely familiar with the aspects of the SIB described in the SIB Agent Primer included in this tool-kit.

Having determined from the 3-legged stool questions that there is an interest in providing for key employees:

Let me take two minutes to describe an uncomplicated, but valuable benefit for the important folks you mentioned who might be attracted away by offers from competitors or other companies.

<u>What if you said to your key EE's</u>

1. I want you to retire with me

2. During that time I don't want you to worry about the care of your family in the event of your premature death

And then you said . . .

3. If something were to happen while you were in my employ, I want to provide for your family.

4. I will pay them [$250,000].

5. This protection will cost you nothing.

Might that be of interest to them?

Marketing Note: Even when an idea sounds good, an employer quickly begins to think of the effect it will have on the business, especially the bottom line. Be ready to modify these concerns quickly.

And for you, [Mr./Ms. Prospect], this plan

1. Is easy to implement

2. It is easy to administer

3. It is cost effective and that cost can be locked in for the employment life of the EE

4. It can have significant tax advantages for you

5. You can award it on a selective basis, and

6. You can vary the benefit amounts from one EE to the next

If there is positive response to this you are prepared to begin asking questions and taking notes concerning what might constitute the right plan for the client using Plan Variable Data Sheet available in the tool-kit.

KEY PERSON BENEFIT VARIABLES – COMMENT SHEET

Marketing Note: The primary purpose of presenting the SIB Plan is to get the business owner thinking about key person benefits. He or she may decide not to do anything. However, if the conversation has gone that far they probably want something, maybe the SIB, but probably a plan with different features. The likely variables that will govern their suggestions are listed below along with questions that can be used to introduce them to different areas of plan options. If more than one key person is being considered and the benefits will vary, use a sheet for each key person. Take notes!

Business Prospect____

Meeting participants ____

Meeting date ____

Key person considered____

PLAN VARIABLE	
BENEFITS PROVIDED	Issue question: The plan I described included only a death benefit during employment. Should the plan include post-retirement death benefits as well; or additional retirement benefits? Are there other benefits you might consider? What level of benefits in each area do you think would be attractive to the key person? Marketing Note: Death and retirement benefits are the usual two elements of a plan, but ask the general question anyway.
Client comments:	

KEY PERSON BENEFIT VARIABLES – COMMENT SHEET continued

TAX EFFECTS	Issue question: It's not always possible to achieve all the desired tax results in a benefit plan. But if you could get different results from those in the plan I described, what would they be? Marketing Note: Generally there is a trade-off. A good tax result for the ER results in a less desirable one for the EE, and vice versa. Unlike the taxation in qualified plans, there is no free lunch.
Client comments:	
VESTING	**Issue question:** In the plan I described the EE controls his or her destiny by remaining with the company so long as the death benefit is irrevocable. Would you want a plan designed where the EE has less or more control over the ultimate receipt of their benefits? **Marketing Note:** Include in the discussion any other benefits the client has raised. Emphasize that too much ER control may not make the benefit attractive enough to keep the EE with the company should another opportunity arise.
Client comments:	

EE CONTRIBUTION	**Issue question:** Would you want the plan structured so that the EE bears some of the cost of the benefits? If so, how much? **Marketing Note:** EE contributions can either increase a sense of ownership or make the plan less attractive. Try to find the balance?
Client comments:	
ER COST RECOVERY	Issue question: How important is it to recovery the expenditures for the benefit, and when?
Client comments:	
BUDGET **Marketing Note:** It is often better to get an idea of how much the client wants to spend later into the discussion after they have mulled over the concept and the benefits of the arrangement. However, if they want you to begin demonstrating what they might do for the EE you need some sort of amount.	
OTHER	

TRADE PUBLICATION ARTICLE

<u>Marketing Note</u>: A good way to generate prospects is to find a trade publication or newsletter looking for content and offer them an article of financial substance that allows you exposure without being too self-promoting. The published piece can be used in prospecting efforts within the industry and one case can then lead to other referrals within that field as you become recognized as an insurance planner who is familiar with that business. The following can be used under your name. The article runs around 500 words which is a desirable range for most publications.

THE SIMPLEST WAY TO KEEP YOUR KEY EMPLOYEES

BY [YOUR NAME WITH PROFESSIONAL DESIGNATIONS]

Every Business Owner's Goal:

To conduct their business profitably until they can pass it

… to whom they want,

… when they want,

… for the amount they want.

…siness owner has the …oals: first, to operate …ny profitably until they …eed it to provide for …t and retirement income …ond, to then pass it to … want, when they want …e they want. All this can …ith proper and timely … The problem is that most …e so focused on the day- …mands of the business … take steps to assure that …chieve those goals.

…ners do take steps toward … planning it usually involves …ting the steps necessary …t the business gets to the …ho are to own the business …he company is to be …ed a buy-sell arrangement … with those in and/or out of the family who will have the right to purchase the company for an agreed price at an agreed time. If the business is to be passed during life or left at death to others, usually family members, then either a gifting program is instituted or proper changes are made to wills or other documents to take effect at death.

Business transition planning is good and necessary, but it is only as effective as the likelihood that the business will survive until the time when the changing of hands is to take place. An important part of the planning process involves doing what is necessary to keep the business functioning profitably until it is time to pass ownership. This involves a process of determining who the key people are that are critical to the effective operation (and the longevity) of the business and what must be done to increase the likelihood that they will stay with the company and not find more attractive employment elsewhere – certainly not with a competitor.

The balance in providing extra incentive for to key people to stay is to provide a benefit that can be offered selectively, and not the workforce at large, and that will lock the recipients to the company until they retire – the phrase "golden handcuffs" is often used. There are three ways to provide extra compensation. The first is to raise salary or offer perks. These options can be applied selectively, but they do not tie the employee to the company. The other is to offer benefits in the event of premature death or promise additional retirement income, or both. These benefits can be offered under legally binding agreements that provide security to the employee, but can be administered in a manner where the employer can maintain control until it is clear that the employee intends to make a long-term commitment to the firm. Plans can provide for employee contributions and can provide attractive tax advantages for all parties involved.

The simplest and easiest popular key person benefit involves offering a stated death benefit to a key person's beneficiaries in the event of death before retirement. The plan requires little or no implementation or administrative hassle or expense. The benefit provides the employee with peace of mind and the employer can even economically fund for the possibility of benefit payment with low cost life insurance structured in a way that offers opportunity for recovery of employer costs. The plan is flexible enough that, as the employee's value to the company increases, the plan benefits can be expanded to include additional retirement benefits or post-retirement death benefits.

Every business owner should

TRADE PUBLICATION ARTICLE

THE SIMPLEST WAY TO KEEP YOUR KEY EMPLOYEES

By [Your name with professional designations]

Every business owner has the same goals: first, to operate their company profitably until they no longer need it to provide for their current and retirement income needs; second, to then pass it to whom they want, when they want for the price they want. All this can be done with proper and timely planning. The problem is that most owners are so focused on the day-to-day demands of the business they don't take steps to assure that they will achieve those goals.

When owners do take steps toward transition planning it usually involves documenting the steps necessary to see that the business gets to the people who are to own the business next. If the company is to be purchased a buy-sell arrangement is made with those in and/or out of the family who will have the right to purchase the company for an agreed price at an agreed time. If the business is to be passed during life or left at death to others, usually family members, then either a gifting program is instituted or proper changes are made to wills or other documents to take effect at death.

Business transition planning is good and necessary, but it is only as effective as the likelihood that the business will survive until the time when the changing of hands is to take place. An important part of the planning process involves doing what is necessary to keep the business functioning profitably until it is time to pass ownership. This involves a process of determining who the key people are that are critical to the effective operation (and the longevity) of the business and what must be done to increase the likelihood that they will stay with the company and not find more attractive employment elsewhere – certainly not with a competitor.

The balance in providing extra incentive for to key people to stay is to provide a benefit that can be offered selectively, and not the workforce at large, and that will lock the recipients to the company until they retire – the phrase "golden handcuffs" is often used. There are three ways to provide extra compensation. The first is to raise salary or offer perks. These options can be applied selectively, but they do not tie the employee to the company. The other is to offer benefits in the event of premature death or promise additional retirement income, or both. These benefits can be offered under legally binding agreements that provide security to the employee, but can be administered in a manner where the employer can maintain control until it is clear that the employee intends to make a long-term commitment to the firm. Plans can provide for employee contributions and can provide attractive tax advantages for all parties involved.

The simplest and easiest popular key person benefit involves offering a stated death benefit to a key person's beneficiaries in the event of death before retirement. The plan requires little or no implementation or administrative hassle or expense. The benefit provides the employee with peace of mind and the employer can even economically fund for the possibility of benefit payment with low cost life insurance structured in a way that offers opportunity for recovery of employer costs. The plan is flexible enough that, as the employee's value to the company increases, the plan benefits can be expanded to include additional retirement benefits or post-retirement death benefits.

Every business owner should begin the process of identifying those employees critical to the operation and begin consideration of the best package of benefits necessary to make them a part of the long-range plan for the life of the business.

[Your name with any professional designations] is [a brief description of your practice]. He/she can be contacted concerning questions or for information at [your phone] or [your email address].

Confidential Business Planning Questionnaire

Prepared for:

Prepared by:

Contents

General Business Information

Name of Business: ADSadadadadasd ____

Address: ____

____

____

Phone Number: ____________________ Fax Number: ___________________

E-Mail Address: ____

Type of Business:

- ○ Sole Proprietorship
- ○ Partnership
- ○ Corporation (State of: _____________)
- ○ S-Corporation (State of: _____________)
- ○ P-Corporation (State of: _____________)
- ○ Limited Liability Company (State of:______________)

Date Established?: _________ If Incorporated, Corporate Tax Bracket: ____%

Current Estimated Fair Market Value of Business: _____________

Owner Information

Name	Title	Date of Birth	Sex	Ownership Interest	Annual Compensation	Personal Tax Bracket
1.				%		%
2.				%		%
3.				%		%
4.				%		%
5.				%		%

Professional Advisor Information			
Attorney:	______________________________		
Firm Name:	______________________________	Phone:	___________
Street Address:	______________________________		
City, State, Zip:	______________________________		
Accountant:	______________________________		
Firm Name:	______________________________	Phone:	___________
Street Address:	______________________________		
City, State, Zip:	______________________________		
Property & Casualty Insurance Agent:	______________________________		
Firm Name:	______________________________	Phone:	___________
Street Address:	______________________________		
City, State, Zip:	______________________________		

Business Planning Priorities

	High Priority	Medium Priority	Low Priority	No Priority
Planning for Business Continuation	○	○	○	○
Attracting and Retaining Key Employees	○	○	○	○
Indemnifying Business for Loss of Key Employees	○	○	○	○
Enhancing Employee Benefit Program	○	○	○	○
Using Business Dollars to Satisfy Owner's Personal Financial Security Needs	○	○	○	○
Planning for an Owner's or Key Employee's Disability	○	○	○	○
Providing Funds for Business Loan Repayment	○	○	○	○
Other: ________________________	○	○	○	○

Employee Census							
Name	Sex	Smoker? (Y or N)	Date of Birth	Date of Hire	Annual Compen-sation	Home Zip Code	Key Employee? (Y or N)
1.							
2.							
3.							
4.							
5.							
6.							
7.							
8.							
9.							
10.							
11.							
12.							
13.							
14.							
15.							
16.							
17.							
18.							
19.							
20.							

Important Information

This fact finder serves to help identify your financial needs and priorities and may be used in developing proposed solutions consistent with your needs and objectives. In completing this fact finder, you are entrusting our organization with certain personal and confidential financial data. We recognize that our relationship with you is based on trust and we hold ourselves to the highest standards in the safekeeping and use of your confidential information.

The information, general principles and conclusions presented in this report are subject to local, state and federal laws and regulations, court cases and any revisions of same. While every care has been taken in the preparation of this report, we are not engaged in providing legal,accounting, financial or other professional services. This report should not be used as a substitute for the professional advice of an attorney, accountant, or other qualified professional.