Business Owners: Your Most Valuable Asset is You.

For many business owners, one of the most valuable business assets is the business owner themselves: their ability to work, generate income and contribute to the business. As such, having insurance to protect the owner can be an essential component to the business. While there are many insurance options available, the needs of the business and the types of insurance required may change as the business evolves: from the business' initial development, through its growth and eventually to succession. Beyond protecting the business owner, insurance can also provide other benefits, including minimizing taxes or supporting asset growth.

Here are some potential insurance considerations for business owners at every stage:

Developing Your Business

For business owners just starting out, it may be difficult to think about allocating cash flow to insurance, instead of investing within the business. That said, obtaining some insurance coverage is important to help protect business owners and their families by replacing income in the event the owner is unable to work. There are cost-effective options that can reserve business cash flow to contribute to the business' growth. Term insurance may be a relatively affordable solution for younger business owners when considering life insurance options to support family members in the event of the business owner's death. While coverage is considered temporary (i.e., protection ends when the term ends), it can be more cost-effective compared to permanent life insurance.

Critical illness insurance on a term basis may be another consideration to provide protection in the event of a critical illness such as cancer, heart attack or stroke.

Growing Your Business

As a business becomes more established, other forms of insurance may be better placed to provide protection. For example, disability insurance may provide protection in the event of illness or injury, but insurers will generally require a few years of self-employed tax returns before providing coverage (as the amount an individual qualifies for is based on what has been earned over a given period). Overhead insurance covers the cost of fixed monthly overhead expenses to keep a business running until the owner returns from a period of disability.

Key-person insurance names the owner or other key staff as the insured, with the beneficiary as the business. This may provide a financial cushion for the business if there is a sudden loss of an individual who is critical to the business' operations. The death benefit may be used to provide liquidity to the business so that the company can continue to operate while finding a potential replacement, or implement other strategies such as a potential sale or the winding down of the business. Business interruption insurance compensates for lost income in the event of a disaster.

In the case of a partnership or a business with multiple shareholders, insurance may also help to support a buyout agreement in the event of a partner's death. If each partner holds a life insurance policy on the other, the proceeds can be used to buy out the partnership interest if something were to happen to one partner.

Insurance can also offer more than just protection. It can help to minimize corporate tax or maximize corporate assets. For example, owning a life insurance policy within the corporation may allow the premiums to be paid with "cheaper" corporate dollars (i.e., income subject to tax at corporate rates that are lower relative to personal tax rates). Or, if a business needs a permanent life insurance policy for key-person, buyout or estate-planning needs, the policy could also be used to invest a portion of the company's excess profits on a tax-deferred basis.

Succession of Your Business

Insurance can also help to facilitate the succession of a business or a shareholder's estate planning. Corporate-owned life insurance has the potential to provide liquidity at the time of the owner's death, which can be helpful to cover terminal tax liabilities when passing along the business. This can be much more effective than taking out a business loan, establishing a sinking fund to address tax payable or having to sell business assets. Funds may also be used as an income-replacement tool for surviving financially-dependent family members. There may also be tax benefits. For example, the death benefit from a life insurance policy held corporately can be distributed to the shareholder(s); anything above the adjusted cost basis can be paid tax-free through the capital dividend account. This often results in 80 percent or more of the death benefit payable without being subject to tax and can be a powerful way to move assets out of a corporation.

As a business owner, you are often the most important asset to your business, so plan ahead and consider protecting yourself. As always, the considerations will depend on your own business' particular situation. For a more detailed discussion, please get in touch.

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