PACIFIC LIFE

ADVANCED SALES SOLUTIONS AT-A-GLANCE

KEY PERSON LIFE INSURANCE

Protect a Business Against the Financial Impact of Losing a Key Employee

A significant portion of a successful business operation relies on the unique skills and expertise of key employees.[1] Some business owners choose key person life insurance to protect their businesses from long-term financial disruption should a key person suddenly passes away or becomes disabled.

What is Key Person Life Insurance?

Key person life insurance is a business protection planning technique. The business purchases life insurance on the life of a key person with the business as the sole beneficiary, for the main purpose of protecting the business from the financial loss that can occur in the event of the premature death of the key employee.

Potential Benefits

Financial Protection	▪ Death benefit proceeds are paid income-tax-free[2] to the business. ▪ Liquidity helps mitigate the financial impact and disruption to the business against the sudden death or disability of a key person.
Cash Value Assets	▪ If cash value life insurance is used, it offers the potential to accumulate cash value over time to help to recruit and train a suitable replacement, in the event the key employee voluntarily leaves the business or for other business needs. ▪ The cash value grows on a tax-deferred basis.
Planning Ease	This strategy can be used for: ▪ Providing benefits under one or more employee benefit plans. ▪ Financing a buy-sell agreement.

[1]In order to preserve the tax treatment of the life insurance death benefit, the key executive should be a shareholder who owns more than 5% of the shares, a director, or a highly compensated employee as defined in IRC Sec. 101(j)(2)(A)(ii).

[2]For federal income tax purposes, life insurance death benefits generally pay income tax-free to beneficiaries pursuant to IRC Sec. 101(a)(1). In certain situations, however, life insurance death benefits may be partially or wholly taxable. Situations include, but are not limited to: the transfer of a life insurance policy for valuable consideration unless the transfer qualifies for an exception under IRC Sec. 101(a)(2) (i.e., the transfer-for-value rule); arrangements that lack an insurable interest based on state law; and an employer-owned policy unless the policy qualifies for an exception under IRC Sec. 101(j).

Investment and insurance products: Not a deposit • Not insured by any federal government agency

Not FDIC insured • No bank guarantee • May lose value

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How it Works

1	**Notice and Consent**	▪ The business provides written notice to the key person that it intends to buy and be the beneficiary of a life insurance policy on the key person's life and may choose to continue the coverage beyond the key person's employment. ▪ The business must also notify the key person as to the maximum amount of life insurance that could be placed on the key person's life. ▪ The key person then provides the business with written consent to purchase the life insurance.
2	**Premiums**	The business pays the non-deductible[3] life insurance premium on the key person's life and retains all ownership rights.
3	**Death Benefit**	At death, the business will receive the life insurance death benefit[4] income-tax-free.[2]

Considerations

- As an asset of the business, the policy may be subject to any creditors of the business.[5]
- Since the business is both the owner and the beneficiary of the policy, the business may not deduct the cost of the life insurance policy premiums.

[3]As a general rule, no deduction shall be allowed for premiums on any life insurance policy, or endowment or annuity contract, if the taxpayer is directly or indirectly a beneficiary under the policy or contract per IRC Sec 264(a)(1).

[4]A potential disadvantage with closely held businesses involving owners with larger taxable estates is that the life insurance proceeds paid to the business may have adverse estate tax. See: Connelly vs United States, 602 U. S.____ (2024).

[5]State law may provide life insurance and annuities with certain asset protection benefits. As a general rule, a debtor may not transfer property with the intent to avoid debt due to his creditors. The laws governing asset protection, however, are complex and the consequences of poor planning may be both civil and criminal penalties. Anyone contemplating an asset protection plan should not undertake such without the advice of legal counsel.

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For help with your next case, please contact our Advanced Designs Unit at AdvancedDesigns@PacificLife.com or (800) 800-7681, ext. 3690.

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The primary purpose of life insurance is to provide death benefit protection in the event of the insured's death.

Life insurance is subject to underwriting and approval of the application and will incur monthly policy charges.

Pacific Life Insurance Company's Home Office is located in Omaha, NE.

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