



# THE SILENT THREAT OF DISABILITY TO ULTRA SUCCESSFUL CLIENTS

Whether your client is a corporation, a business owner, a private equity firm or an employee stock ownership plan, their success goes well beyond figures on a spreadsheet. Although the bottom line is undeniably critical, overlooked contractual obligations can bring even the most stable company to its knees.



By Sean McNiff

These silent threats often lie dormant until a triggering event, such as a disability, sends ripple effects through the organization. Without the right planning and protection in place, the financial consequences can be devastating. Sophisticated clients rely on equally sophisticated advisors to navigate these risks and ensure continuity. Here are five scenarios where proactive insurance planning is essential.

## Disability of a Key Person

Contractual key person insurance obligations are most often found in the mergers and acquisitions arena. They're established when one company buys another company and the acquisition agreement or

purchase agreement requires key person insurance. In this scenario, the average advisor will traditionally recommend life insurance on the named key executive, yet statistics have shown us that a person is up to four times more likely to become disabled than die during their working years.

Take, for example, a private equity firm in Chicago that faced a major disruption when the CEO of one of its portfolio companies suffered a stroke. The firm had purchased key person life insurance, but the executive survived, highlighting a critical gap in its risk management strategy. Without key person disability coverage in place, the firm had to absorb the financial strain of keeping the business afloat and finding a replacement leader.

After reassessing its approach, the firm chose to expand its key person insurance requirements to include disability coverage. For a newly acquired portfolio company, the firm expanded its key person insurance requirements to include both life and disability coverage. To create comprehensive protection for the individual driving the success of the investment, the firm secured \$6 million in key person disability coverage to mirror its key person life requirement.

This shift helped the firm better protect its investments going forward, offering a more balanced approach to managing the risks associated with losing a key executive, whether temporarily or permanently.

## **Disability of a Business Owner in a Buy-Sell Agreement**

Buy-sell agreements are a staple in business succession planning, ensuring that ownership transitions smoothly if a partner dies. But what if the partner becomes disabled?

Real-world scenario: Three partners in a successful New Jersey paving and excavating company had a buy-sell agreement requiring repurchase of a disabled partner's \$15 million equity stake after 12 months. However, there was no funding mechanism in place.

The partners quickly realized the need for two key protections: (1) financial security for the disabled partner and (2) a reliable, nondisruptive funding solution for the business. Customized "own-occupation" buy-sell disability insurance provided a lump-sum benefit, above and beyond traditional U.S. coverage. This ensured the agreement could be executed without jeopardizing the company's financial health.

In cases where equity values exceed traditional market limits, advisors must look to surplus lines carriers, such as Lloyd's of London, to design buy-sell disability solutions with the capacity to fully fund the buyout obligation. These carriers can provide benefits exceeding \$100 million per person, making them indispensable for high-value partnerships.

## **Disability of a Borrower**

Many successful entrepreneurs make the strategic decision to take out loans to fuel business growth — whether to expand operations, invest in talent or acquire new assets. But with this leverage comes an often-overlooked critical risk: the personal obligation to repay that loan, even in the event of a disabling illness or injury.

Unlike operational risks that can be mitigated through planning or delegation, a disability can abruptly halt an entrepreneur's ability to generate income while the loan payments continue. This creates a significant financial vulnerability that deserves careful consideration when evaluating contractual obligations.

Case in point: A successful dermatologist expanded her practice by adding several new clinics and specialized testing labs. To fund the growth, she secured a \$2.3 million loan. As part of the lending requirements, the financial institution requested a disability insurance policy to protect the balance of the loan in case she

became disabled and unable to meet repayment obligations.

To satisfy the lender and protect her growing business, she secured a loan indemnification disability policy that pays \$38,334 per month over five years, matching the loan's amortization schedule. Through a customized policy with a reducing benefit structure, the coverage mirrors the declining loan balance, delivering adequate protection while helping the doctor conserve premium dollars.

**“WHILE DEATH IS AN OBVIOUS PLANNING POINT, DISABILITY IS OFTEN A SILENT SABOTEUR.”**

## **Disability During Severance**

Severance agreements often include continued income promises for a former executive. But what happens if that executive becomes disabled?

Take, for example, a regional bank that recently terminated four senior executives following a merger with a larger partner. As part of their severance packages, each executive was promised post-termination benefits for varied durations. All four had previously been covered under the bank's group long-term disability plan, which provided a monthly benefit of \$10,000 per month, the plan's maximum.

At first glance, the bank's exposure appeared minimal. However, a significant liability emerged when it became clear that the group LTD coverage terminated along with the executives' employment. One executive, age 45, had been guaranteed extended disability benefits for two years, placing the bank at risk for up to \$2.64 million in unfunded liability (\$10,000 per month through age 67) in the event of a permanent disability. To address this, a severance disability insurance policy was delivered that transferred the risk away from the bank, safeguarding

both the executive's benefits and the organization's financial stability.

### Disability of an ESOP Shareholder

Employee stock ownership plans are powerful tools for business succession and employee engagement. But they come with an often-overlooked contractual burden: the obligation to repurchase shares upon a participant's death, retirement or disability.

Many companies protect their ESOP loan structure with key person life insurance on the selling shareholder, but few account for the equally devastating risk of that same key person becoming disabled. In a leveraged ESOP transaction, if a key shareholder who personally guaranteed a loan or was integral to business operations becomes disabled, the company may be left with both a leadership vacuum and an inability to service its debt. Life insurance offers no protection if the individual is alive but unable to work. This is where key person disability insurance becomes critical — providing liquidity during a period of instability and preserving the ESOP structure from early collapse or forced restructuring.

But the risk doesn't end once the ESOP is established. As the plan matures, so do the account values of its shareholders. In many cases, long-tenured employees

and senior executives accumulate balances well over \$1 million. A disabling event for one of these key participants not only removes their contribution to the business but also triggers a potentially large, unplanned repurchase obligation under the ESOP — at precisely the time the company may be least equipped to handle it.

To solve for this, companies are increasingly turning to guaranteed-issue ESOP disability insurance, which provides lump-sum disability benefits specifically designed to fund stock repurchase obligations. These programs can be implemented at the corporate level with simplified census-based enrollment, no medical underwriting and significant premium discounts based on group volume. This ensures that disability doesn't derail the long-term financial health of the ESOP itself.

We live in an era when contractual obligations can either safeguard or sabotage a business, and the difference lies in preparation. While death is an obvious planning point, disability is often a silent saboteur. Advisors who recognize this reality, and who partner with specialized carriers to solve for it, deliver immense value to their clients.

Your ultra successful clients aren't just looking for protection; they're also looking for foresight. They're looking for you. Because the next step they take might trigger a silent threat buried deep in a contract, and by then, it may be too late.

*Exceptional Risk Advisors LLC was founded in 2007 and is the country's foremost expert in insuring complex human capital risks. Exceptional Risk Advisors develops, distributes, and underwrites specialized insurance products for the sports, entertainment, and corporate world. For more information, please visit: <https://exceptionalriskadvisors.com>*

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