THE CHARTERED INSURANCE INSTITUTE

CII

R06

Diploma in Regulated Financial Planning

Unit 6 – Financial planning practice

January 2014 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2013/2014, unless stated otherwise and should be answered accordingly.

It should be assumed that all individuals are domiciled and resident in the UK unless otherwise stated.

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

Ben and Sarah, both aged 45, are unmarried and live together. They have one child, Gareth, aged 18, who intends to go to university in September 2014.

Ben is self-employed with taxable net profits of £10,000 per annum. Sarah is the majority shareholder of her company, BRB Ltd, which currently employs 10 people. Sarah draws a salary of £7,500 per annum gross and net dividends of £50,000 per annum.

Ben and Sarah have recently purchased a house for £350,000. They have a repayment mortgage with an outstanding balance of £125,000. The house is owned as joint tenants and they have a joint life first event life and critical illness policy to cover this liability.

Ben has a personal pension invested in a UK Equity fund and his current fund value is £37,000. He has been paying regular contributions into his pension for the last 10 years and he is currently contributing £300 per month, net. Sarah contributes £100 per month, net, to a personal pension plan invested in a managed fund and her current fund value is £11,000. Sarah intends to sell her shares in BRB Ltd when they both retire at age 65.

Sarah has asked for advice on protecting the business in the event of her death or serious illness.

BRB Ltd is considering setting up a group pension scheme for all staff and Sarah would like advice on workplace pension schemes.

They have the following portfolio of investments:

Ownership	Type	Amount (£)
Ben	UK Equity Income Unit Trust	25,000
Ben	UK Equity ISA	18,000
Sarah	European Equity Income OEIC	26,000
Sarah	With-profits bond	58,000
Sarah	Balanced Managed ISA	10,000
Joint	Current Account	35,000

Ben and Sarah are both in good health and have not made Wills. They both have a medium attitude to risk.

Their financial aims are to:

- improve the tax efficiency of their existing investment portfolio;
- provide funding for university costs for Gareth;
- provide business protection for Sarah in the event of her death or suffering a serious illness;
- ensure they have sufficient income in retirement;
- review the workplace pension requirements for BRB Ltd.

Questions

(a) **(i)** State the initial disclosure documents that an adviser should provide to Ben and Sarah. **(3)**

(ii) Outline the main adviser charging options for the provision of investment advice. **(4)**

(b) Outline the process a financial planner should follow to ensure sufficient funds are available, on a target benefit basis, from Ben and Sarah's personal pensions at age 65. *No calculation is required.* **(13)**

(c) State the additional information that an adviser would require about Ben and Sarah's existing portfolio if they were to use it to pay for Gareth's university costs. **(13)**

(d) Describe the actions Ben and Sarah could take to improve the tax efficiency of their existing investment portfolio. **(7)**

(e) **(i)** State the additional information that an adviser would require when advising Sarah on key person protection in the event of her death or critical illness. **(7)**

(ii) Recommend and justify a suitable protection policy to provide key person protection in the event of Sarah's death or critical illness before age 65. **(10)**

(f) **(i)** State how Ben and Sarah's home and other assets would be distributed in the event of either death. **(7)**

(ii) Explain to Ben and Sarah the impact of not making Wills. **(8)**

(g) List the conditions that will need to be met by employees of BRB Ltd to become eligible jobholders for auto-enrolment into a workplace pension scheme when the requirements apply to BRB Ltd. **(4)**

Total marks available for this question: 76

Questions continue over the page

Case study 2

Usain, aged 64, and his wife Lizzie, aged 60, are both retiring from work and want to draw their pension benefits. They have a son who is financially independent and a grandson, aged two. Lizzie is in good health. Usain takes medication for both high blood pressure and raised cholesterol.

Usain has preserved benefits under a previous employer's contracted-out defined benefit pension scheme, currently valued at £25,000 per annum and a pension commencement lump sum (PCLS) of up to £75,000. He also has a personal pension invested in a Global Equity fund valued at £200,000.

Lizzie has a personal pension invested in a balanced managed fund valued at £125,000.

Both Usain and Lizzie are entitled to the full Basic State Pension.

They have built up a portfolio of unit trusts and ISAs with various different companies. The portfolio is as follows:

Ownership	Type	Amount (£)
Usain	Stocks and Shares ISAs	70,000
Usain	Cash ISAs	50,000
Lizzie	Stocks and Shares ISAs	80,000
Lizzie	Cash ISAs	50,000
Joint	Unit Trusts	150,000
Joint	Bank Deposits	75,000

Their home is worth £600,000 with no mortgage. They have sufficient monies held on deposit for an emergency fund and their day-to-day needs. They have mirror Wills in place and both have a medium level of investment risk.

Their financial aims are to:

- provide sufficient income from their various pension policies;
- receive investment advice regarding their PCLS;
- gift £20,000 to their grandson;
- review the tax efficiency and investment options for their investment portfolio.

Questions

(a) **(i)** Describe to Usain and Lizzie the tax treatment of their ISAs. **(6)**

(ii) State the main benefits of holding unit trusts and ISAs within a wrap or platform. **(7)**

(b) Identify the principal types of investment risk that apply to Usain's Global Equity pension Fund. **(6)**

(c) **(i)** Outline the death benefits options and tax implications before age 75, if Usain were to transfer his existing personal pension to a self-invested personal pension (SIPP) and immediately commence capped drawdown. **(7)**

(ii) State **five** benefits and **five** drawbacks of Usain using a capped drawdown policy. **(10)**

(d) Outline the factors that Usain should consider if he decides to effect flexible drawdown. **(8)**

(e) Identify the additional information that an adviser would require when advising Usain and Lizzie on investing their pension commencement lump sums. **(12)**

(f) **(i)** Explain why a bare trust is suitable for Usain and Lizzie for making a gift of £20,000 to their grandson. **(7)**

(ii) State **four** drawbacks of using a bare trust for such a gift. **(4)**

(g) State **seven** factors that should trigger a review meeting for a capped drawdown policy. **(7)**

Total marks available for this question: 74

The tax tables can be found on pages 9 - 13

INCOME TAX

RATES OF TAX	2012/2013	2013/2014
Starting rate for savings*	10%	10%
Basic rate	20%	20%
Higher rate	40%	40%
Additional rate	50%	45%
Starting-rate limit	£2,710*	£2,790*
Threshold of taxable income above which higher rate applies	£34,370	£32,010
Threshold of taxable income above which additional rate applies	£150,000	£150,000
Child benefit charge from 7 January 2013:		
1% of benefit for every £100 of income over	£50,000	£50,000

**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 if born after 5 April 1948) §	£8,105	£9,440
Personal Allowance (if born between 6 April 1938 and 5 April 1948) §	£10,500	£10,500
Personal Allowance (if born before 6 April 1938) §	£10,660	£10,660
Married/civil partners (minimum) (if born before 6 April 1935) at 10% †	£2,960	£3,040
Married/civil partners (if born before 6 April 1935) at 10% †	£7,705	£7,915
Income limit for age-related allowances	£25,400	£26,100
Blind Person's Allowance	£2,100	£2,160
Enterprise Investment Scheme relief limit on £1,000,000 max	30%	30%
Seed Enterprise Investment relief limit on £100,000	50%	50%
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 (under the income threshold).*
† *where at least one spouse/civil partner was born before 6 April 1935.*

Child Tax Credit (CTC)		
- Child element per child (maximum)	£2,690	£2,720
- family element	£545	£545
Threshold for tapered withdrawal of CTC	£15,860	£15,910

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	Weekly	Monthly	Yearly
Lower Earnings Limit (LEL)	£109	£473	£5,668
Primary threshold	£149	£646	£7,755
Upper Accrual Point	£770	£3,337	£40,040
Upper Earnings Limit (UEL)	£797	£3,454	£41,450

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS	
	Contracted-in rate/contracted-out (money purchase)	Contracted-out rate (final salary)
Up to 149.00*	Nil	Nil
149.01 – 770.00	12%	10.6%
770.01 – 797.00	12%	12%
Above 797.00	2%	2%

**This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £109 per week. This £109 to £149 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 148.00**	Nil	Nil	Nil
148.01 – 770.00	13.8%	10.4%	13.8%
770.01 – 797.00	13.8%	13.8%	13.8%
Excess over 797.00	13.8%	13.8%	13.8%

*** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £2.70 where earnings exceed £5,725 per annum.
Class 3 (voluntary)	Flat rate per week £13.55.
Class 4 (self-employed)	9% on profits between £7,755 - £41,450 2% on profits above £41,450.

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
2012/2013	£1,500,000	£50,000
2013/2014	£1,500,000	£50,000

ANNUAL ALLOWANCE CHARGE
20% - 45% 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	2012/2013	2013/2014
Transfers made after 5 April 2013		
- Up to £325,000	Nil	Nil
- Excess over £325,000	40%	40%
- Lifetime transfers to and from certain trusts	20%	20%

**For deaths after 5 April 2013, a lower rate of 36% applies where at least 10% of deceased's net estate is left to charity.*

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	£325,000
- 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 (CO_2) emissions. There is no reduction for high business mileage users.

For 2013/2014:

- Cars that cannot emit CO_2 have a 0% charge.
- The percentage charge is 5% of the car's list price for CO_2 emissions of 75g/km or less.
- For cars with CO_2 emissions of 76g/km to 94g/km the percentage is 10%.
- For cars with CO_2 emissions of 95g/km to 99g/km the percentage is 11%.
- Cars with CO_2 emissions of 100g/km have a percentage charge of 12% and thereafter the charge increases by 1% for every complete 5g/km to a maximum of 35% (emissions of 215g/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 (£21,100 for 2013/2014) e.g. car emission 100g/km = 12% on car benefit scale. 12% of £21,100 = £2,532.

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

	2012/2013 Rates	2013/2014 Rates
Cars		
On the first 10,000 business miles in tax year	45p per mile	45p per mile
Each business mile above 10,000 business miles	25p per mile	25p per mile
Motor Cycles	24p per mile	24p per mile
Bicycles	20p per mile	20p per mile

MAIN CAPITAL AND OTHER ALLOWANCES

	2012/2013	2013/2014
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£25,000	£250,000
Plant & machinery (reducing balance) per annum	18%	18%
Patent rights & know-how (reducing balance) per annum	25%	25%
Certain long-life assets, integral features of buildings (reducing balance) per annum	8%	8%
Energy & water-efficient equipment	100%	100%
Zero emission goods vehicles (new)	100%	100%
Qualifying flat conversions, business premises & renovations	100%	100%

Motor cars: Expenditure on or after 01 April 2013 (Corporation Tax) or 06 April 2013 (Income Tax)

CO_2 emissions of g/km:	95 or less*	96-130	131 or more
Capital allowance:	100% first year	18% reducing balance	8% reducing balance

*If new

Research & Development: Capital expenditure 100%

MAIN SOCIAL SECURITY BENEFITS

		2012/2013	2013/2014
		£	£
Child Benefit	First child	20.30	20.30
	Subsequent children	13.40	13.40
	Guardian's allowance	15.55	15.90
Employment and Support Allowance	Assessment Phase		
	Age 16 – 24	Up to 56.25	Up to 56.80
	Aged 25 or over	Up to 71.00	Up to 71.70
	Main Phase		
	Work Related Activity Group	Up to 99.15	Up to 100.15
	Support Group	Up to 105.05	Up to 106.50
Attendance Allowance	Lower rate	51.85	53.00
	Higher rate	77.45	79.15
Retirement Pension	Single	107.45	110.15
	Married	171.85	176.15
Pension Credit	Single person standard minimum guarantee	142.70	145.40
	Married couple standard minimum guarantee	217.90	222.05
	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		105.95	108.30
Jobseekers Allowance	Age 16 - 24	56.25	56.80
	Age 25 or over	71.00	71.70
Statutory Maternity, Paternity and Adoption Pay		135.45	136.78

CAPITAL GAINS TAX

EXEMPTIONS	2012/2013	2013/2014
Individuals, estates etc	£10,600	£10,900
Trusts generally	£5,300	£5,450
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	28%	28%
Trustees and Personal Representatives	28%	28%
Entrepreneurs' Relief* – Gains taxed at:	10%	10%
Lifetime limit	£10,000,000	£10,000,000

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

CORPORATION TAX

	2012/2013	2013/2014
Full rate	24%	23%
Small companies rate	20%	20%
Small companies limit	£300,000	£300,000
Effective marginal rate	25%	23.75%
Upper marginal limit	£1,500,000	£1,500,000

VALUE ADDED TAX

	2012/2013	2013/2014
Standard rate	20%	20%
Annual registration threshold	£77,000	£79,000
Deregistration threshold	£75,000	£77,000