Kotak Life
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Life Insurance :: Corporate ::

FAQ's on Keyman Insurance Policy

1. What is a keyman Insurance Policy?

There is no legal definition.
In general, it has the following features.
An employer takes out an insurance policy insuring against loss of profits arising from the death, sickness or injury of a key employee.
The beneficiary is the employer.

In the case of a 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 term does not extend beyond the period of the employee's usefulness to the employer.

The purpose of taking out the insurance is to compensate the employer for the loss of trading income that may result from the loss of the service of the key employee in case of death, sickness or injury.

2. a) Are the premiums paid on the policy by the employer deductible for profits tax purpose? b) Are the proceeds from the policy taxable?

The premiums are deductible (provided the policy has the features as mentioned above).

The proceeds are taxable as trading receipts of the employer, being compensation for loss of profits.

3. If the employer is a sole proprietor or a partnership and the insured person is the sole proprietor or a partner, are the premiums paid on the policy by the employer deductible?
Are the proceeds from the policy taxable?

No, the premiums are not deductible.
Even though the policy may be named as a 'keyman policy', the Department would not accept that it is a real key man policy as described as above.

This is because **a keyman policy is applicable only in the case of an employer and employee relationship.** A sole proprietor or partner is not an employee. The premiums are regarded as private expenses. The proceeds are not taxable.

4. If the employer is a limited company and the insured person is a director who owns substantial shares in the company, are the premiums paid on the policy by the employer deductible? Are the proceeds from the policy taxable?

No, the premiums are not deductible.

The situation is, in substance, similar to the case where the insured keyman is the sole proprietor or a partner.
The Department considers that the purpose of the policy is to protect the value of the shares because the life or well-being of the director, being the keyman, would significantly affect the value of the shares.
The premiums are of a capital nature. In this connection, generally a shareholding of 20% would be regarded as substantial.
The proceeds are not taxable.

5. If the proceeds of a "keyman insurance policy" are payable to the family members of the employee or the employer is contractually required to pay the proceeds to the family members of the employee, are the premiums paid on the policy by the employer deductible?
Are the proceeds from the policy taxable?

No, the premiums are not deductible. The purpose of the policy is not to compensate the employer's loss of profits, but to protect the family of the employee.

The proceeds received by the employee's family are not taxable.

6. If the policy is not a term policy, but is a life policy carrying a surrender value or an endowment policy, are the premiums paid on the policy by the employer deductible?
Are the proceeds from the policy taxable?

(Now a day's only term plans are being offered as Key Man policy. This question is being answered, considering the earlier days, where in the benefit policies also were considered for key man).

No, the premiums are not deductible. They are regarded as expenditure of a capital nature.

The proceeds are not taxable.

7. **Sometimes, the policy may have an add-on element. For example, the employer pays extra premiums on top of the normal premiums so that on the death of the employee certain benefits (e.g. one year salary) would be paid to the family members of the employee. Are the whole premiums paid on the policy by the employer deductible?**
Are the proceeds from the policy taxable?

Only the normal premiums are deductible (provided the policy has the features as mentioned as above in A1).
The extra premiums are not deductible.

The proceeds received by the employer are taxable. The proceeds received by the family members are not taxable

8. **If the policy is an investment-link policy, are the premiums paid on the policy by the employer deductible?**
Are the proceeds from the policy taxable?

(Now a day's only term plans are being offered as Key Man policy. This question is being answered, considering the earlier days, where in the benefit policies also were considered for key man).

The premiums for the investment portion are not deductible because they are of a capital nature. Only the premiums for the risk portion are deductible (provided the policy has the features as mentioned as above in A1). An apportionment of the premiums is necessary.

The proceeds relating to the investment portion are not taxable. The proceeds relating to the risk portion are taxable.

9. If the employer is required under the law to pay compensation to the employee on injury or death etc. and the employer takes out an insurance policy to cover such legal obligation (e.g. workers' compensation under the Employment Ordinance), are the premiums paid on such policy deductible? Are the proceeds from the policy taxable?

Yes, the premiums are deductible, being normal business expenses. Such policy is not a keyman policy.

The proceeds are not taxable.

10. If the employer paid premiums on an insurance policy taken out for the purpose of providing funds to any person (e.g. one of the partners), in the event of death of an insured person (e.g. the other partner), to acquire partnership interests or shares of a limited company, are the premiums paid on such policy deductible?
Are the proceeds from such policy taxable?

(Note: Normally, the main purpose of such insurance arrangement is to prevent cessation of business by reason of the death of an owner of the business.)

No, the premiums are not deductible. The premiums are regarded as private expenses or capital expenditure. Such policy is not a keyman policy referred to in question1.

The proceeds are not taxable.