THE CHARTERED INSURANCE INSTITUTE

R06

Diploma in Regulated Financial Planning

Unit 6 – Financial planning practice

July 2012 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 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 2012 budget.

Instructions

- Three 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 R06 – Financial planning practice

Instructions to candidates

Read the instructions below before answering any questions

- **Three hours** are allowed for this paper.
- This paper consists of **two** case studies and carries a total of 150 marks.
- You are advised to spend approximately 90 minutes on the questions for each case study. You are strongly advised to attempt **all** parts of each question in order to gain maximum possible marks for each question. 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.
- 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 for each case study

Time: 3 hours

Case study 1

Peter, aged 39, was widowed earlier this year when his wife, Susan, died. He has two children, Henry, aged 16, and Emma, aged 17. Peter suffers from asthma.

Peter works as a marketing manager for a retail chain and earns £65,000 gross per annum. His employer closed its defined benefit pension scheme last year and Peter is now a member of the company's money purchase pension scheme.

Peter purchased his house five years ago using a base rate tracker interest only mortgage with a term of 25 years. The current balance of the mortgage is £160,000 and no savings vehicle is in place to repay it. The house is currently worth £350,000.

When Susan died, Peter was the beneficiary of her employer's death-in-service payment of £80,000 and placed it in his current bank account. He has additional savings of £18,000 cash and a stocks and shares ISA, invested in an international fund, which is worth £25,000.

Peter's financial aims are to:

- ensure that the mortgage is repaid in the event of death or serious illness;
- ensure his retirement provision is adequate for his needs;
- review the suitability of his ISA as an investment.

Questions

(a) State the additional information that an adviser would require in order to advise Peter on his:

(i) retirement objective; **(14)**

(ii) protection objective. **(8)**

(b) State **three** benefits and **three** drawbacks of using each of the following options to repay Peter's mortgage:

(i) making increased monthly payments directly into his interest only mortgage; **(6)**

(ii) making regular payments to his stocks and shares ISA to generate a lump sum to repay his mortgage; **(6)**

(iii) making pension contributions to generate a lump sum to repay his mortgage. **(6)**

(c) Explain **four** options available to an underwriter if Peter was unable to obtain critical illness cover on standard terms due to his asthma. For each option identified, state the consequences for Peter. **(8)**

(d) State the factors relating to the existing investment fund that you would take into account when reviewing the suitability of Peter's ISA. **(10)**

(e) State **ten** changes in Peter's circumstances which should trigger a review meeting. **(10)**

(f) Assuming that you have agreed to work on a fee basis, state **four** types of fee that you could charge for advising Peter. **(4)**

Total marks available for this question: 72

Questions continue over the page

Case study 2

Nigel, aged 64, and Louise, aged 60, are married. They have two children, David, aged 25, and Simon, aged 23. Louise works on a self-employed basis as a physiotherapist with taxable net profits of £6,000 per annum.

Nigel has worked for several different employers throughout his working life and, as a result, he has built up a number of pension arrangements. Nigel has always held a senior position wherever he has worked and currently earns £72,000 gross per annum. He expects to retire in eight months' time. The fund value of his money purchase benefits totals £475,000. Louise has accrued £14,000 in a personal pension scheme which is invested in a fixed-interest fund.

Over the years, they have built up a number of investments and are concerned about tax efficiency and the appropriateness of them. Nigel has a medium attitude to risk and Louise has a low-to-medium attitude to risk. They have no mortgage or any other loans.

Their total assets are as follows:

Assets	**Nigel £**	**Louise £**	**Joint £**
Main Residence			650,000
Chattels			60,000
Current Account	34,000	2,000	
Deposit Account	14,000	Nil	
ISAs (Stocks and Shares)	40,000	12,000	
Unit Trust (UK Equities)	175,000	16,000	
Investment Bond (Managed Fund)			320,000
Enterprise Investment Scheme	25,000		

They inherited the investment bond from Louise's mother when she died 12 months ago.

Nigel and Louise would like to help their children to get onto the property ladder and would also like to maximise their children's inheritance when they die. Their Wills leave everything to each other on first death, and then everything to the children on second death.

Their financial aims are to:

- maintain their standard of living in retirement;
- assess the suitability of their existing investments;
- assist David with house purchase.

Questions

(a) State the additional information that an adviser would require in order to advise Nigel and Louise on their investments. **(15)**

(b) List **six** benefits and **six** drawbacks of Nigel using 'capped income drawdown' to take his retirement benefits. **(12)**

(c) **(i)** Calculate, **showing all your workings**, the net cash sum Louise would ultimately benefit from if she took her pension on the grounds of triviality now. **(5)**

(ii) Explain the tax treatment of Louise taking her pension now under triviality rules. **(5)**

(d) **(i)** Comment on the suitability of Nigel and Louise's existing investments and recommend any actions which should be taken to improve tax efficiency. *Ignore any Inheritance Tax issues or its mitigation.* **(11)**

(ii) State **five** benefits and **five** drawbacks of Nigel and Louise appointing a discretionary fund manager to look after their investments. **(10)**

(e) **(i)** Calculate, **showing all your workings**, the Inheritance Tax (IHT) liability that would be payable on second death. **(4)**

(ii) Recommend and justify a suitable type of insurance policy to cover their IHT liability on the second death of Nigel or Louise, and state how this policy should be set up. **(6)**

(f) Nigel and Louise are considering loaning David £100,000 for a deposit to help him to get onto the property ladder. Outline the factors they should take into account before making such an arrangement. **(10)**

Total marks available for this question: 78

The tax tables can be found on pages 9 - 13

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	£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 CO_2 emissions of less than 75g/km have an appropriate percentage of 5%.
- Cars with CO_2 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 CO_2 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% first year	20% reducing balance	10% reducing balance

* If new

Research & Development:	Capital expenditure	100%

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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