

# Key person life insurance

Allianz Life Insurance Company of North America



Key person life insurance can help you retain your key employees and plan for the continuity of your business.

Suppose something were to happen to one of your key employees. What would happen to your business?

Whether a key person leaves for a different position, is unable to work, or passes away, the disruptive effect on your business could be the same.

Although you can't prevent some of these situations, there is much you can do to prepare. One option might involve the purchase of key person insurance.

## What is key person life insurance?

Simply put, key person life insurance is a life insurance policy that covers one (or more) of your key employees, with the primary goal of protecting the value and ongoing operations of your business.

Key person insurance can be the foundation of a succession plan for your business. By offering a death benefit – and in some cases, a cash value account you can access in an emergency – key person insurance can help make sure that, for your business, life will go on.

Key person insurance can also help protect your business from the loss of a key employee, by offering an additional incentive for the employee to stay with your company.

## Who is a key person?

A key person is an employee whose absence would have an adverse economic effect on your business. Adverse effects from the loss of a key person may include a decline in profits, the loss of credit standing, or the extra expense of hiring a capable replacement.

Remember that, as the owner of your business, you're also a key person. All of the benefits we discuss apply to you, too.

## How does key person insurance work?

Your business purchases a life insurance policy on the key employee, pays the premiums, and is the beneficiary in the event of the employee's death. As the owner of the policy, your business may surrender it, borrow against it,<sup>1</sup> and use either the cash value or the death benefits as desired.

For many businesses, the biggest challenge lies in determining how much life insurance is needed. Although there are no hard rules for calculating a key employee's economic value, these guidelines may help:

- **Replacement value** – The appropriate level of coverage could equal the cost of recruiting and training an adequate replacement.
- **Business life value** – Estimate the loss of annual earnings if the key person were to die, and multiply that by the number of years the key person would have worked until retirement.
- **Multiple of salary** – The death benefit could equal the key employee's annual salary, times the number of years a newly hired replacement might take to reach a similar skill level.
- **Contribution to profits** – You may calculate the key employee's value in terms of the amount of income (through sales revenue, for example) their departure would cost your company.

<sup>1</sup> Policy loans will reduce available cash value and death benefits and may cause the policy to lapse, or affect guarantees against lapse. Additional premium payments may be required to keep the policy in force. In the event of a lapse, outstanding policy loans in excess of unrecovered cost basis will be subject to ordinary income tax.

Please note that loans and withdrawals may be subject to regular income tax and, if taken prior to age 59½, a 10% federal tax penalty may apply.

## What are the tax implications?

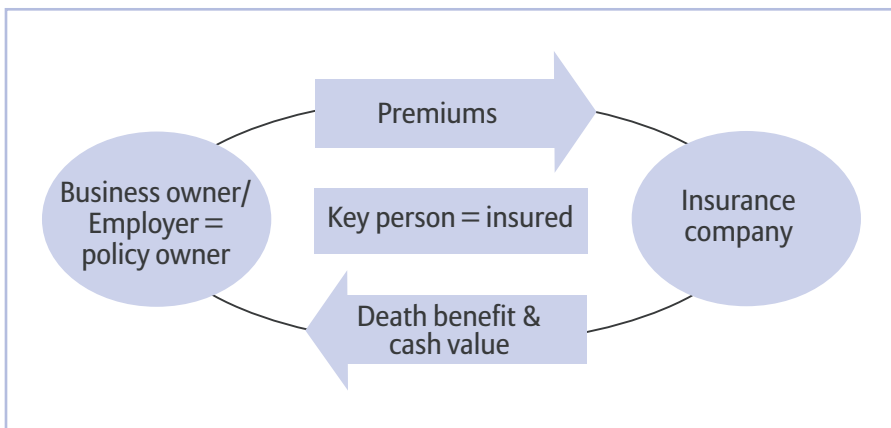
The premiums you pay for key employee life insurance are not deductible from your business' federal income tax, since your business is the recipient of the benefits. The good news is that, in most cases, any death benefit your business receives is not taxable.

Nevertheless, if your business is a C corporation, the receipt of death benefits may increase the corporation's liability for the alternative minimum tax. Before purchasing key person insurance, you should consult a tax professional about your unique circumstances.

## What happens if the key employee leaves – or retires?

If an insured key employee terminates his or her relationship with you, there are various options for disposing of the life insurance policy:

- Your business can continue to pay the insurance premium, and receive the death benefit upon the death of the former key employee.
- If your key employee is retiring, you can offer the policy as a gift, at its present value.
- Your company can surrender the policy to the life insurance company and obtain the cash surrender value.



**Life insurance provides a death benefit – and so much more. Look beyond the death benefit and see how your insurance can be “bigger than life.”**

**Call your financial professional today to learn more about how life insurance can be an important part of your business plan.**

**Allianz. Financial solutions from A – Z.®**

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