EXECUTIVE BENEFITS NETWORK

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# The Many Benefits Of Corporate and Bank Owned Life Insurance (COLI/BOLI)

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# THE MANY BENEFITS OF CORPORATE AND BANK OWNED LIFE INSURANCE (COLI/BOLI)

Companies use Corporate and Bank Owned Life Insurance (COLI/ BOLI) to help fund their employee benefit plans, increase earnings and shareholder value as well as recruit, reward and retain key officers and directors.

## SUPPORTS THE BUSINESS AND ITS COMMUNITY

**Background**

The business initially purchased COLI on a few of its executives and directors to informally finance the cost of deferred compensation plans. Later, the business decided to purchase additional COLI (on a Guaranteed Issued basis - i.e. no medical underwriting) on all of its existing officers where the business was the owner and sole beneficiary without establishing new or additional deferred compensation or other benefit plans.

**Need**

The purpose of this purchase was to provide key person protection for the business, and to offset the business's growing existing employee benefit expenses.

**Results**

Years later, a key officer passed away. The business received the tax-free death benefit from the insurance which helped the business through a difficult financial time: lost revenue, employee transition cost and lost goodwill in the community due to the death of the officer. However, with the additional tax-free gain, the business made a large charitable donation in memory of the deceased officer to one of his passions—a new local community library. Not only did his family love this because of his memory living on in their hometown, but the business was able to make an additional charitable contribution to strengthen the community over and above its normal giving.

**Bottom Line**

BOLI/COLI is not just helpful for deferred compensation and executive benefit plans. COLI, through earnings and life insurance, protects the business from a key person perspective and helps keep the business financially strong to better serve the community. A community and its community business are interdependent - when one is strong, they both thrive.

**"Tax-free key person protection for the business to hire replacements for the executive without incurring extra loss."**

# SUPPORTS BUSINESS SUCCESSION AND THE EXECUTIVE’S FAMILY

**Background**

The business implemented a Salary Continuation Plan as a way to reward and retain certain key executives. The business purchased COLI as way to informally finance this benefit plan while also providing key person protection for the business.

**Need**

One of the Business’s top executives passed away suddenly. Based on the Salary Continuation Plan, the Executive’s widow received 15 years of survivor benefits. This benefit helped her to maintain her lifestyle and keep her family in their home. In addition, the business needed to hire two people to replace the work done by the key executive.

**Results**

The Executive’s widow did not receive this benefit directly from the COLI purchased by the business. However, COLI provided the following for the business:

1. Tax-free income to offset the increase in the liability for the 15 year survivor income stream, and
2. Tax-free key person protection for the business to hire replacements for the executive without incurring extra loss.

**Bottom Line**

It is important to have good benefits on key executives - it is good for the business and also for the Executives’ families. COLI/BOLI helps to finance these benefits and protect the business and family from incurring further monetary losses in an already tough time.

**“A community and its community business are interdependent - when one is strong, they both thrive.”**

# OFFSET INCREASED HEALTH INSURANCE EXPENSES

**Background**

Facing an issue that is not uncommon today, a business incurred an 8.9% increase in its health insurance premiums. Because of lower margins and a low-yield environment, the business passed all of the increased expenses to its employees. The business was unable to compete in its market for top talent with this short-term solution and also incurred the risk of losing some of its key employees.

**Need**

The business was forced to think creatively of ways to offset these increased expenses and, therefore, looked to purchase COLI on key officers. The cash value yield on BOLI provided better incremental income than what was otherwise available in the market (ie: 2% pre-tax yield), which indirectly helped to offset the increased health insurance expenses.

Healthcare cost offset

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 |
|---|---|---|---|---|---|
| Total Medical Insurance Expense (1) | $978,000 | $1,065,042 | $1,159,831 | $1,263,056 | $1,375,468 |
| BOLI Gain Above 2% Investment Performance Yield (2) | $129,600 | $133,424 | $141,818 | $149,446 | $158,876 |
| Net Cost | $848,400 | $931,618 | $1,018,013 | $1,113,609 | $1,216,591 |
| Total Savings | 13% | 13% | 12% | 12% | 12% |

(1) Based on cost of current health insurance premiums with an assumed 8.9% annual increase.
(2) Based on the incremental earnings advantage of BOLI versus a taxable 2% yield in an alternative investment.
**BOLI assumption**: $8 million initial investment at a current net yield of 2.82% after expenses and cost of insurance.
**Alternative Investment**: 2% pre-tax yield and a corporate tax rate assumption of 40%.

**Results**

The business no longer intends to pass the increased healthcare expenses to its employees and also lessened the financial impact of this increased expenses to the business. As an additional strategic byproduct of the COLI, the business provided a Supplemental Life Insurance Plan which saved the business some expense of its group term insurance and decreased the amount of imputed income the officers had to recognize on their W-2's.

**Bottom Line**

BOLI/COLI offers a creative solution to offset the cost of increased healthcare expenses, it reduces the expense of group term life insurance premium for the employer and it provides lower imputed income for all officers.

**"BOLI decreased the amount of imputed income the officers had to recognize on their W-2's."**

# Supports Continued Operations and Cash Need

**Background**

Prior to September 11, 2001, the airline industry went into a deep recession and many airlines were struggling. Cash flow was king and retaining key executives was paramount. This company implemented a nonqualified voluntary deferral plan to rectify the low government limits placed on 401k annual contributions. The participation was good as executives desired to save as much as possible on a pre-tax basis above the 401k limits. This company reviewed various financing alternatives for their nonqualified plan liabilities and turned to Corporate Owned Life Insurance (COLI) as a preferred solution from a tax advantage standpoint as well as a self-completion standpoint.

**Need**

A year into this plan, one of their key executives, who was only 35 years old, passed away of cancer. A claim was paid on the COLI policy owned by the company. The tax-free income received as part of the key man life insurance policy helped finance the benefit liability owed to the deceased executive's family and provided a meaningful amount of cash that the company put back in the operations.

**Results**

During those lean months, airlines carried two weeks of capital on their balance sheet. This cash from informally financing their nonqualified plan liabilities with Corporate Owned Life Insurance was crucial for this company to make it through another month of operations in this trouble time.

**Bottom Line**

While many corporations (over 50% according to a recent survey) utilize Corporate Owned Life Insurance to finance nonqualified plan liabilities, few do it strictly for the death benefits payable to the corporation. When these benefits are received by the corporation, it is typically welcomed cash flow that can be used to subsidize operations or to fill the void in many of their unfunded benefit liabilities.

**"This cash from informally financing their nonqualified plan liabilities with COLI was crucial for this company to make it through another month of operations."**

## ABOUT THE AUTHORS

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David is the Co-Founder of Executive Benefits Network and a 34-year veteran of the financial services industry. David is a frequent speaker and author across the banking industry as an expert in the area of Nonqualified executive benefit plans and Bank Owned Life Insurance programs. David is the Past Chairman of The American College of Financial Services Foundation, Director of the Association for Advanced Life Underwriting (AALU) where he Chairs the BOLI/COLI Nonqualified Plan Committee, Trustee of the Village of River Hills and President of the Milwaukee Country Club. He is a member of the Illinois Bankers Association, Wisconsin Bankers Association, Indiana Bankers Association, Bank Holding Company Association, the Society of Financial Service Professionals and the MDRT Association's Top of the Table.

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Pat is a Co-Owner and Managing Director of Executive Benefits Network and a 20-year veteran of the financial services industry. Prior to entering the financial services industry, Pat worked as a senior accountant in audit for KPMG in the bank service area and as an attorney for Michael Best & Friedrich LLP where he concentrated on general corporate and securities law. Pat's career focus is in the BOLI/COLI marketplace, as well designing creative strategies for executive compensation planning, business succession planning and estate planning. Pat is a shareholder and Director of a bank in Iowa and is an active member in the State Bar of Wisconsin. He is a frequent speaker in industry meetings and seminars. He is a member of the Community Bankers of Iowa, Iowa Bankers Association and Wisconsin Bankers Association.

## ABOUT EXECUTIVE BENEFITS NETWORK (EBN):

As the leading industry advisor, EBN specializes in the customized design, administration, and informal financing of Nonqualified Executive Compensation and Benefit Plans (Deferred Compensation Plans), as well as the procurement of Bank Owned Life Insurance (BOLI) programs to attract, retain, and reward key executive talent. We emphasize the importance of education and build long-lasting relationships with clients in all 50 states, and we have access to the highest rated insurance companies in the nation. Lastly, we believe that no two companies are alike in their needs; therefore, customization of executive benefit and compensation plans is paramount to a successful program.

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