



Cheltenham Independent
Financial Advisors Limited

PROTECTING YOUR BUSINESS

(A GUIDE FOR SMALL TO MEDIUM SIZED BUSINESSES)

“100% of small to medium sized companies believe they have at least one key person whose death or serious illness would impact on company profits”

Over half said they could end up closing within a year, but more than 70% did not have cover in place. As well as being unable to cope with the death of a key person, very few companies will have the cash available to buy a shareholder's shares or a partner's interest if they die. Without this, the interest will automatically pass to the deceased's family and may cause disruption to the company. Others will be sole traders who will need protection in order to keep the business afloat when they are ill.

Types of protection

Key man, shareholder, loan protection, Private Medical Insurance are all forms of business protection that should be considered whether it is a new or existing business. This guide introduces the main areas of consideration.

Key person insurance



“The success of almost all small and medium sized businesses is dependent on a few people who make a significant contribution. Ensuring the business is covered in the event of their death or serious illness is therefore a fundamental step”.

Key people can include owners, senior directors, sales people, production managers, research and development staff – the list is endless. Often the key person has specialist skills or knowledge and their value to the business is reflected in their remuneration package, although this may not always be the case.

Why do they need to be covered?

Whatever the key person’s role, their loss could have disastrous consequences for the business. It could mean loss of profits, loss of contracts, difficulties meeting loan repayments or even having to repay a loan the key person has taken out for the business. It could also mean loss of knowledge of the business and its processes. And it could mean the loss of important business contacts and goodwill going forward. That is why businesses should be keen to have insurance in place for their key people.

What kind of cover is needed?

There is nothing mysterious about key person cover. At its most fundamental, it is simply a case of a business insuring their key people for life and/or critical illness cover, and making sure that if they die or suffer a critical illness, the business is compensated. This can give the business the necessary cash injection to make sure it survives. Businesses can also consider taking out key person income protection to help cover the cost of sick pay or pay for a temporary replacement if a key person is ill and cannot work. And in certain instances it makes business sense for key individuals to take out personal income protection. Many business owners also have big financial commitments beyond the business to consider, such as their mortgage, utility bills and all the normal expenses of providing for a family. These still need to be paid, so protection from all angles needs to be considered.

Ownership protection



Just like key person and loan protection, the approach taken to ownership protection very much depends on the business type, the deceased owner's share in the business and the articles of association or the partnership agreement. All this influences the best structure of the protection plan that is set up to mitigate these problems.

“The owner's family may want to become involved in the business. This can often be disruptive or unacceptable to the other shareholders”

If one of the owners of a limited company becomes critically ill or dies and the remaining owners do not have the funds and the option available to buy their shares, the following issues may arise:

- If they are a majority shareholder and they or their family want to sell their share, control of the business could be lost to someone the other owners are not happy about.
- If the outgoing owner has 75% of the shares or more, they could force the outright sale of the business.
- The owner's family may want to become involved in the business. This can often be disruptive or unacceptable to the other shareholders. A majority shareholding allows a new owner to appoint themselves as a director and to remove other directors. So they could gain day-to-day control of the business if plans are not in place to prevent this from happening.



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Loan protection



“Many businesses take out loans and rely on a key person to repay them. Without protection, a business could suffer severe losses in the event of the key person’s death”.

Many businesses have to borrow funding to start up or expand. Often the ability to repay it lies with a few key people. Businesses need to make sure they have enough cover in place to pay an outstanding loan if something happens to key people. The amount outstanding is generally apportioned between the relevant key people being insured. Lenders usually require this cover.

But many directors may have given personal guarantees and/or used their own residential home as security. So there is the added need to ensure that dependants are protected too. Sometimes directors have made loans to their business, either by making a cash injection when needed, or leaving salary, bonus or dividends in the business. This is generally referred to as a Director’s Loan Account and it becomes repayable to the estate on the death of the director. Businesses therefore need to include this in the life cover sum they are insuring.



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Private Medical Insurance



PMI (sometimes referred to as Personal Medical Insurance) is a health insurance UK plan intended for use when covering the costs of private medical treatment for curable short term medical conditions, referred to frequently as acute conditions. PMI may cover the private health care costs of surgery,

specialists, accommodation and nursing at a private hospital or in a private ward of an NHS hospital.

If managers of businesses could find a way of reducing staff sickness and improve staff loyalty, this would surely be embraced. Research with small to medium sized companies has found the following benefits of having PMI for staff:

“Businesses are losing millions of pounds each year due to staff absence and PMI has now become an important consideration for employers and employees alike”.

- The speed of treatment means your employees can return to work more quickly
- Reduces stress at work and gives peace of mind to employees and employers
- Helps attract and retain quality staff
- Employees have more choice in their treatment; specialists, surgeons and hospitals

For a free independent appraisal relevant to your business contact:

**Cheltenham Independent Financial Advisers Ltd
10 Montpellier Arcade
Cheltenham
GL50 1SU**

Tel: 01242 269656

Email: info@cheltenhamifa.co.uk

www.cheltenhamifa.co.uk

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