

TRAC

The Retirement Advice Centre



The “Your Guide To” Series

Business Insurance

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Your Guide to Business Insurance

The successful running of a business, or its value, can be severely impacted if a business owner or a key employee dies or is unable to work due to illness. Insurance cover can often be used to help protect a business in these situations.

Business expense insurance

Business expense insurance is designed to help a business continue operating if the insured person is unable to work due to temporary illness or injury.

This type of insurance may be appropriate for sole traders or small partnerships, and may also be available if the business is run through a company.

The insurance will usually cover up to 100% of eligible business expenses in the event the insured person is unable to work due to illness or injury. Not all expenses are covered so it is important to check the wording before taking out a policy. Expenses that are generally covered include rent or lease payments, interest costs, accountant's fees, telephone, electricity, etc.

In the event that the business needs to be sold because the insured person is unable to return to work, business expense insurance can help the business retain its value until the sale date.

Premiums for business expense insurance are tax-deductible for the business. In the event of a claim, the proceeds are assessable either to the business or the business owner.

Key person insurance

One of the most valuable assets in any business is the people. The loss of a key person can affect profitability, operational management and goodwill.

Key person insurance protects a business in the event of the loss of a person who makes a significant contribution towards the profitability or stability of the business.

It provides a cash injection into the business to offset the estimated loss caused by the death, disablement or illness of a key person. For example, it may provide the business with a lump sum that could be used to hire a temporary replacement, cover the cost of training a new staff member or just compensate the business for any reduction of profit.

Key person insurance may be used for a revenue purpose (to replace lost income) or a capital purpose (such as repaying creditors). The deductibility of premiums and the taxation of proceeds depend on whether the insurance is to be used for revenue or capital purpose.

Debt protection

Debt protection can provide a business with the ability to satisfy creditors and maintain credit status in the event that a business owner dies or is unable to work due to disablement or trauma.

The insurance cover provides the business with a lump sum which can be used to repay or reduce business debts. Repaying debts helps to free up cash flow and can provide customers and suppliers with confidence that the business will continue to trade.

Debt protection cover is generally regarded as capital in nature. Insurance proceeds are generally not subject to income tax however capital gains tax may apply.

Insurance to fund buy/sell agreements

Buy/sell agreements help to ensure a smooth transition of business ownership to remaining owners in the event that one business owner dies or is unable to work due to illness or disablement. They help to ensure remaining owners retain control of the business and the departing owner receives fair value for the sale of his or her share of the business.

Buy/sell agreements are often funded with insurance policies. There are various options for owning insurance policies and these should be discussed with a financial adviser and/or tax adviser.

To implement a buy/sell agreement, business owners should enter into a legally binding agreement setting out the details of the arrangement. This agreement should cover issues such as who is to receive the departing owner's share of the business, the trigger events that will result in the transfer (eg death, disablement), the formula for determining the value of the business and how the transfer will be funded (eg insurance or other monies).

The tax implications of paying premiums and claiming proceeds will depend on how the insurance policies are owned.

Other things you should know

- Business insurance should be reviewed regularly, to ensure it continues to meet the changing needs of a business.
- Insurance contracts vary. It is important to check the terms of any contract to ensure the cover meets the needs of the business and the owner.

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