



J04

THE CHARTERED INSURANCE INSTITUTE

WEDNESDAY 21 APRIL 2010

**DIPLOMA IN FINANCIAL PLANNING
J04 – PENSION FUNDING OPTIONS**

SPECIAL NOTICES

- **All questions in this paper are based on English law and practice applicable in the tax year 2009/2010, unless stated otherwise and should be answered accordingly.**
- **Assume all individuals are domiciled, resident and ordinarily resident in the UK unless stated otherwise.**
- **Candidates should answer based on the legislative position immediately BEFORE the 2010 Budget.**

INSTRUCTIONS

- **Two hours are allowed for this paper.**
- **Read the instructions overleaf carefully before answering any questions.**
- Fill in the information requested on the answer book and form B.
- 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 and you must enter the serial number, model and make on the 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.**

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J04 – Pension funding options

CANDIDATE INSTRUCTIONS

READ THE INSTRUCTIONS BELOW BEFORE ANSWERING ANY QUESTIONS

Two hours are allowed for this paper.

The paper consists of 15 short answer questions and carries a total of 130 marks.

Read carefully the questions and information provided. You are strongly advised to attempt **all** questions to gain maximum possible marks. The number of marks allocated to each question part is given next to the question and you should spend your time in accordance with that allocation.

Any rough notes made in your answer book must be crossed through before you hand it in.

Tax tables are provided at the back of the paper.

Answer each question on a new page and leave six lines blank after each question part.

It is important to show all steps in a calculation, even if you have used a calculator.

Please ensure that you understand the Special Notices printed in the box on the front page.

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. Outline the requirements that must be satisfied for an individual to be regarded as a relevant UK individual for the purposes of entitlement to tax relief on personal contributions to a registered pension scheme. (6)

2. Harry has a self-invested personal pension (SIPP). The gross assets of the SIPP consist of a commercial property valued at £200,000 plus cash holdings of £180,000.

In 2008, the SIPP took out a loan to purchase the commercial property and the outstanding loan is £80,000. Harry now wishes to use the SIPP to purchase a second commercial property.

Calculate, **showing all your workings**, the maximum that the SIPP can borrow towards the purchase of the second commercial property. (7)

3. A contribution to a registered pension scheme will be treated as an unauthorised member payment if it is deemed to be an artificially recycled pension commencement lump sum.

Outline the circumstances in which such a contribution will be treated as an unauthorised member payment. (5)

4. Yvonne has been working for her employer for one year and is now eligible to join her company's contracted out defined benefit pension scheme. She has gross weekly earnings of £950.
 - (a) Calculate, **showing all your workings**, the amount by which Yvonne's weekly National Insurance contributions will be reduced as a result of joining the pension scheme. (5)
 - (b) Outline the minimum level of benefits that must be provided by Yvonne's scheme in order to meet the Reference Scheme requirements. (7)

5. Carrie is a member of her company's defined benefit pension scheme, which has an accrual rate of $1/60^{\text{th}}$. At the start of the 2009/2010 tax year, which was also the start of the pension input period for the scheme, her pensionable salary was increased from £81,000 to £120,000 per annum. On 6 April 2009, she had been a member of the scheme for 10 years.

Calculate, **showing all your workings**, the notional contribution to the scheme that will be tested against the annual allowance in respect of the pension input period ending on 5 April 2010. (9)

6. Graham and Adam have set up their own company and they have taken on 15 employees. They would like to set the company retirement age at 60 for all employees. They are in the process of setting up a group personal pension scheme (GPP), to which they are planning to contribute. They would like to set up the GPP with a selected pension age of 60.

Outline, giving your reasons, whether their plans satisfy the Age Discrimination Regulations in respect of the:

(a) company retirement age; (3)

(b) GPP selected pension age. (2)

7. In respect of a targeted money purchase occupational pension scheme, describe:

(a) how the initial and ongoing funding level is determined; (5)

(b) the level of retirement benefits payable at normal retirement age. (3)

8. A national marketing company with 250 employees currently operates a defined benefit pension scheme. Following a recent actuarial valuation, the company is considering making changes to future pension benefits. The employer must consult with the employees if any of the planned changes meets the definition of a 'prescribed decision' under The Pensions Act 2004.

(a) Outline the changes to the scheme that would fall under the definition of a prescribed decision. (6)

(b) Briefly describe the minimum period of consultation required. (2)

9. Eleanor, aged 39, is employed by Adcock Ltd as a sales and marketing director. The company, which is unlisted, has only been established for two years and has grown very quickly during that time. Eleanor does not currently own any shares in the company but feels it has significant growth potential.

Eleanor has a self-invested personal pension (SIPP) and has decided to invest her entire SIPP fund in the shares of Adcock Ltd. She has a speculative attitude to risk.

Ignoring the tax treatment, outline **four** benefits and **four** drawbacks of Eleanor's proposed investment strategy. (8)

10. In respect of the requirement for an employer to designate a stakeholder pension, outline the circumstances when an employee would **not** be classed as a relevant employee for the purposes of the employer access rules. (10)

11. Wade PLC offers an employer financed retirement benefit scheme (EFRBS) to employees. The scheme is funded wholly by employer contributions.

Explain, in detail, the tax treatment of the:

(a) contributions; (5)

(b) underlying fund. (4)

12. Colbrite Ltd has a closed defined benefit pension scheme with 60 deferred members and 20 pensioner members. The company is experiencing severe financial difficulties and is struggling to meet the agreed payments in respect of the scheme.

(a) State the circumstances under which the Pension Protection Fund (PPF) will assume responsibility for the pension scheme. (3)

(b) Outline the basis of the economic and financial assumptions that are used in valuing the scheme for insolvency purposes. *This is also known as a section 143 valuation.* (9)

- 13.** Andrew has preserved benefits in a contracted-in defined benefit occupational pension scheme. He is thinking of transferring these benefits to an individual pension arrangement and a Transfer Value Analysis System (TVAS) has calculated that the critical yield to the scheme's normal retirement age of 65 is 7.2% per annum.
- (a) Explain the process that will have been used to calculate the critical yield. (7)
- (b) Explain why Andrew may receive worse benefits under an individual arrangement at age 65 than he would have received under the defined benefit scheme, even if the critical yield is achieved. (4)
- 14.** Outline the factors that should be taken into account in determining the most appropriate level of future personal pension contributions for a client. (10)
- 15.** Ben and Susan, both aged 40, are getting divorced. Ben is a member of his company's private sector defined benefit pension scheme and the courts awarded a pension sharing order in January 2010. Neither Ben nor Susan has elected for transitional protection.
- (a) Explain how the pension share for Susan will be calculated. *No calculation required.* (6)
- (b) Outline the ways in which the scheme may implement the pension sharing order. (4)

TAX TABLES

INCOME TAX RATES

2009/2010		2008/2009	
Rate	Band	Rate	Band
%	£	%	£
10	1 - 2,440*	10	1 - 2,320*
20	1 - 37,400	20	1 - 34,800
40	Over 37,400	40	Over 34,800

* A new 10% starting rate is applied for savings income only from 06.04.2008. Only applicable where non-savings income after allowances is under £2,440 for 2009/2010.

NATIONAL INSURANCE CONTRIBUTIONS

2009/2010 Rates

Class 1 Employee	Weekly	Monthly	Yearly
	£	£	£
Lower Earnings Limit (LEL)	95	412	4,940
Upper Earnings Limit (UEL)	844	3,656	43,875
Upper Accruals Point	770	3,337	40,040

Class 1 Employee contributions 2009/2010

Total earnings £ per week	Contracted-in rate		Contracted-out rate	
	%		%	
Up to 110.00*	Nil		Nil	
110.01 – 770.00	11		9.4	
770.01 – 844.00	11		11	
Above 844.00	1		1	

Class 1 Employer contributions 2009/2010

Total earnings £ per week	Contracted-in rate		Contracted-out rate	
	%		Final salary	Money purchase
	%		%	£
Below 110.00**	Nil		Nil	Nil
110.01 – 770.00	12.8		9.1	11.4
770.01 – 844.00	12.8		12.8	12.8
Excess over 844.00	12.8		12.8	12.8

* This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £95 per week. This £95 to £110 band is a zero rate band introduced in order to protect lower earners' rights to contributory State benefits e.g. Basic State Pension.

** Secondary earnings threshold.

Class 2 (self-employed) Flat rate per week £2.40 where earnings exceed £5,075 per annum.

Class 3 (voluntary) Flat rate per week £12.05

Class 4 (self-employed) 8% on profits between £5,715 - £43,875 plus 1% on profits above £43,875

INCOME TAX RELIEFS

	2009/2010	2008/2009
	£	£
Personal (basic)	6,475	6,035
Personal (age 65-74)	9,490	9,030
Personal (aged 75 and over)	9,640	9,180
Married/civil partners (minimum) at 10% †	2,670	2,540
Married/civil partners (age under 75) at 10% †	N/A	6,535
Married/civil partners (age 75 and over) at 10%	6,965	6,625
Age-related relief reduced by 50% of income over	22,900	21,800
Child Tax Credit (CTC)		
family element	545	545
family element baby addition	545	545
CTC usually reduced by 6.67% of joint income over	50,000	50,000
Blind person's allowance	1,890	1,800
Enterprise Investment Scheme relief limit @ 20%	500,000	500,000
Venture Capital Trust relief limit @ 30%	200,000	200,000

† where at least one spouse/civil partner was born before 6 April 1935

PENSIONS

Lifetime Allowance		Annual Allowance	
2006/2007	£1.5 million	2006/2007	£215,000
2007/2008	£1.6 million	2007/2008	£225,000
2008/2009	£1.65 million	2008/2009	£235,000
2009/2010	£1.75 million	2009/2010	£245,000
2010/2011	£1.8 million	2010/2011	£255,000

Notional Earnings Cap

£123,600 – (For schemes that require post 1989 benefits to be still subject to a cap)

Annual allowance charge

40% 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.

CAR AND FUEL BENEFITS

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

For 2009/2010:

The percentage charge is 15% of the car's list price for CO₂ emissions at or below the qualifying level of 135g/km.

The base percentage charge of 15% increases in 1% steps for every additional full 5g/km over the 135g/km threshold, up to a maximum of 35% of the car's list price.

A lower percentage charge of 10% of the car's list price applies for emissions at or below 120g/km.

If price of car exceeds £80,000 then its price for tax purposes will be fixed at £80,000.

There is an additional 3% supplement for diesel cars not meeting Euro IV emission standards or registered after 31 December 2005. 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 (£16,900 for 2009/2010) e.g. car emission 160g/km = 20% on car benefit scale. 20% of £16,900 = £3,380.

Notes:

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 12.8%.

PRIVATE VEHICLES USED FOR WORK

2009/2010 rates

Cars

On the first 10,000 business miles in tax year 40p per mile

Each business mile above 10,000 business miles 25p per mile

Motor Cycles 24p per mile

Bicycles 20p per mile

INHERITANCE TAX

	2009/2010	2008/2009
Nil-rate band*	£325,000	£312,000
Rate of tax on excess	40%	40%
Lifetime transfers to and from certain trusts	20%	20%
Overseas domiciled spouse/civil partner exemption	£55,000	£55,000

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

	0-3	3-4	4-5	5-6	6-7
% of death charge	100	80	60	40	20
Annual exempt gifts	£3,000 per donor			£250 per donee	

* From 8 October 2007 up to 100% of the unused proportion of a deceased spouse's/civil partner's nil-rate band can be claimed on the surviving spouse's/civil partner's death.

MAIN SOCIAL SECURITY BENEFITS

		From 06.04.09 £	From 06.04.08 £
Child Benefit	first child	20.00	20.00*
	subsequent children	13.20	13.20*
Incapacity Benefit	short-term lower rate**	67.75	63.75
	short-term higher rate**	80.15	75.40
	long-term rate	89.80	84.50
Attendance Allowance	lower rate	47.10	44.85
	higher rate	70.35	67.00
Retirement Pension	single	95.25	90.70
	married	152.30	145.05
Pension Credit	single person standard minimum guarantee	130.00	124.05
	married couple standard minimum guarantee	198.45	189.35
	maximum savings ignored in calculating income	6,000	
	increased from November 2009	10,000	
Bereavement Benefit (lump sum)		2,000.00	2,000.00
Widowed Parent's allowance		95.25	90.70
Jobseekers Allowance		64.30	60.50

* From 5 January 2009

** Under State Pension Age

VALUE ADDED TAX

Standard rate	15%*/17.5%**
Annual registration limit - from 1 May 2009	£68,000

* Effective from 1 December 2008

** Effective from 1 January 2010

CORPORATION TAX

Financial Year	2009 to 31/3/10	2008 to 31/3/09
Full rate	28%	28%
Small companies rate	21%	21%
Small companies limit	£300,000	£300,000
Effective marginal rate	29.75%	29.75%
Upper marginal limit	£1,500,000	£1,500,000

CAPITAL ALLOWANCES

Plant & machinery 100% annual investment allowance (first year)	£50,000
Plant & machinery in excess of annual investment allowance (first year)	40%
Plant & machinery, patent rights, know-how (reducing balance) per annum	20%
Certain long-life assets, integral features of buildings (reducing balance) per annum	10%
Industrial & agricultural buildings (straight line)	2%
Energy & water-efficient investments	100%
Qualifying flat conversions & business premises renovations	100%
Motor cars: with emissions in excess of 160g/km	10%
generally	20%*
with CO2 emissions of 110g/km or less	100%
Research & Development: Capital expenditure	100%
Revenue expenditure - small/medium-size firms	175%
- large firms	130%

* Maximum £3,000

CAPITAL GAINS TAX

Exemptions	2009/2010	2008/2009
Individuals, estates etc	£10,100	£9,600
Trusts generally	£5,050	£4,800
Chattels proceeds (5/3 excess gain is taxable)	£6,000	£6,000
Rates		
Individuals	18%	18%
Trusts and estates	18%	18%

ENTREPRENEURS' RELIEF

Entrepreneurs' Relief 2009/2010

4/9^{ths} of gain tax free. Lifetime limit eligible for relief: £1,000,000

For trading businesses and companies (minimum 5% employee shareholding) held for 1yr+

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