The future success of a business is often dependent on a few key people. A keyperson is any “key” employee, director or consultant (i.e. a fixed term employee brought in to consult on or develop a particular project e.g. – new IT system etc.) on whom the business depends for its continued success or existence. A business may be financially and operationally impacted by the loss of a key person in the event that they die prematurely or become seriously ill.

Some of the ways in which your business may be affected are listed below:

- The business will have to survive without that person’s unique skills, business contacts, management experience or intimate knowledge of your business; this may result in a reduction in service standards and a loss of confidence by both customers and suppliers
- Bank loans could be called in - particularly if the keyperson had given a personal guarantee.
- There could be a withdrawal or reduction of credit facilities by suppliers who are concerned about the future of your company due to the death or serious illness of the keyperson
- Loans made by the keyperson to the business may have to be repaid
- Additional cost of recruiting a suitable replacement (if one can be found)

What is keyperson insurance?

A business puts life insurance in place on its key employees with a view to compensating the business for an anticipated financial loss in the event of death of the individual covered.

The individual can also be covered for serious illness. In the event of death or serious illness of a key individual, the lump sum payment from the policy can help compensate the business for any loss of profit, or it can also be used to repay business loans, and/or to recruit a suitable replacement.
How much cover should be put in place?

Having determined who your key people are, the next question is how much you should cover them for? Businesses can value their keyperson in general by using a multiple of their current gross salary (typically a figure of 5 to 10 times salary is 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 x gross profit or 5 x net profit are figures sometimes used).

You should also take into account the following:

- Any business loans outstanding, including any that the keyperson has made to the business
- Estimated costs of recruiting a suitable replacement for the keyperson

What are the advantages of keyperson insurance?

- The employer pays for the cover so in the event of death or serious illness of a keyperson, the company receives a lump sum amount
- The policy proceeds can be used to repay loans owed by the business (both commercial loans and director’s loans)
- The policy proceeds can be used to replace the profits generated by the keyperson or used to recruit a replacement for the keyperson

Is your business covered?

We provide products that can help businesses and their owners plan for their future. If you haven’t a business protection plan in place, talk to a Financial Broker or Advisor today who will look at your current situation and talk you through the available options. With this information to hand you can then decide what action you need to take.

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