

Case study

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Borrowing for a second property

Summary

An investor would like to purchase a second commercial property, but is unsure how much she can borrow.

The Challenges

Katarina has held a commercial property - an industrial unit - within her SIPP for several years. The property is worth £500,000 and has an outstanding mortgage worth £80,000. Katarina currently uses the rent to make mortgage payments and pay the SIPP's fees. She doesn't leave much of a surplus.

Katarina also has a workplace pension with another provider. She has not consolidated her pensions as her employer can only contribute to the workplace scheme. Katarina also contributes to the workplace scheme as it's simple for her employer to pay the contributions from her salary.

Katarina has been very happy with the property investment in her SIPP. A smaller neighbouring unit is now on the market for £150,000 and Katarina would like to purchase it using her SIPP. She arranges a meeting with her adviser Conor to discuss the plan further.

The Actions

Katarina initially asks about transferring some funds from her workplace pension in order to fund the purchase. Conor confirms that this would be possible. However, doing this would leave Katarina's overall pension provision very heavily invested in property. He thinks it would be better for her to leave the workplace pension as it is.

Katarina then asks about further borrowing, as she is aware that the SIPP can borrow up to 50% of its net fund value. Conor confirms that this is the case.

Katarina asks Conor how much she can borrow, as she tried to quickly work it out before the meeting but is unsure the calculations are correct. At first, she thought that as the property is worth £500,000, she could borrow £250,000 in total. As she already has a mortgage of £80,000, Katarina thought this would leave her able to borrow £170,000 more.

However, Katarina had then realised that the property value is not the same as the SIPP's net value: this would be the

property value minus the loan. Katarina then thought that if the SIPP's value is £420,000, this would mean she could borrow £210,000, but this didn't sound right either, especially as it was more than the first amount she'd calculated.

Conor explains that the calculation involves elements of both of Katarina's approaches. She's correct in thinking that the SIPP's net fund value is the property value less the loan: £420,000. While this gives overall borrowing capacity of £210,000, Katarina then needs to deduct the existing loan again, leaving further borrowing capacity of £130,000.

This won't give Katarina enough cash to purchase the new property, particularly as she will also need to fund costs such as solicitor fees through the SIPP.

Conor suggests that Katarina should leave her workplace pension untouched, and make a single personal contribution to her SIPP to make up the shortfall.

Results

Katarina pays the personal contribution and Conor makes the arrangements for the new loan. Katarina's SIPP provider is happy to work with the high street lender of their choice. Katarina continues to regularly contribute to her workplace scheme, but is happy to know that she could make a personal contribution or part transfer to the SIPP if it needed additional cash.

Important points to consider

The value of pension funds may fall as well as rise. Your money is tied up until you take your benefits. Benefits can generally be taken any time after age 55. Always take financial advice to find out if a SIPP is suitable for you.

Contact details

If you'd like to speak to us about anything on this fact sheet, please contact us on:

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We may record and monitor calls. Call charges will vary.

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