

Property purchase

Guidance Notes

This document is provided for use by professional advisers in conjunction with products provided by Talbot & Muir. The information in this document is based on our interpretation of the relevant HMRC guidelines, which are subject to change.

Overview

Investment regulated pension schemes (such as SIPPs and SSASs) can purchase certain types of real estate, either from the scheme member or their employer, or from an unconnected third party.

What types of property can a pension scheme purchase?

- Commercial property, including industrial units, offices, hotels, and certain types of permitted job-related residential property.
- Land, including agricultural property (but not including any residential accommodation, apart from where a specific exemption from the taxable property rules applies).
- Property in the process of being converted from commercial use to residential, or vice versa, provided the property is not suitable for use as a dwelling whilst owned by the scheme.
- Certain types of residential properties that have been specified by HMRC as being permissible investments, such as a hall of residence for students, or a home or institution for those in need of personal care by reason of disability, old age, etc.

A pension scheme can also pay for improvements and structural work to a property that it owns, but not for any tangible moveable property (e.g. chattels, plant and machinery), and an investment regulated pension scheme cannot purchase properties regarded by HMRC as residential. Both of these types of assets are taxable property if purchased by a registered pension scheme.

Registered pension schemes that are not investment regulated pension schemes (for example, most large occupational pension schemes) can purchase residential properties, as the rules on taxable property do not generally apply to them.

Can a pension scheme have a mortgage?

It is possible for pension schemes to borrow money to provide extra liquidity for any type of investment, including for a property purchase. The borrowing does not have to be secured, although a high street bank is unlikely to offer an unsecured loan to a pension scheme.

A pension scheme is limited to borrowing only up to 50% of the net value of the scheme assets at the point a mortgage is taken out. Although a fall in the value of the pension fund may mean that at certain points during

the lifetime of the loan this limit is exceeded, provided no additional borrowing is taken out the limit will not be judged to have been breached. Re-financing a mortgage, except where the terms of the new loan are substantially different, will also not trigger a test of the 50% limit.

If the 50% limit is breached (for example, where a pension scheme takes out additional borrowing) the excess is treated as a scheme chargeable payment subject to a 40% tax charge.

Does a property manager need to be appointed?

Although some scheme members may prefer to appoint a property manager to look after their property, and any service charges payable as a result can be paid by the pension scheme, we do not insist that a property manager should be appointed in every case.

We do require, however, that at all times the properties held by our pension schemes should be adequately insured.

Will the scheme member need to hire a solicitor?

A solicitor will need to be instructed to perform the usual local searches of the property, to identify any potential problems of which the pension scheme trustees should be aware. A solicitor will also need to draft the documentation relating to the transfer of the legal title of the property to the trustees, and if applicable they will need to draft a lease for the property.

The member may prefer to use their own solicitor for this process, but alternatively we have a panel of solicitors from which they are also free to choose. Even where the scheme member uses their own solicitor, however, if the purchase is being made via a SIPP the corporate trustees of the pension scheme will instruct one of our panel of solicitors to represent them in a checking capacity, for a reduced fee. This arrangement does tend to lead unavoidably to an element of double-billing and many scheme members prefer, therefore, that one of our panel of solicitors should represent both them and the corporate trustees.

If the purchase is being made via a SSAS, we are happy for the members' solicitor also to represent the corporate trustees of the scheme.

Environmental Risks

Before proceeding with a property purchase we will perform a desktop environmental survey of the site, to identify any environmental risks of which we need to be aware. If the survey highlights areas of concern, in many cases the existing owners of the property can provide suitable documentation (from the previous acquisition of the property) that will address those concerns adequately. In some instances it will be necessary for us to contact the local Environment Agency for details of any action they are planning to take in relation to the identified environmental hazards. This may necessitate that a more expensive insurance policy is put in place by the scheme members (although insurance premiums can be paid by the pension scheme).

An alternative arrangement available to SSAS schemes is to have the property purchased by the scheme subject to a Restriction of Title. The corporate trustees of the scheme will not be the legal owners of the property, and so are not liable for any expenses relating to the actions of the Environment Agency, but the property cannot be disposed of without our agreement. The members may still wish to make their own arrangements to identify and insure against environmental hazards.

Can a pension scheme purchase property that is owned by the scheme member?

Pension schemes are able to purchase assets from the scheme member and connected parties (including connected companies, such as the member's employer). However, it must be demonstrated to the satisfaction

of HMRC that any such purchase takes place “at arm’s length”. In practice this means that the pension scheme will have to purchase property from a connected party for its market value, as determined by an independent valuation. The same goes for the level of rent that the pension scheme should charge a tenant with a connection to the scheme member.

Can property be transferred from the member’s existing pension scheme?

A registered pension scheme can accept an “in specie” transfer of property from another registered pension scheme. Although many of the legal and administrative processes are the same as a normal acquisition, this is not treated as a disposal for money’s worth, and so there is no Stamp Duty liability (and the existing pension scheme is already exempt from CGT).

Taxation

Investments in property attract the same tax advantages as other investments held by registered pension schemes: any income received from the investment (i.e. rental income) is exempt from income tax, and any gains made on the disposal of the property by the pension scheme are free from Capital Gains Tax.

On the death of the scheme member any cash funds raised by the sale of the property are also normally exempt from Inheritance Tax, along with any other pension benefits. The same applies if, instead of being sold, the property is transferred directly from the pension scheme to the member’s beneficiaries.

However, the acquisition of property by a pension scheme is treated as a disposal for money’s worth, so certain tax charges may be incurred at the point of acquisition. The vendors of the property may be liable for CGT/Corporation Tax on any gains made from the sale of the property to the pension scheme, and depending on the value of the property the pension scheme may be liable for Stamp Duty Land Tax.

If the property purchase is subject to VAT then the pension scheme will also be liable for this additional expense, although a pension scheme can be registered for VAT to reclaim any VAT paid. Provided the normal conditions are met, a pension scheme can also accept a transfer of property as a going concern, which will mean no VAT is payable at the point of purchase.

The pension scheme may also be required to charge VAT on rental income, and account to HMRC for the tax charged.

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