

A Whitechurch
Understanding Investment
Publication



A Guide to SIPPs

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This document has been prepared by the Investment Team of Whitechurch Securities Ltd which is the sister Company of The Whitechurch Network Ltd. Nexus Financial Planning is an appointed representative of The Whitechurch Network Ltd which is authorised and regulated by the Financial Services Authority.

Any views and opinions expressed are those of Whitechurch Securities Ltd and the intention of this document is to provide a guide to SIPP investing.

Introduction

A pension is, in all likelihood, the most important single investment that you will make in your lifetime. Why is it then that the vast majority of people place little emphasis upon maximising the performance potential of their pension investments?

One of the fastest growing areas in the pension investment marketplace is the Self Invested Pension Plan – or SIPP for short. Introduced in 1990, SIPPs are rapidly increasing in popularity as more and more private investors become disillusioned with the disappointing returns produced by traditional pension schemes.

What is a SIPP?

A SIPP is a type of pension that gives you greater choice and control over where you can invest your money. It is different to other pensions because rather than constrain you to a limited list of fund choices it allows you to select from a wide range of funds and investments.

A SIPP allows you to potentially select the most profitable investments available to provide you with the ability to maximise your returns. In other words, a SIPP is a pension that really works with you towards your retirement.

Similar in many ways to other personal pension schemes, a SIPP receives the same tax benefits, is subject to the same contribution limits and is available to employed and self employed individuals alike. The major difference it has to a conventional personal pension is that it has separate administrative and investment functions.

As with Personal Pensions and annuities, SIPP Wrapper are now regulated by the Financial Services Authority (FSA) and offer the protection of the Financial Services and Markets Act 2000,

Who should consider SIPP investment?

Everyone who is eligible for a personal pension is eligible for a SIPP, so the question is – why invest in a personal pension when you can invest in a SIPP?

Historically, SIPPs have been seen as expensive, high threshold products. However, since post pension simplification, administration and investment charges have reduced and so have the associated costs of running a SIPP. The effect of this is that the threshold for a cost-worthy SIPP is coming down too and that you now only need a fairly modest pension pot to access a cost efficient SIPP.

SIPPs can be considered for investors of all ages. They are ideal for those aged 20 and upwards who realise that they may have many different jobs and enjoys the flexibility that a SIPP offers because, for example, they are not required to set up a new pension each time they change employment.

A SIPP is also ideal for people who have been working in a number of different jobs where they have received pension benefits. The SIPP can be used to consolidate existing personal and company schemes by bringing them all under one roof thereby reducing administration, charges and allowing a clear investment strategy to be pursued.

A SIPP could also provide the solution for investors who have built up a significant lump sum to invest for retirement but who still want control over where this money is invested. SIPPs may be appealing to investors disillusioned by the performance of their existing pension plan. Many pensions schemes have traditionally been invested in With Profits – and area which has shown very disappointing returns in recent years.

Finally, investors who are keen to postpone buying an annuity can use income draw-down (see the section on benefits) to take an income and still offer the potential for the SIPP to increase in value after they retire.

Range of investments

The most attractive feature of SIPPs are the flexibility they provide regarding the choice of investments you can hold in them. The only restrictions are those imposed by law, or internally by the SIPP provider. The table below highlights the massive difference in investment options between SIPPs and personal pension contracts:

SIPP vs. Personal Pension

Type of investment	SIPP	Personal Pension
Unit trusts	Yes	Yes
Open Ended Investment Companies (OEICs)	Yes	Yes
Investment Trusts	Yes	No
Individual UK shares	Yes	No
Overseas shares	Yes	No
Insurance company investment funds	Yes	Yes
UK gilts	Yes	No
Corporate bonds and other fixed interest securities	Yes	No
Permanent interest bearing shares (PIBS)	Yes	No
Cash and deposit accounts	Yes	Yes
Commercial property	Yes	No
Traded Endowment Policies	Yes	No
Hedge funds	Yes	No
Traded options and futures contracts	Yes	No

Certain investments are allowable but are not attractive due to the high tax charges, residential property being the most common area.

After viewing the table above though it should also be noted that not all SIPP providers offer all of the range of investment options listed and some SIPP providers do not even offer a provision to hold commercial property.

Are SIPPs expensive?

With the Government's current emphasis on the provision of easy access, low charging pension plans, a key question asked about SIPPs are – do they provide value for money?

Naturally, SIPPs are not as cheap as stakeholder pensions, which are limited to levying a maximum annual management charge of 1.5% in the first 10 years reducing to 1% thereafter. But this also means that SIPPs are not as limited in what they can offer (as highlighted in the previous section).

SIPP costs can vary considerably between different providers but what you generally find is that the charge for the SIPP wrapper is separate from the contents – i.e. the pension administrators' charges are separate from the investment managers' charges. Because the administration and investment costs are separated, SIPP charges tend to be more transparent than with traditional pensions where everything is normally rolled into one, which makes it difficult to gauge if you are receiving value for money.

SIPPs can and do levy a wide range of charges and this is an important consideration to take into account, though it is not just about finding the cheapest. Charges are merited as long as you are receiving the service quality both in terms of the SIPP administration and the SIPP investment management.

As with any investment it is important to be clear regarding the charging structure of the SIPP before making a commitment.

Tax advantages

In the same way as all UK personal pensions, SIPPs provide a tax efficient way of investing to provide an income in your retirement and can prove a compelling way of reducing your income tax! The tax benefits are summarised as follows:

Summary of Pension Tax Benefits

- Contributions invested in a SIPP qualify for tax relief at your highest rate (see example below).
- Growth on investments inside a SIPP are free from capital gains tax and income tax (though tax on dividend income is deducted at source and cannot be reclaimed).
- At retirement you can choose to receive up to 25% of the total value of your SIPP as a lump sum that is completely free of tax.
- Contributions made by an employer into your SIPP qualify for corporation tax relief.
- In certain cases, like death, the total value of your SIPP can be paid to your dependents tax-free.

All taxation statements above are based on our understanding of current regulations. The bases, reliefs and rates of tax may change in the future.

Tax relief examples

	Basic rate, starting rate and non taxpayers	
Your net contribution amount		£ 2,808
Tax relief from government @ 22%		£ 792
Gross contribution amount		£ 3,600
	Higher rate taxpayers	
Your contribution amount		£ 7,800
Tax relief from government @ 22%		£ 2,200
Gross contribution amount		£10,000
	Plus	
Additional amount claimable on tax return @ 18%		£ 1,800
Your net contribution amount		£ 6,000

Pensions simplification – changes implemented as of 6 April 2006

Contributions

As from the 6 April 2006, the contribution limits have changed. There is now an upper limit for contributions in any one tax year for everyone and this is known as the annual allowance, which are as follows:

Tax year	Annual Allowance
2006/07	£215,000
2007/08	£225,000
2008/09	£235,000
2009/10	£245,000
2010/11	£255,000

However you will only receive full tax relief up to your current income, for example if you earn £30,000 you will only receive full tax relief if you contribute £30,000. You are able to contribute more than your salary but you will not receive tax relief.

If you do not have an income you can still contribute up to £2,808 net (£3,600 gross) per annum and receive basic rate tax relief of 22%.

In the year before you take your benefits there is no maximum contribution limit.

Lifetime Allowance

With effect from 6 April 2006 there is a maximum fund value you can have in your pension plan, which is as follows:

Tax year	Standard Lifetime Allowance
2006/07	£1.50m
2007/08	£1.60m
2008/09	£1.65m
2009/10	£1.75m
2010/11	£1.80m

If your fund value exceeds this limit there will be a tax charge of 55% of the amount over the lifetime allowance.

Transfers

You do not need to set up a new SIPP with a contribution. If you have an existing pension (or pensions) in place then you can transfer any benefits from your existing arrangements to a SIPP.

Transfers into a SIPP can be made from a variety of other personal or company pensions, without any limits on the amount you can transfer and irrespective of your level of earnings and employment status. However, a test may be applied in some circumstances where money has come from an employer's scheme.

Please note, at present you are not allowed to transfer the benefits from the State Second Pension (S2P) into your SIPP through contracting out. If you are in employment and do want to contract out you need to set up an appropriate personal pension (APP) or occupational pension. Self-employed people do not qualify for the S2P. This will change from April 2007.

Benefits

You can choose to take your pension benefits at any age between 50 and 75, irrespective of whether you have stopped working or not. (In special circumstances such as ill health it may be possible to take your benefits before 50).

This is changing though – from April 2010 the minimum retirement age will be 55 years.

The benefits taken on retirement can be done so in the following four ways:

Annuities

An annuity is a contract made with an authorised insurance company where they undertake to pay you a regular income for the rest of your life in return for all or part of your pension fund.

You can choose to take an annuity upon retirement. It is important to be aware that you are not restricted to using the insurance company that built up your pension to buy your annuity. It can be purchased on the open market in order to get the best rate.

There is a wide range of annuities available and it is important to seek independent advice before making a commitment.

Income Drawdown

In simple terms income drawdown allows you to take an income from your fund up until the age of 75 when you have the choice to either purchase an annuity or move to an 'alternatively secured pension' (see below).

Income drawdown within a SIPP allows you to take a flexible income to suit your needs, whilst retaining control of your capital. You can choose the amount of income you require, providing it comes within certain limits set down by the Government's actuary department. These limits are calculated every five years up until your 75th birthday. The amount you can drawdown will be dependent upon your age, fund size and current interest rates.

If you do take income drawdown and die before the age of 75, the capital within the SIPP is paid to your dependants – however, this is currently subject to a 35% tax charge.

Phased Retirement

Another option to receive your benefits is through phased retirement, whereby benefits can be taken all at once or spread over a number of years.

In this case your SIPP is split into pre-determined segments (typically 1,000) and each segment is treated separately. This allows benefits to be spread over a period of time between 50 and 75 depending upon personal requirements. This can prove tax efficient too as you can take ¼ of each segment as a tax free lump sum, to supplement draw-down or annuity income.

Alternatively Secured Pension

This is an option open to everyone over 75 who have decided not to buy an annuity.

It allows you to continue to make your own investment decisions about where the fund should be invested, without the requirement to purchase an annuity, with the hope that annuity rates will improve, or until your circumstances change when an annuity becomes more attractive.

The income limits will be between 90% of the Government Actuary Department Rates (GAD) the minimum income of 65% of the GAD Rates and will be calculated every five years.

If you die whilst taking Alternatively Secured Pension, there is no automatic return of fund. If you have a surviving spouse then the fund will have to pay an income. If you die without a spouse then the balance of the fund less a tax charge – possibly as high as 82%! – can be paid to another policyholder of the same SIPP, or tax free to a registered charity.

Do you need advice?

We hope that you find this guide useful and that it has gone some way in answering your questions regarding SIPPs. Our guide is quite in-depth but does not examine all areas of SIPP and pension investments, which can be a very complex area.

Ultimately, after reading this guide, if you feel that you need to seek expert, independent financial advice regarding SIPPs, other pensions and / or your investments or any decisions concerning these areas then we recommend that you contact us and ask to speak to one of our financial advisers.

To speak to one of our qualified financial advisers please call Nexus Financial Planning on 01278 439 494 or e-mail us at office@nexusifa.co.uk

Important notes – please read

This guide was prepared by Whitechurch Securities Ltd using sources believed to be reliable and accurate. The opinions are our judgement at the time of writing.

Do you need advice?

This publication contains product specific details only and unless we have complete up to date written details of your financial circumstances and requirements we cannot and will not offer any opinion as to the suitability of any investment for any client. Any response to this publication will therefore be on the basis that client specific advice has not been given. These investments are not suitable for everyone. If you have any doubt whether they are suitable, you should obtain expert advice.

Ensure you obtain and read the literature

It is essential before you consider purchasing any of the products mentioned that you obtain, read, and fully understand the Terms of Business and Key Features relating to the specific products(s) in which you are interested, as each have different risk levels and some are more volatile than others dependent on where and how they are invested. They also set out the risks, charges, cancellation rights and terms of the investment. Do not invest unless you have read this information.

Important notes

It is important to always bear in mind that any stock market and equity linked investment carries risk and are subject to market and economic forces and can go down in value as well as up. Past performance is not a guide to future returns and may not be repeated. Investment into the stock market, whether directly or indirectly should not be considered as suitable for short term investment. Where a fund has holdings in fixed interest securities, these are likely to be impacted by changes in interest rates and/or inflationary expectations. Where the main objective of the fund is to provide an income, the level of income is not guaranteed and can fluctuate up or down.

Overseas investments

You should also bear in mind exchange rate fluctuations may cause the value of overseas investments to fall as well as rise.

Taxation

Levels and bases of, and relief's from, taxation are subject to change. Please read the product prospectus carefully to ensure you understand how the investment product is taxed and how this may affect your personal tax position.



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