Hanbury Wealth Product Guide

Self-Invested Personal Pensions

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Self-Invested Personal Pensions

What is it?

Self-Invested Personal Pensions (SIPPs) are subject to the normal rules and regulations for registered pension schemes, but offer the freedom of choice over investment management, whilst keeping the administration in one place. This means that you are able to change the investment manager when you wish, without incurring the expense of changing the provider of the administration.

Additionally, you can achieve greater flexibility in the benefits you can take during retirement without necessarily having to transfer your funds again. You can elect to purchase an annuity or follow the route of phased retirement and / or drawdown pension. There is now no upper age limit at which benefits must be taken.

SIPPs are money purchase schemes with contributions receiving tax relief. An employer may contribute to an individual's SIPP, but this is not obligatory (unless being used to meet auto enrolment obligations). SIPPs can move with individuals when they change jobs.

Investments

You are free to give direct investment instructions, or more typically, indirectly via an appointed investment manager or adviser.

Most types of conventional investments are freely permitted including quoted stocks and shares, unit trusts, insurance policies and commercial property but there are some restrictions designed solely to prevent abuse. Any SIPP holding prohibited assets directly or indirectly will have all tax advantages removed which will broadly mean that it is at least no more advantageous to hold such assets in a pension scheme than it is to hold them personally. Prohibited assets include direct or indirect investment in residential property and certain other assets such as fine wines, classic cars and art and antiques.

If a SIPP directly or indirectly purchases a prohibited asset the purchase will be subject to an 'unauthorised member payments charge'. This will recoup all tax relief given on the amounts used to purchase the asset. This means that:

- The member will be subject to an income tax charge at 40% on the value of the prohibited asset
- The scheme administrator will become liable to the scheme sanction charge, which will usually be a net amount of 15% of the value of the asset
- If the set limits are exceeded the cost of the asset may also be subject to the unauthorised payments surcharge, which is a further charge on the scheme member of 15% of the value of the asset
- If the value of the prohibited asset exceeds 25% of the value of the pension scheme's assets, the scheme may be de-registered which would lead to a tax charge on the scheme administrator on the value of the scheme assets at the rate of 40%

Commercial property risk factors

Investing in commercial property involves considerable costs, such as legal fees and stamp duty land tax / land and buildings transaction tax / land transaction tax. However, any rental income received by the pension scheme will be free of income tax and gains will be free of capital gains tax. In addition, if a company rents property from its pension scheme, that company can normally deduct the rental payment as a business expense.

An investment in property does not produce a guaranteed return with rental income and market values being affected by general economic conditions and/or by the political and economic climate. Factors that could impact include employment trends, inflation, and changes in interest rates.

The use of borrowings will increase returns if the value of a property is rising but conversely, it will reduce returns if values are falling.

Investment in property is a long term one and at times, markets may prove to be illiquid. It may not therefore be possible to realise an investment at a time of your choosing and any forced sale could produce returns that are considerably below market valuations.

The failure of a tenant to meet the terms of any rental / lease agreement will adversely affect yields and possible capital values.

If a SIPP invests in residential property, it is likely to be classified as a prohibited asset and therefore subject to stringent tax charges.

Loans and borrowing

A SIPP may make loans to unconnected third parties, but not the members, provided they are on a prudent, secure, and commercial basis.

A SIPP will be able to borrow for any legitimate purpose intended to further the aims of the scheme and such borrowing will be limited to 50% of the scheme's net assets at that time.

Payment on death

The value of the pension fund is available to your beneficiaries on your death and can normally be withdrawn as a lump sum or left within the pension wrapper to be drawn on to provide a regular or ad-hoc income – further details are contained in the accompanying literature.

Death benefits, whether drawn as a lump sum or income, are normally payable free from income tax to your beneficiaries if you die before age 75 (in the case of lump sums, as long as they are within your available Lump Sum and Death Benefit Allowance). If you die after age 75, death benefits withdrawn as either a lump sum or income are taxable on the recipients as earned income.

Most pensions are currently free from inheritance tax. For deaths after 5 April 2027 the government intends that most pension death benefits will form part of the deceased's estate.

Eligibility

To be eligible to invest in a SIPP and receive tax relief on personal contributions, an individual investor must be under 75 years of age and resident in the UK (there are some exemptions for individuals who work for the UK Government or have left the UK in the last few years).

Contributions can also be made by your employer or a third party, for example parent or spouse.

Contribution limits

The minimum contribution will vary between providers but is usually around £20 per month, contributions can be stopped at any time.

Given the many tax advantages that are available with regard to funding a personal pension there are limits to the tax-relievable contributions that can be paid. Individuals are able to make contributions of up to the greater of £3,600 or 100% of their annual earnings to all of their pensions each tax year and receive tax relief on them.

There is an annual limit on the total amount of pension contributions that each person can make without incurring a tax charge (this includes employer and employee contributions). This is called the Annual Allowance. Where the total employer and/or individual contribution exceeds the Annual Allowance a tax charge will apply. Depending on your taxable income the excess pension savings can be charged to tax in whole or in part at 20%, 40% or 45% (up to 48% in Scotland). For the current tax year the Annual Allowance has been set at £60,000. However it may be possible for contributions in excess of the Annual Allowance to be paid in some circumstances under the rules which allow unused Annual Allowance from the three previous tax years to be brought forward and added to the current year’s Annual Allowance.

Individuals who have adjusted income (income plus employer pension contributions) for a tax year of greater than £260,000 will have their annual allowance for that tax year restricted. It will be reduced, so that for every £2 of income over £260,000, their annual allowance is reduced by £1.

The maximum reduction will be £50,000, so anyone with income of £360,000 or more will have an annual allowance of £10,000. High income individuals caught by the restriction may therefore have to reduce the contributions paid by them and/or their employers or suffer an annual allowance charge.

The tapered reduction doesn't apply to anyone with threshold income (income less personal / employee pension contributions) of no more than £200,000.

Taxation

Contributions to SIPPs generate direct tax savings. Contributions are made net of basic rate tax relief, which means that you will only actually contribute £80 net for every £100 of contributions paid. Higher and additional rate taxpayers likewise make contributions net of basic rate tax and can then claim additional relief via their Inspector of Taxes / Self-Assessment return.

Your pension contributions once made will be invested in funds where there is no liability to tax on capital gains and where all forms of investment income are also tax free. Your money may therefore grow faster in a Personal Pension than in most other forms of investment.

An employer is able to contribute and receive corporation tax relief on any amount that their local Inspector of Taxes is satisfied meets the ‘wholly and exclusively for the purposes of the business’ test.

All statements concerning the tax treatment of products and their benefits are based on our understanding of current tax law and HM Revenue and Customs’ practice. Levels and bases of tax relief are subject to change.

Withdrawals

The earliest age upon which you can take benefits is age 55. The minimum age will increase to 57 from 2028 with further increases expected as the State Pension Age goes up.

At retirement you have the option to take up to 25% of the fund as a tax free cash lump sum (within defined limits), the remaining funds will be taxed as income at your marginal rate(s) of income tax.

There is now no upper age limit by which retirement benefits must be taken.

There are no restrictions on people’s ability to draw down from their defined contribution pension pots after age 55, this will increase to 57 from 2028, this will allow flexible access to your pension savings.

This means there is no particular product that you must purchase or invest in when accessing your savings. It will be up to you to decide how you want to access them, either as a lump sum or through some sort of financial product.

Before 6 April 2023, if the total value of your pension benefits exceeded the ‘Lifetime Allowance’ the excess benefits were subject to a tax charge of up to 55%. The Lifetime Allowance charge no longer applied from 6 April 2023 and the lifetime allowance has been completely abolished from 6 April 2024. Instead, there are two new limits relating only to the amount of lump sum benefits that can be taken tax free, either during lifetime or on death. For most people the Lump Sum Allowance is £268,275 and this is the limit on the amount of tax free lump sums that can be taken during lifetime (at any age) and the Lump Sum and Death Benefit Allowance is £1,073,100 which covers tax free lump sums paid during your lifetime (at any age) and following your death if before age 75. If you have lifetime allowance protection, your limits will be higher. Any lump sum benefits that exceed available allowances are subject to income tax on the recipient.

Pension credit

Pension Credit is a State benefit that provides additional income to pensioners on a means tested basis.

The Guarantee Credit, available from State Pension Age, tops up weekly income to a prescribed level (£218.15 (for single people) or £332.95 (for couples – living together, not necessarily married) in 2024/25.

There used to be a savings credit element of pension credit but that was abolished for those reaching state pension age after 5 April 2016 (unless your spouse / civil partner had reached state pension age before 6 April 2016 and was already in receipt of savings credit).

The guaranteed element of pension credit will remain as a last resort for those who need it.

By the mid-2030s, the government estimates that over 80 per cent of people reaching their State Pension age will receive the full single tier pension which is set above the level at which Guarantee Credit would be payable. This means that the number of people eligible for Pension Credit will reduce over time.

If your estimated income in retirement means that you could be eligible for Pension Credit this might mean that some or all of the benefits from this pension plan are merely replacing income that you would have received via Pension Credit anyway.

The qualifying age for Pension Credit is gradually increasing as State Pension Age increases. It reached age 66 for all in 2020 and will have reached age 67 for all by 2028 with a further increase to at least age 68 expected in future.

Risk considerations

There are a number of risk considerations that need to be taken into account. It is important that you are aware of these.

- Past performance is no guarantee of future returns.
- The price of units and the income from them can fall as well as rise.
- Investment values may go down as well as up and you may not get back the full amount invested.
- Some investments, for example property may not be readily realisable and will be subject to market conditions at that time.
- This investment is intended as a long-term investment and under current HM Revenue & Customs' practice it is not normally possible to access the fund(s) prior to the age of 55 (this will increase to age 57 from 2028 with further increases expected as the state pension age goes up).
- The current tax treatment and annual contribution limits may change in the future.
- Please be aware that there may be occasions when an individual fund or funds may have a higher risk rating than your overall stated attitude to risk. If this is the case, then the overall risk rating applied to all of the combined funds being recommended is still designed to meet your stated tolerance.
- The illustration uses certain assumed rates of growth, as prescribed by the Financial Conduct Authority, these rates are not guaranteed.
- If you have accessed a pension plan of any type before 6 April 2024 and might benefit from increasing your tax free lump sum entitlement through obtaining a Transitional Tax-Free Amount Certificate (TTFAC), then if you take a Pension Commencement Lump Sum (PCLS or tax free cash sum) or Uncrystallised Funds Pension Lump Sum (UFPLS) on or after 6 April 2024 before obtaining a TTFAC you will have lost the chance to do so. This may mean a lower entitlement to tax free lump sums during your lifetime or for your beneficiaries if you should die before age 75 than might have been the case if you had obtained a TTFAC.