

# The High Cost of Inaction!

Adapted from an article in Life Insurance Selling, January 2011

This is a summary of the High Cost of Inaction regarding the funding of a Buy-Sell Agreement.

## Background Facts

- \$2MM Business
- 20% Shareholder passes away
- Buy-Sell agreement requires company to purchase estate's interest @ pro-rata value – valued at \$400K
- Agreement calls for 5 year installment note at 6% interest.
- Tax Rate of 35%
- Profit Margin of 5%
- Deceased shareholder is also key employee (will need to be replaced)
- Current sales and net cash flow required are not sufficient to pay out estate
- Company is at debt capacity so borrowing is not an option

Year	Principal Balance	Principal Payment	Pre-Tax Earnings	Interest Expense	Total Pre-Tax Earning Required	New Sales Required @5% (\$ Millions)
1	\$400,000	\$80,000	\$123,077	\$24,000	\$147,077	\$2.941
2	\$320,000	\$80,000	\$123,077	\$19,200	\$142,277	\$2.845
3	\$240,000	\$80,000	\$123,077	\$14,400	\$137,477	\$2.749
4	\$160,000	\$80,000	\$123,077	\$9,600	\$132,677	\$2.653
5	\$80,000	\$80,000	\$123,077	\$4,800	\$127,877	\$2.557
Total	\$0	\$400,000	\$615,385	\$72,000	\$687,385	\$13.7477
<b>15 Year Term Life Premium – Alternate Funding Solution</b>	<b>\$0</b>	<b>\$2,000 / yr Or \$30,000 for 15 years</b>	<b>\$3,076 / yr</b>	<b>\$0</b>	<b>\$40,000</b>	<b>\$61,538.00</b>

Had the Business Owner properly funded the Buy-Sell Agreement with a life insurance policy when the Valuation was done and the Buy-Sell Agreement was written, the cost a 15 year term life policy would have been about \$1,000 - \$2,000 annually for 15 years, depending on age and health.

**Net, a \$30,000 expense over 15 years would have prevented draining \$13.7 million in sales and \$687 thousand in pre-tax earnings to fund the buy-out.**