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Adviser factsheet

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SSAS or SIPP

Summary of key points

Introduction

This factsheet is designed to give an overview of the differences between a Small Self Administered Scheme (SSAS) and a Self-Invested Personal Pension (SIPP). It is the client's needs and circumstances which dictate the most appropriate vehicle for their retirement provision.

Features

- Structure
- Scheme Assets
- Loanback
- Final comment

Structure

SSAS

A Small Self Administered Scheme (SSAS) is an occupational scheme established under trust by the employer who is otherwise known as the sponsoring employer. It will have its own Pension Scheme Tax Reference (PSTR), which is a unique reference given by HM Revenue & Customs (HMRC) when the scheme has been registered for tax relief and exemptions.

A SSAS is normally limited to 11 or fewer members, and in many instances these individuals will be key employees, including directors of the sponsoring employer. Membership of the scheme is normally at the discretion of the sponsoring employer. Every member is normally a trustee, and is responsible for the running of the scheme as well as compliance with all legal, HMRC and regulatory requirements. It is not, however, a product regulated by the Financial Conduct Authority.

Where all members are trustees this gives the scheme certain exemptions from Department of Work and Pension requirements in respect of employer-related investments, such as purchasing shares in and making loans to the sponsoring employer.

While it is possible for the member trustees to act as scheme administrators, due to the onerous nature of the duties imposed on them, in many instances scheme administration and reporting requirements are delegated to an independent company, who will sometimes also act as an independent trustee. The scheme administrator's responsibilities include reporting certain events to HMRC. The appointment of an independent trustee does not remove all responsibilities from the member trustee.

The vast majority of SSASs are defined contribution; however there are some defined benefit SSASs. The latter is very much a niche offering, and with the introduction of the "pension freedoms" in 2015, their appeal has perhaps reduced further.

SIPP

The structure is usually one whereby a pension scheme is established by a Self-Invested Personal Pension (SIPP) provider, typically under trust, with each member holding an individual arrangement or arrangements under that scheme. It is fairly unusual to have an individual's SIPP separately registered with HMRC and with its own PSTR. The SIPP provider appoints a corporate trustee and under some schemes the members may be co-trustees but normally only in respect of the funds held under their own SIPP.

Members usually have little involvement in the day to day running of the scheme with all responsibility for running the scheme resting with the scheme administrator. This role is normally undertaken by the SIPP provider.

Comment

Under a SSAS, the client has three potential conflicting responsibilities; member, trustee and director. As well as fulfilling the role of a member trustee, the individual is concurrently fulfilling the roles of scheme member and company director.

Returning to trustee responsibilities regardless of whether or not an independent trustee has been appointed or not, the member trustee must:

- act in accordance with the trust deed and rules;
- act in the best interests of scheme beneficiaries;
- act impartially; and
- act prudently, responsibly and honestly.

This could have the effect that although legislation may permit an action or a particular type of investment, the scheme rules may preclude it, and therefore the rules take precedence. This can be exacerbated particularly in the case with a small business, where many directors are used to doing "their own thing". For example, where the business property is an asset of the scheme, the directors might want to spend capital on extending the property. Nevertheless, as trustees they could in theory deem it not to be in the best interest of the members, namely themselves, if the development failed to add or even detracted from the value of the property and thereby the scheme itself.

Failure to carry out trustee duties can lead to a breach of trust, which in turn can lead to personal liability. The liability is "joint and several", for example, if there are three trustees joint and several liability means that each trustee is liable for the whole amount and not just a third of the amount. However, bear in mind that being a trustee of the scheme, the member has a greater say in the running of the scheme (previous comments accepted about the duties and liabilities of being a trustee).

Under a SIPP, this conflict of interest is less of an issue, as although some arrangements allow the member to be a trustee, the responsibility for running the scheme will still rest with the provider. A SIPP may be more attractive for some individuals for these reasons.

Scheme Assets

SSAS

Traditionally assets are pooled and no individual member has a right to any particular asset. Investments are decided jointly by the member trustees, with potential input from the independent trustee if required, and agreement from all trustees on investment/disinvestment strategy is necessary. It is possible though to appoint a discretionary adviser to make decisions on behalf of the members.

With pooled funds the question is whether the investment strategy of the scheme is in line with each member's attitude to risk. Since 5 April 2006 it is not a requirement that assets are pooled though the scheme rules might still dictate this. If there is the freedom to do so, then it may be possible to earmark a particular investment(s) for a certain member. This option can therefore alleviate the potential problem of the 'pooled' investment strategy not satisfying each individual member's investment and risk profile.

A benefit of a pooled fund is where a particular investment has a high initial investment level, but under an earmarked arrangement the members do not have sufficient capital individually to access the investment.

SIPP

In a SIPP the assets are earmarked, and so the financial adviser can design the investment portfolio specific to the client's needs and attitude to risk.

Comment

Is a pooled investment an advantage or a disadvantage? Potentially it could lead to conflict between the members where there is disparity in their retirement needs and attitude to risk, but equally it could facilitate the scheme being able to invest in an asset with a value in excess of the individual member's own fund value. Also, if the scheme has the ability to earmark assets, then many of these potential conflicts could be overcome.

Whether assets are earmarked or pooled makes no difference in terms of the protection offered by the Financial Services Compensation Scheme (FSCS). Claims under the FSCS would be made by the trustees at member level. In determining the compensation due to members the FSCS will also consider members' personal exposure to the particular investments outside of the SIPP or SSAS.

Loanback

SSAS

A SSAS is able to lend money to the sponsoring employer, subject to a maximum of 50% of the net value of the scheme. There are certain conditions attaching to a loanback, but in theory it could be used for any purpose, such as to deal with short term cash flow issues, purchase stock or plant and machinery or even finance a purchase of commercial property. The only guidance HMRC gives on the loan is that it should be prudent, secure and on a commercial basis, and it is for the trustees to ensure that the loan is in keeping with the spirit of the legislation and is used for the benefit of the scheme. Where there is a professional scheme administrator and independent trustee, they are likely to insist on additional checks and balances before agreeing to the loan.

For a loan from a SSAS to a sponsoring employer to be an authorised employer payment it has to satisfy the following five criteria:

- maximum of 50% of net fund value;
- secured as a first charge on an asset that is of at least equal value to the amount of the loan including interest;
- interest must be charged at no less than 1% above the average base lending rate of six leading High Street banks;
- the loan must be repaid in equal instalments of capital and interest, and
- a loan term not exceeding five years.

In many situations these loans do not proceed due to the inability to find a suitable asset as security. Often companies have borrowing through their bank and the bank in turn has a floating charge over the company's assets. It is therefore not possible for the SSAS to have a first charge on a company asset and so the loanback criteria cannot be met. The security doesn't have to be a company's asset though it cannot be a scheme asset, so one option is for the directors to use a personal asset as security. However, there are risks associated with this approach, for if the company defaults on the loan, the director loses their personal asset and if the asset was what is termed "taxable property" then the scheme would suffer penalties for holding this type of asset. An example of taxable property is residential property.

If any of the conditions are not met regarding a loanback, then an unauthorised payment results. The tax charges that apply are the unauthorised payment charge at 40% and the scheme sanction charge which is also charged at 40%. However, if the former is paid then the scheme sanction charge is reduced. The reduction is the lesser of either 25% of the unauthorised payment or the tax paid by the recipient of the payment; the combination of the two charges equates to a 55% tax charge if the unauthorised payment charge is met in full.

There is the potential for another charge where an unauthorised payment has been made. If a registered pension scheme makes an unauthorised payment to a member or sponsoring employer a surcharge will also be payable if the amount of the unauthorised payment exceeds 25% of the fund value. The unauthorised payments surcharge will be 15%, bringing the total unauthorised payment tax charge to 55%, to reflect the higher level of tax relief likely to have been received on such a large amount of the scheme's fund. If the scheme sanction charge is added on top of this then the total tax charge becomes 70%.

SIPP

A SIPP, which is not an occupational scheme and therefore does not have a sponsoring employer, cannot make loans to connected parties. If the SIPP member is connected to the company, then any loan to the company would result in unauthorised payment charges, the tax consequences of which were covered previously.

Comment

The financial crisis of 2008 and subsequent tightening of legislation and guidance for banks has led to many of them restricting their lending, particularly to small businesses. The ability of a SSAS to lend money to a sponsoring employer is one of the reasons for SSASs resurfacing in people's consciousness.

Final comment

The question of whether a SIPP or a SSAS is more appropriate for an individual comes down to their circumstances and needs. It is an advice issue rather than a legislation question and will therefore dictate a full understanding of the particular client's circumstances and their hopes for the future.

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