

Insurance Needs of a Growing Company

Examine the insurance needs of a business as it grows from a sole proprietorship to a larger company. In the example below, John's company follows just one of several possible growth paths a business may take.

[Sole Proprietorship
Partnership and Growth
S Corporation](#)

[C Corporation
Going Public](#)

Other Products Of Interest

- [Payroll Services](#)
- [Health Insurance](#)
- [Workers' Compensation](#)

All business owners should check with their tax consultants and advisers before selecting which form of business is best for them. When considering the purchase of any form of insurance, first determine the needs of the business. There are many different insurance companies selling similar, if not the same, products. Shop around to find the company and agent who can deliver a solution to your needs in a manner that works for your business.

Sole Proprietorship

John starts a custom business in his basement. He does all the work himself. Even if he hires someone to help him, he is still a sole proprietor, unless he takes on a partner or incorporates the business. (Many businesses begin as partnerships or corporations.)

As the owner and only employee, John needs to protect his ability to earn a living and replace the benefits he previously received from his former job. He also needs to borrow money to cover start-up costs.

Life Insurance

As a sole proprietor, John's estate is responsible for his company's debts. He needs enough life insurance to cover family and business debts and estate taxes. Additionally, creditors may require life insurance when John borrows money. Since John's funds are limited now, a flexible policy could increase as the value of his business grows.

Disability Insurance (DI)

As the only employee, John's business could go under if he is unable to work, and there's no big company to pay him sick days. However, John may have trouble purchasing DI as a new business owner — many companies require three years of stable earnings before they issue DI policies. Ideally, John should have purchased individual DI before he left his previous job.

Medical Insurance

COBRA benefits from his previous job will generally run out in 18 months after termination of employment.

[Back to top](#)

Partnership and Growth

John's sales are booming. He takes on a partner, his former colleague Mary. They hire five new employees and a secretary and move the growing company into a small office. They name the business J&M Company.

Partnerships, like sole proprietorships, are not taxable entities. Instead, all of the business profits and losses are passed to the owners, making personal asset protection essential. John and Mary need to be able to keep the office running if they are unable to work. They also want to provide basic employee benefits to help attract and retain employees.

Life Insurance

John and Mary still need life insurance to cover business debts. Like a sole proprietorship, partnership debts must be paid by personal assets if business assets are insufficient. In a partnership, each partner is personally liable for 100 percent of the business' debts.

Disability Insurance (DI)

Mary needs coverage since she is also active in the daily operation of the company.

Medical Insurance

Mary needs coverage since she will be losing benefits from her former job.

Succession Plan

The J&M Company needs a buy/sell agreement to ensure that it does not dissolve with the death or disability of a partner (funded by life and disability insurance on each partner). The insurance should be able to grow as the value of the business increases. Partnerships cannot be inherited without an agreement.

Business Overhead Expense Insurance (BOE)

Business expenses need to be covered if John or Mary becomes disabled.

Liability Insurance

The J&M Company needs liability coverage.

Employee Benefits

The J&M Company can cover employees through small-group insurance plans. Employees may purchase additional benefits through a payroll deduction plan. The company could provide health insurance, life insurance, and disability insurance.

[Back to top](#)

S Corporation

Sales are so great that John and Mary open another office across the state. They increase the staff at the original office and hire an office manager, secretary, and additional staff for the second office. John and Mary incorporate the J&M Company into an S corporation. John and Mary's personal finances are legally protected (limited liability) and ownership transfer becomes easier. Unlike a sole proprietorship and partnership, a corporation is a separate entity from its owners.

John and Mary still need personal protection even though the company is a corporation. They also want to improve the company's employee benefits and retirement plans to attract top employees.

Life Insurance

In many cases, a corporation's business debts cannot become the owners' personal debts. However, creditors often require corporation owners to provide a personal guarantee that debts will be repaid, making life insurance ownership important to cover those debts. Owners should also cover their personal life insurance needs.

Employee Benefits

The company can offer a flexible benefit plan.

Keyperson Insurance

The business needs protection if the manager dies.

[Back to top](#)

C Corporation (Closely Held Business)

The J&M Company opens five more factories and hires five new managers and many new employees. It becomes a C corporation but is still owned solely by John and Mary. Since stock is not traded publicly, it is called a closely held business.

With the business becoming more valuable, John and Mary should expand their keyperson insurance and buy/sell protection. They also want to offer selective benefits to attract, retain, and reward top managers.

Succession Plan

Succession planning is still important since stock is not traded publicly. John and Mary want to continue to ensure that one of them retains ownership if the other dies. They may want to keep their buy/sell agreement, possibly using a Section 303 stock redemption (funded through life and disability insurance).

Keyperson Insurance

The company needs to cover any new managers hired.

Executive Benefit Plans

The J&M Company can provide special benefits for the owners and selected managers, such as:

- split dollar life insurance,
- deferred compensation,
- Section 162 executive bonus plan,
- reverse split dollar,
- phantom stock plan (provides non-owner managers with a piece of the business profits even though John and Mary retain full ownership of the business).

[Back to top](#)

Going Public

The J&M Company changes from a closely held business to a publicly held corporation. The business sells stock publicly and allows managers to purchase stock at a lower price. John and Mary should intensify their estate planning as the value of their business grows.

Since stock is traded publicly, ownership is transferred easily. John and Mary, however, want to ensure that they or their managers retain majority ownership.

Succession Plan

John and Mary should consider key managers in their business succession plans.

Stock Option Plan

This enables managers to purchase stock at a lower price.

Estate Planning

Now that their business has significant value, John and Mary need to make sure their estate planning is up-to-date. They should consider:

- a by-pass trust to reduce estate taxes,
- life insurance to balance unequal bequests of illiquid assets to children;
- life insurance to pay estate taxes.

[Back to top](#)