



STIRLING HOUSE A-DAY PREPARATION

From 6th April 2006, it will be possible for all types of pension schemes to invest in a much wider range of investments than they can now. However this will only be possible if a self-investment option is made available to you. Any investments are subject to the agreement of the scheme trustees or scheme administrator.

Investments: Key Facts

- Pension schemes will be able to invest in commercial property and Real Estate Investment Trusts.
- The Pre-Budget Report on 5th December 2005 announced that the tax advantages expected to arise from direct pension scheme investment in residential property and other esoteric assets (such as fine wine and art) will no longer be available. This effectively removes any attraction from holding such assets in a pension scheme.
- If you, or any of your family, use any of the assets held within your pension scheme (on a non-commercial basis), you will have to pay a 40% tax charge. Non-commercial use would include a family member using a property owned by your pension scheme as their business premises, but not paying the full market value rent.
- If your pension scheme makes a loan to a connected employer i.e. an employer connected to you, or your close family, you will have to pay a tax charge. The exception is an occupational pension scheme, which may loan up to 50% of the market value of the assets held to a sponsoring employer, provided the terms of the loan require that it is repaid within 5 years. However, a 5-year extension can be granted, if necessary. Any loan to a sponsoring employer should be secured, and made on a commercial basis.
- It will not be possible for you to take a personal loan from your pension scheme.
- The new rules will allow your pension scheme to borrow an amount equal to up to 50% of the net market value of the scheme. Any amount borrowed previously must also be taken into account when calculating the 50% limit. Before 6 April 2006 a higher level of borrowing may be possible under a Self-Invested Personal Pension.



Investments: Questions & Answers

Q: Can my pension scheme invest in property?

A: The new rules will allow for a registered pension scheme to invest in commercial property. While residential property is a permitted investment, the Government has announced that it will act to remove any tax advantages that would normally be available from investment through a pension scheme. This is likely to make direct investment in residential property through a pension scheme unattractive.

Q: How is commercial property affected when invested in a pension scheme?

A: The property will become an asset of the pension scheme, and cannot normally be released until you take your pension benefits. The same applies to any rental income generated by the property. If the property is made available to a member of your scheme, or members of your immediate family, it will give rise to a benefit in kind tax charge if rent is not paid at the normal commercial rate.

INVESTMENTS: CASE STUDY

Mike has a personal pension worth £70,000 and some paid-up benefits in an occupational pension scheme with a transfer value of £30,000. He plans to buy a commercial property next year and let it out to a local business. On the advice of his financial adviser, after completing a transfer value analysis, he transfers both funds into a new Self-Invested Personal Pension (SIPP). He also contributes £500 a month into his new SIPP. The property he is interested in will cost him £140,000 (including all legal and other fees). Under the new rules, Mike's SIPP can borrow an amount equal to 50% of his fund – provided that someone is prepared to lend it the money. If the SIPP borrows the full 50% to help purchase the property, the residual fund can remain invested in other assets.

Once let, the rent is paid by the business tenants straight into Mike's SIPP, with no income tax being paid. Of course, the loan used to buy the property must be repaid from the SIPP funds. The SIPP will also be responsible for paying any maintenance or other costs. By borrowing the full 50%, not all of Mike's SIPP will be invested in the property, helping him to spread the investment risk.

When Mike retires, he can choose to take unsecured pension from his SIPP, meaning that there may not be an immediate need to sell the property. (See FACTSHEET "Retirement Options"). As the SIPP is written under Trust, the value of the property should be excluded from his estate, therefore helping to reduce any potential Inheritance Tax bill on his death. However, potential changes to Inheritance Tax legislation from April 2006 could mean that inheritance tax is payable if unsecured pension or alternatively secured pension is chosen instead of an annuity.

When the SIPP sells the property in the future, there will be no Capital Gains Tax to pay as it is an asset of the pension scheme and not the individual.

Important Information

Please note that the information provided in this document is based on Stirling House Financial Services' understanding of existing and proposed legislation and HMRC practice, all of which may be subject to change in the future. The information is based on the assumption that tax legislation is not changed.