

# HOW TO BUY COMMERCIAL PROPERTY USING A PENSION (SIPP) A REAL EXAMPLE

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Many property investors are now looking at making pension contributions from their company to their pension scheme. Pension schemes can't own residential property, but the 'next best' alternative for many people is to own a commercial property.

## Why are Pensions becoming More Popular with Property Investors?

1. The forthcoming (tax year 2018 onwards) mortgage interest relief restrictions will push many property investors into the Higher Rate (40%) of income tax. Making pension contributions helps to alleviate this by increasing the Basic Rate (20%) band. (This assumes the investor has 'net relevant earnings' from a PAYE job, or from a sole trade, to pay more than the standard £3,600 gross into a pension scheme).
2. More and more landlords are making use of a company to either purchase or manage property. Companies can make pension contributions of up to £40,000 per year and get 20% tax relief on the payment – meaning an £8,000 corporation tax saving.
3. Many landlords have dormant pension schemes from old employers, and often scattered in several schemes, which may amount to a sizeable amount. These funds can be consolidated and put to good use so that the investor gets some use of the funds prior to retirement.

As a result of all three reasons above, many landlords are now taking more of an interest in the tax benefits of a pension, and what they can do with the pension funds to invest in property.

## 1. Create and fund a SIPP

Find a SIPP provider who can accommodate the purchase of a commercial property, and transfer old pension funds and perhaps new funds into the SIPP to create a pot of investable funds. And, a SIPP can also borrow up to 50% of its value to boost its property-buying power.

TOP TIP

Friends can 'bolt' SIPPS together to boost their buying power and share risks and rewards. For example, myself and a school friend bought our office building by each creating a SIPP, and then pooling our funds to buy the office that Fylde Tax Accountants operates from (see pictures).



## 2. Find and purchase a property

SIPPs can invest in many types of commercial properties, with a popular choice being an office from which the SIPP-owner's business can be run. This enables the landlord to own the building they may operate their letting agency or other business from, and make use of their SIPP to benefit themselves directly.

TOP TIP

Choose a property that is currently being used as a commercial property, but that could be switched back to residential use in the future. Our own office was recently valued at over 50% higher if its use was switched back to residential – which we will do at some future point. See picture #1 – as you can see the building itself looks like a house, as it had previously been used as a house in the past (hence, getting planning permission to convert back is assured).

TOP TIP

Buying BMV (or, just getting a good deal) applies equally to commercial property purchases by a SIPP as to residential purchases. So look for motivated sellers and opportunities to add value. Our office was a doctors' surgery, and when we viewed, it smelled and was dark due to the many small consulting rooms. The doctors were desperate to sell and had few offers, so we offered around 65% of the asking price, as there were planning issues as well as a smell issue.



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## 3. Complete your refurb

Just like any property purchase, add value with a refurb – and, don't forget to leave sufficient SIPP funds available for the works. Bear in mind that your SIPP provider will be writing the cheques to the tradesmen, so use insured and reliable trades to complete the work (so, no 'cash in hand' types!).

TOP TIP

Refurb your commercial property with the tenant in mind – as ultimately a tip-top property means that an incoming business needs to spend less on getting the property to their spec, and so a higher rent can be charged. Businesses generally prefer to conserve capital for expanding their business (marketing, equipment etc) rather than spend 'dead money' on basic property costs.

## 4. Let and forget

Unlike residential property, commercial property is normally let on an 'FRI' basis: Fully Repairing and Insuring. This means that the tenant pays for general repairs and pays to insure the property. For many residential property investors, this comes as a revelation – no more tenant call-outs for leaky taps! However, the SIPP still has general responsibility for the building itself (eg the roof), although the tenant would typically pay for cosmetic works, tarmacking, etc.

Typical leases are for ten years with a five-year break clause, and there may be an 'upward only' rent review at specified intervals. Of course, as moving premises is often incredibly disruptive for a business, assuming that the tenant has a sound business there may not be a tenant change for many years, and the gross rent could be all profit with no deductions.

TOP TIP

If the commercial property has had an 'opt to tax' put in place by the vendor, then VAT would generally be payable on the purchase (assuming the property isn't to be converted to residential, which wouldn't be possible within a SIPP). So, an office on which VAT is payable on the rent would be more attractive to VAT-registered tenants. Also, bear in mind that VAT could be reclaimed on refurb costs by the SIPP (normally the SIPP provider would file quarterly VAT returns).

## Summary

Until recently, many property investors took little interest in pensions as part of their overall investment strategy. However with the new mortgage interest relief rules making pension contributions more attractive and with many investors already having pension funds languishing in existing schemes, using a pension to fund commercial property investment is an interesting, and tax-free, option to look into.

**DISCLAIMER:** Please note that this article is intended to provide a brief introduction to how a SIPP can be set up and used to fund commercial property investment. Nothing in this article is intended to amount to financial advice and you should seek your own independent financial advice before making any decision regarding your pension.

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