



# Keyperson Protection

Keyperson Assurance is life assurance and/or specified illness cover taken out by an employer on a key director or employee, to protect the employer from the financial consequences of that individual's death or illness.

Putting Keyperson Assurance in place provides the business with a lump sum payment which can help protect against loss of profits that may arise from the death or diagnosis of a specified illness of a key director or employee, much in the same way as a company will normally insure against loss of trading profits resulting from fire and other risks.

## Who is a Keyperson?

The future success of a business is often dependent on a few key people. A keyperson is any "key" employee, director or consultant (e.g. a fixed term employee brought in to consult on or develop a particular project.) on whom the business depends for its continued success or existence. A business may be financially impacted by the loss of a key person - if they die or become seriously ill the business may lose:

- Knowledge of the business
- Experience
- Expertise
- Unique skills
- Business contacts
- Management expertise

## Business Interruption – What Happens if a Keyperson Dies or becomes Seriously Ill?

What would happen if one of these key people were to die or suffer an illness of a serious nature? In such circumstances, the profitability of the business could be interrupted and threatened by any of the following:

- The calling in of bank loans, for which the Keyperson had given a personal guarantee.
- The reduction or withdrawal of credit facilities by banks or suppliers worried about the future profitability of the business following the death or illness of the individual.
- The repayment to the Keyperson (or their estate) of any loans made by them to the company.
- The loss of the individual's expertise.
- The loss of the individual's business contacts and relationships, i.e. loss of goodwill.
- The need to commit resources to the recruitment of a suitable replacement.

## Why Insure a Keyperson?

Putting life assurance and/or specified illness cover in place on a keyperson can help a business overcome the financial repercussions of losing a valued member of staff. The keyperson life assurance policy provides a lump sum to the business as policy owner on the death or serious illness of an insured keyperson. This lump sum benefit can help compensate the business for any loss of profit, or it can be used to repay loans and/or recruit a suitable replacement.

## The Benefits:

By having Keyperson Assurance, the company will receive an immediate pre-determined lump sum payment on the death or diagnosis of a specified illness of the individual insured under the policy. The company is free to use these funds in any way it wants including:

- Pay off outstanding bank loans
- Repay any loans made by the individual to the company
- Recruit a suitable successor
- Invest the funds in the business

## How Much Cover?

When an employer has determined who their key people are, the next question is how much cover they should put in place on each key employee.

Businesses typically can value their keyperson by using a multiple of their current gross salary (typically a figure of 5 to 10 times salary is often used). However, the salary a keyperson is drawing (if they are also a business owner) may not be representative of their worth to the business. The keyperson may be drawing a low salary to keep costs down, or may be keeping their income within limits so that standard tax rates apply. In this situation, a multiple of the profits attributable to the keyperson may be more appropriate (2 times gross profit or 5 times net profit are figures sometimes used).

Definite amounts of cover should be decided upon by the accountant or auditor of the business. If cover is intended to repay outstanding business loans, the level of cover should equal the loan amounts. Note that loans made by a director to a business can be covered, as can loans from commercial lending institutions.

## What are the Tax Implications?

Generally speaking premiums are not deductible for corporation tax purposes however if the following four conditions are in place tax relief may be available on premiums paid to a keyperson policy.

- The sole relationship between the company and the insured keyperson must be an employer/employee relationship.
- The life assured must own less than 15% of the shares in the company.
- The cover must be for loss of profits only.
- The policy must be a short period fixed term assurance policy (typically a 5 year term).

It is quite unusual for a keyperson arrangement to meet all these criteria. The company accountant can confirm whether premiums paid on a life assurance policy for keyperson cover are allowable against the company tax bill. The proceeds of a policy taken out for loan cover are seen as a capital receipt and are normally not taxed. The proceeds of a policy taken out to replace profits are seen as profits and are normally taxed.

Separate policies are normally taken out for each risk to clearly demonstrate to Revenue the nature of each risk covered.

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