

A Guide to Business Protection



SUCCESSION
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Welcome to Succession Wealth

Our Wealth Planners are here to help you take control of your finances and provide you with the confidence you need to go after the things that matter to you. Succession Wealth Management Limited is a large national UK financial advice firm. Our teams of Wealth Planners deliver high quality independent advice to thousands of clients across the UK, and we're committed to helping people achieve more with their money.

Our clients are at the heart of everything we do and looking after their wealth journey is a privilege to us. The relationships we build last longer than a lifetime, and we are proud to provide advice across generations. When you choose to work with us, we promise to provide an exceptional personal service tailored to your unique financial aspirations.

How to minimise the impact should the worst happen

Whether you've been running a successful business for many years or have only recently started up your own enterprise, it's important to understand the challenges and potential pitfalls, and to think of ways of minimising their impact.

How much is a key employee worth to a business? And how would, or could, that business cope without them? Many private businesses rely on one key person which can leave them exposed. Financial protection is vital to allow businesses to recover quickly and minimise the impact should the worst happen.



Types of business protection

Key employees are vital to a business

Key employees are vital to a business, and business protection can help should a director, partner, or key employee suffer a critical illness, become unable to work due to a disability or die. It can help to make a situation a little easier when things go wrong.

There are several different types of business structure in the UK, all governed by different rules which determine the legal status of the business and how it is run, for example, the amount of tax you pay, who is entitled to the profits and who is liable for any debts run up by the business.

Type of business and its particular needs

Business protection is available for partnerships (including limited liability partnerships), shareholders, sole traders, and key employees. It can also be used to ensure repayment of a business loan in the event of death or critical illness of a partner, key person, or sole trader. How the arrangement is set up will depend on the type of business and its particular needs.

The loss of one or more of your key employees can cause disastrous problems. Sales may be lost, credit could become more difficult to obtain, profits may shrink, and momentum may be lost. Hiring and training a replacement will cost you time and money. Most astute business owners insure physical assets from destruction, but when it comes to a business owner's most valuable assets – key employees – you should take the same precautions.

Whatever type of operation you manage, if successful it will grow and evolve over the years. If you're just setting up your first business, the challenges you face may be very different to those you may encounter ten or twenty years down the line.

Key person insurance

This is designed to compensate a business for the financial loss brought about by the death or critical illness of a key employee, such as a company director or other integral member of staff. It can provide a valuable cash injection to the business to aid a potential loss of turnover and provide funds to replace the key person.

You cannot replace the loss of a key person, but you can protect against the financial burden such an event may cause. Without the right cover in place, you could also risk losing your business. Key person insurance can be utilised in a number of different ways – for example, to repay any loans taken out by the key person, to help recruit and fund the training costs for replacement staff, to meet the ongoing expenses while the level of sales recover, or to facilitate payments for outside consultants or expert advice that may be required.

Whatever the key person does, their loss could have disastrous consequences. Some of the problems the business may face are:

- Loss of profits
- The need to recruit or train a replacement
- Loss of important personal or business contacts
- Difficulties in meeting existing loan repayments
- Loss of confidence from suppliers and customers
- Difficulties in raising new finance for new developments
- Loss of detailed knowledge of the business' processes and systems
- Having to repay a loan the key person has made to the business
- Loss of goodwill

Types of business protection

Shareholder and partnership protection

This provides an agreement between shareholding directors or partners in a business, supported by life assurance to ensure that there are sufficient funds for the survivor to purchase the shares. It is designed to ensure that the control of the business is retained by the remaining partners or directors, but the value of the deceased's interest in the business is passed to their chosen beneficiaries in the most tax-efficient manner possible.

If a shareholding director or partner were to die, the implications for your business could be very serious indeed. Not only would you lose their experience and expertise but consider too what might happen to their shares. The shares might pass to someone who has no knowledge or interest in your business. Or you may discover that you can't afford to buy the shareholding. It's even possible that the person to whom the shares are passed then becomes a majority shareholder and so is in a position to sell the company.

The shareholding directors or partners in a business enter into an agreement that does not create a legally binding obligation on either party to buy or sell the shares, but rather gives both parties an option to buy or sell, i.e., the survivor has the option to buy the shares of the deceased shareholder, and the executors of the deceased shareholder have the option to sell those shares. In either case, it is the exercise of the option that creates a binding contract; there is no binding contract beforehand. This type of agreement is generally called a 'cross option' agreement.

Cross option agreement

By taking out a cross option agreement, you will determine what will happen to the shares in the business if one of the owners were to die or become critically ill. It is important that this agreement is not binding regarding sale of the shares, because this will prevent you from claiming relief from Inheritance Tax.

Other protection options available

There are other protection options available which may also be relevant to your business and situation. These include life cover only, critical illness cover, or combined life cover and critical illness cover. You can select different levels of cover and terms depending on your specific requirements, and there are also policies available that pay out a regular income in the event of sickness.

Relevant life cover

A relevant life policy is an alternative way for an employer to set up life cover for a key employee in a tax-efficient manner, without using a registered death in service group life scheme to benefit the employee's dependents.

Key person critical illness cover

Pays a tax-free sum of money to key employees or the business owner in the event of a specified or serious illness, such as a heart attack or stroke.

Key person income cover

Protects key individuals by paying their salaries while they're unable to work.

Key private health insurance

Funds private healthcare for key employees. As well as being an extra benefit of employment, it could help them to return to work more quickly after an illness by paying for rehabilitation treatment.

Business loan protection

With business loan protection, owners, partners, or directors can insure the size of any outstanding debt, and in the event of their death this will be repaid. The larger the debt, the higher the premiums will be, but for simple life cover, this is one of the cheapest forms of business protection insurance.

When a business borrows money from a bank or other financial institution, it is common that the business will want some form of protection cover to repay all, or some, of that loan on the death of a key person. It could also be that the business owners have lent money to their own business. These are called 'director's, or partner's, loan accounts' and need to be repaid on death. Financial protection is vital in the current economic environment to ensure that a business can repay corporate loans should the worst happen.

Calculating the level of cover required

The cover required is typically measured by reference to the key person's contribution to the profits of the business. This may be based on the information such as:

- Past profits and projections for the future.
- The effect that the loss of the key person would have on future profitability.
- The anticipated cost of recruiting and/or training a replacement.
- The expected recovery period, for example, the length of time before a replacement is effective; and the amount of any loan(s) that would be called in on the death of the key person.

Summary

To summarise, the death or prolonged illness of a business partner, key employee or shareholder could put your business under considerable financial strain. No one can predict what will happen in the future, but you can make sure that you have the right protection in place to keep your business successful should the worst happen.



Contact us

If you would like to discuss how business protection could help you, or any other aspect of financial advice with one of our Wealth Planners, feel free to email us at hello@successionwealth.co.uk or call us on 0800 051 4659 and we will arrange for someone to contact you.



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