



Exploring Pensions is designed and written for practising chartered accountants, with its focus pension issues of greatest interest to the owner-managers of privately owned businesses.

The authors, Mattioli Woods, specialise in this area of pensions consultancy, providing a trouble-shooting service for clients and advisers throughout the UK.

# Exploring Pensions

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## Pensions & property investment post April 2006

Our last news letter looked at the window of opportunity for property purchase within SSAS and SIPP under the current legislation. We now take a look at the opportunities available post A-day.

Whilst the pension changes due in 2006 are not set in stone, at Mattioli Woods we have looked (with caution) at the transactions our clients are keen to consider.

There is a common concern and perception that pension administrators can and do make hard work of property transactions, resulting in delays and, in some cases, deals have fallen through. With our bespoke approach, and the fact that we limit the number of schemes our account managers handle, we pride ourselves on our ability to push through transactions, often with tight timescales. So rather than react to the changes at the point of A-day,

Mattioli Woods is looking ahead to ensure procedures and guidelines are in place in good time, so that a property purchase under the new legislation can be completed promptly, without the concern of losing the purchase opportunity.

In addition to looking at the new investment opportunities following A-day, Mattioli Woods is also spending time reviewing clients' pension funds to check the appropriate action is taken to ensure the most advantageous protection is in place. This is most applicable for larger funds or for those with larger tax-free cash entitlements. Ultimately, this may involve restructuring the schemes.

The newsletter looks at a few examples of these issues to highlight the need for careful planning in the run up to A-day.

**Mattioli Woods**  
**Pension Consultants**



## A place in the sun – points to consider

There has been a lot of focus and interest regarding the ability of self-administered schemes to invest in holiday homes (both in the UK and abroad) after A-day.

Currently, individuals generally purchase holiday homes via a bonus/dividend payment from their company or with existing personal assets, all of which are taxed. This is why the relaxing of investment restrictions in pensions has caused raised eyebrows.

One of our clients who is looking to purchase a property in Croatia has been considering how to fund the transaction. His initial thoughts were to extract approximately £105,000 as a dividend payment from his company. In order to do this, the total cost to his company is £156,134. After discussing the situation with us, the client is delaying the purchase and planning to make an employer pension contribution of £105,000 (costing the company £105,000). In fact, a contribution could be made up to £215,000!

There are other things to consider when purchasing property abroad. The French and Spanish do not

recognise UK trust law and as such, foreign property will potentially be taxed on any income derived. If a property were to be purchased personally, the same tax would be applied. The only difference between these two situations is that, if the property were purchased personally, there would be no need for rent to be paid if the client occupied the property.

If the client purchased the property via a pension scheme, he would have to pay either the market value rent to the pension scheme or suffer a tax charge. Obviously, the first option would be the most cost-effective as the rent being paid would be used to enhance the client's pension benefits.

In summary, the obvious benefit is the tax-relief achieved from the company in order to purchase the property (in the above case, an initial tax saving of £51,134). In addition to this, even though European tax law does not recognise UK trust law, if on death the foreign property were to be reallocated to the next generation within the scheme, this would still be outside the scope of IHT, assuming the individual was still domiciled in the UK.



# A home for your pension scheme

From April 2006, pension funds can invest in residential property. The pension fund can buy from the open market, or acquire the client's existing buy-to-let properties.

Moving property from personal ownership to the pension fund can dramatically increase long-term gains due to the tax-relief available.

For example, a husband and wife who together earn £100,000 gross before tax own a buy-to-let property, with a tenant in situ, worth £200,000. They are able to pay a contribution of £78,000 (£39,000 each), where the pension fund then claims £22,000 from the Inland Revenue. The couple then have sufficient funds in their pension to purchase half the property.

They also obtain higher-rate tax-relief at 18% on the contribution they paid in the next self-assessment tax return - £9,000 each. The total tax saved amounts to £40,000 combining basic and higher-rate tax relief.

A similar exercise can be carried out in the next tax year, which will mean the pension fund acquiring the entire property.

The property held in the pension fund is exempt from tax compared with holding the property privately.

The pension fund has paid £100,000 for half the

property, which ends up in the clients' hands, which they can then use to repay the existing mortgage debt, either on a buy-to-let property or their own main residence. They can even use it to repay any debt taken out to make the pension contribution in the first place.

All rent received by the pension fund is gross (no tax). Holding property personally attracts higher rate tax, as the couple are both earning above the higher rate tax threshold. When they come to sell the property the pension scheme is not liable to capital gains tax.

On transfer of the property to the pension fund, stamp duty and capital gains tax need to be considered.

The latter depends on how long the property has been owned and how much it has increased in value.

However, given the tax-reliefs, including higher rate tax-relief, being received and the fact that the property value is being paid back in cash straight to the members, these need not be a problem.

The value of a property owned by a pension scheme will increase a lot faster than a personally held buy-to-let property because of the tax-reliefs, whereas capital gains tax would become due on a property held personally.



## Keep an eye on your property values

Mattioli Woods was introduced to a client with an existing SSAS, who wanted to obtain a second opinion regarding the issues affecting his scheme as a result of the introduction of the new pensions legislation. During our meeting with the client, it became apparent that the scheme's property, which represented its most significant asset, had not been valued for a number of years. In addition, the member's business had enjoyed healthy profits over the same period and, as a result, his pension fund was fully funded. This could be seen as an ideal position but, with the introduction of the new legislation, there are some very serious consequences if full consideration is not given to all aspects.

The client's existing adviser had already recommended he elect enhanced protection to mitigate the imposition of the lifetime limit, after April 2006. However, the proposed legislation stipulates that protection may only be granted to schemes to the extent that they are not over-funded. When we investigated the case further, it became apparent that the increase in value of the scheme's property meant that the client was substantially over-funded under current regulations, thereby preventing the client from adopting protection under the new regulations. What the client had believed to be a very secure position in respect of his pension scheme and impending retirement was in fact an over-funding problem, which ultimately can result in a significant tax liability.

Mattioli Woods then met with the client again, highlighted the problem and provided a solution.

The client immediately agreed to appoint Mattioli Woods as adviser to the scheme and we then set about resolving the situation. The first action was to assess in detail the scheme's current actuarial position, as the client's spouse and son were also members of the scheme. We then obtained a valuation of the scheme's property, which confirmed our previous assessment of its value.

Having determined the maximum amount of fund the client would be able to protect, Mattioli Woods advised that, through a combination of increased remuneration for the spouse and son, an adequate amount of fund could be reallocated from the father. The result is that the client will now be able to adopt enhanced protection for his entire fund share, with the excess being distributed to his spouse and son.

The most important issue to be drawn from this case study is the importance of thoroughly reviewing clients' pension arrangements in plenty of time prior to April 2006. This is particularly important for clients who have invested in property utilising their pension schemes, especially if the property has not been revalued in the past few years. Currently, clients may feel that they are in a suitable position to take advantage of the new legislation, but be completely unaware that their funds could be at a significant disadvantage unless appropriate action is taken.

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