



# BUSINESS PROTECTION.

State of the nation's  
SMEs report.

Fifth edition.

FOR ADVISER USE ONLY.

# ▶ INTRODUCTION.



“We have been running this research since 2009 and have become the experts in the market. Not only in the need for Business Protection but also the lack of awareness of the risks that face many small and medium size businesses which they may not be aware of. Insuring buildings, equipment and vehicles is commonplace but businesses need to consider the risks to their business if they were to lose a key person or business owner due to death or a critical illness. I am determined to raise the awareness both among business owners of these risks and the need to seek some sound financial advice.”

Richard Kateley  
Head of Intermediary Development



The Rough Guide to Business Protection in partnership with Legal & General is a comprehensive e-guide giving no-nonsense, practical and clear information on Business Protection. Written by financial journalist Emma Simon, the e-guide is packed with top tips and useful information to help business owners understand the risks their businesses may face and the types of insurance products available.

**Download your copy today.**

**This is our 5th edition of our research into business protection which has continued to give a great insight into the market and the risk businesses face.**

We've found that there continues to be a clear lack of awareness of business protection, showing that some businesses have not evaluated the potential risks. They have not considered the impact on their businesses, its ability to continue to trade and their own livelihoods.

- What would happen to a business if the owner suddenly died?
- Is the business able to repay any debts if an owner or key employee died?
- What if the majority shareholder was diagnosed with a terminal illness?

In fact, the research shows that 53% of businesses would cease trading in under a year if a key person died or became critically ill.

We also asked these business people if they held any form of personal protection insurance. 41% had life cover in place, so there is some awareness of the importance of protection in their personal/family life, but the majority did not.

With the right knowledge, businesses are better placed to make the right decisions in protecting themselves against certain unexpected events. This begins with adviser/client conversations and properly evaluating the risks a business faces.

It's all about helping to **Get Business Assured.**



**Legal & General provide in-depth training workshops and webinars.**

# WHO DID WE SPEAK TO?

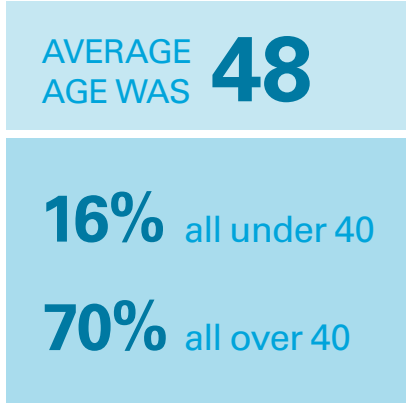
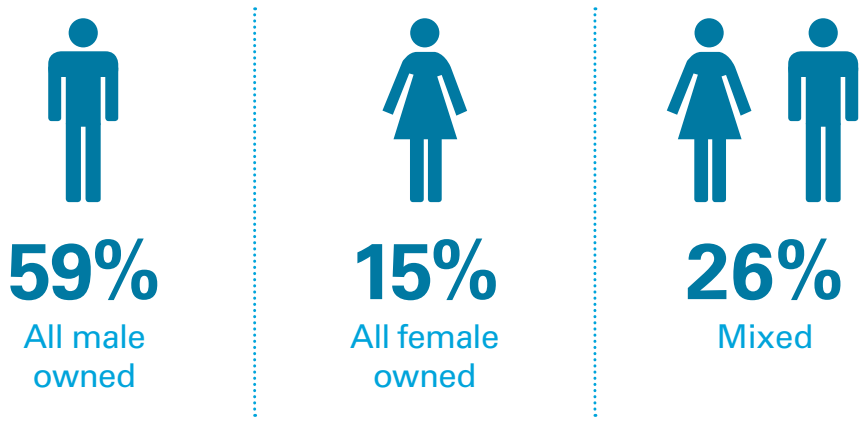
We spoke to a range of businesses in the UK – from limited companies and sole traders to partnerships and limited liability partnerships. Sectors include health, retail, financial services, public sector, IT and construction. The businesses we spoke to also varied in stages of their development, as well as being a mixture of solely male owned, female owned or with a combination.

We can see from the research sample, 92% of SMEs have three owners or less. This could perhaps indicate that their businesses would be most affected in the event of a death or critical illness of a key person and so key person cover could be an essential product for smaller businesses.

**i** **DID YOU KNOW?**

- There were a record 5.5 million private sector businesses in the UK at the start of 2016. 99% were small or medium sized (SMEs).
- 95.6% have fewer than 10 employees.

Department for Business, Energy & Industrial Strategy

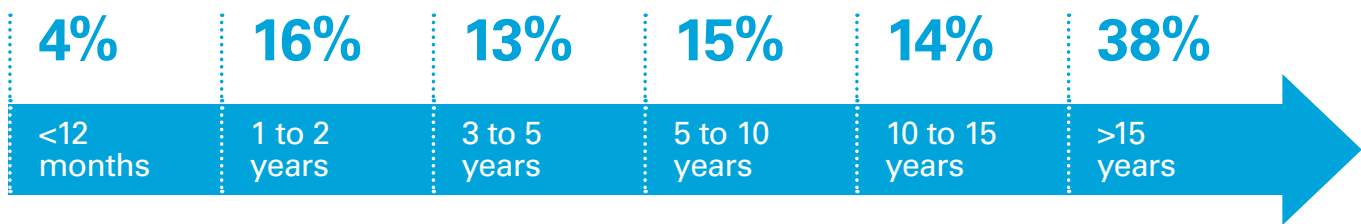


IN THE UK THERE ARE:

**5.5 MILLION**  
PRIVATE SECTOR BUSINESSES

MAKE UP INCLUDES  
**1.8M COMPANIES**  
**421K PARTNERSHIPS**

YEARS BUSINESS ESTABLISHED



# OUR RESEARCH SEGMENTS.

Of our research sample, the following business segments could be identified. This can help us to understand the make-up of SMEs in the UK market and their business types. The key findings from within these segments are highlighted below.

<b>Newer businesses</b> (established within last 2 years) 12% of the total	<b>Maturing businesses</b> (aged between 3-10 years) 36% of the total	<b>Established businesses</b> (set-up more than 10 years ago) 52% of the total
<p><b>More likely to be sole traders</b></p> <ul style="list-style-type: none"> <li>• 22% of the surveyed results compared with 19% overall</li> </ul> <p><b>More likely to be small businesses</b></p> <ul style="list-style-type: none"> <li>• 48% have less than £50,000 net profit</li> <li>• 70% have less than 10 employees with an average of only 20 employees</li> <li>• 63% value the business under £250,000</li> </ul> <p><b>More likely to be younger all male or all female owners</b></p> <ul style="list-style-type: none"> <li>• 23% all under 40 vs. 16% overall</li> <li>• 69% all male and 19% all female compared to 59% and 15% overall</li> </ul>	<p><b>High proportion of limited companies and partnerships (almost 70%)</b></p> <p><b>Business are starting to grow</b></p> <ul style="list-style-type: none"> <li>• Almost 1/2 have profits in excess of £150,000 with average net profit £455,000</li> <li>• Average of 30 employees</li> </ul> <p><b>Highest proportion of family businesses</b></p> <ul style="list-style-type: none"> <li>• 51% are family owned</li> </ul> <p><b>Large proportion of younger age owners</b></p> <ul style="list-style-type: none"> <li>• 22% under age 40</li> </ul> <p><b>Highest proportions where they have given security against any borrowings</b></p> <ul style="list-style-type: none"> <li>• Includes a mixture of personal guarantees, charges against business or personal properties</li> </ul>	<p><b>More likely to be limited companies</b></p> <ul style="list-style-type: none"> <li>• 57% are limited companies</li> <li>• Smaller proportion of sole traders only 16%</li> </ul> <p><b>Are larger with more profit</b></p> <ul style="list-style-type: none"> <li>• 19% have over £1.5m profit with an average of £584,000</li> <li>• Trend for this to increase with the age of the business</li> <li>• Have average of 36 employees</li> <li>• 21% have over 50 compared with just 17% overall</li> </ul> <p><b>More likely to older owners</b></p> <ul style="list-style-type: none"> <li>• 76% all aged over 40</li> <li>• Average age is 51</li> </ul> <p><b>Most likely to have director's loan accounts</b></p> <ul style="list-style-type: none"> <li>• Highest proportion unaware it needed to be repaid on death</li> </ul>



## DID YOU KNOW?

ENTREPRENEURS ARE STARTING NEW COMPANIES AT A RECORD PACE OF



according to data collected from StartUp Britain, a Government-backed national enterprise initiative.

# 342,927

NEW BUSINESSES WERE REGISTERED WITH COMPANIES HOUSE BETWEEN JANUARY AND JUNE 2016

compared with 608,110 for the whole of 2015, itself a record year.



# ABOUT BUSINESS PROTECTION.

Many businesses across the UK take the time to consider employment benefits, pension schemes or staff protection, yet the business itself can be overlooked. However, the business is pivotal to everything else. Without it, none of the other components would link together.

## BENEFITS OF BUSINESS PROTECTION

Business protection can help businesses continue to trade if an owner or other person key to the business dies or becomes terminally or critically ill. Proceeds from the policy could help ensure that key individuals are replaced, debt is protected and shares from the deceased partner's/director's estate are purchased.

Many people think that arranging business protection is a lengthy, complicated process. In fact, the principles are similar to most other types of protection. The main differences are that business protection generally involves higher sums assured.

**As with all insurance plans, limitations and exclusions apply.**

# BUSINESS LOAN PROTECTION.

## WHAT IS IT AND HOW DOES IT WORK?

The loss of the person who has guaranteed a loan is particularly serious for a business. Business Loan Protection helps a business pay an outstanding overdraft, loan or commercial mortgage, should the person covered die or is diagnosed with a terminal or critical illness (if chosen) during the policy term. When a valid Business Loan Protection claim is made, a sum equal to the outstanding debt could be paid to either the business or directly to the lender.

## INCREASING AWARENESS

Although awareness is getting better and more people are considering cover, a large proportion of businesses do not have cover in place to repay debt.

Of those who did not have cover, **75%** did not see the need or hadn't considered it. This shows that an education piece has to be done.

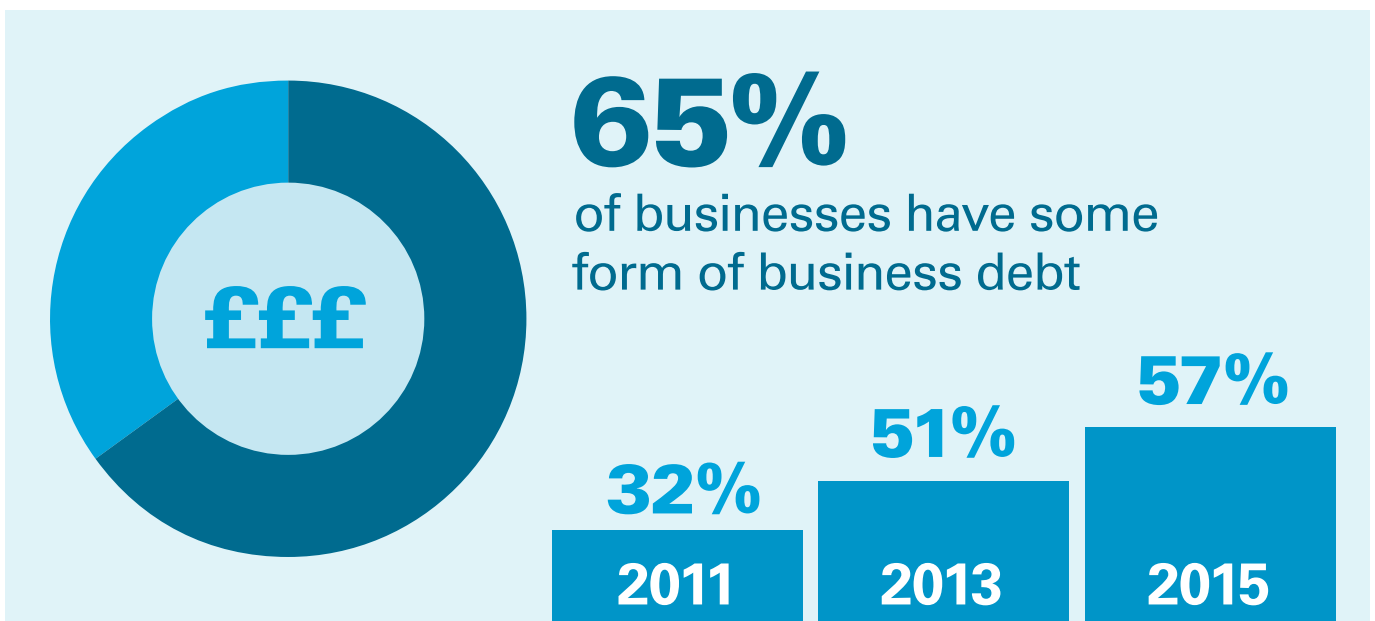
**The good news is, of those who had cover 84% were given advice by a financial adviser or their bank. Highlighting that once business owners are made aware, they tend to see the benefits.**



### KEY QUESTION:

**Does the business have any unprotected loans or debts?**

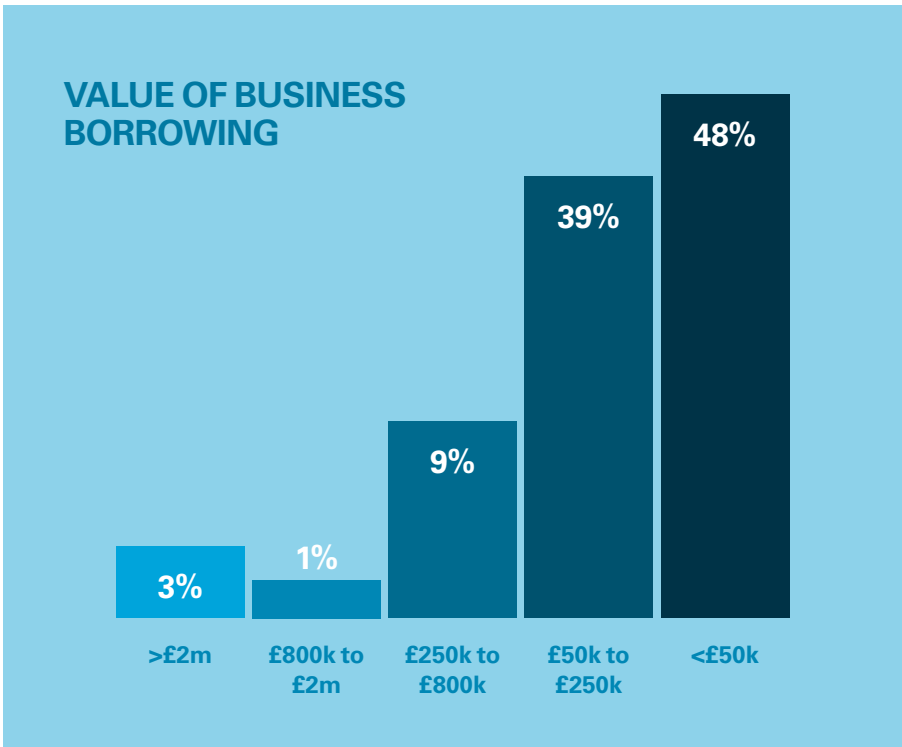
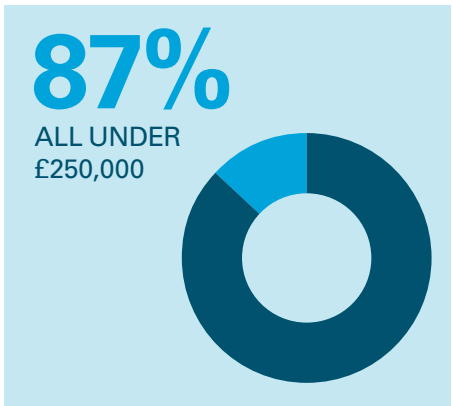
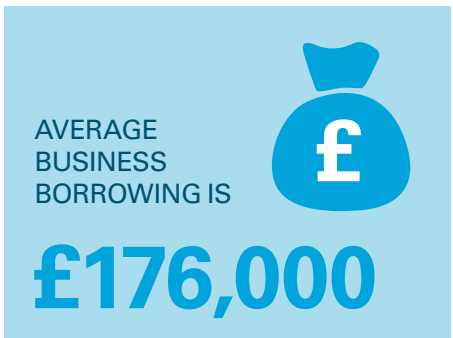
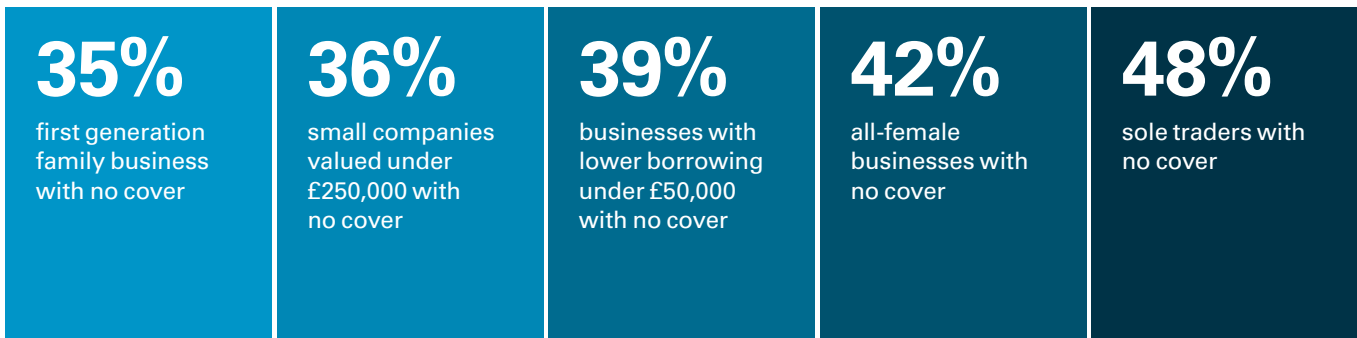
Business Loan Protection can help the business pay any outstanding borrowings such as a loan, overdraft or commercial mortgage, should the person(s) covered be diagnosed with a terminal or critical illness (if chosen) during the policy term.



We can see from the research results that business debt has increased 14% since 2013 and 33% since 2011, yet a large proportion of businesses do not have cover in place to repay debt.

# WHO'S RUNNING THE BIGGEST RISK?

Those least likely to have any cover in place are shown below. As you can see, most of these are smaller or newer businesses, showing that personal wealth could be at risk.

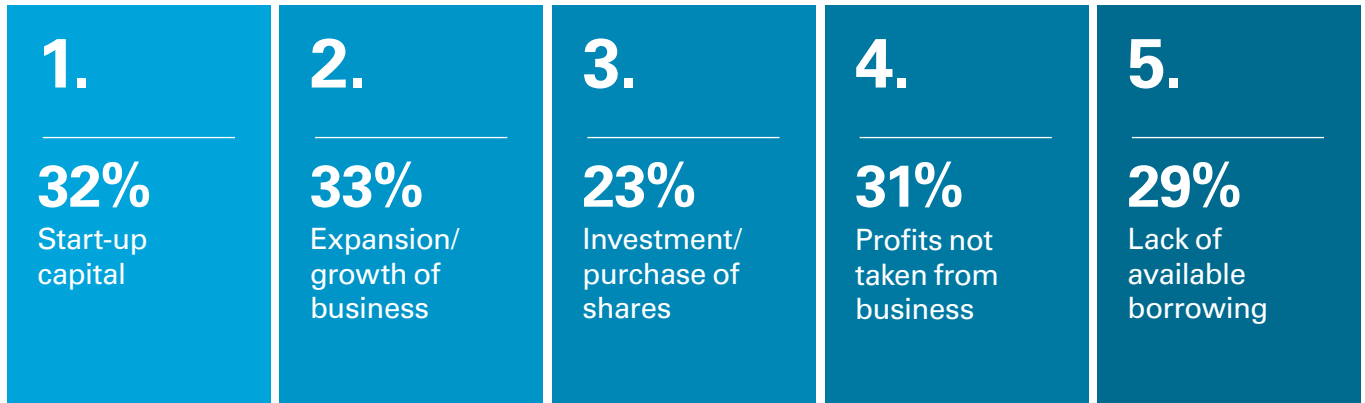


WITH BORROWING OVER £50,000



# DIRECTORS' LOAN ACCOUNTS.

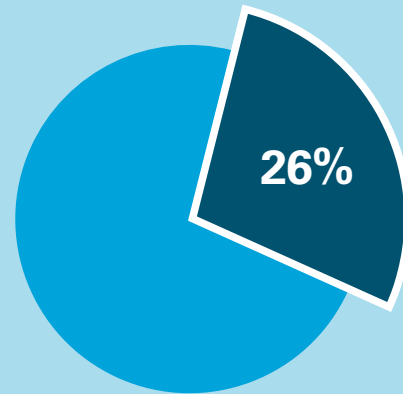
## TOP FIVE REASONS FOR DIRECTORS' LOAN ACCOUNTS



**97%**

had borrowing  
up to £250,000

AVERAGE WAS £81,000



were not aware that a  
Director's Loan account needs  
to be repaid on death



## WHAT WE CAN LEARN FROM THE RESEARCH

Of those who had cover to ensure the repayment of a Director's Loan account, we can see certain profiles emerge – this may help identify clients who would benefit from this product.

They were:

Larger companies  
valued at

**£250,000 +**

Companies with

**11 or more  
employees**

Younger age  
business owners

**under age 40**

More than

**£50k  
borrowing**



# KEY PERSON PROTECTION.

When running a business, most owners are focused on day to day delivery and doing the best for their customers. Unfortunately, this means they don't always have the time to think about the 'what ifs'.

## ABOUT KEY PERSON PROTECTION

Key Person Protection enables a business to insure itself against the financial loss it would suffer if a key person died or was diagnosed with a specified critical illness (if critical illness was chosen as part of the policy) during the policy term.

## WHO IS A KEY PERSON?

A key person is an individual whose skill, knowledge, experience or leadership contributes to the financial success of a business directly or indirectly. A key person could be one of a number of people within the business.

For example: **Chairman, Managing Director, Marketing Manager, IT Specialist, Finance Director, Sales Manager, Paraplanner.**

Or anyone whose death could lead to financial loss for the business through:

- Loss of profit
- Having to recruit or train a replacement
- The loss of important business contacts if the key person is not there to maintain relationships
- Customers and suppliers losing confidence in the business.



### KEY QUESTION:

**Do you have any key individuals who contribute heavily to profits and whose absence would affect them?  
Have you identified these individuals?**

A Key Person Protection policy can help protect the profits of a business directly attributed to one or more individual(s) if they were to die or be diagnosed with a terminal or critical illness (if chosen) during the policy term. This may allow a business to continue without financial hardship while a replacement is found or member of staff trained.

It gives them breathing space to make the right decisions – not rushed ones.



# LOOKING BEYOND THE PERCEPTIONS.

We can see from the research that current perceptions of what could happen if a key person were to die, or is diagnosed critically ill, are in fact misguided and not aligned with the reality of a business being properly protected.

## ATTITUDES TO UNFORESEEN RISKS

- **Only 39%** mentioned the business owner or employee dying/being diagnosed with a critical illness.
- **27%** talked about the business being badly damaged by a fire.
- **Only 6%** thought being broken into would cause any impact (most likely because they already have insurance in place to cover such an eventuality).

## CURRENT PERCEPTIONS

After speaking to a number of businesses about the negative effects of a key member of staff dying or being diagnosed critically ill, we can see that current perceptions are somewhat confused.



## THE REALITY

From our research we can see that

# 53%

of businesses think they would cease trading in under a year after the death/critical illness of a key person. Many would struggle to find a replacement and could they fund the cost of replacing and getting their business back up and running.

# BETTER KNOWLEDGE, GREATER AWARENESS.

More than half of the businesses did not have Key Person Protection – it's not something they had ever thought about.

## REASONS FOR NOT HAVING KEY PERSON PROTECTION

**32%**

Not considered

**31%**

Not got round to it or looked into it

**28%**

Cost would be an issue

## OTHER REASONS

Too complicated, don't have adviser to help me  
Got enough additional staff

Of those who did not have Key Person Protection, we can begin to build the following profiles:

**72%** are sole traders or those with just one business owner (63%)

**77%** are smaller businesses with a profit of less than £50,000

**69%** have a value of less than £250,000

**66%** are all-female businesses

## KEY QUESTION:

**In the event of the death or critical illness of a key person or business owner, could a cash injection help secure the future of the business?**

If a cash injection is needed, has the business thought where this money would come from? Would a bank loan be possible?

Consider the timing of the finance – would the business know when this will happen? The following things may need to be considered:

- Will market conditions dictate the lending policy?
- What is the credit rating of the business if it has just lost a business owner or key employee that plays a key role in profits?
- What personal security may apply to any borrowing?

## WHO WOULD BE MOST AFFECTED?



### SOLE TRADERS

**73%**

think they would cease to trade immediately



### NEW BUSINESSES

**67%**

think they would cease to trade immediately

# SHARE PROTECTION.



## OVER 1/2

of businesses have left no instructions in a Will or any special arrangements regarding shares.

### WHY CONSIDER SHARE PROTECTION?

The loss of a business owner may destabilise a business and can quickly lead to financial difficulties. Share Protection allows the remaining partners, directors or members to remain in control of the business following the death of a business owner. If there is no share protection in place, the owner's share in the business may be passed to their family. This means that the surviving business owners could lose control of a proportion or, in some circumstances, all of the business.

The family may choose to become involved in the ongoing running of the business, or could even sell their share to a competitor. A Share Protection policy can help avoid these issues by providing the funds to purchase the shares and also a suitable mechanism for the existing shareholders to retain ownership of the business.

### KEY QUESTIONS:

**1. Would you want your estate to receive the value of your share in the business in the event of your death?**

Share Protection could help cover you for the value of your share in the business and give the other business owners the cash to buy the shares from your family/beneficiaries.

**2. If a fellow business owner died, would you want to retain total control of the business?**

Share Protection can be written under Trust, so that should one member in a business die or be diagnosed with a terminal illness, the remaining member(s) could receive a lump sum of money. This could enable them to buy the shares from the deceased member's estate and so maintain ownership of the business.

# ADDRESSING UNCERTAINTY.

The research sample highlighted a level of uncertainty when it comes to share protection and what would happen if a shareholder died.

**26%** said they would buy the business owner's shares, with most of this group saying they would raise the funds from the personal wealth of the remaining owners.

**21%** acknowledged that any beneficiaries of the business owner would become active in the business.

Other perceptions were that the beneficiaries would retain ownership and receive an income without taking an active role in the business, or that they would receive nothing and the shares would automatically be passed to the other business owners.

## PARTNERSHIP AGREEMENTS AND LIMITED COMPANIES ARTICLES OF ASSOCIATION

Another area where companies are leaving themselves exposed to unnecessary risk is partnership agreements. If it is a limited company, this would be their articles of association.

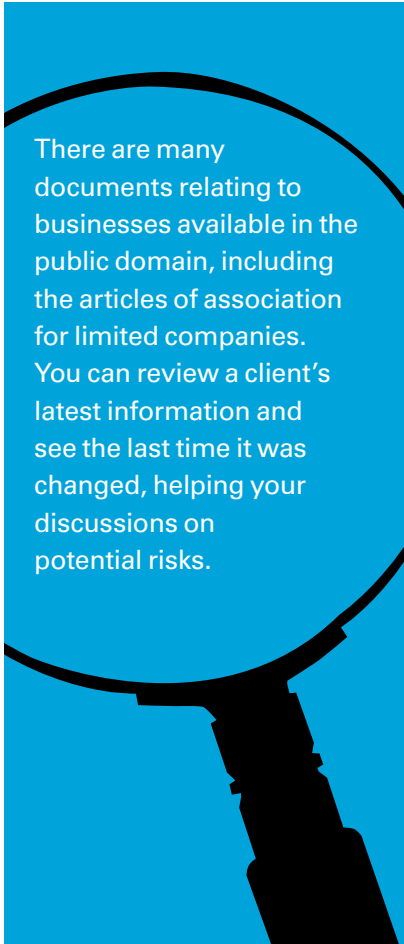
In fact, only **4/10** partnerships or limited companies have viewed these in the past year.

### AND WORRYINGLY:

**1/3**

of partnerships have not reviewed their partnership agreement since the business started.

of limited companies have not reviewed their articles of association since the business started.



There are many documents relating to businesses available in the public domain, including the articles of association for limited companies. You can review a client's latest information and see the last time it was changed, helping your discussions on potential risks.

### BUSINESS OWNERS WANTING TO BUY THE SHARES NEED TO ASK THEMSELVES SOME KEY QUESTIONS:

Would they have enough personal wealth?

Will a bank loan be available?

Will there be any reserves left over?

What value would they put on the shares?

# RELEVANT LIFE PLANS.

Although not a Business Protection product, a Relevant Life Plan is a term assurance plan available to employers to provide a lump sum benefit for an employee. It is designed to pay a lump sum if the person covered dies or is diagnosed with a terminal illness, while in employment during the term. A Relevant Life Plan is paid for by the employer. As with all insurance plans, limitations and exclusions apply.

## THIS PLAN IS AIMED AT:

- Employers looking to provide lump sum benefits, but with too few employees to set up a group scheme.
- Directors wishing to provide their own individual 'death in service' benefits in a tax-efficient manner.
- High earning individuals, such as directors, who are looking for lump sum benefits without affecting their Pension Lifetime allowance.

## COMPARING THE COST OF A LIFE POLICY TO A RELEVANT LIFE PLAN

		NON-RELEVANT LIFE PLAN	RELEVANT LIFE PLAN
ANNUAL PREMIUM		£1,000	£1,000
EMPLOYEE TAX	National Insurance contribution (assuming 2%)	£34.48	-
	Income Tax (assuming 40%)	£689.65	-
EMPLOYER TAX	National Insurance contribution (assuming 13.8%)	£237.93	-
	Less Corporation Tax (assuming 20%)	-£392.41	-£200*
TOTAL COST		£1,569.65	£800

A saving of **£769.95** which is a saving of almost 50%.

\*An employer that wishes to treat Relevant Life Plan premiums as an allowable business expense should speak to their accountant, who may want to liaise with the employer's local inspector of taxes.

This example is fictitious and provided for illustration purposes only.

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## DID YOU KNOW?

A Relevant Life Plan is a personal life insurance policy which can be treated as an allowable business expense, so the business would qualify for Corporation Tax relief. There's no additional Income Tax or NI to pay.



# AWARENESS OF RELEVANT LIFE PLANS.

There is a large opportunity to increase the awareness of Relevant Life Plans and it can prove a useful way to open the discussions with a business. Once the plan is clearly explained to companies, they do start understanding the benefits, with around half of them taking the policy out. Of those who haven't taken one, it's often because they either did not understand the product or did not know enough about it.



## THERE IS AN OPPORTUNITY

Of those who had not heard of Relevant Life Plans, 73% were receptive to the product after it was explained to them. Only 9% said they would definitely not take out cover.

### LEAST LIKELY TO HAVE HEARD OF A RELEVANT LIFE PLAN

**76%**

Small businesses with a value of under £250,000

**80%**

Businesses set up within the last two years

**86%**

Small business with profit under £50,000

**76%**

Small businesses with 1-10 employees

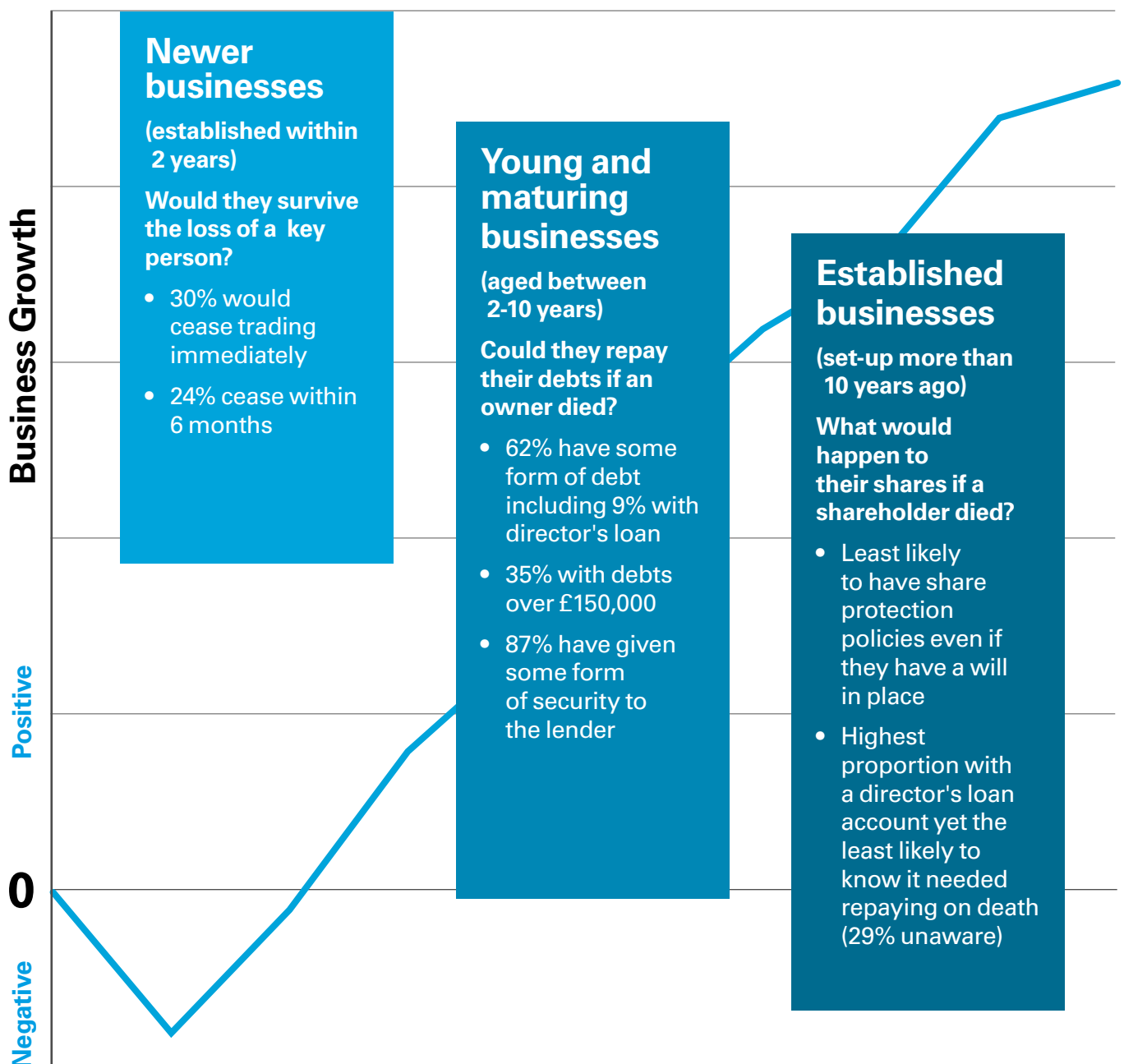


**30%**

HEARD OF RELEVANT LIFE PLAN

# CHANGING NEEDS.

As a business grows and goes through various stages of development the needs for protecting it will change. In the early stages of initial development it may be reliant on just a few key people, however, as it becomes more established then the use of loans will play a bigger part. Finally, as it moves to an established position or towards maturity then the continued ownership of the business will be a point for consideration. Our research has highlighted the changing needs (below) which can help businesses to identify their likely risks.





# FINANCIAL ADVICE.

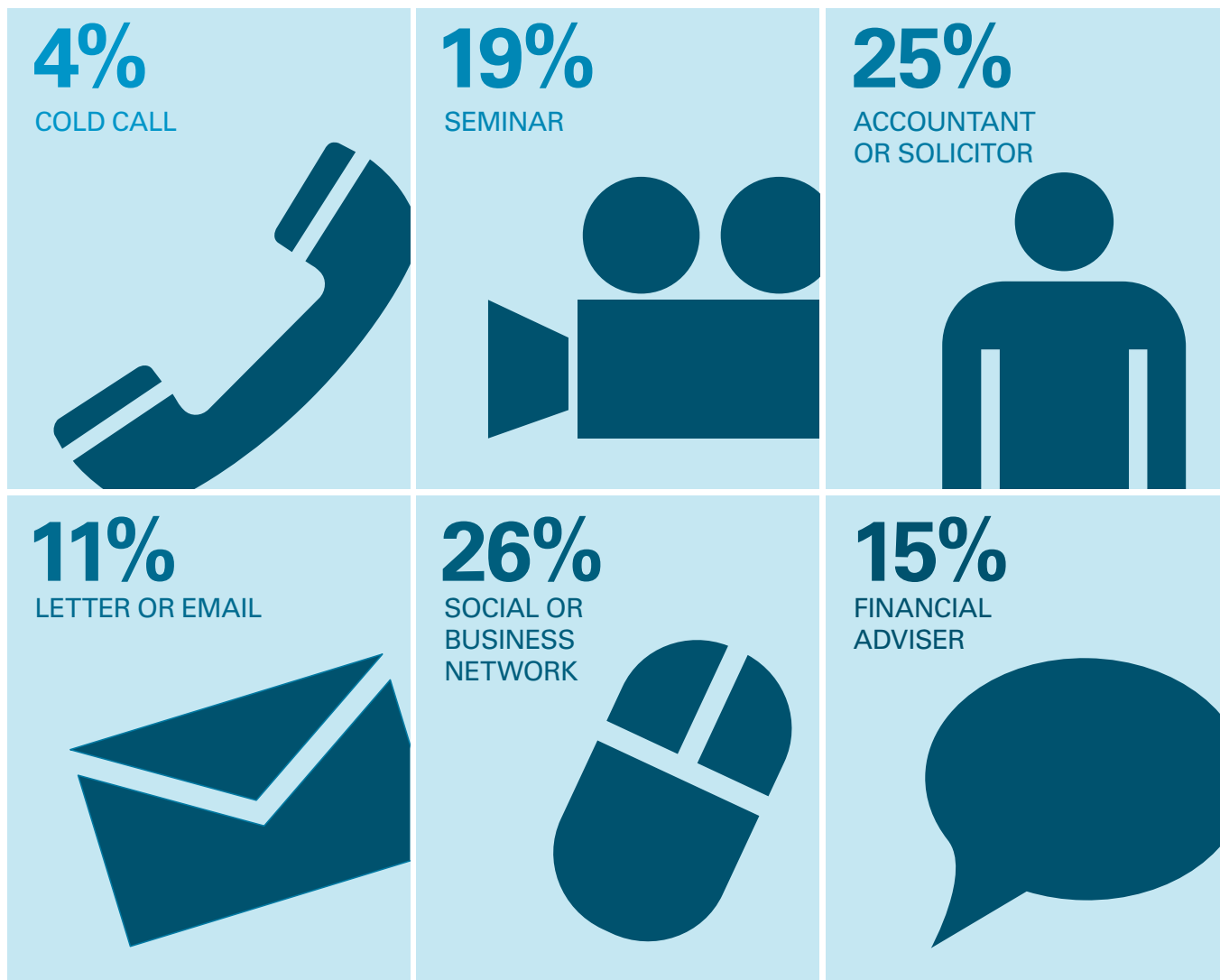
Financial advisers and accountants play an important role in prompting businesses to consider the benefits of business protection and the risk of not having cover.

For example, of those businesses who had Key Person Protection in place, the top three types of professional who brought up its value are listed to the right:

1	Financial adviser
2	Accountant
3	Solicitor

Of our sample, **only 56% had a financial adviser**; although most confirmed they would be happy to be contacted by one. A resounding **90%** of our sample expected to hear about the products from professional financial advisers.

## HOW BUSINESSES WERE CONTACTED BY A FINANCIAL ADVISER



# DIFFERENT TYPES OF PROFESSIONAL ADVICE.

The use of professional financial advisers varies by business type, value, tenure and gender mix of the business owners.

For example, we can see from our research that sole traders, those businesses valued under £250,000, those in existence for less than two years, or those with all female owners, are the least likely to use professional services outlined below. All businesses are more likely to have an accountant than a financial adviser.

## 86%

OF BUSINESSES HAVE AN ACCOUNTANT

## 52%

HAVE A RELATIONSHIP WITH A BANK MANAGER

## 45%

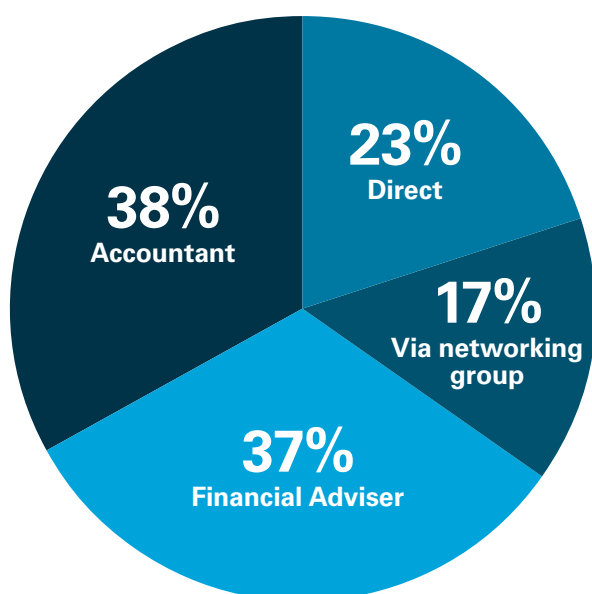
OF BUSINESSES HAVE A SOLICITOR

## 56%

HAVE A RELATIONSHIP WITH A FINANCIAL ADVISER



## HOW WOULD BUSINESSES PREFER TO LEARN ABOUT BUSINESS PROTECTION?



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### WHAT DOES THIS TELL US?

There are many different ways to start talking to businesses about business protection. It might be worth exploring businesses' other professional relationships, and look to collaborate with accountants, for example, as a way in to speak about this important cover.

# ▶ AT A GLANCE.

## BUSINESS LOAN PROTECTION

Two thirds of businesses have some form of borrowing, increasing over time - average value £176,000.

Most common types of borrowing over £50,000 are business loan, overdraft and Directors' Loan accounts.

For those who have protected their loans, 84% sought professional advice.

Of those who haven't protected their loans, around 1/2 of these didn't see the need and 1/4 haven't thought about it.

74% know a Director's Loan Account needs to be repaid on death – 97% of these are up to £250,000.

## KEY PERSON PROTECTION

Business owner and/or key person dying/ being diagnosed critically ill would have most impact on business

53% of businesses would cease trading in under one year (especially sole traders and new businesses).

Over 1/2 of businesses do not have Key Person Protection:

- Didn't think about this type of cover
- About 1/3 of all businesses think this is a risk they should have recognised themselves
- Those who have cover were advised to take it out.

## SHARE PROTECTION

Over 1/2 have left no instructions in their Will or special arrangements regarding shares in their business.

- Most never thought about it.

26% of shareholders would buy owner's shares.

- Most say they would use personal wealth to do this.

Only 4 out of 10 partnerships or limited companies have reviewed their partnership agreements or articles of association in the past year.

- 1/3 have never reviewed these since their business was established.

## RELEVANT LIFE PLAN

Only 30% have heard of a Relevant Life Plan:

- Just over 1/2 of these have taken out a policy
- Of those who didn't, most lacked knowledge/information
- When it was explained 73% were receptive to the product.

Among those who haven't heard of a Relevant Life Plan, only 9% said they would definitely not be interested.

Small business and those with up to 10 employees are least likely to have heard of Relevant Life Plan.

# NEXT STEPS.

**The one finding in our research which stands out beyond all others is that most business owners have never considered how the loss of a person may affect their business.**

"I think fundamentally that most business owners are too busy simply running their businesses that they simply have never considered the devastating effect losing a key member of staff or business owner can have. An amazing 53% of the businesses we spoke to in this research said that their business would fold within a year if they lost a key person or business owner.

Very much like family protection, death or critical illness and its implications are not a common topic of conversation around the board table. But it should be, along with what will happen if the office burns down, or the computer system was hacked. The death of a key person or business owner should form part of any business disaster recovery plan. Let's face it a computer or a building can be

replaced or rebuilt; the same is not always the case when it comes to replacing our human capital. Scottish-born **Andrew Carnegie** (1835-1919) who became an American industrialist and amassed a fortune in the steel industry then became a major philanthropist once said "Men and women, not machines are the real source of profits in any business."

The first step, that any business needs to take, is to seek out knowledge and then assess the risks to their business of these, unforeseen risks. Talking to an outsider can sometimes be the best course of action and this is when a financial adviser can really bear fruits. A knowledgeable and qualified adviser can explain what solutions companies like Legal & General can offer to help safeguard the future of UK businesses."

**Richard Kateley,**  
**Head of Intermediary Development**

## FIND OUT MORE

### FINANCIAL ADVISERS/PROFESSIONALS

Should you wish to know more about our range of Business Protection products, please speak to your usual Legal & General contact. Or visit our website:

**[www.legalandgeneral.com/business](http://www.legalandgeneral.com/business)**

### Sales Support

We offer a range of adviser and client-facing support material full of information about the business protection market. This suite of literature is available online on our Business Protection website along with:

- Range of online calculators which can assist you in the advice process
- Selection of short videos from our experts to help improve your knowledge and
- Business owner and adviser testimonial videos to help you in your approach with clients.