

Think about this: “Do you ever wonder what would happen to a small business you visit often (your local coffee shop, the bakery down the street, family run dry cleaning shop, etc) if the owner is no more?”

Many small businesses do not continue after the first generation of owners due to lack of succession planning. As a financial advisor, you could talk to them about “Buy-Sell arrangements”.

What is this?

This is an arrangement for the sale of a business interest upon the owner’s death, disability, or retirement. To facilitate continuation of the business, the buy-sell arrangement should be well-drafted and properly funded.

How does this work?

Depending on the number of owners and business structure, you could suggest

- an entity purchase arrangement– company buys out its deceased owners
- a cross-purchase arrangement- owner buys out each other.

Where does life insurance fit in?

Small businesses usually are more concerned about the cash flow problems. One partner might not be able to save enough to buy out another partner’s shares. Life insurance is generally cost effective, provides predictable amount of cash upon death or in some cases, policy’s cash values might be enough to fund a buy-out prior to death.

Bill and John are partners in your local bakery. They both agree that in the event of an unfortunate event happening to either of them, they would like the business to continue. They enter into a cross purchase buy-sell arrangement and fund it with life insurance. Each is the owner and beneficiary of the policy on the other. John, unexpectedly dies in a car accident. Per their agreement, Bill uses the life insurance proceeds to buy John’s share of the business and the business continues. John’s family is also helped with the cash they receive from Bill.

You can help with succession planning by talking about some of the benefits of a buy-sell arrangement to your client: guaranteed buyer for the business, liquidity is created, value of business is fixed and harmony is maintained in a difficult time.

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