Guide to buy/sell funding insurance ownership structures

Self-owned insurance	
Advantages / Benefits	**Disadvantages / Risks**
Simple: Easiest to implement and administer, maintain privacy and explain ownership structure to business owners.	Success depends on an effective buy/sell agreement: Insurance proceeds are paid to the departing owner (or their nominated beneficiary) as deemed consideration for the transfer of the ownership interest to the surviving owners. If there is no buy/sell agreement then the departing owner/beneficiary retains both the insurance proceeds and business ownership interest.
Tax effective: No CGT payable on life insurance proceeds if the recipient is the original owner of the policy (or they acquired the policy for nil consideration). CGT is not payable on TPD or crisis policies under this model.	Potential inefficient tax outcomes: Can result if an operating entity pays premiums on behalf of the business owners without declaring the amounts as salary or wages, dividends, or distributions (e.g. Division 7A provisions or fringe benefits tax liability may be triggered, or premium payment may be deemed a repayment of shareholder loan).
Flexible and portable: Owners departing the business can retain their policy for personal protection purposes, with no assignments or transfers of ownership required.	Perceived inequality: Some business owners may pay a higher premium relative to other owners in the group. (Note, this can be addressed in a number of ways).
Ease of administration: New owners coming into the business take out their own policy in accordance with the prevailing buy/sell agreement, avoiding the need for remaining business owners to alter ownership percentages of existing policies.	Perception and understanding of owners: The model is not necessarily a natural or traditional commercial transaction – each business owner is effectively funding their own buyout from the business.

Trust ownership (via the establishment of a special purpose insurance trust)	
Advantages / Benefits	**Disadvantages / Risks**
Taxation: In the event of a claim no CGT is generally payable on Life, TPD or crisis payments.	Costs: Unless a suitable trust exists, this model requires the establishment and ongoing maintenance of a trustee entity and trust deed.
Ease of administration: Multiple insurance policies are owned by a single entity, (either an independent trustee or one including a representative of each of the business owners), and administration of policies and premium payments are centralised.	Expertise and administration requirements: Appropriate trust structuring and distribution of any capital to relevant beneficiaries is required to ensure CGT free payments, particularly for TPD and crisis cover.
Certainty: Business owners may be confident in knowing that insurance proceeds will not be paid to the departing business owner (or their beneficiary) until the relevant ownership interest is transferred to the remaining business owners.	Portability: Unlike self-ownership, if an owner departs the business, the policy must be assigned/ transferred by the trustee in order to be retained by the departing business owner for personal protection purposes.
Flexibility: If a new owner comes into the business the trustee can simply take out a new insurance policy(s) on that owner's life - ownership of existing policies does not need to be altered.	

Superannuation fund ownership	
Advantages / Benefits	**Disadvantages / Risks**
Tax effective: Insurance premiums can be funded from pre-tax or tax deductible super contributions (subject to contributions cap).	Superannuation and taxation legislative risk: Legislative change may detrimentally affect the arrangement and there may also be a risk of breaching super laws such as the sole purpose test, or providing assistance to members or relatives.
Tax effective options post claim: A surviving spouse may retain the death benefit within super via the commencement of a death benefit income stream (subject to prevailing transfer balance cap).	Taxation: Tax will apply to the extent that a lump sum death benefit is paid to non-tax dependants. Tax may be levied on super benefits paid out prior to age 60 (e.g. if TPD proceeds are accessed on the grounds of permanent incapacity).
Retention and cash flow: Insurance premiums can be paid from accumulated retirement savings where necessary, minimising the impact on the client's cash flow and ensuring the policy stays intact.	Depletion of retirement savings: Premiums deducted from retirement accounts or contributions utilised to pay premiums rather than investing in assets may result in poorer retirement outcomes. The ability to supplement super account balances that fund insurance premiums, by making additional contributions, is limited due to reduced contribution caps.
	Inappropriate distribution of death benefits: Non-binding or invalid nominations may result in super death benefits being paid to unintended beneficiaries. (Note, this may be addressed through the use of valid binding death benefit nominations).
	Limited policy features: Since 1 July 2014, no new TPD 'own' occupation policies can be taken out within super. Nor is crisis cover available through super.
	Success depends on an effective buy/sell agreement: There needs to be a crediting provision in the agreement to ensure that when the departing owner transfers their ownership interest to the remaining business owner/s, there is deemed credit received in the form of the super proceeds that were paid out.

Cross insurance (Business owners jointly take out insurance policies on each of the other owners)	
Advantages / Benefits	**Disadvantages / Risks**
Easy to understand: There is a logical flow of cash in the event of claim as insurance proceeds are paid to the surviving business owner/s and are used to purchase the business interest of the outgoing owner.	Inflexible: If new owners come into the business, or an owner leaves, the ownership percentage interests in all the policies need to be altered via assignment.
	Taxation: Unless the business owners are related, CGT will be payable on TPD or crisis insurance proceeds.
	Success depends on an effective buy/sell agreement: It needs to enforce transfers and reduce any risk that the remaining owner/s will use the insurance proceeds to start a new business, leaving the departing owner with no insurance proceeds and an interest in a non-existent business.
	Portability: If an owner leaves, they are reliant on the other owners all assigning the policy across to them. This is important where the departing owner may no longer be insurable and wants to maintain the policy for personal protection purposes.

Company ownership	
Advantages / Benefits	**Disadvantages / Risks**
Cash flow benefits: Premiums can be funded directly out of the company's assets.	Inefficient tax outcomes for departing owner: It can be difficult to get the insurance proceeds from the company out to the departing owner (or their estate) tax effectively. This will generally require a share buyback or dividend, which is likely to provide a poorer tax outcome, at least compared to direct disposal of the business interest/assets by the departing owner.
Ease of administration: If a new owner comes into the business, existing policies do not need to be altered.	Inefficient tax outcomes for departing owner: This model may compromise the ability of the departing owner from taking advantage of small business CGT concessions they may otherwise have accessed had they sold their business interest/ assets directly.
	Inefficient tax outcomes for remaining owner/s: The cost base of their interest remains unchanged despite their overall equity stake in the company increasing follow injection of insurance capital proceeds.
	Taxation: CGT will be payable on TPD or crisis insurance proceeds received by the company
	Portability: If an owner leaves, they are reliant on the business entity (other owners) assigning the policy across to them. This is important where the departing owner may no longer be insurable and wants to maintain the policy for personal protection purposes.

Priority Protection and Priority Protection for Platform Investors is issued by AIA Australia Limited (ABN 79 004 837 861 AFSL 230043). This publication has been prepared for distribution to financial advisers only and is not for wider distribution. This information is current at the date of this publication and is subject to change. This provides general information only, without taking into account the personal circumstances of any individual and is not intended as financial, medical, health or other advice. AIA Vitality is available with eligible products issued by AIA Australia. For full terms and conditions of AIA Vitality partners, benefits and rewards, and to view the AIA Vitality Terms and Conditions and Benefit Guides see aiavitality.com.au. Partner terms and conditions may also apply. 04/17 – IAS3344