

Concept Profile

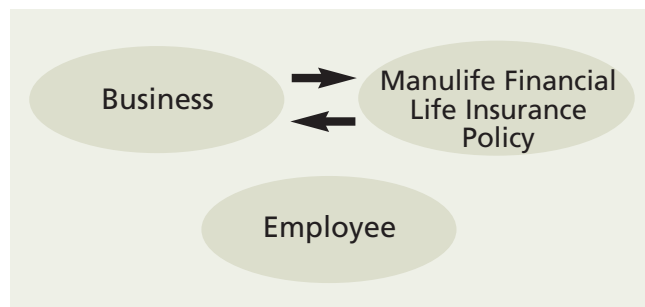
KEY PERSON INSURANCE

A Way to Protect Against the Unexpected

The unexpected has just happened: your key employee, William West, goes on vacation and dies in a serious accident. He has been part of the business since day one, and all his knowledge and experience will be hard to replace. It is going to take awhile to find a suitable replacement and the business is going to go through a rough period that it may not survive. Cash flow will be tight. Too bad the company did not have the foresight to purchase key person insurance on William to help it through this tough time.

WHAT IS KEY PERSON INSURANCE?

Key person insurance is an insurance policy taken out by a corporation on the life of a key employee to protect the business in case of a sudden death. The key employee can be anyone in the business whose loss would be significant to the company or could result in a loss of business. This could be the owner, a partner, or an employee whose knowledge and contributions to the company are invaluable.



HOW DOES IT WORK?

The corporation buys a life insurance policy on the life of the key employee, and the business is the owner and the beneficiary of the policy. The business will pay the entire premium and at the death of the employee, the business will receive the entire death benefit. This income tax free death benefit may be used to replace lost profits, recruit and/or retain qualified replacements, or protect the company's credit position. The employee does not have any interest in the policy, nor does his or her family typically receive any benefits from the policy when death occurs.

BENEFITS OF KEY PERSON INSURANCE

Key person life insurance is simple to implement. It does not need IRS approval and may include many people. With key person life insurance the business has death benefit protection in case of a sudden and unexpected death, and is able to access the potential cash values of the life insurance policies for cash flow, retirement benefits, or for unanticipated expenses.¹

TAX IMPLICATIONS²

A key person life insurance arrangement, in most situations, benefits the business and the only involvement that the executive has is being the insured. The business does not receive an income tax deduction on the premium, but it will receive the death benefit free from income taxes upon the death of the insured. However, potential for alternative minimum tax may arise in limited circumstances if the business is a "C" corporation.

SUMMARY

Key person life insurance is one way a corporation can protect itself against the loss of a key employee, partner, or owner. It is a contingency plan for the unexpected. Key person life insurance arrangements are easy to set up and implement. Small businesses whose day-to-day and possible long term performance may be hurt if something happens to one of the important people in the organization, should consider key person life insurance.

For more information, please contact your local Manulife Financial Representative or call The Advanced Markets Group at (888) 266-7498, option 3.

1 Withdrawals and loans from life insurance policies which are classified as modified endowment contracts may be subject to tax at the time the withdrawal or loan is made. A federal tax penalty of 10% may also apply if the withdrawal or loan is made prior to age 59½. Withdrawals and loans also have the effect of reducing the death benefit and cash surrender value and may cause the policy to lapse. Lapse of a life insurance policy may cause adverse tax consequences.

2 This piece briefly mentions the tax implications of key person life insurance. A full tax discussion goes beyond the scope of this piece. This piece is intended to provide an overview of key person insurance and the tax consequences that it may face. For more information on the tax consequences of key person insurance, please contact your tax consultant.

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73 Tremont Street, Suite 1300, Boston, MA 02108 (888) 266-7498
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