

FURBS

Effective remuneration planning for senior executives

When examining remuneration planning for your company you may wish to consider any arrangements which afford tax advantages as well as considerable improvements to pension arrangements for directors and key employees. FURBS (Funded Unapproved Retirement Benefit Schemes) may offer such opportunities.

What is a FURBS

Funded Unapproved Retirement Benefit Schemes are pension arrangements which were originally conceived to provide retirement benefits for senior executives in respect of their remuneration in excess of the earnings cap (£95,400 for 2002/03). They can also be used for a number of other purposes.

Who should consider using FURBS?

Any company which:

- pays bonuses
 - has capped executives
- or

- is in a start-up position

should consider how FURBS can meet its objectives.

Why are FURBS becoming more popular?

Recently the attractions of FURBS have become much wider. There has been increasing interest in establishing new FURBS, and in more effective use of existing FURBS.

For those joining approved pension schemes after May 1989, there is a cap (the Earnings Cap) on the earnings on which the fund pension can be based. Because increases in the Earnings Cap,

linked to RPI, have not kept pace with increases in salary, the number of capped senior executives is increasing rapidly. While it is possible for an employer to provide an unfunded promise, the funded alternative is becoming increasingly popular as the benefits that FURBS offer become more widely appreciated. FURBS are now seen as providing opportunities even for executives who are not capped.

Furthermore, FURBS are not affected by the charges announced in the November 2002 Green Budget on tax relief for contributions made to Employee Benefit Trusts and similar vehicles.

What are the issues for employers?

FURBS offer employers the opportunity for more creative remuneration planning. Most companies now have a mixture of capped and uncapped senior executives and they need to consider this imbalance. Compensating for the negative effect that the Earnings Cap has on executive mobility means that employers have to be able to offer a genuinely attractive policy on this issue if they are to attract and retain high calibre employees. Putting together such a policy involves addressing a variety of issues such as:



- Whether some form of alternative benefit should be provided, or whether salary should be adjusted.
- Whether the alternative benefit should replicate the main approved pension scheme, or whether a different set of benefits should be offered.
- How the appropriate level of compensation should be determined.
- Whether the disclosures required under the Combined Code will demonstrate a clear and consistent policy.

If an unapproved pension arrangement seems appropriate, employers need to identify whether a funded or unfunded arrangement best meets the needs identified. The two options are very different from the perspective of the employer and the capped executive.

Why is a FURBS often preferable to an unfunded arrangement?

- A FURBS establishes a fund of investments for the executive's retirement, which provides both security and flexibility. Unfunded arrangements are more suitable for replicating final salary promises, and are not as secure, flexible or portable.

- With a funded scheme the employee is liable to income tax on employer contributions as they are paid, so that final benefits, taken in lump sum form, are tax free. Benefits under an unfunded scheme are taxable as income.

What is the tax and National Insurance (NI) position of a FURBS?

- The employer obtains relief on the contributions paid, and the amount of the contribution will be subject to income tax under Schedule E for the employee at the time of the contribution. The employer can consider compensating the employee for this tax charge.
- The Inland Revenue's position has always been that contributions to a FURBS are subject to employer NI contributions. However following a recent court case, some doubt over this has arisen and a number of employers are lodging protective claims for recovery of NI, in case there is a change of policy by the Inland Revenue.
- The income accruing within FURBS will be taxed at advantageous rates.
- Capital gains arising within FURBS will be taxed at 34%, but subject to taper relief and the availability of an annual exempt amount.
- If the employee receives the benefits from a FURBS on retirement in the form of a lump sum this will generally be paid free of tax and NI.
- Inheritance tax is normally avoidable on FURBS.
- Benefits payable on death before retirement are free of tax and NI.

What other uses do FURBS have?

- There is no limit to the amount which can be contributed each year, or to the eventual benefits; the only requirement is that the scheme be for retirement purposes. Therefore once maximum benefits are provided by the approved scheme, unlimited additional contributions can be paid into a FURBS.
- Since the tax burden on the investments held in the FURBS is less than for personally held investments, in some circumstances FURBS contributions may be preferable to receipt of salary, bonus or other cash remuneration. This may be useful in the sacrifice of a bonus or of redundancy payments for high earners.
- A FURBS can be used as a tax effective vehicle for high net worth individuals, to hold shares or other securities.

Are FURBS suitable for expatriates?

FURBS are not normally suitable for expatriates outside the UK, as the tax position both in the UK and overseas is likely to be different from that mentioned above. Significant tax advantages could be obtained by using a different type of UK pension plan specifically designed for expatriates - see KPMG's factcard "Expatriate Pensions" for further details.

How can KPMG help?

KPMG's team of actuarial, human resource, pension and taxation professionals can provide a comprehensive service on all aspects of FURBS. We are able to help in each of the necessary stages:

- advice on how a FURBS could be used for particular companies and executives;
- design of contribution structure, to ensure appropriate benefit levels;
- determination of investment strategy and selection of fund manager; and
- preparation of the necessary documentation.

How can I find out more?

For further details, please speak to your usual KPMG contact or one of the following:

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