

J02

Diploma in Financial Planning

Unit J02 – Trusts

October 2011 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2011/2012, unless stated otherwise in the question, and should be answered accordingly.

Assume all individuals are domiciled, resident and ordinarily resident in the UK unless stated otherwise.

Instructions

- Two hours are allowed for this paper.
- **Do not begin writing until the invigilator instructs you to.**
- **Read the instructions on page 3 carefully before answering any questions.**
- Provide the information requested on the answer book and form B.
- You are allowed to write on the inside pages of this question paper, but you must **NOT** write your name, candidate number, PIN or any other identification anywhere on this question paper.
- The answer book and this question paper must **both be handed in personally by you** to the invigilator before you leave the examination room. **Failure to comply with this regulation will result in your paper not being marked and you may be prevented from entering this examination in the future.**

Unit J02 – Trusts

Instructions to candidates

Read the instructions below before answering any questions

- **Two hours** are allowed for this paper which consists of 15 short answer questions and carries a total of 130 marks.
- You are strongly advised to attempt **all** questions to gain maximum possible marks. The number of marks allocated to each question is given next to the question and you should spend your time in accordance with that allocation.
- Read carefully all questions and information provided before starting to answer. Your answer will be marked strictly in accordance with the question set.
- You may find it helpful in some places to make rough notes in the answer booklet. If you do this, you should cross through these notes before you hand in the booklet.
- It is important to show all steps in a calculation, even if you have used a calculator.
- If you bring a calculator into the examination room, it must be a silent battery or solar-powered non-programmable calculator. The use of electronic equipment capable of being programmed to hold alphabetic or numerical data and/or formulae is prohibited. You may use a financial or scientific calculator, provided it meets these requirements.
- Tax tables are provided at the back of this question paper.
- Answer each question on a new page and leave six lines blank after each question part.

Subject to providing sufficient detail you are advised to be as brief and concise as possible, using note format and short sentences on separate lines wherever possible.

Attempt ALL questions

Time: 2 hours

1. State **five** ways in which a trust may be created. **(5)**

2. Wendy received a large inheritance in September 2009. She now wants a significant proportion of this inheritance to be held principally for the benefit of her two children who are aged three and five and any future grandchildren.

Wendy does not want to benefit in any way but wants to retain control over when, and to what extent, the beneficiaries can have funds made available in the future. She also wants the option of others being able to benefit. A discretionary trust has been recommended.

Explain in detail the advantages to Wendy of this type of trust. *Do not comment on the tax treatment of the assets entering or within the trust.* **(10)**

3. Alan, aged 45, is divorced and has two minor children, John and James. He has an estate worth approximately £450,000 and is concerned that he needs to make provision for his children or any other beneficiaries should he die.

Describe briefly the advantages of a Will trust by comparison to reliance on the intestacy rules. **(6)**

4. Elsie holds the life interest in a trust set up by her late husband 20 years ago. The remaindermen are Elsie's three grandchildren all aged under 12. Elsie's two brothers have indicated that they now wish to retire as trustees, and two further trustees are being appointed in their place.

Describe briefly:
 - (a) the criteria that the two new trustees must satisfy to enable them to act as trustees; **(2)**
 - (b) the investment strategy that the trustees of this life interest trust should consider; **(5)**
 - (c) what specific factors the trustees should consider before investing into a life investment bond. **(3)**

5. Describe briefly the tax treatment of transfers of both capital and regular payments to a registered charity:
 - (a) on gifting to a registered charity; **(4)**
 - (b) in the hands of the trustees of the registered charity. **(4)**

6. State the **five** key principles regarding decision making on which the Mental Capacity Act 2005 is based. **(5)**

7. Marcus has a progressive degenerative muscular illness and seven years ago he granted Enduring Power of Attorney (EPA) to his brother, Lawrence. Marcus has an adult disabled son, Vincent, who lives independently with support from a local charity.
- (a) Explain when Lawrence would be able to start using the EPA. (4)
 - (b) State what action Lawrence needs to take if he believes that Marcus is becoming mentally incapable. (2)
 - (c) Explain what restrictions are placed on Lawrence if he wishes to make gifts on behalf of Marcus. (6)
8. Robert and Sandra had been married for three years and had not made Wills prior to Robert's death in July 2011. They have no children of their own, but Sandra has two children from a previous marriage, aged eight and six. Both of Robert's parents are deceased and he has a surviving brother, Tom.
- Robert had personal possessions worth £15,000, a portfolio of investments worth £700,000, and an interest in his and Sandra's joint bank account containing £20,000 on his death. Their house was owned on a joint tenant's basis.
- Describe briefly who will benefit from Robert's estate on his death, and how much they will receive. (7)
9. Tony has gifted £3,000 each year to his grandchildren and in April 2006 he gifted a further £100,000 into a discretionary trust for them. Tony died in October 2008 and his wife Joan, who was in poor health at the time of his death, died in the tax year 2011/2012, having been the sole beneficiary of Tony's estate on his death. Neither Tony or Joan made any other gifts.
- Explain briefly how the gifts will affect the Inheritance Tax payable. *No calculation is required.* (9)
10. Frank, a non-UK resident, aged 58, set up an offshore life investment bond, with an Isle of Man based company, in a life interest trust in order to make payments to his UK resident minor grandchildren. The trustees are all UK resident.
- Describe briefly the tax treatment if the trustees of the trust were to fully encash the bond:
- (a) during Frank's lifetime while still a non-UK resident; (6)
 - (b) during Frank's lifetime following transfer of the bond to a beneficiary. (4)
11. State how interest received from a bank account is assessed to Income Tax, and who has the primary liability for payment of the tax in respect of:
- (a) a bare trust; (2)
 - (b) an interest in possession trust; (2)
 - (c) a discretionary trust. (4)

Questions continue over the page

12. A discretionary trust's assets are a mixture of gilts, bank deposits and various unit trusts, some of which have fallen in value recently.
- Explain briefly the Capital Gains Tax treatment of these assets when they are disposed of by the trustees. (8)
13. Billy set up a discretionary trust in February 2002, primarily for his grandchildren, with a transfer of £500,000. In view of Billy's increasing age his son Carl has now been appointed as a trustee. Carl is assessing the tax situation applicable to the trust. He is aware that this type of trust has Inheritance Tax charges associated with it. Explain:
- (a) when these tax charges are incurred for this type of trust; (3)
- (b) how the amount of the first periodic charge is calculated, assuming that the fund is worth £600,000 at the time. *No calculation is required.* (4)
14. Angelique has serious financial difficulties and had a meeting with an adviser at the Citizens Advice Bureau to discuss the possibility of bankruptcy. The advisor explained what options she has and also told her about restrictions in the event of the bankruptcy.
- (a) List **three** alternatives to bankruptcy. (3)
- (b) List **eight** legal restrictions on a bankrupt. (8)
- (c) Explain briefly the actions a trustee in bankruptcy could take to prevent automatic reversion of Angelique's principal private residence back to her, following the Enterprise Act 2002. (3)
15. Harold set up a discretionary trust in 2009 for his four grandchildren aged 4, 9, 15 and 17. The assets of the trust are various bank deposits, shares and corporate bonds.
- List **eleven** events which could trigger a review of this trust, both now and in the future. (11)

The tax tables can be found on pages 8 – 12

INCOME TAX

RATES OF TAX	2010/2011	2011/2012
Starting rate for savings*	10%	10%
Basic rate	20%	20%
Higher rate	40%	40%
Additional rate	50%	50%
Starting-rate limit	£2,440*	£2,560*
Threshold of taxable income above which higher rate applies	£37,400	£35,000
Threshold of taxable income above which additional rate applies	£150,000	£150,000

*restricted to savings income only and not available if taxable non-savings income exceeds starting rate band.

MAIN PERSONAL ALLOWANCES AND RELIEFS

Income limit for Personal Allowance §	£100,000	£100,000
Personal Allowance (basic) §	£6,475	£7,475
Personal Allowance (age 65-74) §	£9,490	£9,940
Personal Allowance (aged 75 and over) §	£9,640	£10,090
Married/civil partners (minimum) at 10% †	£2,670	£2,800
Married/civil partners (age 75 and over) at 10%	£6,965	£7,295
Income limit for age-related allowances	£22,900	£24,000
Blind Person's Allowance	£1,890	£1,980
Enterprise Investment Scheme relief limit on £500,000 max	20%	30%
Venture Capital Trust relief limit on £200,000 max	30%	30%

§ the Personal Allowance reduces by £1 for every £2 of income above the income limit irrespective of age.
 † where at least one spouse/civil partner was born before 6 April 1935.

Child Tax Credit (CTC)		
- family element	£545	£545
- family element baby addition	£545	Withdrawn
CTC usually reduced by 41% of joint income (6.67% for 2010/2011) over	£50,000	£40,000

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	Weekly	Monthly	Yearly
Lower Earnings Limit (LEL)	£102	£442	£5,304
Primary threshold	£139	£602	£7,225
Upper Accrual Point	£770	£3,337	£40,040
Upper Earnings Limit (UEL)	£817	£3,540	£42,475

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS	
	Contracted-in rate	Contracted-out rate
Up to 139.00*	Nil	Nil
139.01 – 770.00	12%	10.4%
770.01 – 817.00	12%	12%
Above 817.00	2%	2%

* This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £102 per week. This £102 to £139 band is a zero rate band introduced in order to protect lower earners' rights to contributory State benefits e.g. Basic State Pension.

Total earnings £ per week	CLASS 1 EMPLOYER CONTRIBUTIONS		
	Contracted-in rate	Contracted-out rate	
		Final salary	Money purchase
Below 136.00**	Nil	Nil	Nil
136.01 – 770.00	13.8%	10.1%	12.4%
770.01 – 817.00	13.8%	13.8%	13.8%
Excess over 817.00	13.8%	13.8%	13.8%

** Secondary earnings threshold.

Class 2 (self-employed)	Flat rate per week £2.50 where earnings exceed £5,315 per annum.
Class 3 (voluntary)	Flat rate per week £12.60.
Class 4 (self-employed)	9% on profits between £7,225 - £42,475 plus 2% on profits above £42,475.

PENSIONS

TAX YEAR	LIFETIME ALLOWANCE	ANNUAL ALLOWANCE
2006/2007	£1,500,000	£215,000
2007/2008	£1,600,000	£225,000
2008/2009	£1,650,000	£235,000
2009/2010	£1,750,000	£245,000
2010/2011	£1,800,000	£255,000
2011/2012	£1,800,000	£50,000

ANNUAL ALLOWANCE CHARGE

20% - 50% member's tax charge on the amount of total pension input in excess of the annual allowance.

LIFETIME ALLOWANCE CHARGE

55% of excess over lifetime allowance if taken as a lump sum.

25% of excess over lifetime allowance if taken in the form of income, which is subsequently taxed under PAYE.

INHERITANCE TAX

RATES OF TAX ON DEATH TRANSFERS

	2010/2011	2011/2012
Transfers made after 5 April 2011		
- Up to £325,000	Nil	Nil
- Excess over £325,000	40%	40%
- Lifetime transfers to and from certain trusts	20%	20%

MAIN EXEMPTIONS

Transfers to		
- UK-domiciled spouse/civil partner	No limit	No limit
- non-UK-domiciled spouse/civil partner (from UK-domiciled spouse)	£55,000	£55,000
- UK-registered charities	No limit	No limit
Lifetime transfers		
- Annual exemption per donor	£3,000	£3,000
- Small gifts exemption per donor	£250	£250
Wedding/civil partnership gifts by		
- parent	£5,000	£5,000
- grandparent	£2,500	£2,500
- other person	£1,000	£1,000

100% relief: businesses, unlisted/AIM companies, certain farmland/building

50% relief: certain other business assets

Reduced tax charge on gifts within 7 years of death:

- Years before death	0-3	3-4	4-5	5-6	6-7
- Inheritance Tax payable	100%	80%	60%	40%	20%

CAR BENEFIT FOR EMPLOYEES

The charge for company car benefits is based on the carbon dioxide (CO₂) emissions. There is no reduction for high business mileage users.

For 2011/2012:

The percentage charge is 15% of the car's list price for CO₂ emissions at or below the qualifying level of 125g/km.

- Cars with CO₂ emissions of less than 75g/km have an appropriate percentage of 5%.
- Cars with CO₂ emissions of 76g/km to 120g/km have an appropriate percentage of 10% and thereafter the rate is 15% increasing by 1% for every 5g/km to the current maximum of 35% (emissions of 225g/km and above).

There is an additional 3% supplement for diesel cars not meeting Euro IV emission standards. However, the maximum charge remains 35% of the car's list price.

Car fuel The benefit is calculated as the CO₂ emissions % relevant to the car and that % applied to a set figure (£18,800 for 2011/2012) e.g. car emission 155g/km = 21% on car benefit scale.
21% of £18,800 = £3,948

1. **Accessories** are, in most cases, included in the list price on which the benefit is calculated.
2. **List price** is reduced for capital contributions made by the employee up to £5,000.
3. **Car benefit** is reduced by the amount of employee's contributions towards running costs.
4. **Fuel scale** is reduced only if the employee makes good **all** the fuel used for private journeys.
5. **All car and fuel benefits** are subject to employers National Insurance Contributions (Class 1A) of 13.8%.

PRIVATE VEHICLES USED FOR WORK

2011/2012 Rates

Cars	
On the first 10,000 business miles in tax year	45p per mile
Each business mile above 10,000 business miles	25p per mile
Motor Cycles	24p per mile
Bicycles	20p per mile

MAIN CAPITAL AND OTHER ALLOWANCES

2011/2012

Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£100,000
Plant & machinery (reducing balance) per annum	20%
Patent rights & know-how (reducing balance) per annum	25%
Certain long-life assets, integral features of buildings (reducing balance) per annum	10%
Energy & water-efficient equipment	100%
Zero emission goods vehicles (new)	100%
Qualifying flat conversions, business premises & renovations	100%

Motor cars: Expenditure on or after 01/04/09 (Corporation Tax) or 06/04/09 (Income Tax)

CO ₂ emissions of g/km:	110 or less *	111-160	161 or more
Capital allowance:	100%	20%	10%
	first year	reducing balance	reducing balance

* If new

Research & Development:	Capital expenditure	100%
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MAIN SOCIAL SECURITY BENEFITS

2010/2011 2011/2012

		£	£
Child Benefit	first child	20.30	20.30
	subsequent children	13.40	13.40
Employment and Support Allowance	Assessment Phase		
	Age 16 – 24	N/A	Up to 53.45
	Aged 25 or over	N/A	Up to 67.50
	Main Phase		
	Work Related Activity Group	N/A	Up to 94.25
	Support Group	N/A	Up to 99.85
Attendance Allowance	lower rate	47.80	49.30
	higher rate	71.40	73.60
Retirement Pension	single	97.65	102.15
	married	156.15	163.35
Pension Credit	single person standard minimum guarantee	132.60	137.35
	married couple standard minimum guarantee	202.40	209.70
	maximum savings ignored in calculating income	10,000.00	10,000.00
Bereavement Payment (lump sum)		2,000.00	2,000.00
Widowed Parent's allowance		97.65	100.70
Jobseekers Allowance	Age 16 - 24		53.45
	Age 25 or over	65.45	67.50

CAPITAL GAINS TAX

EXEMPTIONS	2010/2011	2011/2012
Individuals, estates etc	£10,100	£10,600
Trusts generally	£5,050	£5,300
Chattels proceeds (restricted to five thirds of proceeds exceeding limit)	£6,000	£6,000

TAX RATES

Individuals:		
Up to basic rate limit	18%	18%
Above basic rate limit	18%/28%*	28%
Trustees and Personal Representatives	18%/28%*	28%
Entrepreneurs' Relief – Gains taxed at:	10%	10%
Lifetime limit	£5,000,000/ £2,000,000**	£10,000,000

For trading businesses and companies (minimum 5% employee or director shareholding) held for at least one year.

*18% rate applies to disposals on or before 22/06/10. 28% thereafter.

**For disposals 06/04/10 to 22/06/10: £2,000,000. £5,000,000 until 05/04/11

CORPORATION TAX

	2010/2011	2011/2012
Full rate	28%	26%
Small companies rate	21%	20%
Small companies limit	£300,000	£300,000
Effective marginal rate	29.75%	27.5%
Upper marginal limit	£1,500,000	£1,500,000

VALUE ADDED TAX

	2011/2012
Standard rate	20%
Annual Registration limit	£73,000

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