

Cross-Purchase vs. Entity-Purchase Buy/Sell Arrangement Considerations

For Partnerships, "C" Corporations and "S" Corporations

	Partnership		C-Corporation		S-Corporation	
	Cross Purchase	Entity Purchase	Cross Purchase	Stock Redemption	Cross Purchase	Stock Redemption
Purchaser	The Partners	The Partnership	The Shareholders	The Corporation	The Shareholders	The Corporation
Number of Purchasers	Each partner buys one policy on each of the other partners in order to buy a portion of the deceased partner's interest.	One policy is purchased on each partner. As the number of partners increases, the entity plan becomes more attractive	Each shareholder buys one policy on each co-shareholder in order to buy a portion of his or her stock.	The corporation buys one policy on each shareholder. As the number of shareholders increases, the stock redemption plan becomes more attractive.	Each shareholder buys one policy on each co-shareholder in order to buy a portion of his or her stock.	The corporation buys one policy on each shareholder. As the number of shareholders increases, the stock redemption plan becomes more attractive.
Relative Interests	A partner can increase or decrease his or her relative interest in the partnership by committing to buy a larger or smaller proportion of the deceased partner's interest.	Each partner will hold the same relative interest after the buyout.	A shareholder can increase or decrease his or her relative interest in the corporation by committing to buy a larger or smaller proportion of the deceased owner's stock.	Each shareholder will hold the same relative interest after the buyout.	A shareholder can increase or decrease his or her relative interest in the corporation by committing to buy a larger or smaller proportion of the deceased owner's stock. Surviving shareholder's percentage of ownership increases proportionately.	Each shareholder will hold the same relative interest after the buyout.

Funding the Policies						
	Partnership		C-Corporation		S-Corporation	
	Cross Purchase	Entity Purchase	Cross Purchase	Stock Redemption	Cross Purchase	Stock Redemption
Purchaser	The Partners	The Partnership	The Shareholders	The Corporation	The Shareholders	The Corporation
Funding the Policies	Individual partners pay the premium on the policies they own on the other partners. Younger partners pay larger premiums on the lives of older or unhealthy partners. An escrow arrangement can hold the policies, collect the premiums and pay the insurance company.	The partnership pays the premium. Each partner shares in the total premiums paid in proportion to his or her partnership interest. An entity plan can assure the partners that the premiums will be paid and that the policies stay in force.	The individual shareholders pay the premium on the policies they own on the other shareholders. A split dollar or executive bonus arrangement can assist the shareholder.	The corporation pays the premiums. If the shareholders are in a higher tax bracket, it can make good business sense for the corporation to pay the premiums.	The individual shareholders pay the premiums on the policies on the other shareholders.	The corporation pays the premiums. The corporate income used to pay the premiums is taxed pro rata to the shareholders.

Impact of Policy Values						
	Partnership		C-Corporation		S-Corporation	
	Cross Purchase	Entity Purchase	Cross Purchase	Stock Redemption	Cross Purchase	Stock Redemption
Purchaser	The Partners	The Partnership	The Shareholders	The Corporation	The Shareholders	The Corporation
Valuation	The insurance proceeds do not increase the value of the business.	The policy cash values and death proceeds increase the value of the partnership unless the buy-sell agreement allocates the death proceeds to the surviving partners.	The insurance does not increase the value of the stock.	Cash value affects the value of the stock. At redemption, the value of the stock increases if the corporation retires stock.	The insurance does not increase the value of the stock.	The cash value affects the value of the stock.
Relative Interests	The purchasing partner receives an increase in basis equal to the purchase price. While the entity plan can also increase a partner's basis, the cross-purchase plan results in a higher basis.	When the insurance is paid to the partnership, the death proceeds in excess of the cash value increase each partner's basis proportionately, including the deceased partner's interest.	The surviving shareholders receive an increase in basis equal to the purchase price of the stock.	The surviving shareholders do not receive an increase in basis when the corporation buys the deceased's stock.	The surviving shareholders receive an increase in basis equal to the purchase price of the stock.	The surviving shareholders can receive an increase in basis by electing a short tax year (cash basis taxpayer only).

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Creditors, Attribution Rules & Taxes						
	Partnership		C-Corporation		S-Corporation	
	Cross Purchase	Entity Purchase	Cross Purchase	Stock Redemption	Cross Purchase	Stock Redemption
Purchaser	The Partners	The Partnership	The Shareholders	The Corporation	The Shareholders	The Corporation
Creditors	The policy values are not subject to the firm's creditors unless the firm is insolvent.	The policy values are subject to the firm's creditors.	The corporate creditors cannot reach the policy values. State law dictates whether personal creditors can attach policy values.	The policy values are subject to corporate creditors.	The corporate creditors cannot reach the policy values. State law dictates whether personal creditors can attach policy values.	The policy values are subject to corporate creditors.
Family Attribution	N/A	N/A	No	Redemption is subject to the family attribution rules.	No	S-Corporations with E&P are subject to the family attribution rules.
Section 302 Regs	A partner can increase or decrease his or her relative interest in the partnership by committing to buy a larger or smaller proportion of the deceased partner's interest.	Each partner will hold the same relative interest after the buyout.	A shareholder can increase or decrease his or her relative interest in the corporation by committing to buy a larger or smaller proportion of the deceased owner's stock.	Each shareholder will hold the same relative interest after the buyout.	A shareholder can increase or decrease his or her relative interest in the corporation by committing to buy a larger or smaller proportion of the deceased owner's stock. Surviving shareholder's percentage of ownership increases proportionately.	Each shareholder will hold the same relative interest after the buyout.
Taxation of Deceased Shareholder Heirs	N/A	N/A	Basis is stepped up at the death of shareholder and no gain is recognized.	Basis is stepped up at death and no gain is recognized, provided redemption meets either IRC §302 or §303 requirements.	Basis is stepped up at the death of shareholder and no gain is recognized.	Basis is stepped up at death and no gain is recognized if redemption qualifies for IRC §302 or §303 treatment.
Alternative Minimum Tax	N/A	N/A	No	Yes	No	No

A Limited Liability Company (LLC), Limited Partnership (LP) and Family Limited Partnership (FLP) buy-sell agreement should be similar to a partnership arrangement.

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