Agent and Advisor Guide to
Advanced Markets Concepts

AVIVA

Cross Purchase Buy-Sell

Buy/sell planning is a critical element of any successful business

- It provides a definite market for transferring the ownership interest. The co-owners or business entity must purchase the interest
- It specifies a set or determinable price. This price may also set the value used for estate tax calculation
- It provides some or all of the funds necessary to execute the agreement – when properly funded with life insurance.
- It maintains "closeness" of the business by restricting and planning who/what can receive the business interests
- It provides liquidity to pay estate taxes (due 9 months from date of death)
- It makes the entity a better credit risk because of the probability of business continuing past an owner's death

All businesses can benefit from buy-sell planning – sole proprietorship, C Corporation, S Corporation, Partnerships, LLCs, etc.

How cross-purchase works:

1. At an owner's death, disability or departure, the surviving/remaining owners agree to purchase the business interest – this is documented in a formal agreement between/among the owners.
2. Each business owner applies for (and is beneficiary of) a life insurance policy on every other owner
3. At death, each surviving owner receives the policy death proceeds.

   If departure is for reasons other than death (i.e. disability) the policy's cash values can be accessed to partially or totally fund the purchase.
4. Each surviving owner purchases the agreed business interest from the decedent's estate (e.g. if only one surviving shareholder, he/she purchases all of the business interest from the estate).

Results:

Estate's non-liquid asset (i.e. the business interest) is sold to the remaining owners at an agreed upon price (little or no gain should be taxable due to step-up in basis at date of death – assumes death in other than 2010 when there is a modified carryover basis rule in effect).

The business interest passes to those intended to receive that interest.

Surviving owners receive basis in the acquired interest equal to the price paid (step-up in basis).

Why life insurance:

Cash value inside a policy grows tax-free (tax-deferred if withdrawals exceed policy basis).

Death proceeds are received income-tax free and received at just the right time to fulfill the agreement.

Individually owned policies are generally not subject to the business' creditors.

Disadvantages:

Business owner uses personal funds to pay premiums on the policy they own. A split-dollar (loan arrangement or employer endorsement) arrangement can be implemented to assist in paying premiums.

Possible disproportional premium payments – the younger/healthier owners will pay more in premiums to insure the older/less-healthy owners

Policies are potentially subject to the individual's creditors.

Administratively complex – the more business owners the more policies that must be purchased and maintained. For example: if there are three owners, each owner will own and maintain two policies (6 policies total) – if there are six owners, each owner will own and maintain 5 policies (30 policies total).

The preceding summary is intended to be a general discussion of the topic presented, and is based on our current understanding of applicable tax laws, regulations and rulings. In actual practice, the transaction discussed may be more complex and will require the attention and expertise of professional advisors. In no way should this summary be construed to constitute tax or legal advice. **For agent use only.**

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