

## Sole trader Protection

### Important Note

**The information to follow is intended as guidance only and is not intended to provide taxation advice. In all cases the insured and the business should seek specialist taxation advice based upon their own specific circumstances. It should also be noted that taxation rules change and this guidance has been prepared based upon our understanding of current tax legislation at the release date. Zinc Insurance Services can accept no responsibility for actions taken as a result of this release.**

**Release date 28 February 2009**

### General Tax Guidance

The tax treatment of a policy will depend on the particular mix of benefits provided.

From the perspective of obtaining tax relief for insurance premiums, it is necessary to review the benefits which can be expected to be obtained. In general, tax relief is only available to a business if the expense is wholly and exclusively incurred for the purposes of that business. For example any part of a premium which is intended to provide a future benefit to the sole trader personally rather than the business, (as under the Sole Trader Protection cover) will not be allowable for tax purposes and is likely to "taint" the deductibility of the whole premium. HMRC may however allow a proportion of the premium as a tax deduction so far as it only relates to protecting the business but for Sole Trader Protection it is unlikely that the premium will be allowable.

The treatment for tax purposes of the proceeds arising from a claim will depend upon the terms under which the insurance payments are due. **In general, if tax relief is obtained for the policy premium then the insurance proceeds will be taxable.** Further guidance for each section under the policy is given below.

**As a general point where the cover reimburses a tax deductible cost of the business the overall position should be tax neutral.** There could however be a timing difference between the tax due on the insurance receipt and the tax relief due on the costs, particularly if those costs are not incurred in the same accounting period as the insurance proceeds are received (noting that reimbursement is usually paid a month in arrears).

## Sole trader Protection

Provides **protection to the sole trader's enterprise** by providing:

- a lump sum payment or
- monthly benefit (representing average salary)

following a disability to the proprietor who is permanently disabled or partially or totally disabled and unable to carry out his usual occupation.

To qualify for tax relief against the profits of a sole trader a cost must be wholly and exclusively for the purpose of the trade. As there is no differential between the sole trader and the business entity for tax purposes HMRC **usually regard the premiums as having an intrinsic personal benefit to the sole trader and so are not usually regarded as being allowable costs for tax purposes.**

**A lump sum or monthly payment for sole trader protection should not be taxed as income in the hands of the recipient as specific tax exemptions are available (ss735 to 742 ITTOIA 2005). Similarly any rehabilitation provided to the sole trader should not give rise to any tax implications.**

The lump sum receivable following the accidental death of the insured will however be included in the policyholder's taxable estate for inheritance tax purposes. **The policyholder should take specific inheritance tax advice for ways of mitigating any future liabilities (for example by writing the policy in trust).**

### Accidental Death

The cover will **pay the sole trader** a lump sum.

The lump sum is likely to be viewed by HMRC as compensation for a decrease in business profits arising as a result of the absence of one its key persons. The lump sum is therefore likely to be a taxable trading receipt of the company or partnership. Mitigation of the tax charge may be possible if the business utilises the lump sum by incurring qualifying expenses to replace the insured person.

**For sole traders accidental death cover for themselves may be tax exempt but in this case no tax relief will be available for the premiums paid.**

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