

Promotion of home ownership

Pension fund and residential property /

Withdrawing or pledging Pillar 2 assets
for purchasing residential property



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Raising capital to purchase a home /

Financing is the first and last hurdle that needs to be overcome when acquiring residential property. If the available funds are insufficient, an advance withdrawal or pledge of Pillar 2 assets may well be an alternative worth considering. In other words, the scheme to promote home ownership opens up a range of options, provided the consequences are manageable.

Advance withdrawal or pledge

Under the Swiss Federal Law on Occupational Retirement, Survivors' and Disability Benefits Plans (BVG), there are two options for using Pillar 2 assets when purchasing residential property for own use:

- Withdrawing Pillar 2 assets in advance (own capital)
- Pledging the claim to pension benefits (borrowed capital)

The assets may be drawn from the mandatory or the extra-mandatory part of the occupational benefits plan, or from vested benefits policies or accounts.

Use of Pillar 2 assets

Pillar 2 assets can be withdrawn or pledged for the following purposes:

- Purchasing or constructing owner-occupied property
- Investing in a home
- Repaying a mortgage
- Purchasing shares in a building cooperative or similar investment

However, such assets may not be used to finance normal maintenance work on residential property or to pay mortgage interest.

Own use

Withdrawing Pillar 2 assets is permitted only for investments in property being used by the owner. Residential property must therefore be used at the domicile or usual place of residence.

Rental

Renting the property to a tenant is permissible only if there is proof that the owner is temporarily unable to use it himself, e.g. for professional or health reasons, or because of having moved away for a specified period.



Property abroad

An advance withdrawal or pledge for purchasing residential property abroad requires the owner to have his domicile there or to use it as the usual place of residence.

Vacation homes

Pension fund assets may not be used to finance a vacation home.

Own capital through advance withdrawal /

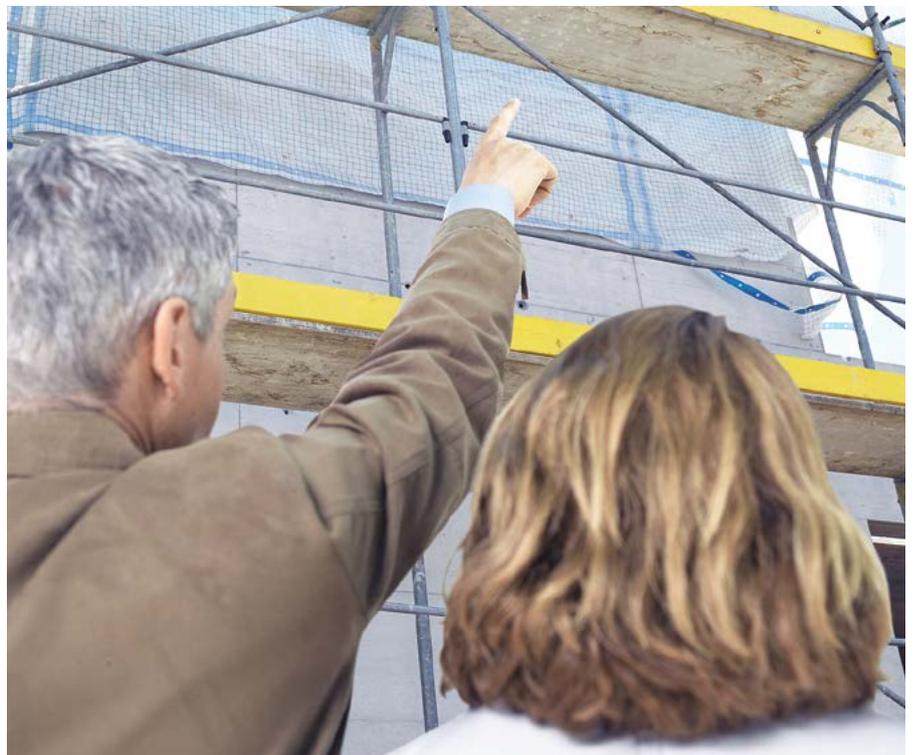
An advance withdrawal is one of two possibilities of using Pillar 2 assets to fund residential property. Increasing the equity portion will lower the interest burden, but also harbors certain risks.

Implications of advance withdrawal

An advance withdrawal is one way of raising capital. Because the borrowed amount is lower, the mortgage interest will be lower as well. On the other hand, only a smaller amount in interest can be deducted for tax purposes. If, for example, the property must be sold below its value because of a divorce or because the owner has lost his job, he may face a situation that threatens his livelihood. In general, an advance withdrawal will reduce the future pension benefits.

Reduced benefits

The occupational benefits institution provides information on the amount of the reduction. Any reduction in coverage for the risks of disability and death may be compensated by taking out private insurance (Pillar 3). On the other hand, the full original pension coverage can be restored by repaying the advance withdrawal separately.



Limits

In the case of an advance withdrawal, the occupational benefits institution will pay a cash amount up to the maximum in vested benefits.

Minimum amount

The minimum advance withdrawal is CHF 20,000. However, this limit does not apply to share purchases in building cooperatives or similar investments or to vested benefits policies or accounts.

Maximum amount

Up to age 50, the advance withdrawal may not exceed the accrued vested benefits. From age 50, the amount withdrawn can equal the vested benefits at age 50, or half of the current vested benefits, whichever is greater.

Payment

The occupational benefits institution will pay the amount to the creditors (seller, lender, builder, etc.) no later than 6 months after the advance withdrawal was requested and the necessary documents were submitted. The Swiss Federal Tax Administration is notified automatically about any advance withdrawal within 30 days. If the advance withdrawal will be used to repay a mortgage, the occupational benefits institution may, in the event of a shortfall in coverage, limit the amount of the payment or even refuse it altogether. In this case, it will inform the applicant of the duration and scope of the measure.

Restriction

An advance withdrawal is possible only up to 3 years before regular retirement.

Sale of the residential property

A sales restriction is entered in the land register in order to ensure that the advance withdrawal continues to serve the original purpose. The restriction stipulates that the advance withdrawal must be repaid to the occupational benefits institution if the property is sold. The occupational benefits institution must have this restriction entered in the land register when it pays out the advance withdrawal.

Taxes

Tax notification

The occupational benefits institutions must notify the tax authorities of the advance withdrawal. This notification then forms the basis of the assessment. The amount is taxed automatically at both the federal and the cantonal level.

Annual taxes

The advance withdrawal is entered as a lump sum payment that must be declared as income; however, it is subject to a preferential annuity rate. The tax must be paid to the authorities at the place of residence at the time of the withdrawal. Both the federal government and the cantons levy an annual tax on advance withdrawals. The tax must be paid to the canton (regardless of the duration of the tax liability) as well as to the federal government as a single amount. The advance withdrawal may not be used to pay the tax.

Tax rate for benefits

In general, taxes on advance withdrawals are assessed separately from other income. Whether or not an advance withdrawal is assessed at the annuity rate or the special rate depends on the canton of residence.

Rate for annuities

The Swiss Federal Tax Administration publishes a table that is used to convert the advance withdrawal into a lifelong pension. The rate that applies to this imaginary pension then becomes the basis for the tax.

Special rate

The advance withdrawal is taxed below the normal tax rate.

Tax amount

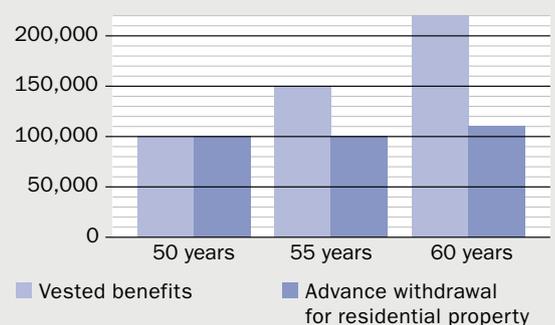
The tax rate depends on the tax base of the community and may vary from year to year.

The following may help in estimating the tax burden:

- Contacting the tax office at the place of residence
- Calculating an approximate amount in tax using the online tax calculator. Information can also be obtained directly from the cantonal tax office over the internet.

The maximum advance withdrawal for residential property equals the total in vested benefits only until the person reaches age 50.

Ratio of vested benefits to advance withdrawals



Rules on repayment /

As soon as the conditions for an advance withdrawal are no longer met, the amount must be repaid to the occupational benefits institution.



Mandatory repayment

The repayment obligation applies if

- the property is sold, in which case the proceeds (sale price less any mortgage-secured debt and taxes) must be repaid.
- rights to the residential property resembling a sale are granted to a third party (e.g. rental, residential privileges, usufruct right).
- no occupational benefits are due on the death of the insured person. (This scenario, however, is rare because occupational benefits also involve payments of accrued retirement assets to surviving dependants or legal heirs.)

Exceptions

The repayment obligation does not apply if

- the property is sold and the proceeds are reinvested in the purchase of another owner-occupied residence within 2 years. The amount withdrawn can be deposited in a new vested benefits policy or account.
- using the property has been proven to be impossible for a certain period, (e.g. for professional or health reasons, or because the owner has moved away for a specified period). During this time the property may be rented out.

Voluntary repayment

In principle, the amount withdrawn can also be repaid voluntarily to the occupational benefits institution. Here, certain restrictions must be observed, which also apply to the repayment obligations.

Restrictions

The following restrictions apply to mandatory as well as voluntary repayment:

- Repayment is possible
 - up to 3 years before retirement;
 - until another insured event (disability or death) occurs;
 - until the vested benefits are paid out in cash.
- The minimum repayment amount is CHF 20,000. If the remaining amount is smaller, it must be paid as a single installment.

Effect on pension coverage

By repaying the advance withdrawal, the insured benefits under the occupational benefits institution's regulations will increase.



Tax implications

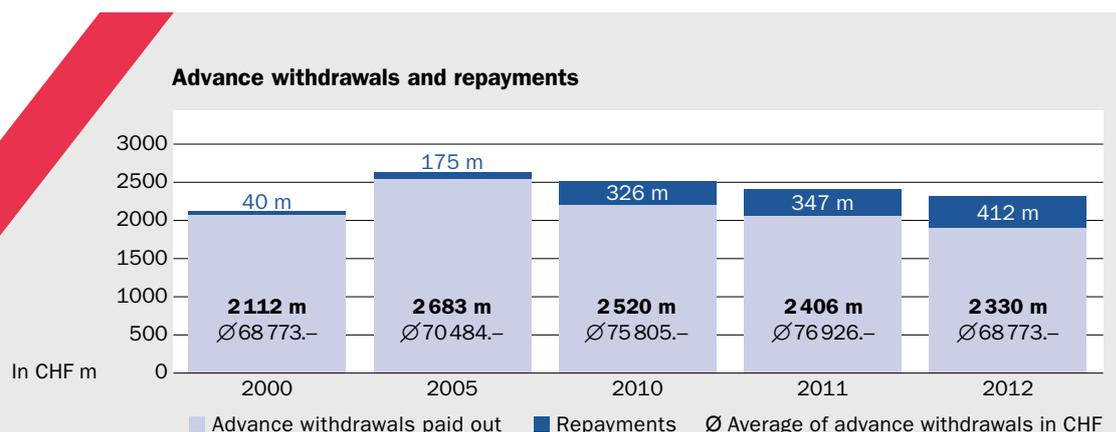
The occupational benefits institution will notify the Swiss Federal Tax Administration of the repayment within 30 days and issue a form as confirmation. This form is needed when reclaiming taxes paid on the advance withdrawal from the cantonal tax authorities. The tax amount paid at the time will be refunded without interest. The repayment itself cannot be deducted from the taxable income.

Tax refund

The first step involves submitting a written request to the cantonal tax authority that levied the tax on the advance withdrawal. They will also indicate to which cantonal authority the following documents must be submitted:

- Confirmation of the amount repaid (issued by the occupational benefits institution at the time of the repayment)
- Confirmation of the pension capital still invested in the residential property (issued by the Swiss Federal Tax Administration upon written request)
- Confirmation of federal, cantonal and local taxes paid on the advance withdrawal (issued by the Swiss Federal Tax Administration upon written request)

A tax refund can be claimed within three years following repayment of the advance withdrawal. After 3 years, entitlement to a refund lapses.



Source: FSIO 2013

Borrowing capital through a pledge /

A pledge is the other option for raising capital from your Pillar 2 account. The main criteria in this decision are the tax advantages and the fact that benefits remain unchanged.

Consequences of a pledge

A pledge provides borrowed capital. Because the property is now largely financed with borrowed funds, the interest due on the debt will increase as well. On the other hand it gives rise to certain tax advantages, while your retirement benefits as well as insurance coverage under your occupational benefits plan remain fully intact. A pledge leads to reduced pension benefits only if it is realized.

Types of pledge

There are two types of pledge, which can also be combined. Pledge of the claim to occupational benefits (retirement, disability, death):

- The pledge holder bears the risk of occupational benefits being paid. If they lose their validity, the pledge becomes worthless for the pledge holder. This type of pledge is not an option for vested benefits policies or accounts.
- Pledge of vested benefits (currently accrued retirement assets): The pledge holder bears no risk. Realizing the pledge is guaranteed.

It is also possible to agree a higher mortgage loan or lower interest rate with the pledge holder.

Maximum amount

- Up to age 50: the maximum in vested benefits currently available
- As of age 50: the maximum in vested benefits at age 50 or half the vested benefits currently available, whichever is greater.

The loan or pledge contract can include a provision whereby the amount in question adjusts continually to changes in vested benefits.





Asserting a claim

The pledge becomes valid only when the occupational benefits institution has been notified in writing. It needs to be informed in good time of any intentions regarding a pledge so that it can clarify the purpose and prevent multiple pledges. In general, claims to occupational or vested benefits can be pledged for purchasing residential property for up to 3 years prior to retirement.

The pledge holder's consent

The pledge holder's written consent is needed in the following cases:

- When vested benefits are paid out in cash
- When occupational benefits are paid out
- When transferring a proportion of the vested benefits to the occupational benefits institution of a divorced spouse

If the pledge holder refuses to give his consent, the occupational benefits institution must collateralize a corresponding amount. The judge will decide on the pledge holder's claim. The former institution must inform the pledge holder in case of a change in occupational benefits institution.

Consequences of a pledge being realized

When realizing a pledge, a distinction must be made between realizing vested benefits and realizing pension benefits.

Realizing a pledge on vested benefits

The pledged vested benefits amount is forfeited, whereby the situation becomes the same as in the case of an advance withdrawal. This, in particular, means a reduction in the occupational benefits on retirement, disability or death.

Realizing a pledge on occupational benefits

The pledged pension or lump sum benefit is forfeited. However, the pledge on retirement benefits can be realized only once the benefit has matured. This means, for example, that the pension becomes due only when the insured reaches retirement age.

Estimating the financial burden /

The decision of whether to build or purchase a house or condominium requires careful consideration.

Own capital vs. borrowed capital

Using these possibilities and assuming a certain amount of risk or leaving the occupational benefits untouched is a decision that must be made individually. In each case, however, all the facts must be included in the process.

Rule of thumb

The annual mortgage interest, repayment amount, and any ancillary costs incurred through owning the property should never exceed one-third of the gross annual income.

Sample affordability calculations

| Value of property (in CHF) | 400 000 | 600 000 | 800 000 | 1 000 000 | 1 200 000 |
|---|---------------|----------------|----------------|----------------|----------------|
| Financing | | | | | |
| Deposit (20%) | 80 000 | 120 000 | 160 000 | 200 000 | 240 000 |
| First mortgage 66.67% | 266 680 | 400 020 | 533 360 | 666 700 | 800 040 |
| Second mortgage 13.33% | 53 320 | 79 980 | 106 640 | 133 300 | 159 960 |
| Total costs | | | | | |
| Interest on first mortgage 5.0%* | 13 334 | 20 001 | 26 668 | 33 335 | 40 002 |
| Interest on second mortgage 5.5%* | 2 933 | 4 399 | 5 865 | 7 332 | 8 798 |
| Repayment of second mortgage (15 years) | 3 556 | 5 332 | 7 109 | 8 887 | 10 664 |
| Ancillary and maintenance costs, 1% of the property's value | 4 000 | 6 000 | 8 000 | 10 000 | 12 000 |
| Total annual costs | 23 823 | 35 732 | 47 642 | 59 554 | 71 464 |
| Total monthly costs | 1 985 | 2 978 | 3 970 | 4 963 | 5 955 |
| Affordability | | | | | |
| Required gross income | 71 473 | 107 207 | 142 940 | 178 680 | 214 413 |

* Affordability is calculated using predicted long-term interest rates, not current interest rates. These calculation principles are used in almost exactly the same way by all lenders (banks and insurance companies).

Next steps /

When considering the possibilities offered under the homeownership scheme, the decision hinges on the concrete numbers provided by the occupational benefits institution.

Detailed information

The occupational benefits institution will review the following if requested to do so in writing:

- What Pillar 2 assets are available for purchasing residential property? This amount is generally also shown on your personal insurance certificate or statement.
- What benefit reductions result when making an advance withdrawal or realizing a pledge?

In order to evaluate the tax consequences of an early withdrawal, it is best that you contact your tax office directly.

Procedure

Once the decision has been made to raise capital with funds from the occupational benefits plan, it becomes necessary to convince the occupational benefits institution of the venture.

Written request

A written request must be submitted to the occupational benefits institution when making an advance withdrawal or a pledge. Persons who are married or living in registered partnerships must also obtain written consent from their spouse or partner. The occupational benefits institution may charge a fee for processing the application.

Required documentation

The following documentation must be submitted to the occupational benefits institution to prove how the funds and the property will be used:

- Contract documents (when purchasing or constructing residential property or repaying a mortgage)
- Regulations or the rental lease or loan contract with the building cooperative association concerned (when buying shares in a cooperative)

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*in German, French and Italian

All consequences
must be considered
when making decisions
on financing.

Advantages and disadvantages at a glance

| | Advance withdrawal | Pledge |
|---------------|------------------------------------|--------------------------------------|
| Advantages | Lower mortgage and interest burden | Lower tax burden |
| Disadvantages | | Unchanged pension benefits |
| | Higher tax burden | Greater mortgage and interest burden |
| | Reduced pension benefits | |

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