Advanced Designs
Pocket Guide

Succession Planning for the Family Business Using Life Insurance

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PACIFIC LIFE

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Introduction

Family businesses make up a large segment of all business enterprises in the United States. Many business owners want their businesses to stay in the hands of family members after their retirement or death. Fortunately, there are many strategies that can be utilized to accomplish that goal. This pocket guide focuses on some of the different strategies and tools, such as life insurance, that can be used to achieve the family business owner's objectives.

What are some factors to consider for a family business succession plan?

First, the business owner needs to determine who will own and operate the business after his or her retirement or death. Taxes also need to be taken into account because the transfer of a business will likely involve gift, estate[1] and/or income taxes. Other technical considerations include the business owner's retirement plans, his or her projected financial needs during retirement, and the financial needs of the surviving spouse after the business owner's death if both spouses are not active in the business. Moreover, if some heirs are not active in the business, wealth equalization will also be an important concern.

Second, the business owner should take into consideration some family factors. For example, if the business owner has more than one successor, he or she must determine whether joint management of the business by the successors is a realistic option. An equal division of the business may seem equitable but it may not necessarily be fair if there has been or will be an unequal contribution to the running of the business. This may be the case where, for example, one family member contributes more energy and resources than other family members. While family conflicts

[1] According to the American Taxpayer Relief Act of 2012, the federal estate, gift and generation skipping transfer (GST) tax exemption amounts are all $5,000,000 (indexed for inflation effective for tax years after 2011); the maximum estate, gift and GST tax rates are 40%. As of January 1, 2013, the annual gift tax exclusion is $14,000 per donee (indexed for inflation).

can be avoided while the business owner is alive and available to mediate, those family conflicts may ruin a succession plan when the business owner dies. The business owner, therefore, should consider these issues in advance.

Other family factors may include distrust of in-laws, realistic assessment of the expertise of the successor(s) to continue the business, and “reluctant successors” (family members who feel trapped in the family business to please their parents). Gathering all the facts and identifying family issues are the first steps in choosing the appropriate succession plan because a plan that focuses solely on technical factors can often fail to provide a successful transition of the business.

When should the transfer of the business take place?

The answer to this question depends largely on the business owner’s objectives. The transfer of the business can occur during life or after death. Often, the business owner will begin transferring the business during life and transfer the balance at death. Beginning the transfer of the family business during the business owner’s life can have many advantages. First, lifetime transfers can serve as an estate freezing technique and help transfer some of the appreciation of the business to the successor(s). Second, gradually gifting business interests to the successor(s) can help the business owner alleviate personal family concerns. For example, if the business owner is not confident in the expertise of the successor(s), a gradual transfer of the business can allow the business owner to provide guidance on the management and the operation of the business. Also, the business owner can better observe the relationship between various family members active in the business.

How can a lifetime transfer of the business be structured?

The lifetime transfer of a business will involve a gift, a sale or a combination of the two. The following are some tools that can be used to transfer the business during the business owner’s life.

Outright Gift. The simplest way of transferring the business during life is to gift the business directly to the successor. Gradually gifting portions of the business can give the business owner the ability to maintain control while giving the successor(s) an increasingly meaningful role in running the business. There are, however, several disadvantages. First, the business owner would lose the income from the gifted business interest. The business owner should, therefore, consider whether he or she will have sufficient funds for retirement and whether the surviving spouse will have sufficient funds for living expenses after the death of the business owner if the surviving spouse is not active in the business. Second, the gifts would likely be subject to gift taxes. While the use of the annual exclusion and lifetime exemption amounts can help shield some of those gifts from the gift taxes, any gifts exceeding these amounts will be subject to gift tax.[2]

Discounted Entities. Since an outright gift may trigger gift taxes, a business owner may consider the use of a discounted entity. For example, if the business is an S-Corporation (S-Corp), the business owner could recapitalize the corporation into voting and non-voting shares and then gift the non-voting shares to the successor(s).[3] The gift tax value of the non-voting shares would be discounted for lack of control and marketability. The same would also be true for gifts of family limited partnership (FLP) interests or restricted limited liability company (LLC) shares. The use of discounted entities, however, can be a costly endeavor and can be subject to attacks by the Internal Revenue Service (IRS). Over the years, the IRS has been successful in bringing the partnership assets back into the estate pursuant to IRC Sec. 2036 where the taxpayer retained an express or implied benefit from the partnership.[4] A business owner, therefore, should consult his or her

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[2] See Note 1.

[3] Gifts of S-Corp stock should only be made to recipients who are permitted S-Corp shareholders. Otherwise, the gift will terminate the S-Corp's S election pursuant to IRC Sec. 1362(d)(2).

[4] Estate of Reichardt v. Comm'r., 114 T.C. 144 (2000); Harper, T.C. Memo. 2002-121; Thompson, 382 F.3d 367; Estate of Strangi v. Comm'r., 115 T.C. 478 (2000) aff'd in part, rev'd in part, and remanded (for consideration of IRC Section 2036 issue), (Strangi

legal counsel to determine the appropriateness of such a technique in a particular situation.

For more information on family limited partnerships (FLPs), please see Pacific Life's pocket guide titled *Advanced Estate Planning Techniques and Life Insurance for the Ultra Wealthy*.

Grantor Retained Annuity Trust (GRAT). The business owner may consider gifting the business to a GRAT if the business is highly appreciating and income-producing. A GRAT is an irrevocable trust that provides the business owner with an annuity stream for a term of years. If he or she survives the predetermined GRAT term, the remainder passes to the GRAT beneficiaries without the imposition of additional gift taxes. The benefit of using a GRAT is that the gift tax value of gifting the business is reduced by the grantor's retained annuity interest. It is possible to set the annuity income percentage high enough to "zero out" the gift tax for that transfer. Another benefit of using a GRAT is that the business owner retains an income stream from the property transferred to the GRAT that can be used to supplement retirement income.

GRATs, however, also have some disadvantages. First, if the business fails to produce income as expected, there may be nothing left in the trust at the end of the GRAT term. Second, if the grantor dies during the GRAT term, the value of the retained annuity

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I), Gulig v. Comm'r., (Estate of Strangi), 293 F.3d 279 (5th Cir. 2002), on remand, Estate of Strangi v. Comm'r., T.C. Memo. 2003-145,aff'd, (Strangi II), Estate of Strangi v. Comm'r., No. 03-60992 (5th Cir. 2005) (Strangi III); Estate of Abraham v. Comm'r., T.C. Memo. 2004-39, aff'd, 408 F3d 26 (1st Cir. 2005); Estate of Hillgren v. Comm'r., T.C. Memo. 2004-46; and Estate of Virginia A. Bigelow, T.C. Memo. 2005-65; Estate of Schauerhamer v. Comm'r., T.C. Memo. 1997-242; Estate of Stone v. Comm'r. T.C. Memo. 2003-309; Estate of Bongard v. Comm'r., 124 T.C. 95 and Estate of Rosen v. Comm'r., T.C. Memo. 2006-115. In general, the courts have considered the following factors indicative of an implied agreement to retain benefits over transferred property: (1) contributing substantially all of the person's assets to the partnership without retaining assets outside of the partnership sufficient to support the person; (2) post-death payments of debts and expenses; (3) testamentary characteristics resembling an estate plan versus an arms-length joint enterprise; (4) commingling of personal and entity funds; (5) disregard for entity formalities and treating the partnership assets without regard to the partnership entity and operations; and (6) making disproportionate distributions not in accordance with the terms of the partnership agreement.

payments (not the asset itself) will be includible in the grantor's estate and will not accomplish the transfer of the business. Finally, a GRAT should not benefit grandchildren because the generation-skipping transfer tax exemption cannot be allocated to the initial transfer of assets.[5]

For more information on GRATs, please see Pacific Life's pocket guide titled *Advanced Estate Planning Techniques and Life Insurance for the Ultra Wealthy.*

Installment Sale. The transfer of the business can also take the form of a sale. There are various ways of structuring the sale. For example, the business owner may sell the business directly to the successor(s) at fair market value[6] in exchange for an interest-bearing installment note.[7]

One advantage of an installment sale is that it can serve as an estate freeze without any gift tax cost because it is a sale rather than a gift. In addition, the note and interest payments would provide the business owner with funds that may be used for retirement. There would, however, be income tax consequences to the business owner. In addition, the unpaid balance of the note would be includible in the business owner's estate if he or she dies before the end of the note term, and liquidity may be a concern if the estate does not have sufficient liquid assets to pay the estate

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[5] Unless the grantor has sufficient GST tax exemption to allocate to the GRAT assets distributed to the GRAT beneficiaries at the end of the GRAT term, the GST tax may be imposed at either termination of the trust or distribution to a skip person. IRC Sec. 2642(f) prohibits the allocation of generation-skipping transfer tax exemption during an estate tax inclusion period (ETIP) such as a GRAT term. Also, according to the American Taxpayer Relief Act of 2012, the federal estate, gift and generation skipping transfer (GST) tax exemption amounts are all $5,000,000 (indexed for inflation effective for tax years after 2011); the maximum estate, gift and GST tax rates are 40%.

[6] A sale for less than fair market value would be a bargain sale and would have gift tax ramifications for the business owner.

[7] Interest rate should be equal to the applicable federal rate (AFR) under IRC Sec. 1274(d).

taxes that may be due. Moreover, intra-family sale arrangements must be carefully structured to avoid bargain sale treatment.[8]

Self-Cancelling Installment Note (SCIN). If the business owner is unhealthy, but not terminally ill, he or she may also consider structuring the installment sale with a self-cancelling feature (SCIN) that will cancel the note upon the death of the business owner. The SCIN arrangement must bear a "risk premium" to compensate the seller for the possibility that the business owner's death may cancel the installment obligation.[9] If the business owner dies before the expiration of the note term, the SCIN will provide estate tax savings because the note payments will stop upon death. If the business owner lives to or beyond life expectancy, however, the successor(s) would have overpaid for the business and would have been better off with an installment note without the self-cancelling feature.

For more information on SCINs, please see Pacific Life's pocket guide titled *Advanced Estate Planning Techniques and Life Insurance for the Ultra Wealthy.*

Private Annuity. For unhealthy business owners who are not terminally ill, a private annuity arrangement may also be considered. The business owner would transfer the business to the successor in exchange for a private annuity, which is an unsecured promise to a stream of income for life. The business owner can use the retained income for retirement. One disadvantage of using a private annuity is the immediate recognition of any gain upon the transfer of the asset.[10] Similar to SCINs, private annuity

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[8] Intra-family sale arrangements are subject to stringent rules and must be carefully structured. See IRC Sec. 453(e) resale rule and Sec. 453B disposition of installment obligation rules.

[9] The risk premium can be reflected as an increase in the sales price or as an increase in the interest rate.

[10] The Department of Treasury and the IRS issued proposed regulations on October 16, 2006 that drastically change the tax treatment of private annuity arrangements. Under these regulations, the seller of the property would be in the same position as if he or she had sold the property for cash and then used the proceeds to purchase an annuity contract. These regulations eliminate the tax deferral of private annuity arrangements. Proposed Regs. 141901-05.

arrangements are generally used only by individuals who are unhealthy but not terminally ill.[11] Since the annuity payments are determined using IRS life expectancy tables as opposed to the business owner's actual life expectancy, there can be significant savings to the successor if the business owner dies before life expectancy. However, if the business owner lives to or past life expectancy, the successor may overpay for the business.

For more information on private annuities, please see Pacific Life's pocket guide titled *Advanced Estate Planning Techniques and Life Insurance for the Ultra Wealthy*.

Installment Sale to Intentionally Defective Irrevocable Trust (IDIT sale). Instead of selling the business directly to the successor, the business owner may consider selling the business to an IDIT created for the benefit of the successor(s). Using an IDIT can provide many benefits. First, there would be no income tax on the sale of the business to the IDIT or on the note interest because transactions between a grantor and his or her IDIT (also referred to as a grantor trust) are ignored for income tax purposes.[12] Another benefit is that the business owner, as grantor, pays any income tax generated inside the IDIT. The payment of income tax is similar to additional gifts to the successor generation without any gift tax consequences.[13] An IDIT sale would also serve as an estate freeze with little or no gift tax cost because the transfer would be a sale rather than a gift.[14]

An IDIT sale, however, is not appropriate for every business. It would only be successful if the business is highly appreciating and

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[11] If there is a greater than 50 percent probability that the transferor will die within one year, the Treasury Regulations mandate that the annuity factor reflects the actual life expectancy of the transferor. Therefore, a private annuity arrangement will rarely make sense for a terminally ill individual.

[12] Rev. Rul. 85-13, 1985-1 C. B. 184.

[13] Rev. Rul. 2004-64.

[14] Prior to the IDIT sale, the business owner will need to gift some funds to the IDIT to "seed" the trust. Otherwise, the IRS may argue that the IDIT's promise to pay the installment note is illusory and deem the sale to be a transfer with a retained interest under IRC Sec. 2036.

income-producing. Moreover, if the business owner dies before the end of the note term, the unpaid balance of the note will be includible in his or her estate for estate tax purposes. Estate tax liquidity, therefore, should be considered.

For more information on IDIT sales, please see Pacific Life's pocket guide titled *Advanced Estate Planning Techniques and Life Insurance for the Ultra Wealthy*.

How can the business be transferred to the successor after the death of the business owner?

Outright Bequest. The business owner can leave the business to the family member(s) active in the business via a will and/or a trust. The advantage of a bequest is that it is a simple transaction. The disadvantage is that the value of the business would be fully includible in the estate of the deceased and may trigger estate taxes unless additional planning is completed. If the business makes up a large portion of the estate, the estate may be faced with a lack of liquidity to pay the estate tax.[15] Furthermore, wealth equalization may be a concern if the business makes up a large part of the estate and only some family members are active in the business. Dividing the business equally among all family members would not be fair to those family members who contribute more to the business. On the other hand, if the business is passed only to those family members active in the business, other heirs may be disinherited. Life insurance may serve as a source of liquidity to pay any estate taxes and help equalize the estate among various family members.

Buy-Sell. If the business owner is married to a spouse who is not active in the family business, a family buy-sell arrangement may make sense. With a family buy-sell, the successor of the business buys a life insurance policy on the life of the business owner. At the owner's death, the death benefit proceeds are paid income tax-

[15] The use of Sec. 6166 estate tax deferrals and Sec. 303 redemptions are discussed on pages 11-12 of this pocket guide.

free[16] to the successor, who may use the proceeds to purchase the business from the business owner's estate. By using a family buy-sell, the business passes to the family member active in the business while the surviving spouse uses the sales proceeds to maintain standards of living until his or her death. Additional life insurance on the life of the business owner (or the lives of the business owner and his or her spouse) may help equalize the estate by providing an inheritance to the non-business heirs.

What role does life insurance play in a family business succession plan?

Life insurance can play an important role in a business succession plan. Because life insurance death benefit proceeds are generally paid income tax-free[16], life insurance can be an effective tool for the following:

Estate Tax Liquidity. Life insurance on the business owner's life can serve to provide liquidity for estate taxes that may be due at the death of the business owner. To avoid the estate taxation of the death benefit, an irrevocable life insurance trust (ILIT) is generally used as owner and beneficiary of the policy.

Wealth Equalization. Life insurance can be used to equalize wealth among family members active in the family business and those family members not active in the business.[17]

[16] For federal income tax purposes, life insurance death benefits generally pay income tax-free to beneficiaries pursuant to IRC Sec. 101(a)(1). In certain situations, however, life insurance death benefits may be partially or wholly taxable. Situations include, but are not limited to: the transfer of a life insurance policy for valuable consideration unless the transfer qualifies for an exception under IRC Sec. 101(a)(2) (i.e., the "transfer-for-value rule"); arrangements that lack an insurable interest based on state law; and an employer-owned policy unless the policy qualifies for an exception under IRC Sec. 101(j).

[17] As with all uses of life insurance, the amount of life insurance coverage asked for in conjunction with this concept may be limited by Pacific Life's financial underwriting guidelines. Financial underwriting is an assessment of whether the proposed death benefit is a reasonable replacement for the financial loss caused by the death of the insured.

Funding for an Installment Payment Arrangement or SCIN. If the successor is buying the business from the business owner using an installment note or a SCIN, life insurance insuring the life of the successor can help ensure that the successor's family will be able to continue the installment payments if he or she predeceases the owner before the installment arrangement is completed.

Key Person Protection. A key person policy on the life of the business owner may provide the business with needed funds while the business is adjusting to management and ownership changes after the business owner's retirement or death.

Funding for a Buy-Sell Arrangement. Life insurance can be an efficient funding tool for a buy-sell arrangement. For example, with family buy-sell, the successor purchases a life insurance policy on the business owner's life. At the business owner's death, the death benefit proceeds are paid income tax-free[18] to the successor, who uses the proceeds to purchase the business from the estate.

What is a Sec. 6166 election?

IRC Sec. 6166 (Sec. 6166) allows an executor of an estate to make an election to pay the estate tax attributable to a closely held business interest (e.g., family business or farm) in up to ten equal annual installments starting no later than five years after the regular due date.[19] The requirements for a Sec. 6166 election are that (1) a "closely held business interest" is included in the gross estate of a decedent who was a U.S. citizen or resident at the time of death, and (2) the value of the business interest exceeds 35% of

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[19] IRC Sec. 6166(a)(1).

the decedent’s adjusted gross estate.[20] During the deferral period, the interest on the unpaid tax balance is due annually. After the deferral period, the tax plus interest installments are due annually.

There are several possible disadvantages of relying on a Sec. 6166 election. First, the deferral payment is available only for the closely held business interest, not for other assets in the estate. Second, the IRS can place a lien on the business and/or may require that the estate furnish a surety bond to secure the payment of estate tax under a Sec. 6166 election.[21] Third, relying on a Sec. 6166 deferral can be difficult because the estate may cease to qualify if non-business assets in the estate appreciate faster than the business assets or if the value of the business declines. Finally, the full amount of deferral will become due if (1) a payment is late or missed, (2) 50% or more of the assets from the business are withdrawn, or (3) 50% or more of the value of the business interest is sold, exchanged, distributed or otherwise disposed of.

What is a Sec. 303 redemption?

IRC Sec. 303 (Sec. 303) gives an estate a one-time opportunity to remove cash or other property from the family business at a reduced tax cost through a partial redemption of stock that will not be treated as a fully taxable dividend from the corporation to the shareholder or the estate. The redemption must be to pay funeral costs, estate and administrative expenses and federal estate taxes. To qualify, the decedent’s adjusted gross estate must consist of 35% or more of stock in a closely held corporation. The

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[20] “Closely held business” means (A) an interest as a proprietor in a trade or business carried on as proprietorship; (B) an interest as a partner in a partnership carrying on a trade or business if (i) 20% or more of the total capital interest in such partnership is included in determining the gross estate of the decedent, or (ii) such partnership had 45 (15 for decedents dying before 2002 or after 2010) or fewer partners; or (C) stock in a corporation carrying on a trade or business if (i) 20% or more in value of the voting stock of such corporation is included in determining the gross estate of the decedent, or (ii) such corporation had 45 (15 for decedents dying before 2002 or after 2010) or fewer shareholders. IRC Sec. 6166(b)(1).

[21] In Roski v. Commr., 128 T.C. No. 10 (April 12, 2007), the Tax Court held that the IRS has no authority to require a bond or a special lien *in every case* in which an estate seeks the installment tax payment relief permitted by IRC Sec. 6166.

redemption amount cannot be more than the total of the estate and GST tax,[22] inheritance, legacy, and succession taxes, plus the funeral and administrative expenses.[23] Life insurance owned by the corporation can be an effective way of providing the funds necessary for a Sec. 303 redemption.

What is a qualified family-owned business interest (QFOBI) deduction?

The qualified family-owned business interest (QFOBI) deduction was designed to provide federal relief for small, family-operated businesses by assisting with estate liquidity concerns. If the requirements of IRC Sec. 2057 are satisfied, the QFOBI deduction allows an estate to deduct from its taxation the lesser of (1) the value of the QFOBI property, or (2) $1,300,000 less the applicable exemption amount.[24] The QFOBI deduction, however, has been obsolete for decedents dying since January 1, 2004 and all successive years due to the gradual increase of the federal estate tax exemption and decreased estate tax rates through 2009, the estate tax "repeal" in 2010, and the two-year temporary patch for the federal estate tax system for 2011 and 2012 (pursuant to the Tax Relief Act of 2010[25]) and the extension of the $5,000,000 exemption amount (indexed for inflation for tax years after 2011; $5,250,000 in 2013) under the American Taxpayer Relief Act of 2012 (ATRA). If the QFOBI is reinstated in the future, family business owners may be able to take advantage of its tax-saving benefits.

What are the special use valuation rules and when do they apply?

The special valuation rules contained in Sec. 2032A allow qualifying real estate in a farm, trade or business to be valued at its “actual use” as opposed to its “highest and best use.” Sec. 2032A

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[22] See Note 1.
[23] IRC Secs. 303(a)(1)-(2).
[24] IRC Sec. 2057(a). To see requirements of Sec. 2057, please see IRC Sec. 2057(b).
[25] The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (“The Tax Relief Act of 2010”) was passed by congress on December 16, 2010.

is most often used to value agricultural real property (e.g. farms and ranches) because the valuation of such property is based on a formula that will usually produce a low taxable value. The special formula is not available for any other type of real property.

In order to qualify, at least 50 percent of the decedent's estate must consist of property used for "qualified use" (e.g. farming or ranching) by the decedent or a member of his family.[26] 25 percent of the estate must consist of real property used in the farming business. The decedent or a member of the family must have owned and materially participated in the farming business for five out of the eight years preceding the decedent's death, subject to certain exceptions.[27] The property must pass to a "qualified heir" and the qualified heir must continue to farm the property for ten years after the death of the decedent.[28] A proper election and a tax recapture agreement must also be filed.[29]

The maximum valuation decrease on account of the special valuation election is $1,070,000 (in 2013 indexed for inflation, rounded down to the next lowest multiple of $10,000).[30]

Are there any special considerations if the family business is an S-Corporation (S-Corp)?

The only permissible S-Corp shareholders are certain individuals who are U.S. citizens or residents, certain estates (for a limited period of time), certain types of trusts, and, in certain cases, another S-Corp. It is, therefore, important to consider who will own the S-Corp shares after the business succession. Transfers of S-Corp stock should only be made to recipients who are permitted S-Corp shareholders. If the business owner is contemplating using a trust as part of the succession strategy, the trust should be drafted

[26] "Qualified use" means the devotion of property to use as a farm for farming purposes. IRC Sec. 2032A(b)(2).
[27] IRC Sec. 2032A(b)(1).
[28] IRC Sec. 2032A(c)(1).
[29] IRC Sec. 2032A(d)(1)-(3).
[30] IRC Secs. 2032A(a)(2)-(3).

carefully to be an eligible S-Corp shareholder. IRC Sec. 1361(c)(2)(A) provides the requirements for trusts that qualify as shareholders of S-Corps.

These trusts include:

- "grantor trusts" under Subchapter J of the IRS Code;[31]
- a trust is that is a "grantor trust" before the death of the grantor for a two-year period after the grantor's death;
- a trust to which stock is transferred pursuant to a will, but only for a two-year period;
- an "electing small business trust" (ESBT);
- a trust created primarily to exercise the voting power of stock transferred to it; and
- a "qualified subchapter S trust" (QSST).

[31] Examples of trusts that might qualify under this category are revocable trusts, IDITs and GRATs.

Business Succession Strategies

Does this describe you?	Strategy	How Life Insurance Can Help[32]
Business owner who has remaining annual exclusions and lifetime exemption amounts and who is willing to lose income and control of gifted interest.	**Outright gift:** Business owner gifts business interest to family members active in the business.	• Estate tax liquidity • Wealth equalization • Key person
Business owner who wants to minimize gift tax cost of transferring assets and who understands risks associated with discounted entities.	**Discounted entities:** Business owner gifts non-voting interest of S-Corp, limited partnership interest of an FLP, or restricted LLC shares at a discount.	• Estate tax liquidity • Wealth equalization • Key person
Business owner with a highly appreciating and income-producing business who wants to reduce the gift tax cost of gifting the business.	**GRAT:** Business owner gifts business to a GRAT. GRAT pays an annual income stream to the business owner for a term of years. If grantor outlives GRAT term, remainder will pass to heirs without additional gift or estate tax.	• Estate tax liquidity • Wealth equalization • Key person
Business owner with a highly appreciating and income-producing business who wants to sell the business to family member(s) directly.	**Installment sale to family members:** Business owner sells business to successor pursuant to an interest-bearing installment note.	• Estate tax liquidity • Wealth equalization • Key person • Funding for installment sale (life insurance on life of buyer)
Business owner with less than normal life expectancy, but not terminally ill, who wants to transfer a highly appreciating and income-producing business at a reduced gift tax cost.	**SCIN:** Business owner sells business to successor in exchange for an installment note that will extinguish at the death of the business owner.	• Funding for installment sale (life insurance on life of buyer) in case buyer dies before completion of installment sale

[32] For more details on the use of life insurance in the family succession plan, please see page 9 of this pocket guide.

Business owner with less than normal life expectancy but not terminally ill who wants to transfer a highly appreciating and income-producing business at a reduced gift tax cost.	**Private annuity:** Business owner sells business to successor in exchange for a private annuity arrangement. Payments will end at the death of business owner.	• Life insurance on life of buyer to allow buyer's estate to continue private annuity payments in case buyer dies before business owner
Business owner with highly appreciating and income-producing business who wants to minimize gift tax cost of transferring business and does not want to recognize immediate gain for the sale.	**Installment sale to an IDIT:** Business owner sells business to an IDIT in exchange for an interest-bearing installment note.	• Estate tax liquidity – IDIT can use any income in excess of note payments to purchase life insurance in the IDIT. • Wealth equalization • Key person
Business owner who does not want to transfer entire business during life and who has planned for estate tax liquidity need.	**Outright bequest:** Business owner leaves remaining business interest to successor via terms of will or living trust.	• Estate tax liquidity • Wealth equalization • Key person
Business owner who wants to pass business to family member active in the business while providing financial security to spouse not active in the business.	**Family buy-sell:** Active family member enters into cross purchase buy-sell agreement with business owner to purchase business at death from estate or surviving spouse.	• Funding for buy-sell • Wealth equalization • Key person

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