

Business Protection

doesn't have to be hard.....

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Learning objectives

To be able to explain the concept of business protection in the simplest terms possible.



To be aware of the issues faced by businesses on the death or critical illness of a key person, shareholder employee.



To be able to identify key people, calculate the sum assured, set the policies up correctly and explain the tax treatment of the premiums and benefits.



To understand the different methods of business succession planning, including setting up the scheme, the use of trusts and option agreements and the tax treatment of the premiums and benefits.



To explain the benefits of a relevant life policy, including who can have one, why they might want one and the tax treatment of the premiums and benefits.



To be able to demonstrate your recommendations in a way which is easy for the client to understand.



Introduction to the business market



Introduction to the business market

Keeping it simple



Protect the business

Key person protection

Business liability protection

Protect the business owners

Shareholder protection

LLP protection

Partnership protection

Protect the employees

Relevant life policy

Group death in service

Group critical illness

Group income protection

Introduction to the business market

Different business entities (UK exc Scotland)

Limited Companies

Limited Liability Partnerships

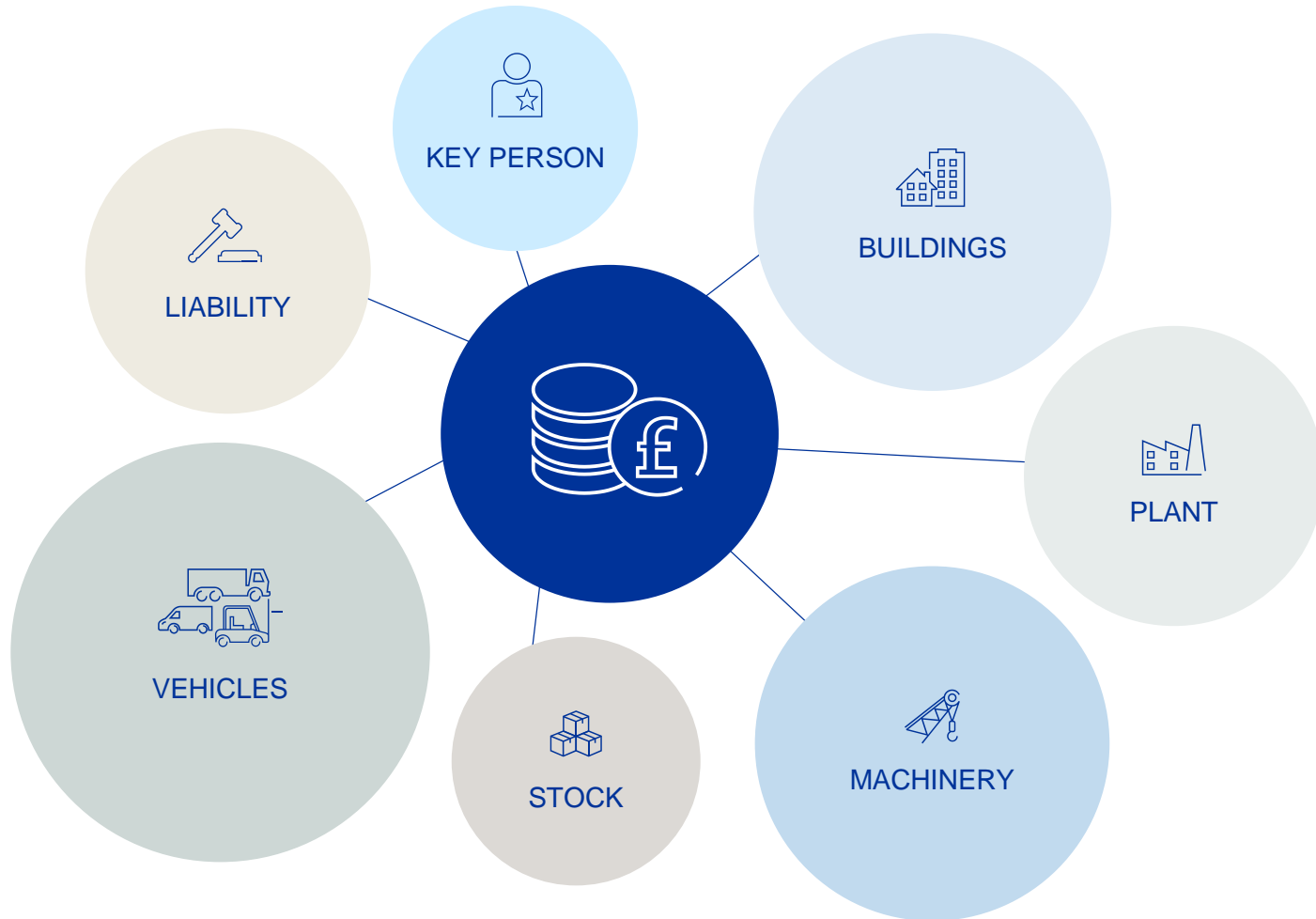
LEGAL
ENTITIES

Partnerships

Sole traders

Introduction to the business market

Putting the cost into perspective



Protect the business



Protect the business

Structure your advice

Design a process

01

Identify the company

02

Identify the key people

03

Calculate the sum assured

04

Select the type and term of the policy

05

Determine the tax treatment of premiums and benefits

Protect the business

Identify the company

“

I don't have any
business
clients...

”

Existing client bank

– mortgages, Pensions, investments, group risk, general insurance, commercial insurance

Professional connections

- accountants, solicitors, business consultants

New clients

- referrals, mailshots, campaigns, seminars

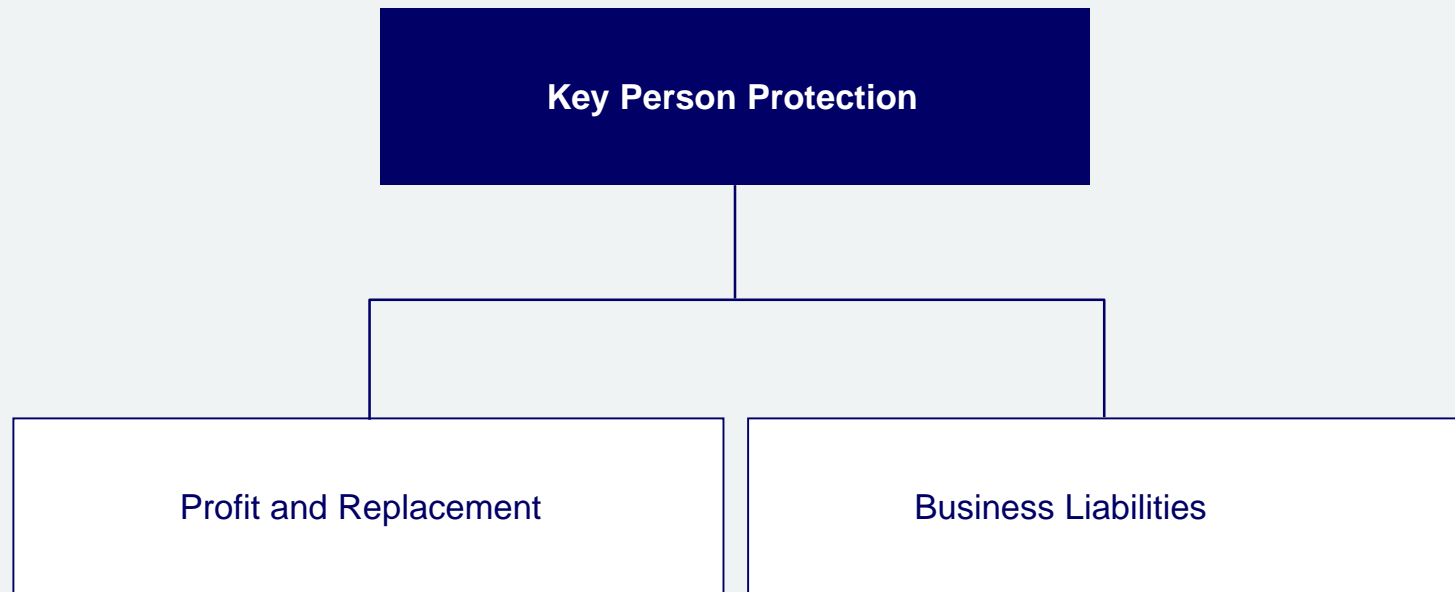
Protect the business

Identify the key people



Anyone whose loss, either **permanent** or **temporary**, would affect the company's ability to maintain turnover and generate

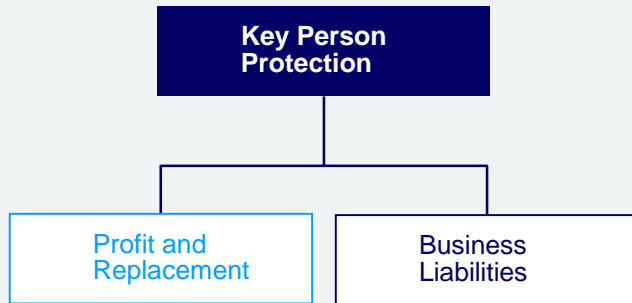
Protect the business
Calculate the sum assured



Protect the business

Calculate the sum assured

Loss of profit and replacement costs



Loss of profit

Gross profit attributable to the key person Years to recover

$$\frac{\text{Gross profit}}{\text{Number of key people}} \times \text{Years to recover}$$

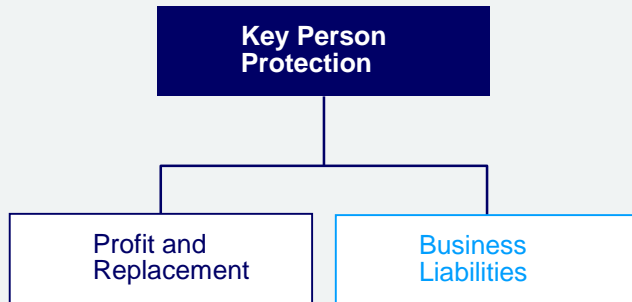
Replacement costs

Salary of replacement recruitment costs training costs

Protect the business

Calculate the sum assured

Business liabilities



Business liabilities

Directors' loan accounts

Business loans and mortgages

Overdrafts

Other liabilities as per the factfind

Apportion the liabilities

Cover all key people for all liabilities

Divide equally amongst key people

Divide based on shareholding

Divide based on importance to profit

Protect the business

Select the type and term of the policy

Life only

Life with earlier critical illness

Specific term e.g. 5 years

Term to selected age e.g. 65

Renewable term e.g. five-year renewable

Convertible term

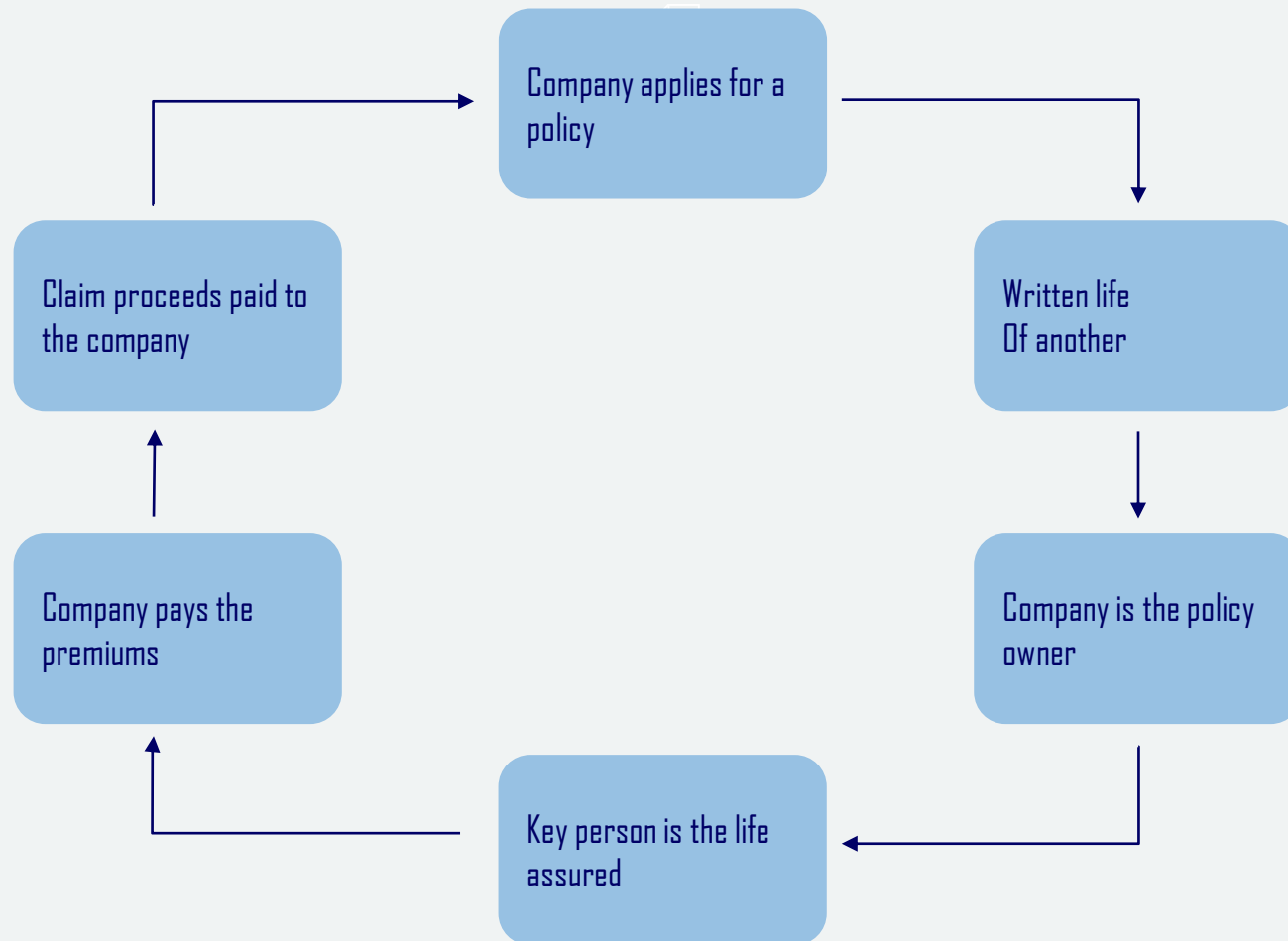
Whole of life



Protect the business

The solution

Company owned policy



Protect the business

Tax treatment of premiums

HMRC Business Income Manual Section 45525.

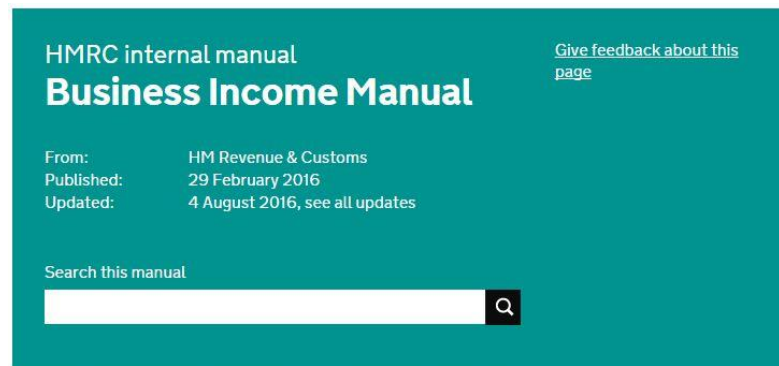
Loosely based around the Anderson Guidelines of 1944.

The sole relationship between the insuring party and key person must be that of employee and employer.

The life assured cannot be a significant shareholder.

The plan must be intended to compensate for revenue requirements.

The term of the plan should be appropriate to the usefulness of the life assured.



[Contents](#) > [BIM40000](#) > [BIM42450](#) > [BIM45500](#) > [BIM45525](#)

Specific deductions: insurance: employees and other key persons

An employer may take out in their own favour a policy insuring against loss of profits resulting from the death, critical illness, sickness, accident or injury of an employee, director or other 'key person'.

The premiums on such a policy will be allowable if all the following conditions are met:

- The sole purpose of taking out the insurance is the trade purpose of meeting a loss of trading income that may result from loss of the services of the key person, and not a capital loss. Guidance on possible non-trade purposes is at [BIM45530](#).
- In the case of life insurance policies, they are term insurance, providing cover only against the risk that one or more of the lives insured dies within the term of the

CHECK WITH HMRC – Draft letters available

www.gov.uk/government/collections/business-income-manual-bim

Protect the business

Tax treatment of policy proceeds

If premiums ***are*** allowable for Corporation Tax Relief, **whether taken or not**, the policy proceeds will be treated as a trading receipt

If premiums ***are not*** allowable for Corporation Tax Relief, normal taxation principles will apply:

- proceeds used for REVENUE purposes – trading receipt
 - proceeds used for CAPITAL purposes – capital receipt
-

Based on Zurich understanding of current HMRC practice

Protect the business owners



Protect the business owners

Care required

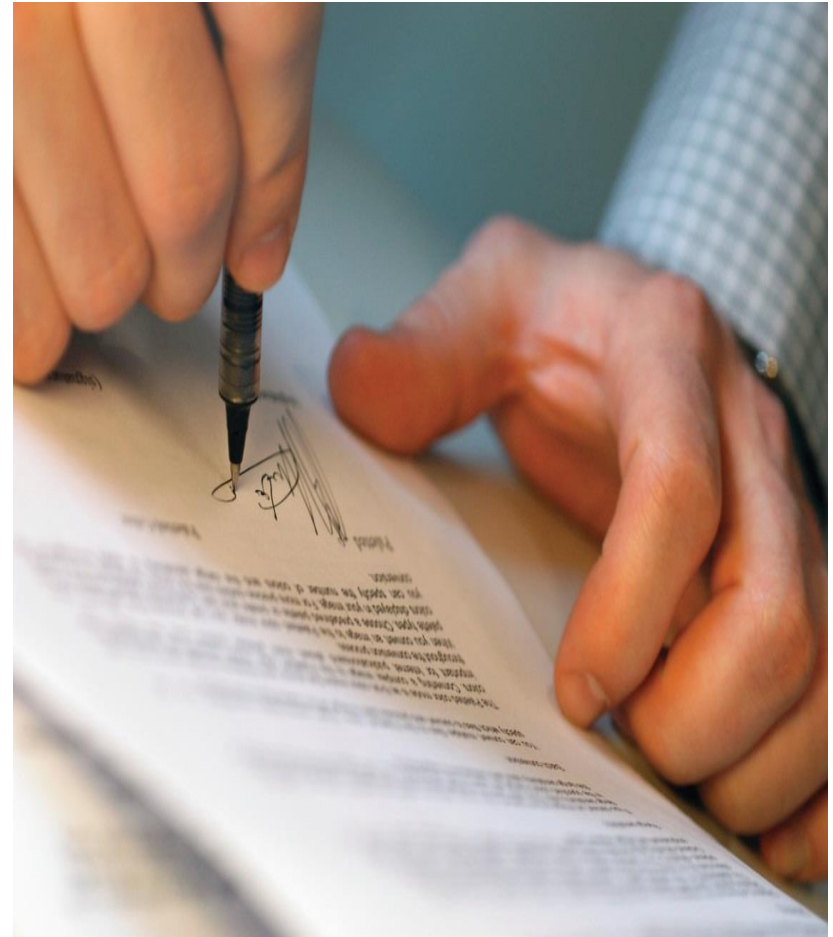
Check for existing agreements

Memorandum of Association

Articles of Association

Shareholder agreement

Partnership agreement



Protect the business owners

What are we trying to achieve?

Who and what are we trying to protect?



Protect the business owners

Protect the families

Protect the business

Protect the employees

Protect the business owners

Different methods to achieve the objectives

Company Share Purchase

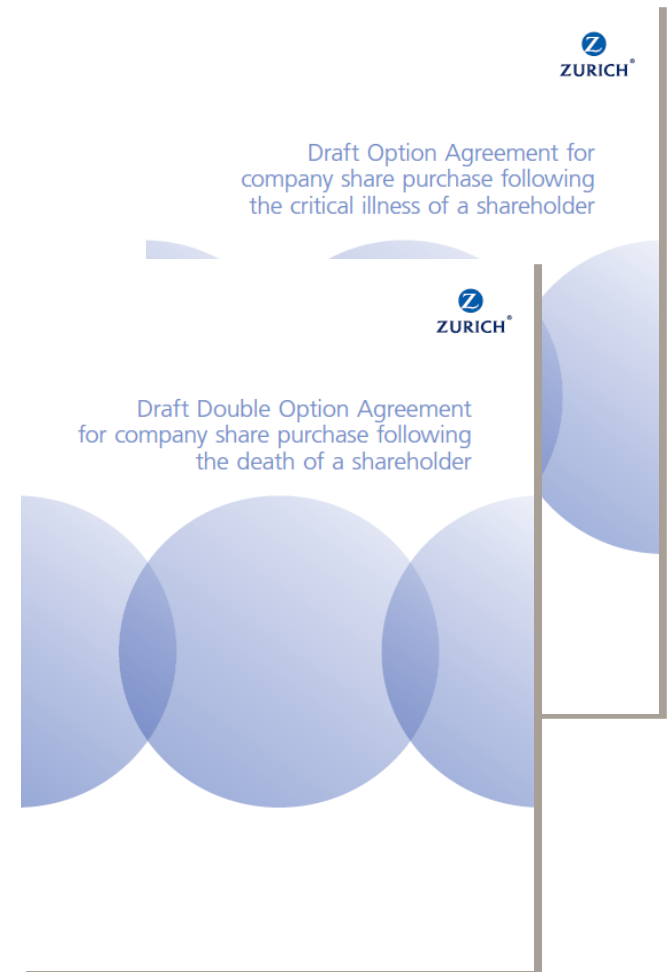
Shares purchased by surviving shareholders

Protect the business owners

Company share purchase The basics

Company enters into an agreement with each shareholder.

Company effects a life policy or life with earlier critical illness policy on the life of each shareholder.

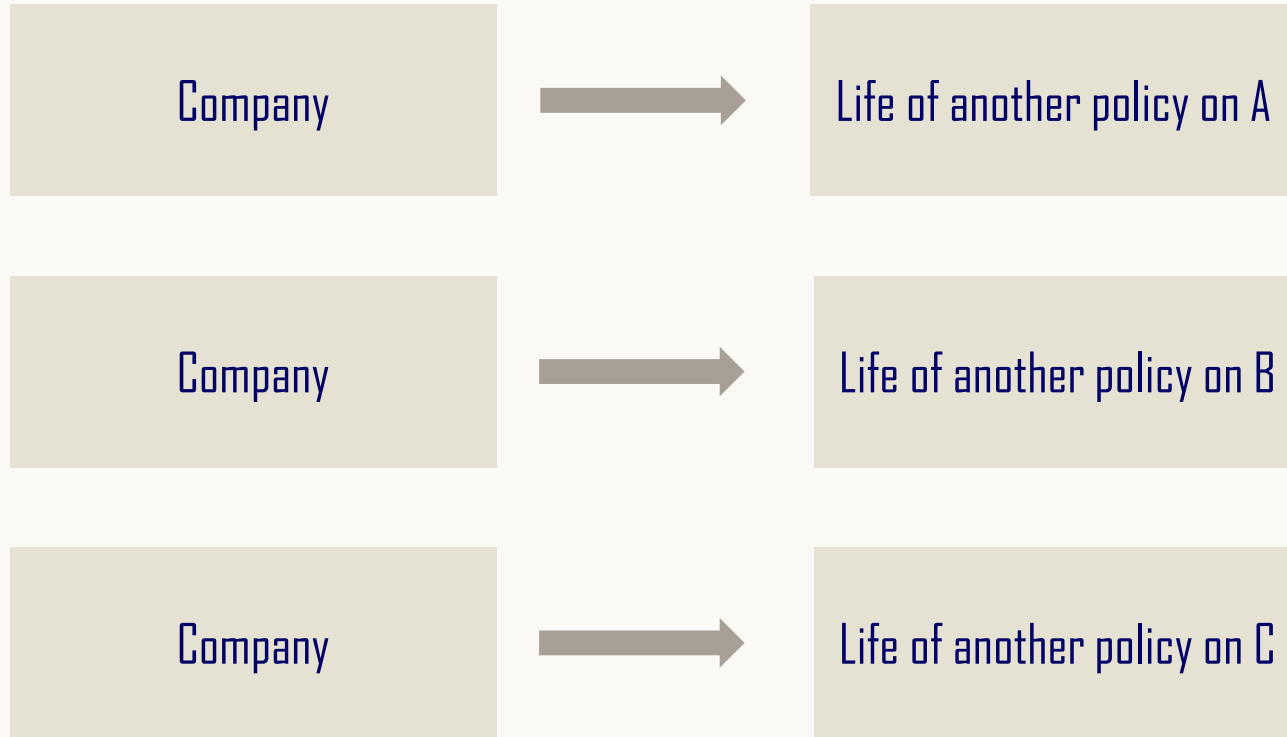


Protect the business owners

Company share purchase

Setting up the scheme

Policies written life of another



Option agreement for company share purchase on death
Option agreement for company share purchase on critical illness

Protect the business owners

Company share purchase The basics

Company enters into an agreement with each shareholder.

Company effects a life policy or life with earlier critical illness policy on the life of each shareholder.

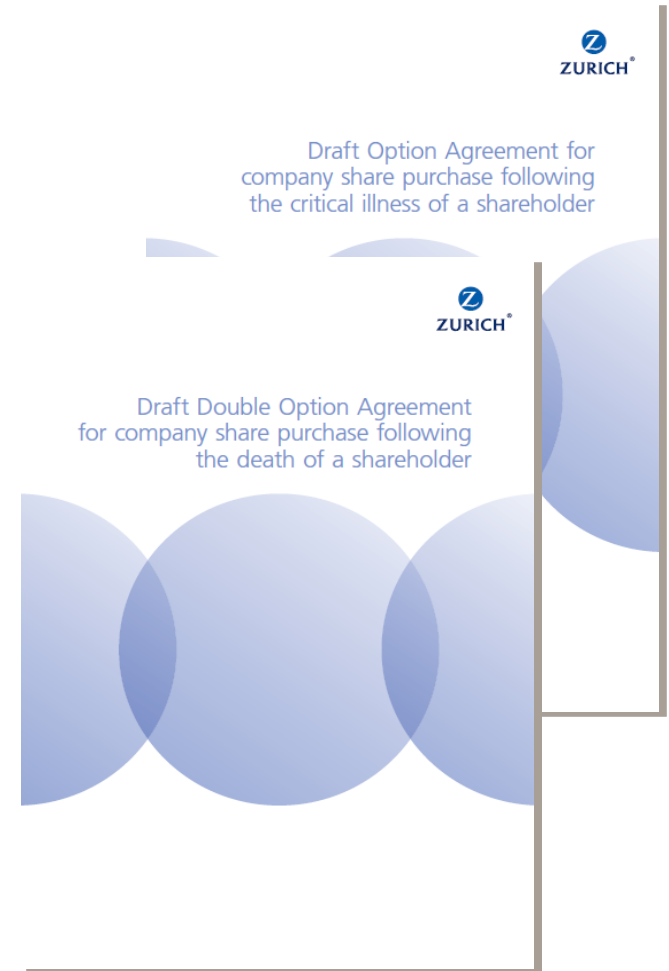
Company pays the premiums.

No tax relief on premiums, benefit tax free.

On death of shareholder, company has the option to buy the shares and personal representatives have the option to sell the shares.

On suffering a critical illness, only the critically ill shareholder has an option to sell their shares.

Company buys and cancels shares; value of remaining shareholdings increase proportionately.

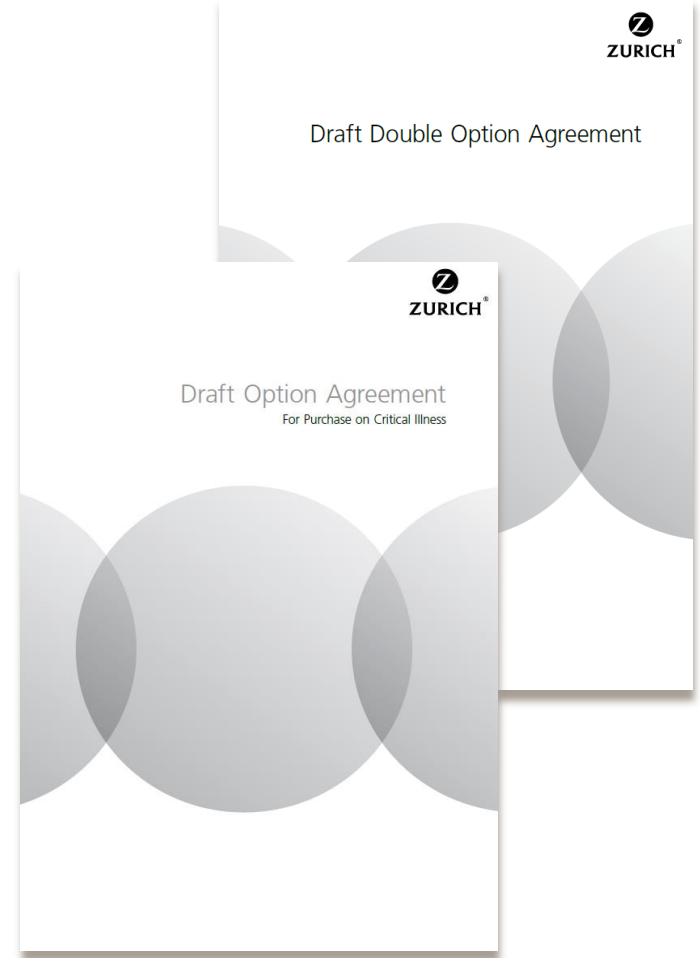


Protect the business owners

Shares purchased by the surviving shareholders
The basics

Shareholders enter into an agreement with each other.

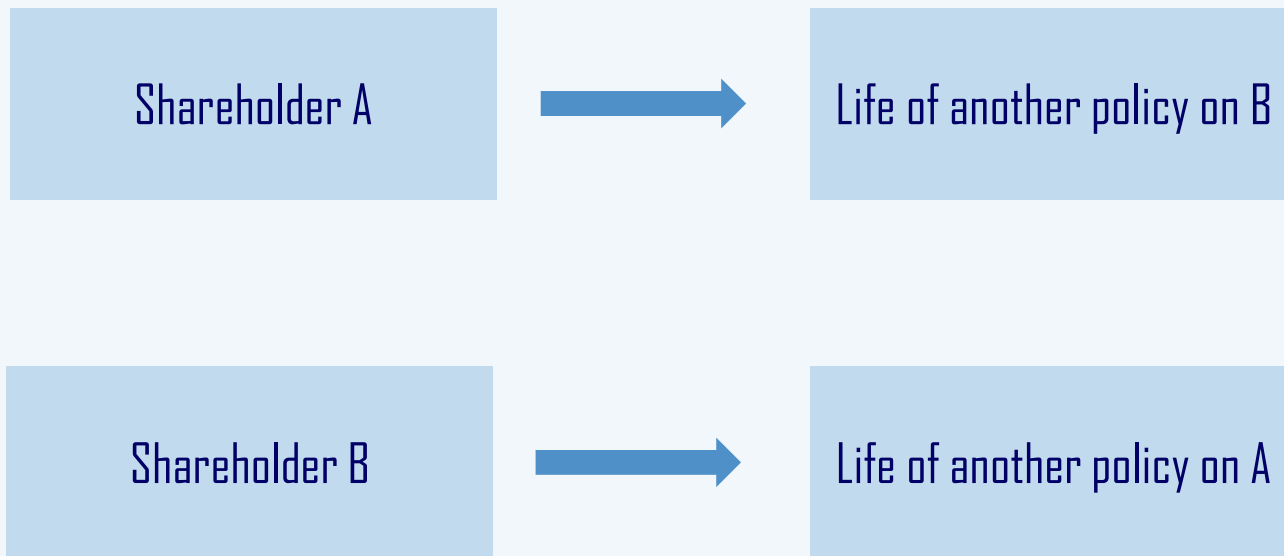
For 2 shareholders, each shareholder effects a life of another policy on the other shareholder.



Protect the business owners

Shares purchased by the surviving shareholders

Policies written life of another

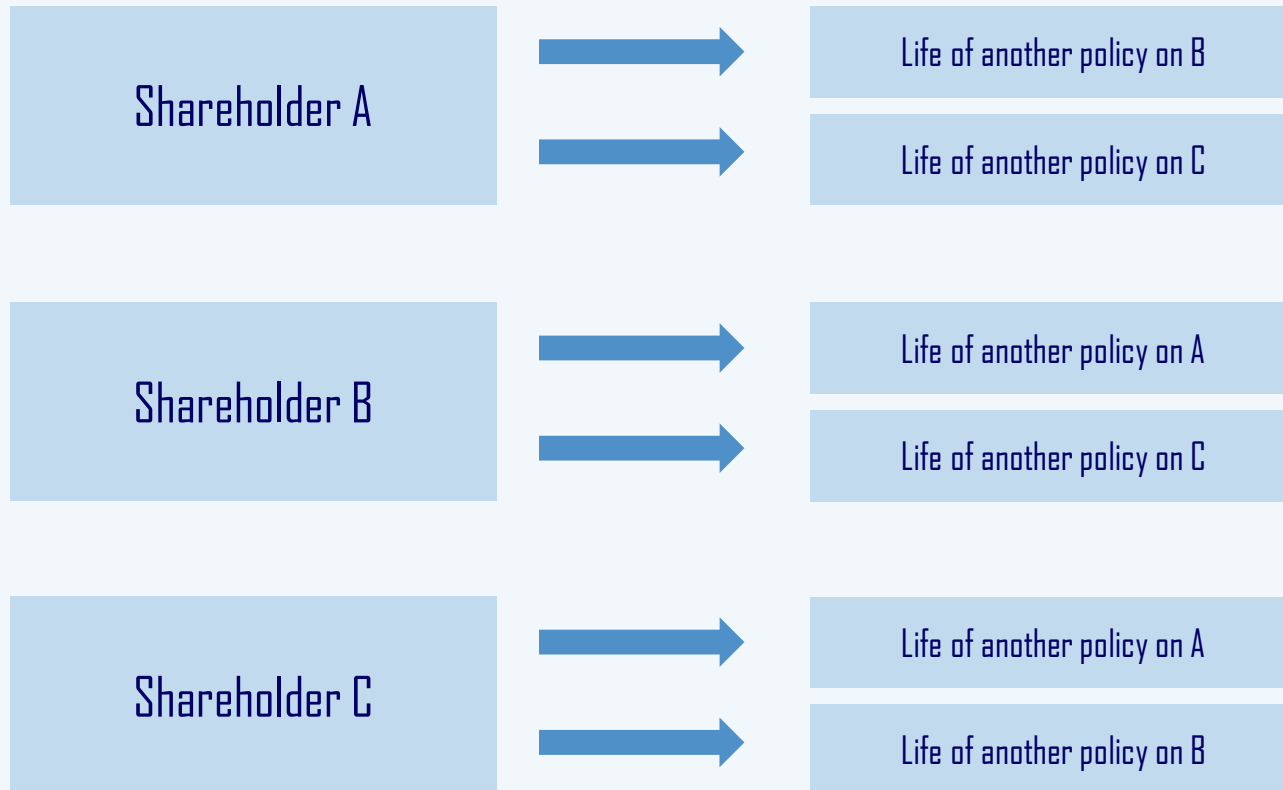


Double option agreement
Option agreement for purchase on critical illness

Protect the business owners

Shares purchased by the surviving shareholders

Policies written life of another



Double option agreement
Option agreement for purchase on critical illness

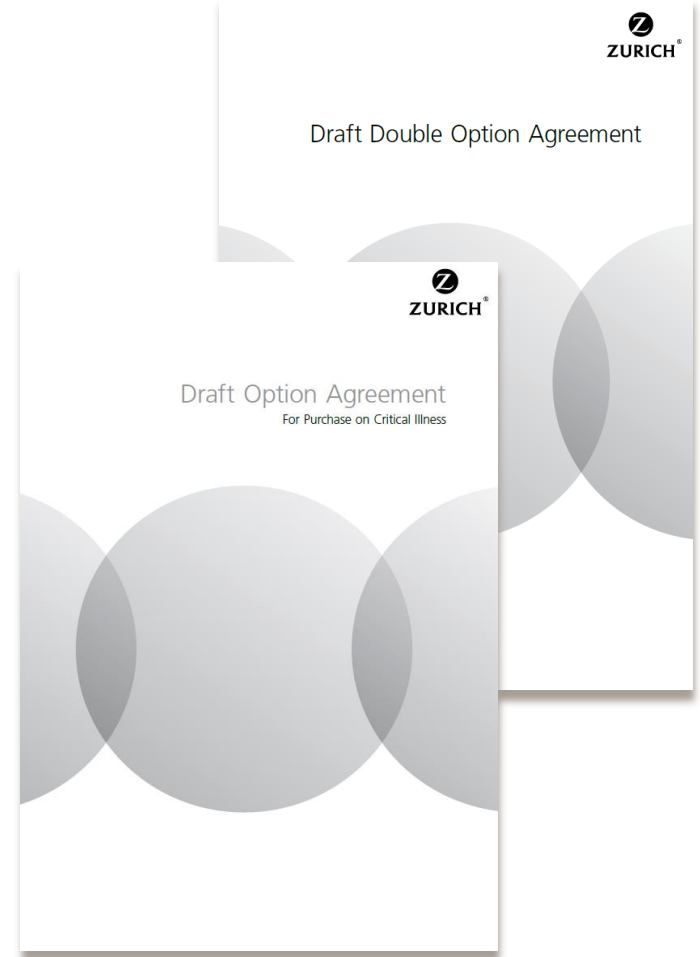
Protect the business owners

Shares purchased by the surviving shareholders
The basics

Shareholders enter into an agreement with each other.

For 2 shareholders, each shareholder effects a life of another policy on all other shareholders.

For 3 or more shareholders, each shareholder effects a policy on their own life, written into a flexible business trust.

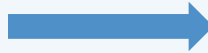


Protect the business owners

Shares purchased by the surviving shareholders

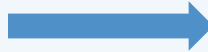
Policies written own life in trust

Shareholder A



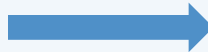
Life policy written own life
in trust for B and C

Shareholder B



Life policy written own life
in trust for A and C

Shareholder C



Life policy written own life
in trust for A and B

Double option agreement
Option agreement for purchase on critical illness

Protect the business owners

Shares purchased by the surviving shareholders
The basics

Shareholders enter into an agreement with each other.

For 2 shareholders, each shareholder effects a life of another policy on all other shareholders.

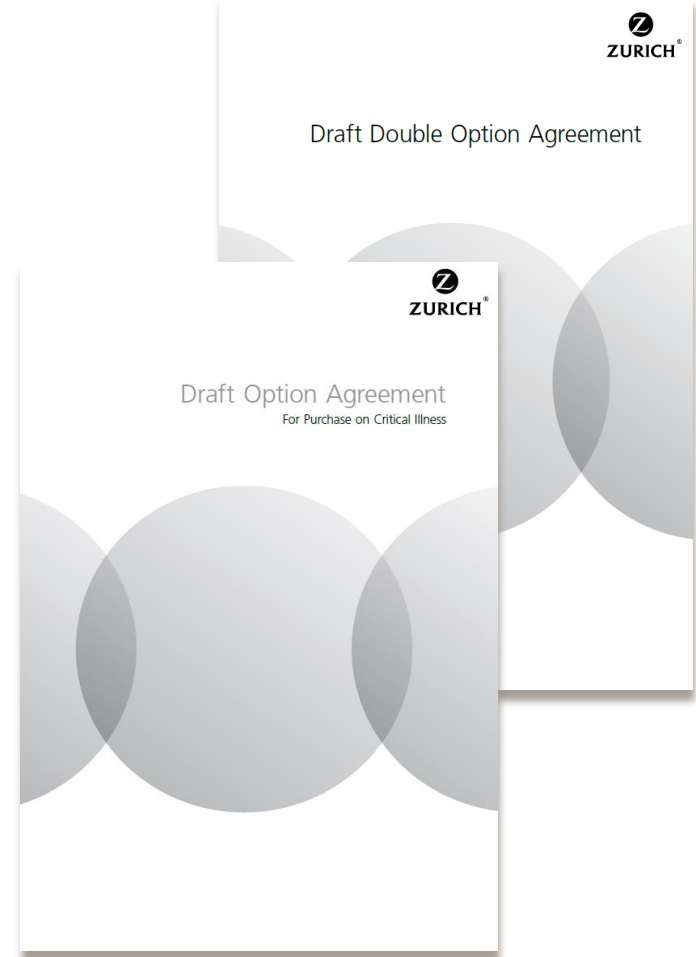
For 3 or more shareholders, each shareholder effects a policy on their own life, written into a flexible business trust.

Company pays the premiums (more on this later!)

On death of shareholder, personal representatives of the deceased have option to sell; surviving shareholders have option to buy.

On suffering a critical illness, the critically ill shareholder has an option to sell to the other shareholders.

Critically ill shareholder cannot be forced out of the business against their will.



Protect the business owners

Shares purchased by the surviving shareholders
The flexible business trust deed

For NEW policies only.

Only to be used for Shareholder / Partnership protection.

For death and critical illness benefits.

Ensures the plan proceeds on death or critical illness
are paid into trust for the benefit of the beneficiaries.

Beneficiaries are the surviving shareholders / partners
in the business **in the same ratio they own the
remaining shares.**

Trust caters for changes in shareholders / partners.

Ensures proceeds are paid to remaining shareholders
and partners free of tax.

Trust proceeds distributed to the beneficiaries after 2 years.

Taxed under the discretionary trust regime – entry,
periodic and exit charges are possible but unlikely.

Flexible Business
Trust Deed



Protect the business owners

The draft double option agreement

For the sale and purchase of shares on death

Used for shareholder and partnership protection.

Allows personal representatives of the deceased to force surviving shareholders to purchase the shares of the deceased.

Allows surviving shareholders to force personal representatives of the deceased to sell the shares of the deceased.

Flexible arrangement which allows for nothing to happen if both parties agree.

Allows for sale / purchase to take place at specified or market value.

Retains Business Property Relief where available.

Draft Double Option Agreement



Protect the business owners

The draft double option agreement
For the sale and purchase of shares on death
Business property relief

Keeps the value of the share outside the estate for IHT purposes.

Available on "relevant business property" .

A business or an interest in a business.

The shares in an unquoted company.

Relevant business property must be held for at least 2 years.

There is no BPR if the business is "wholly or mainly" dealing in securities, stocks or shares, land or buildings or in the making or holding of investments.

There is no BPR if the share of the business is subject to a binding contract of sale.



[Home](#) > [Births, deaths, marriages and care](#) > [Death and bereavement](#)

Business Relief for Inheritance Tax

1. Overview

Business Relief reduces the value of a business or its assets when working out how much [Inheritance Tax](#) has to be paid.

Any ownership of a business, or share of a business, is included in the estate for Inheritance Tax purposes.

You can [get Business Relief of either 50% or 100%](#) on some of an estate's business assets, which can be passed on:

- [while the owner is still alive](#)
- as part of the will

Protect the business owners

The draft option agreement for purchase on critical illness
For the sale and / or purchase of shares on critical illness

Used for shareholder and partnership protection.

Allows the shareholder who has suffered a critical illness to force the remaining shareholders to buy his/her shares.

Gives no right (unless specifically noted in the agreement) for the remaining shareholders to force a critically ill shareholder to sell his or her Shares.

Allows for sale / purchase to take place at specified price or market value.

Draft Option Agreement For Purchase on Critical Illness

Protect the business owners

Shares purchased by the surviving shareholders
Tax treatment of premiums and benefits

The company pays the premiums

The company receives corporation tax relief on the premiums

Equalise the premiums

Equalised premiums treated should be treated as additional income and subject to income tax and NIC

Claim benefits paid tax free via the Flexible Business Trust or the life of another policies

Business Protection

Payment Equalisation

As part of effective business succession planning, business owners may choose to take out life assurance to enable the remaining owners to buy their share of the business from them or their beneficiaries upon their death or after suffering a critical illness. For this arrangement to work, the plan will need to be written in trust with an appropriate option agreement in place.

The cost of each individual's plan is likely to vary due to the following:

- the business owner's age,
- the business owner's health (including smoking status),
- the sum assured required (if they own different proportions of the business).

The need for 'payment equalisation' usually occurs as those who are least likely to benefit, say due to their age or health, are the people that will pay the highest payments. It is also to ensure the arrangement is viewed as 'commercial', which is essential for tax purposes.

Example: ABC Ltd. is owned by three shareholders with the following shareholdings and life assurance payments. There are 100 shares in ABC Ltd.

Shareholders	Age	Shares	Payment
A	45	40	£500
B	55	35	£1,000
C	40	25	£200
Total		100	£1,700

If A died, it has been agreed that the surviving directors B and C will purchase A's shareholding in proportion to their own shareholding. Therefore, if A was no longer part of the business, B would own 35 out of the 60 remaining shares and C would own 25 out of the 60 shares. So B would receive 35/60ths of A's share and C would receive 25/60ths of A's share. To ensure the arrangement is fair, they should pay the same proportion of the payment as the share they will receive. So...



A's payment is £500, therefore B should pay $£500 \times 35/60 = £291.67$ and C should pay $£500 \times 25/60 = £208.33$

If B died, the same would apply for the other shareholders.

If B was no longer part of the business, A would own 40 out of 65 shares and C would own 25 out of 65 shares. So A would receive 40/65ths of B's share and C would receive 25/65ths of B's share.



B's payment is £1,000, and so A should pay $£1,000 \times 40/65 = £615.38$ and C should pay $£1,000 \times 25/65 = £384.62$

Protect the employees



Protect the employees

Relevant life policies
How does it work?

Policy taken out by the employer to provide death in service benefits for an employee

Company owns the policy and pays the premiums

Corporation tax relief available on the premiums but not treated as a benefit in kind to the employee

Written under a Relevant Life Policy Trust for the benefit of nominated beneficiaries

Employee completes Nomination of Beneficiary form

Premiums do not form part of the annual allowance and sum assured is not part of the lifetime allowance



Protect the employees

Relevant life policies
How does it work?

Single life

Life only (including terminal illness)

No disability benefits

Must end before age 75

Trust must be received pre-issue

Life assured must be in receipt of schedule E earnings

Maximum sums assured:

up to age 39 attained	- 30 x
40 – 49 attained	- 20 x
50 attained and over	- 15 x



Protect the employees

Relevant life policies

Who might be interested?

Businesses with too few employees for a Group DIS

Employees who are members of a group DIS based on salary only

Employees who have built up significant pension benefits within a money purchase or final salary scheme

Clients with large Pension Term Assurance policies

Business owners looking for the most tax efficient way to provide family protection



Protect the employees

Relevant life policies

Case study

John Smith owns 100% of the shares in his own limited company. He currently has a personal life assurance policy, written into a discretionary trust for the benefit of his wife and children, for which he pays £200 per month by direct debit from his personal bank account.

Cost to John as a Director paying personally

Monthly premium	£200.00
-----------------	---------

Pre-tax Income to fund £200 at Income Tax rate of 40%* and National Insurance at 2%*	£344.83
--	---------

Cost with employers National Insurance Contributions at 13.8% on this salary	£392.41
--	---------

Gross Salary and National Insurance are allowable deductions against Corporation Tax at 19%*

Total monthly cost to John and XYZ Ltd Company	£317.86
---	----------------

Protect the employees

Relevant life policies

Case study

John Smith owns 100% of the shares in his own limited company. He currently has a personal life assurance policy, written into a discretionary trust for the benefit of his wife and children, for which he pays £200 per month by direct debit from his personal bank account.

XYZ Ltd pays premiums through a relevant life plan

Monthly premium	£200.00
-----------------	---------

No employee Income Tax or National Insurance

No employer National Insurance

Relevant life policy is an allowable deduction against corporation tax at 19%*

Total cost to XYZ Ltd Company	£162.00
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Cost to John and XYZ Ltd company paying personally	£317.86
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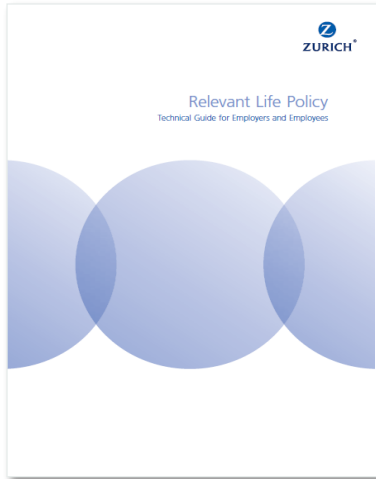
Cost to XYZ Ltd Company paying through RLPT	£162.00
--	----------------

Saving	49% or £155.86
---------------	-----------------------

Protect the employees

Relevant life policies

Literature



RELEVANT LIFE POLICY EMPLOYER AND EMPLOYEE TECHNICAL GUIDE

NOMINATION OF BENEFICIARY FORM



RELEVANT LIFE POLICY TRUST DEED



SALES AID

Protect the employees

Relevant life policies

RLP calculator



Relevant life policy Calculator

Complete boxes with employee and employer tax rates. For employee enter the rates against the highest proportion of their salary.

Name	Mr Client
Premium	£200
Highest Income Tax Rate	40%
Employee National insurance rate	2%

Employer National Insurance rate	13.8%
Company corporation tax rate	19%

Employee pays premium (from net salary)

Cost to employee

Premium (net payment required to pay premium)	£200
Employee National Insurance	£6.90
Employee Income Tax	£137.93

Cost to employer

Premium	N/A
Employer National Insurance (on gross pay)	£47.59

Total cost to employer and employee £392.41

Less: Corporation Tax £74.56

Total £317.86

Relevant life policy

Cost to employee

Premium	n/a
Employee National Insurance	n/a
Employee Income Tax	n/a

Cost to employer

Premium	£200
Employer National Insurance	n/a

Total cost to employer and employee £200

Less: Corporation Tax £38

Total £162.00

Saving via a relevant life policy

£155.86

or

49.0%

Protect the employees

Relevant life policies

Flexibility

Premium payments can be taken over by a new employer.

Need a new direct debit.

New employer can claim corporation tax relief on the premiums.

Premium payments can be taken over by the life assured.

Need a new direct debit.

Life assured pays the gross premium with no tax relief.

Need to retire old employer as trustee and appoint new trustee.

Protect the business

Case study
TDH Ltd

TDH Ltd

Gross profit	£800,000						
Net profit before tax	£150,000						
Company value	£1m						
Business loan	£400,000 with 5 years remaining						
Overdraft	£120,000 – rolling annual review						
Directors' loan accounts	<table> <tr> <td>Tom</td><td>- £70,000</td></tr> <tr> <td>Dick</td><td>- £75,000</td></tr> <tr> <td>Harriet</td><td>- £25,000</td></tr> </table>	Tom	- £70,000	Dick	- £75,000	Harriet	- £25,000
Tom	- £70,000						
Dick	- £75,000						
Harriet	- £25,000						

- Harriet is sales director and responsible for 50% of the gross profit; Tom and Dick are equally responsible for the remainder
- It is estimated that on death or critical illness, gross profit attributable to the key people would drop by 50% and it would take 1 year to recover
- Replacement cover for first year at 1 x salary + 20% recruitment costs
- All business liabilities to be protected
- Key person, shareholder protection and Death in Service cover required

	Age	Salary	Bonus	Dividend	Share	Value
Tom	50nb	£60,000		£40,000	40%	£400,000
Dick	45nb	£60,000		£40,000	40%	£400,000
Harriet	35nb	£50,000	£30,000	£20,000	20%	£200,000

Protect the business

Case study model answer

Loss of profit and replacement costs

	Loss of profit	Replacement salary	Recruitment cost	Total sum assured
Tom	£100,000	£60,000	£12,000	£172,000
Dick	£100,000	£60,000	£12,000	£172,000
Harriet	£200,000	£50,000	£10,000	£260,000

Protect the business

Case study model answer

Business liabilities

	Business loan	Overdraft	Directors' loan	Total sum assured
Tom	£100,000	£30,000	£70,000	£200,000
Dick	£100,000	£30,000	£75,000	£205,000
Harriet	£200,000	£60,000	£25,000	£285,000

Protect the business

Case study model answer

Total sums assured

	Loss of profit & replacement	Business liabilities	Total sum assured
Tom	£172,000	£200,000	£372,000
Dick	£177,000	£200,000	£377,000
Harriet	£260,000	£285,000	£545,000

Protect the business owners

Case study model answer

Shareholder protection

	% Share of business	Sum assured
Tom	40%	£400,000
Dick	40%	£400,000
Harriet	20%	£200,000

Protect the employees

Case study model answer

Relevant life policies

	Salary + bonus + dividends	Sum assured
Tom	£100,000	£400,000
Dick	£100,000	£400,000
Harriet	£100,000	£400,000

Comprehensive business protection

Summary of recommended cover

Name	Key Person	Shareholder	Relevant Life Policy	Totals
Tom	£372,000	£400,000	£400,000	£1,172,000
Dick	£377,000	£400,000	£400,000	£1,177,000
Harriet	£545,000	£200,000	£400,000	£1,145,000
Totals	£1,294,000	£1,000,000	£1,200,000	£3,494,000

NO FINANCIAL EVIDENCE NEEDED FOR THIS SCHEME

Comprehensive business protection

Costs and commissions



Cost to the Company

Key Person £ 597 pm

Shareholder £ 562 pm

Relevant Life Policies £ 110 pm

Tax Relief @19% £ 127 pm

Net cost to company £1,142 pm

Annual net cost £13,704 pa

Your Reward

Key Person* £ 6,472

Shareholder* £ 6,008

Relevant Life £ 2,350

Total initial reward £14,830

Plus new initial commission every
5 years on the renewable policies*

Two blue protective suits, likely for chemical or biological hazards, are shown. They have hoods with clear viewing ports and black straps with buckles. The suits are laid out on a white background.

Zurich service and support



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Zurich Intermediary Group

For use by professional financial advisers only

Protection

Wealth

Have you talked about?

How Zurich helps you

About Zurich

Advice Matters

Document library

Zurich Intermediary Group > Protection > Business protection

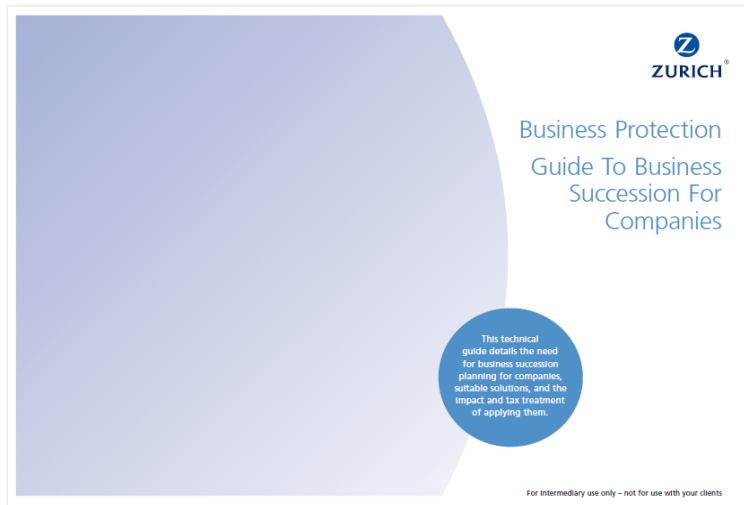
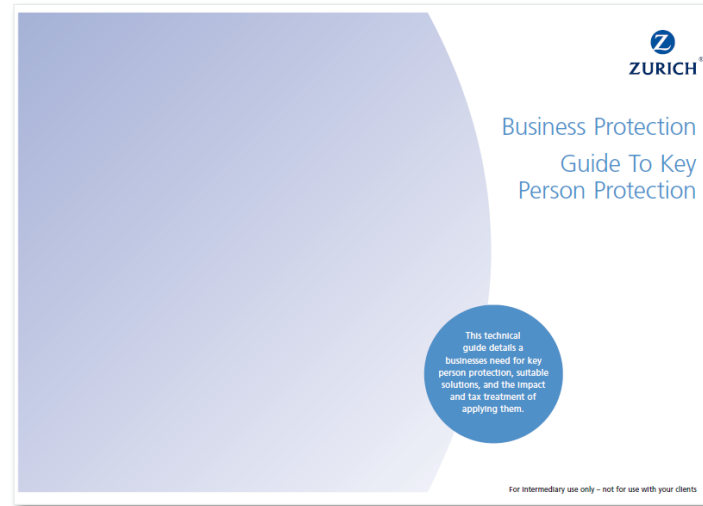
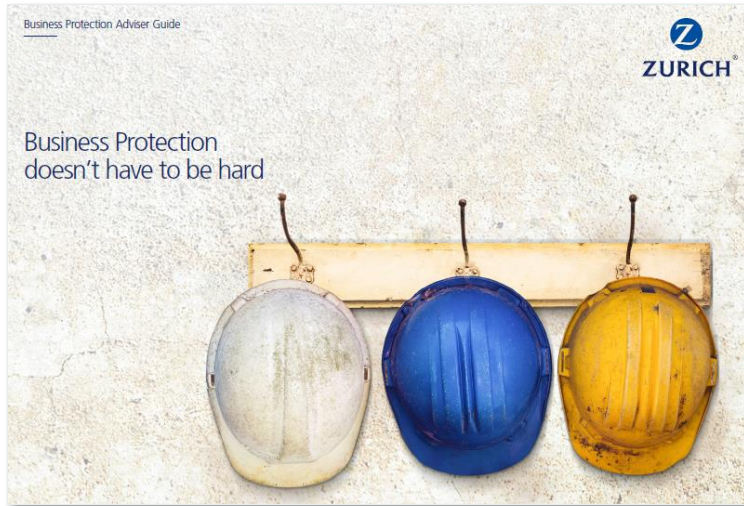


Business protection



Service and support

Adviser technical guides



Learning outcomes

I am able to explain the concept of business protection in the simplest terms possible.



I am aware of the issues faced by businesses on the death or critical illness of a key person, shareholder employee.



I am able to identify key people, calculate the sum assured, set the policies up correctly and explain the tax treatment of the premiums and benefits.



I understand the different methods of business succession planning, including setting up the scheme, the use of trusts and option agreements and the tax treatment of the premiums and benefits.



I can explain the benefits of a relevant life policy, including who can have one, why they might want one and the tax treatment of the premiums and benefits.



I am able to demonstrate your recommendations in a way which is easy for the client to understand.



Questions



Thank you for listening



Important information

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