



**Protecting your business
from the unexpected**



In business, it takes vision, preparation, skills and desire — not to mention a focused dedication to achieving your goals. If you are like most business owners, you have worked hard and made many sacrifices to grow your business. That is why you should put just as much energy into protecting it as you did building it.



You know what it takes to build a successful business.

Your business is most likely your largest asset. It is used to provide a majority of current income to support your family, will be looked to as a source of wealth at retirement, and may be the legacy you wish to leave to future generations.

Developing a business continuation plan — in the case of death or disability — is critical to the continued well-being of the business and the family. Businesses can transition expectedly or unexpectedly. That's why it's important to plot a course toward protecting the business and minimizing the impact an unexpected change in ownership could have on those who depend on the business most.

The reality is three out of ten business owners do not have any type of formal succession or continuation plan in place.¹ Think about what would happen to your business if you, your business partner, or a key employee were to die unexpectedly or become too sick or injured to work. There is no doubt that this would have a huge impact on your business. But there is good news: this is something you can plan for.

The following are some common business continuation strategies designed to help you protect the business you've put so much energy into building.

¹ 2018 MassMutual Business Owner Perspectives Study conducted by HawkPartners for MassMutual.



Buy-Sell Agreement

A buy-sell agreement is a foundational document for any sound business continuation strategy. Yet, only 60% of business owners have a buy-sell agreement in place that protects the business from the death of an owner, and even fewer (50%) have one that protects against disability.²

A buy-sell agreement is a legally binding document that requires one party to sell and another party to buy ownership interest in a business. A buy-sell agreement can be designed to protect the business from certain triggering events, the most common of which are referred to as the five D's — death, disability, divorce, departure (either voluntary or involuntary), and disqualification (malfeasance that would require an individual to be removed from an ownership position).

By establishing a buy-sell agreement, you can help ensure a smooth transition of ownership, reducing disruption to the day-to-day activities of the business. An effective buy-sell agreement should establish:

- Which triggering events are covered.
- Who will purchase the decedent's or disabled owner's share of the business.
- At what price the ownership shares will be sold, or the method that will be used to determine the business value at the time of the triggering event.
- How the transaction will be funded.

The funding portion of the buy-sell agreement is key, but often overlooked. Only about half of buy-sell agreements are properly funded with insurance products, such as life insurance and disability buy-out insurance.³ These insurance policies make it possible for the remaining owner to purchase the business interests of the deceased or disabled owner without liquidating business assets or taking cash out of the business. This allows the family of the seller to receive full value for the business interest and allows the remaining owner to be focused on continuing business operations.

In addition, buy-sell agreements should be reviewed at least every three to five years to ensure they reflect the current structure and value of the business.

^{2,3} 2018 MassMutual Business Owner Perspectives Study, conducted by HawkPartners for MassMutual.

Key Person Insurance

You value your key employees and the contributions they make to your business every day. However, have you thought about the impact losing one of them would have on your business?

Think about the value they bring — whether it's their creative genius, sales acumen or leadership qualities — and what those characteristics are worth to the business. Is it something worth protecting?

Having the foresight to protect your business against the loss of an essential employee — perhaps a company's most valuable asset — can mean the difference between business as usual or closing up shop. Key person life insurance can help offer peace of mind in knowing that the financial stability of your business is protected in the event of a valued employee's untimely death.

The way it works is simple: you purchase a life insurance policy on the life of the key employee, naming your business as the beneficiary. If the key employee dies, the policy's death benefit proceeds are paid to the business to help keep it going while you seek to fill the void left by the deceased employee. The funds could be used to temporarily replace lost revenue, hire a recruiter to help find a replacement employee, or provide specialized training to a new or existing employee.

Key person insurance is ideally suited for businesses with:

- Owners, partners or executives that have a direct impact on company earnings.
- Salespeople who continually exceed goals or have relationships with important clients.
- Individuals who have specialized skills or technical knowledge that cannot easily be replaced.



Business Overhead Expense (BOE)

Just over 1 in 4 of today's 20-year-olds will become disabled before reaching retirement age.⁴ Yet, not enough business owners give sufficient thought to how disability can impact their ability to run their businesses day-to-day.

As a business owner, you have expenses to pay and obligations to meet. So if you were to become disabled, and couldn't cover the basic expenses of running your business, the future of your company could be in jeopardy. However, with a business overhead expense (BOE) disability insurance policy in place, the business can continue to operate even while you are unable to work.

BOE helps cover the day-to-day business expenses that help keep the company's doors open – for up to two years – should you become totally disabled. Employee salaries, rent, leases, interest on debt and insurance premiums can all be covered by the policy – even your temporary replacement's salary.

BOE covers owners and professionals who are actively involved in the business on a full-time basis and whose presence is critical to its ongoing operation. Even more importantly, BOE can provide your employees with some assurance that you've taken the precautions to help keep your business, and their source of income, viable in the event you become disabled.

⁴ Social Security Administration, Fact Sheet, 2018.

Qualified Sick Pay Plan

Imagine if a key employee were to become seriously sick or injured. Maybe it's your top salesperson or an employee who has been with you since the beginning. In addition to the potential impact to your business, the financial impact to that employee's family and loved ones could be devastating. In a scenario like this, you might choose to continue paying that employee's salary while they recover.

However, doing so is not quite as simple as you may think. The IRS will not consider the salary you pay while your employee is ill or injured to be a "wage," since they are not actually working. This means you can't deduct the wages from your company's taxes or claim them as a business expense. But there is a solution. By planning ahead with a Qualified Sick Pay Plan (QSPP), your business can be better prepared — and reduce the risk of unforeseen tax consequences — if something unexpected were to happen to an employee.

A QSPP is an agreement that sets company policy before a disability occurs. It establishes who should be included, how much salary they will be paid, when payments start, and how long the payments will last. The plan must be instituted prior to a covered employee becoming disabled, and that employee must be aware of the terms of the plan. Additionally, the agreement must be in writing. With a QSPP in place, you can pay the employee's salary and deduct their wages from the company's taxes just as you would for a regular full-time employee.



Cash Reserve

Not all unexpected events are going to require the use of insurance proceeds or a legally binding partnership agreement. Some events, such as economic downturns, natural disasters, increased competition, slow receivables, and other regular challenges businesses face, simply require available cash on hand to get the business through the rough patch.

The amount of cash reserves your business should keep on hand varies based on considerations such as whether you make a product or sell a service, your available credit, and payroll needs. For many businesses, three to six months' worth of operating capital is a reasonable target. While there is no set ratio or amount for business cash reserves, you can use these benchmarks to determine how much money you should keep in your bank account to get you through the tough times.

Production Costs: If you make a product, for example, you'll need to keep enough money on hand to continue ordering materials and supplies, hiring workers and keeping your plant running.

Overhead Costs: If you have no sales for a time, you won't have production costs, but you will have overhead costs, such as rent, utilities, insurance, payroll, leases and other expenses that you will need to calculate on a monthly basis.

Total Costs: Calculate your total operating costs per month to determine how long you can continue to run your business while producing your product or service without pay.

Review Your Credit and Assets: Look at other sources of funding, such as short-term bank loans or lines of credits and personal savings, to determine how much they can help offset any of your identified shortfalls.

A courageous decision is a good decision.

Choosing the path of business ownership is truly an honorable and courageous endeavor. A successful business begins with planning for and building a strong financial foundation. Business planning is not something that's done overnight, but having an understanding of the ways in which you can protect your business for the long-term is a smart first step toward helping set your business on the road to a more financially secure future.

At MassMutual, we recognize the challenges you face and are equipped to help you prepare for the future with more confidence. Our goal is to help you stay focused on the task at hand — running your business — while working in concert with your trusted advisors to help you create a financial road map for the long term success of your business.

Put our qualities of strength, experience and stability to work for your business.



MassMutual...

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