Business Insurance

When Business owners are often so focused on building their business, they neglect to protect the investment to ensure the survival of the business if something unexpected occurs.

Insurance can help by providing lump sums if a key person or business owner dies or suffers a serious illness or injury. Business owners need to assess the risks in their businesses and considering the options and strategies to minimise these risks or to cover the financial downsides.

There are various business insurance purposes to consider.

Business Succession Plan

Succession planning is simply a strategy for the handover of a business from one owner to another in particular circumstances, such as the planned or unplanned departure of a principal from the business.

A comprehensive plan helps to ensure the business survival and can minimise disputes between owners and families. This plan includes a documented buy/sell agreement to cover issues such as:

- Establishing who should retain ownership and control of the business, by providing an orderly transition with the departing owner (or their estate) selling their interest in the business to the remaining owner(s).
- Determining the 'trigger' events which may result in the departure of a principal.
- Ensuring that the departing owner (or estate) receives an agreed and predetermined value for their interest in the business.
- Providing the remaining owner(s) with funding options to purchase the departing owners interest in the business

The use of insurance as a funding source provides greater certainty for all parties and can be less expensive than taking on debt. It will help to eliminate the need for:

- The business to be wound up or
- A forced sale of the business or assets to pay out the departing owner (or estate) or
- The remaining owner(s) to use personal assets or borrowings to pay out the departing owner (or estate)

Policies can be owned under a number of structures but in most cases self-owned policies are the most tax effective option. This also provides greater flexibility if new owners enter the business or existing owners exit as there is no need to transfer ownership of policies.

Premiums paid on insurance policies used for Business Succession purposes are generally not tax deductible. There may be tax implications including CGT for the departing owner and continuing owners and you should seek specialist taxation advice.

Debt Personal Guarantee

Taking out insurance for the purpose of guarantor protection ensures that if death, TPD or a trauma event occurs to a business owner who has provided a guarantee for a business loan, that the loan can be repaid.

This strategy benefits the guarantor by protecting personal assets which have been used to secure business loans. It also ensures that the business does not face an unexpected financial burden if the lender requires the loan to be repaid or renegotiated. Ideally a guarantor should be insured for 100% of the loan whether they are jointly or severally liable for the debt to provide the best protection.

Premiums paid on insurance policies used to repay debts are not tax deductible.

Business Insurance

Policies can be self-owned (by the person who acted as guarantor) or be owned by the business entity. The tax implications on claim proceeds can vary depending on the option selected.

Business Entity Ownership	Self-Ownership
• Life policy – tax is not payable on claim proceeds received • TPD/trauma policy – capital gains tax will apply	• Tax does not apply on the claim proceeds received on life, TPD or trauma policies
• The business entity receives the proceeds and can directly repay the debt	• The insured person receives the proceeds and needs to pay the debt on behalf of the business. • A written agreement should be in place setting out the respective parties' obligations. This may result in further tax implications and the debt reduction agreement should exclude 'rights of contribution' from arising

With this strategy, care should be taken with any contractual arrangements to ensure capital gains tax is not triggered. The use of insurance to repay debt may also affect valuations of the business. You should seek specialist legal and tax advice.

Key Person Insurance

Key Person insurance protects the business against the loss of a principal or other person who is integral to the business. The loss of key people can have significant adverse financial impacts on the business.

Key Person insurance helps to ensure that a business survives following the loss of a key person in the event of death, disablement or trauma. There are two different purposes - 'revenue purpose' or 'capital purpose'. It is necessary to distinguish between them for taxation purposes.

Key Person – Capital Purpose

The sudden loss of a key person means the business may need to:

- Repay loans made between the key person (principals) and the business. Repay loans or debts to creditors which have been called in because of the loss of the key person
- Compensate the business for any goodwill lost
- Replace lines of credit (i.e. working capital)

The business may take out an insurance policy on each key person to offset the anticipated financial loss. In this instance, the insurance required is for 'capital purposes' as it adds to the value of the business.

The business owns the policy, pays the premiums and receives the proceeds if something happens to the key person. The proceeds are not assessable as income and the premiums are non-deductible. However proceeds received by the business for Total & Permanent Disability or Trauma insurance are subject to Capital Gains Tax (CGT). Life insurance proceeds are exempt.

Key Person – Revenue Purpose

The sudden loss of a key person means that a suitable replacement may need to be found and the business may face unexpected costs for recruitment. The business may also want compensation for reduced revenue, sales and profit to help meet other expenses.

Business Insurance

The business may take out an insurance policy on each key person to offset the anticipated financial loss. In this instance, the insurance required is for ‘revenue purposes’.

The business owns the policy, pays the premiums and receives the proceeds if something happens to the key person. If the business made a declaration at the time of paying the premium that the purpose was of a ‘revenue’ nature, then generally the premiums would be tax deductible and the proceeds would be assessable income of the business.

Business Expenses Insurance

Business Expenses insurance is designed specifically for business owners or sole traders and aims to minimise the financial impact of their sickness or injury by paying a monthly benefit to cover eligible business expenses during a prolonged absence from work. This will allow a business owner to focus on recovery.

Business Expenses policies will usually pay a benefit up to 100% of your gross (eligible) expenses for a set term of 12 months after a waiting period has expired.

To be eligible you need to be a sole trader, in a partnership or a working director and be responsible for paying the business’s expenses. Eligible expenses may include costs for premises, services/utilities, equipment and leasing costs, salaries and associated costs for non–income generating employees, and accounting fees.

The policy is owned by the business entity with the business owner as the insured person. Generally premiums for Business Expenses insurance are fully tax deductible. The proceeds are taxable but the business can claim tax deductions for expenses paid.