

# **When Accountants meet Financial Planners – How to Join Hands and Assists Clients**

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Organized by:

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# Business Succession

# Partnership Law

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- ◆ Partnership dissolves upon death of a partner
- ◆ Deceased's estate is entitled to share partnership asset

# Limited Liability Company and Joint Venture

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- ◆ Shares in a limited company
- ◆ Shares in a joint venture

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# What is Business Succession (“BS”)?

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- ◆ “Business Succession” is the process whereby the interest of a deceased’s Business is acquired by Co-owners, with the aim of bringing about the smooth continuation of the Business

## The Problem

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- ◆ What happens to a Small Business when one of the co-owners dies unexpectedly?
- ◆ What happens to the control of the Business?
- ◆ Can the surviving owners quickly get together enough cash to buy out the deceased person's interest at a fair and reasonable price?

## The Problem (Con't)

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- ◆ Will the surviving owners be forced into business with outsiders or with their former associate's heirs?
- ◆ Could the Business collapse because the survivors cannot get their hands on an immediate source of cash?
- ◆ Does the Business have to be sold in order to pay out the diseased's Estate?

# How does insurance policy help?

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- ◆ Insurance policy provides pre-agreed pre-estimated, ready fund for the purpose of business succession



# The Insurance Product

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◆ Term Life

Tax deductible – running expenses of business

◆ Endowment (?)

◆ Whole Life (?)

# The Answer

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A Term Life Policy

Plus

A Business Succession Agreement

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## How does Business Succession Operate?

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- ◆ The Business takes out a Policy on each co-owner's life and nominates itself as the Beneficiary.
- ◆ If an insured co-owner of the Business dies or retires the Proceeds are paid by the Insurance Company to the Business.

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## The BS Agreement

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- ◆ The BS Agreement should be signed by the shareholders / partners at the time of taking out the policies
- ◆ It sets out the arrangement in details and each co-owner

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## Tax

- ◆ Since the Business is the owner of each policy, and pays the premiums, each co-owner shares the total cost of all policies in proportion to his share in the Business

# Difference between Keyman Insurance policy

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◆ No legal definition

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## What is a “keyman insurance policy”?

- ◆ The employer takes out an insurance policy insuring against the loss of profits arising from the death, sickness or injury of a key employee
- ◆ The beneficiary is the employer

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## What is a “keyman insurance policy”? (con’t)

- ◆ In life insurance policy, it is a term insurance covering the life of the employee within the term of the policy, with no other benefits.
- ◆ The terms does not extend beyond the period of the employee’s usefulness to the employer.



# Are premiums deductible for profit tax? Are proceeds taxable?

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◆ Premiums : deductible

◆ Proceeds : taxable as trading receipts of the employer, being compensation for loss of profits (Arguable)

# Sole proprietor or Partnership

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- ◆ Premiums : not deductible as IRD would not recognize the policy as a genuine keyman policy.
- ◆ Premium is regarded as private expenses
- ◆ Proceeds: not taxable

# Limited company and the insured person is a director and a substantial shareholder

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- ◆ Premiums: not deductible (arguable)
- ◆ The policy is to protect the value of the shares

(Con't)

- ◆ The life/well-being of the director, being the keyman, would significantly affect the value of the shares
- ◆ IRD's view: Premiums is regarded as of a capital nature and shareholding of 20% is regarded as substantial
- ◆ Proceeds : not taxable

## Family members of the employee

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- ◆ Premiums: not deductible as the policy is not to compensate the employer's loss of profits but to protect the family of the employee
- ◆ Proceeds: not taxable

Christine M. Koo & Ip, Solicitors & Notaries

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# *Q & A Session*

## **PLEASE NOTE**

The law and procedure on this subject are very specialised. This article is a general explanation for your reference only and should not be relied on as legal advice for any specific case. If legal advice is needed, please contact our solicitors.

## **請注意**

本題目之法律及程序十分專門。此文章只屬一般性之解釋，供你參考，而不應被依賴為關於任何特定事件之法律意見。如需法律意見，請與我所律師聯絡。

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