Key Person Assurance

Keyperson assurance is another very useful business assurance with the main purpose being to provide funds to the business in the event of the premature death or critical illness of a key member of staff.

It is often the case in many SME's that certain individuals are key to the running of the business and the generation of substantial parts of its revenue and profits. Not only this, these individuals often nurture key relationships with customers, suppliers and bankers, who, if the person was not here anymore, might choose to buy their goods or services elsewhere, alter supply arrangements or withdraw essential funding. These and many other problems could arise if you lost key personnel and in turn this could have a significant and/or disastrous effect on the businesses finances.

It is however possible to protect your business financially by arranging suitable life assurance and/or critical illness cover on any key individuals so that the business would receive an agreed sum in the event of their premature death or diagnosis of one of an agreed list of critical illnesses.

The amount of cover required can often be quite large and therefore needs to be well thought through and may even need to be substantiated by either the insurance underwriters and/or HMRC in order that the cover requested was deemed relevant and within HMRC parameters..

Tax Relief on Premiums

Unlike Co-Shareholder or Partnership assurance, Keyperson assurance is wholly and exclusively for the benefit of the business and therefore so long as certain criteria are satisfied the premiums can be deducted against business income for tax purposes.

One of these conditions is that the person insured is not a significant stakeholder in the business as HMRC would consider them able to benefit, in-directly, under the arrangement. A significant stake is deemed by HMRC to be anything in excess of 5% and therefore if any of the key persons identified hold more than 5% of the businesses shares, they would be deemed significant and it would therefore unfortunately not be possible to claim tax relief on the premiums relating to them.

Tax Treatment of any Payout

The tax treatment of any payout depends on the purpose for which the cover was arranged. If it was to replace loss of profits then any amount identified for this purpose would be taxed as a trading receipt. If however part of the sum assured was to repay identified debts then this element of the payout would not be potentially taxed.

To explain further, the taxation of any payout assigned to replace profits will only be limited to any of the payout that remains as profit at the end of the year. For example a sum of £100,000 is paid out to cover loss of profits and so is potentially taxable as a trading receipt. However £50,000 of this is used to provide a replacement person's salary, £30,000 is used to contribute towards normal overheads and therefore only £20,000 remains as profit. The company would therefore pay its relevant tax rate on the £20,000 and not the £100,000.

Term of the Policy

HMRC stipulates that in order to be eligible to claim tax relief on any premiums “the insurance term should not extend beyond the period of the employee’s usefulness to the company”.

Dealing with HMRC

If you decide to set up this kind of protection for your business then it is advisable, once established, to inform HMRC of the details of any contract and the basis on which it has been arranged i.e. £X,000 for loss of profits, £Y,000 for repayment of existing debts. We can help you with this letter following which HMRC will write back and confirm the tax treatment basis on the elements of the insurance so that you have this in case of any future payout.

I hope the above has been reasonable enough to follow however if you have any questions then please do not hesitate to give me a call on 01792 234875.

Many thanks for your time and interest.