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Briefing note

Purchasing Commercial Property through your Barnett Waddingham pension

Commercial property is an allowable investment in both our SIPP and SSAS. Many of our clients take the opportunity to use their pension savings for direct purchases, whether from a third party or a 'connected' party (see below for more details).

Please note that this piece is for information purposes only and should not be construed as formal advice.

Depending on affordability, this can vary from owning several properties outright within your scheme, to joint ownership of one or more properties with another investor (which may or may not be another pension scheme).

Note that not all property investments are necessarily permissible. Most notably, investment in residential property would lead to heavy tax penalties being levied by HMRC.

Benefits of purchasing Commercial Property through your SIPP or SSAS

Investing in commercial property through a pension offers many advantages, including:

- Income tax and/or National Insurance relief on contributions to the scheme.
- Exemption from capital gains tax when the property is sold out of the scheme.
- Exemption from income tax on any rental payments received by the scheme.
- Increased cash flow and protection from potential creditors if property is purchased from you or your company.
- Joint purchase opportunities should your pension not have cash available for the entire purchase.
- The scheme can borrow up to 50% of its net fund value – another way of increasing its property purchasing power.
- When the time comes to draw benefits, the property can be sold and you can use that money to help fund your retirement.

"Property is generally indivisible and unlike shares, cannot be sold in tranches."

Drawbacks of Commercial Property investment via a pension

Potential drawbacks, along with possible solutions, that should also be borne in mind include:

- Property is generally indivisible and unlike shares, cannot be sold in tranches. In cases where liquid assets (such as cash) are depleted, clients should take care to ensure that pension contributions and rental income cover the payment of ongoing fees and any retirement benefits.
- Potential void periods can leave the scheme with insufficient cash to pay benefits and/or fund borrowing repayments, depleting the value of the scheme as a whole. Appointing a property manager and/or putting in place landlord's rental cover can help to manage this risk.

> “” If the purchase is subject to VAT, you should consider whether the pension scheme needs to be VAT registered and the property opted for tax.

- Clients largely invested in several commercial properties may find that all of their values drop at the same time, in line with the property market as a whole. Financial advice should be sought as to diversification amongst asset classes.
- Investing in property via your pension adds a layer of fees that wouldn’t apply to personal holdings. However, the above tax exemptions normally more than compensate for this.
- Connected party tenants must be treated at “arm’s length”, i.e. trustee(s) cannot stop charging rent solely on the grounds that their business is struggling.

Where do I start?

Once you have identified a property, the steps are:

1. Assess the financial feasibility – we can assist with this, if necessary. A valuation should be considered an essential part of the purchase process, (particularly if the vendor is a connected party – see information on “connected party transactions” below). You should consider how the purchase is to be funded (e.g. cash purchase, borrowing), allowing for legal fees, Stamp Duty, etc.
2. You are free to find a suitable solicitor, surveyor and bank (if appropriate) for your needs. Your solicitor will be the main point of contact for you: we will liaise with the solicitor directly. A solicitor who has experience of property purchase via pension schemes is advisable.

> **How we can help:**
> *We have carefully selected a panel of solicitors with extensive experience in dealing with property transactions across Scotland, England and Wales within a pension scheme environment; please contact your usual Client Manager for more information.*

3. Complete our Property Purchase Questionnaire (here for SIPP; available on request for SSAS) and submit it to us for our approval.
4. Address any environmental and/or energy performance issues identified by your solicitor.

> **How we can help:**
> *Please see here for more information on imminent changes to Energy Performance Certificate legislation and a convenient solution that we have arranged for our clients at a discounted rate.*

5. If the purchase is subject to VAT, you should consider whether the pension scheme needs to be VAT registered and the property opted for tax. Please note that we are not experts on VAT affairs. Your accountant should be consulted at this stage but, generally speaking, doing so will allow the scheme trustee(s) to reclaim the VAT paid on purchase, though will compel the trustees to charge VAT on rent, going forward.
6. Your solicitor will arrange for contracts to be exchanged and the transfer of the property to take place. We will review all legal documentation to ensure the trustee(s) of the scheme are protected against potential liabilities.

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> “”
> By paying too much for buying a property that they (or their wife, brother, son, etc) own, a client can effectively take extra money out of their pension scheme.

7. Ahead of completion, arrange for suitable building insurance to be put in place.

> **How we can help:**
> *Please see information about our comprehensive and highly competitive ‘block insurance policy’ solution below).*

8. A lease can then be put in place between the scheme and the tenant or, if there is an existing tenant in situ, the lease can be assigned to the pension scheme. From that point on, rental income will be payable directly to the scheme.

How long will the process take?

In our experience a property purchase is likely to take a minimum of eight weeks from the appointment of the solicitor to act on behalf of the scheme trustee(s), although in many cases, the transaction may take much longer.

The trustee(s) must also ensure that the finance is readily available when the purchase takes place. They must also ensure that the scheme is able to finance any extra costs if the property purchase is delayed.

What is a ‘connected party transaction’?

Wherever there is a ‘connection’ between a pension scheme and either the seller or buyer of the property, and/or the tenant, HMRC require us to keep evidence that the transaction has been carried out on “arm’s length” commercial terms. It is quite easy to see why this requirement is in place.

By paying too much for buying a property that they (or their wife, brother, son, etc) own, a client can effectively take extra money out of their pension scheme. Charging too little for selling a property would effectively be a ‘back handed’ contribution to the pension scheme, which would otherwise be tested against limits set by HMRC. The same is true of rental payments between pension schemes and connected parties.

We therefore ask clients to obtain professional independent advice, normally in the form of a property valuation, which in these circumstances, backs up the rental price, sale price and/or purchase price. We also ask that a surveyor is a member of the Royal Institute of Chartered Surveyors (RICS).

Are all property investments allowable?

HMRC impose heavy tax charges on pension schemes which invest in residential property, which more than cancel out the tax benefits detailed above. We undertake checks before we proceed with any property purchase to make sure that the property we are buying is strictly ‘commercial’.

There are some exceptions to this rule but generally speaking, if you can live in it, it’s residential. There are also properties that might at first appear to be commercial, but have a small part of them which could be considered residential.

Most commercial property or bare land will be acceptable. However, we might decide not to allow someone to buy a property if we think there is a risk to the pension scheme losing money, due to, for instance, environmental contamination problems.

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Further Information on acquiring/ owning a property can be found within our SSAS Property Purchase Guidance Briefing Note or our Flexible SIPP Property Guide.

Building insurance

All properties that are owned by our SIPPs and SSASs must have landlord's insurance in place.

This insurance will provide cover if a building is damaged; providing the SIPP or SSAS holds enough money to repair or, if necessary, rebuild it. The cost of this is based on the building's 'Reinstatement Value', which is usually provided in the property valuation. The policy also provides the trustee(s) with Public Liability insurance and Rental Cover.

To make things easier for both, our clients and ourselves, we now have a block (or 'group') insurance policy with Hettle Andrews - a Chartered Insurance Broker based in Birmingham. The policy provides comprehensive cover, including:

- £10m Public Liability Insurance;
- Terrorism Cover; and
- 36 months' rental cover.

We are able to produce a quote for a SIPP property within minutes, using a website that Hettle Andrews have created. If you are interested in receiving a quote, we will ask Hettle Andrews to produce a formal quotation for you. SSAS members should contact their usual Client Manager.

Ongoing property management

The trustee(s) are responsible for the management of the property, the collection of the rent and ensuring that the terms of the lease are fully adhered to. We would recommend that a Direct Debit or standing order payments are established wherever possible to reduce the risk of rent arrears accruing.

Should the trustee(s) wish to carry out any additional works on the property, it is important (particularly with listed buildings) that they contact us in advance to discuss this. In addition, consideration must be given as to whether such developments will sufficiently enhance the property's value.

Please contact your Barnett Waddingham client manager if you would like to discuss any of the above topics in more detail. Alternatively contact us via the following:

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0333 11 11 222
www.barnett-waddingham.co.uk