Forbes

What If?

The Corporate Equivalent Of A Kevlar Vest

By Mark C. Minichiello, 07-21-10

Does your company run on the work of a few heroes? Consider key-person insurance.

Death wasn't on Doug Murphy's day planner. The 41-year-old co-owner of the popular Moby Dick bar in San Francisco's Castro District got the sniffles on vacation last year. Within days, he was dead of complications from the H1N1 virus. Robert Dixon Hart, co-owner of Montana's Red Lodge Snowboard camp, died last year in a skiing accident. Just a few months ago, three top executives of Tesla Motors, the California electric carmaker, were killed when their small plane hit 60-foot-high transmission lines in dense Bay Area fog.

If you have any form of life insurance, you've pondered your own untimely demise and the disaster it would wreck on your family. But what about protecting your business from the shock of losing one of its heroes?

You can't stop a speeding bullet, but you can get the corporate equivalent of a Kevlar vest. It's called key person insurance---a term-life policy, payable to the business, on the owner of a company or the employees who are considered uniquely valuable to the operations.

Depending on your age, health and possibly your hobbies (Frank Wells, president and CEO of Walt Disney Co., died in a heli-skiing accident), the premiums can be fairly modest. A healthy 40-year-old might pay $750 a year to a major insurance company for a $500,000 policy---and still ride her Harley on the weekends.

Full disclosure: I don't sell insurance. But my past company, Opportunity Research Group, LLC, had key person insurance on its top three managers. (Each cost roughly $400 a year for a $250,000 policy.) I have recommended it at Quincy Cass, my current firm.

There are plenty of reasons to look into key person insurance. For starters, the cash will be something of a tonic to your traumatized employees, vendors, customers, creditors and banks. Some lenders may require you to have key person insurance when evaluating your firm.

These policies also spare your grieving heirs the potentially petrifying prospect of having to take control of your company. The cash gives corporate successors the luxury of time and choice to recruit a new manager, hire a temporary executive or train someone already in the firm.

Even better, key person insurance provides the cash that your partners can use to buy out your heirs' interests---without depleting their bank accounts or wiping out the firm's future cash flow.

Choosing the size of your policy means having a decent idea of what your company is worth. There are scads of business valuation consultants. Once you determine an amount, remember to update it periodically as your company matures and have a buy/sell agreement in place long before disaster strikes. Trust me: Planning ahead will save a tremendous amount in legal bills and spare everyone a lot of extra emotional strain.

Key person insurance represents a gamble you never want to win. But it's a great way to impose your corporate will after you give up corporal control.

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