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Business Life Insurance Options

A guide to the tax advantages

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Using Business Life Insurance Options for key person protection

Tax relief on premiums

Premiums on life policies taken out by employers for key person protection will be allowable deductions and get tax relief if:

- the sole purpose of taking out the policy is to cover any potential loss of trading income (not capital loss or as security for a loan) from the loss of the key employee.
- the term of the policy does not go beyond the period of the employee's usefulness to the company.
- there's an employee/employer sole relationship between the person covered and the company that will benefit from the policy.
- It's a term/pure protection policy i.e. there is no investment element.

With an own life policy, a sole trader may not qualify for tax relief on the premiums as HMRC may see it as a personal benefit for them and their family.

Tax on claim proceeds

If HMRC **gives** tax relief on the premiums, it will normally tax any money from the policy as a trading receipt.

If HMRC **doesn't give** tax relief, it will decide how to tax any money from the policy, but won't generally tax it as a trading receipt.

If premiums are tax deductible and your client decides not to claim, the policy benefits would still be taxable as a trading receipt.

If you're using Business Life Insurance Options to set up key person protection for your client, we recommend they consult their local tax inspector to confirm the tax treatment.

Inheritance tax

Getting a sum of money from a key person protection policy can increase the value of a business and consequently the value of shares held by an individual. This may increase both the value of the estate and the inheritance tax liability of a shareholder or person owning the business.

Your client may be able to use business property relief to help reduce any inheritance tax that may be due. You can find out more about this on the HMRC website.

Using Business Life Insurance Options for shareholder/partnership protection

Tax on premiums

Each partner/shareholder usually pays the premiums for policies they take out for shareholder/partnership protection on their own life. This means they don't benefit from tax relief.

If the premiums are paid by the business on behalf of a partner/shareholder, they will be classed as a deductible expense for the business.

A company will also be liable to pay National Insurance on behalf of the director.

The partner/shareholder will be liable for income tax and National Insurance on the value of the premiums.

Tax on claim proceeds

There is no income tax liability on the policy proceeds in the event of a life and/or critical illness claim.

Life policies are usually exempt from capital gains tax in the hands of the original owner.

Inheritance tax

The money from a claim won't be part of the policyholder's estate if it's placed in an appropriate trust.

Relevant property inheritance tax rules will apply if you use a flexible Partner's or Director's Trust. The gift of a policy into our Partner or Director Trust is a chargeable lifetime transfer. However, you'll create the trust at the start of the policy, so the policy will have no initial value. This means there won't be an inheritance tax charge at that time.

There may be an inheritance tax charge if the value of the trust property is greater than the available nil rate band on any 10 year anniversary of the creation of the trust. However, the policy will have little or no value if the key person covered is in good health and likely to survive the policy term.

Premiums paid for a policy in trust would normally count as gifts for inheritance tax purposes. However, HMRC may accept there is no gifting where there is a reciprocal commercial arrangement requiring all partners/shareholders to enter into a share protection agreement.

If your client has any doubt over tax, they should contact their local tax inspector before setting up a business protection policy.

Using Business Life Insurance Options for business loan protection

Tax on premiums

The premiums are not deductible as a business expense because the policy is set up for a capital purpose (i.e. to repay a loan).

Tax on claim proceeds

The policy proceeds are not taxable as they are treated as a capital receipt.

Find out more

For more information, please read our guides:

- Business Life Insurance Options At a glance
- Business Life Insurance Options In focus

Or you can speak to your account manager for more information.

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