THE CHARTERED INSURANCE INSTITUTE

CII

R06

Diploma in Regulated Financial Planning

Unit 6 – Financial planning practice

October 2014 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2014/2015, 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

Read the following carefully, then carry out ***ALL*** *of the tasks* ***(a), (b), (c), (d), (e)*** *and* ***(f)***

Jon, aged 62, is married to Sue, aged 62. They own their own home outright and are both in good health. They have two adult children who are financially independent.

Jon is a semi-retired senior manager and is in receipt of his final salary pension of £48,000 gross per annum which commenced in 2013. He runs a private management consultancy and this business has an annual turnover of £50,000. Jon has a self-invested personal pension (SIPP) into which he continues to make annual contributions, depending on his earnings from the management consultancy. His SIPP has a current value of £150,000 and Jon has not yet drawn any benefits from this plan. Jon is planning to retire by March 2015.

Sue has not been employed for a number of years and has no pension plans. She is due to receive her State Pension in 2015.

Jon and Sue have an investment portfolio, which includes a jointly-owned onshore investment bond with a current value of £100,000 which they have held for ten years, along with a range of jointly-owned collective investment funds held in fixed-interest securities and UK equity funds. These are valued at approximately £800,000 in total. They also hold a number of NISAs held in collective investment funds and they estimate that these have a current value of £300,000 in total. Jon and Sue hold £30,000 in cash in an instant access account for emergencies and they also hold £100,000 in a five year fixed-rate account in Sue's name.

Jon is a higher-rate taxpayer and Sue is a basic-rate taxpayer. Jon is keen to learn more about investments and considers himself to be a medium-risk investor. Sue considers herself to be a low to medium-risk investor. Jon has read an article about Venture Capital Trusts and would like to know more about this type of investment.

Both have mirror Wills leaving everything to each other on first death and then to the children on second death. These have been updated recently. They have no protection policies and no outstanding debts or liabilities.

Jon and Sue's financial aims are to:

- ensure that they have adequate income in retirement;
- improve the tax-efficiency of their current investment portfolios;
- mitigate any future higher-rate Income Tax liability;
- purchase a new car for Sue in the next few months.

Questions

(a) State the additional information that you would require to prepare a full review of Jon and Sue's existing pension arrangements. **(12)**

(b) **(i)** Following the reduction in the lifetime allowance this year, explain briefly to Jon how this may affect his pension plans. **(3)**

(ii) Recommend what action Jon could take to mitigate any impact on his pension plans from these changes to the lifetime allowance. *No calculation is required.* **(5)**

(c) Jon would like more details on Venture Capital Trusts.

(i) Explain the main tax **advantages** for Jon of investing in a Venture Capital Trust. **(9)**

(ii) State five **drawbacks** for Jon of investing in a Venture Capital Trust. **(5)**

(d) **(i)** Summarise the options available for Sue with regard to her State Pension benefits when she reaches her State Pension Age in 2015. **(5)**

(ii) Sue is able to purchase additional entitlement to the Basic State Pension through voluntary National Insurance contributions.

Explain briefly to Sue the benefits of purchasing additional State Pension entitlement using this method. **(6)**

QUESTIONS CONTINUE OVER THE PAGE

(e) Sue wishes to purchase a new car.

(i) Explain in detail to Jon and Sue how they could obtain a tax-efficient lump sum from their investment bond to purchase a new car. **(8)**

(ii) List the additional information you would require to enable you to calculate the most tax-efficient method of drawing funds from the Investment Bond. *No calculation is required.* **(8)**

(f) Recommend and justify what actions Jon and Sue could take to generate a tax-efficient income in retirement from their investment portfolio. **(14)**

Total marks available for this question: 75

Case study 2 can be found on pages 8 - 10

Case study 2

Read the following carefully, then carry out ***ALL*** *of the tasks* ***(a), (b), (c), (d), (e), (f)*** *and* ***(g)***

Tom, aged 44, is married to Lucy, aged 41. Both are in good health. Tom is a marketing manager for a large telecoms provider and Lucy is employed as a copywriter. They have two children, David aged nine and Caroline aged seven.

Tom's mother died recently and Tom is expecting an inheritance of £100,000 in the next few months. No further inheritances are expected for either Tom or Lucy.

Tom earns a salary and bonuses totalling £60,000 gross per annum and Lucy earns £25,000 gross per annum.

Tom is a member of his employer's defined benefit pension scheme and the scheme also provides Tom with four times his salary as a lump sum death-in-service benefit. Tom also has three paid-up personal pensions from previous employments. Lucy is a member of her employer's group personal pension scheme and has no previous pensions. She has no additional benefits from her current employer.

Tom and Lucy have an interest-only mortgage of £200,000, which is due to be repaid in 10 years' time. To repay the mortgage, Tom and Lucy have invested in a range of collective investment funds, some of which are held within NISAs. These investments have a current value of £50,000 and have never been reviewed. Most of the funds are invested in UK smaller companies and high-yield fixed-interest securities. They hold £10,000 in an instant access savings account in joint names.

Tom and Lucy have made mirror Wills leaving everything to each other on the first death and then to the children on the second death. Tom is a medium-risk investor and Lucy is a low to medium-risk investor. Tom and Lucy have no personal protection policies.

Tom and Lucy's financial aims are to:

- ensure sufficient funding is in place to repay the mortgage in 10 years' time;
- ensure adequate protection is in place whilst the children are in full-time education and university;
- maximise the benefits of their existing personal pension plans for retirement;
- review the suitability of their existing investment portfolio;
- maximise their entitlement to Child Benefit.

Questions

(a) List the additional information you will require to be able to advise Tom and Lucy on their following financial aims:

(i) ensure sufficient funding is in place to repay the mortgage in 10 years' time; **(8)**

(ii) provide adequate financial protection until the children have completed full-time education and university. **(8)**

(b) You intend to use a stochastic modelling tool to assist in analysing the asset allocation of Tom and Lucy's investments.

(i) Explain briefly to Tom and Lucy the purpose of a stochastic modelling tool and the type of information it can provide. **(8)**

(ii) Comment on the suitability of Tom and Lucy's existing investment portfolio. **(4)**

(c) State **four** main advantages and **four** main disadvantages of using Tom's inheritance to repay part of the mortgage, compared with placing the money in an investment portfolio. **(8)**

(d) Recommend and justify suitable protection policies to enable Tom to repay the mortgage in full and meet the childcare costs in the event of the death or disability of Lucy. **(15)**

(e) Outline **five** benefits and **five** drawbacks of consolidating Tom's personal pensions into a single personal pension plan. **(10)**

QUESTIONS CONTINUE OVER THE PAGE

(f) Explain briefly the actions that Tom and Lucy could take to maximise their entitlement to Child Benefit. **(7)**

(g) State **seven** financial areas to discuss at your next review meeting with Tom and Lucy. **(7)**

Total marks available for this question: 75

The tax tables can be found on pages 12 – 18

INCOME TAX

RATES OF TAX	2013/2014	2014/2015
Starting rate for savings*	10%	10%
Basic rate	20%	20%
Higher rate	40%	40%
Additional rate	45%	45%
Starting-rate limit	£2,790*	£2,880*
Threshold of taxable income above which higher rate applies	£32,010	£31,865
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) §	£9,440	£10,000
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% †	£3,040	£3,140
Married/civil partners (if born before 6 April 1935) at 10% †	£7,915	£8,165
Income limit for age-related allowances	£26,100	£27,000
Blind Person's Allowance	£2,160	£2,230
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)	£2,720	£2,750
- family element	£545	£545
Threshold for tapered withdrawal of CTC	£15,910	£16,010

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	Weekly	Monthly	Yearly
Lower Earnings Limit (LEL)	£111	£481	£5,772
Primary threshold	£153	£663	£7,956
Upper Accrual Point	£770	£3,337	£40,040
Upper Earnings Limit (UEL)	£805	£3,489	£41,865

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS	
	Contracted-in rate	Contracted-out rate (final salary)
Up to 153.00*	Nil	Nil
153.01 – 770.00	12%	10.6%
770.01 – 805.00	12%	12%
Above 805.00	2%	2%

**This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £111 per week. This £111 to £153 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 153.00**	Nil	Nil	Nil
153.01 – 770.00	13.8%	10.4%	13.8%
770.01 – 805.00	13.8%	13.8%	13.8%
Excess over 805.00	13.8%	13.8%	13.8%

*** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £2.75 where earnings exceed £5,885 per annum.
Class 3 (voluntary)	Flat rate per week £13.90.
Class 4 (self-employed)	9% on profits between £7,956 - £41,865 2% on profits above £41,865.

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
2014/2015	£1,250,000	£40,000

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.

CAPITAL GAINS TAX

EXEMPTIONS	2013/2014	2014/2015
Individuals, estates etc	£10,900	£11,000
Trusts generally	£5,450	£5,500
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.*

INHERITANCE TAX

RATES OF TAX ON DEATH TRANSFERS	2013/2014	2014/2015
Transfers made after 5 April 2014		
- 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 2014, 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)	£325,000	£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 2014/2015:

- 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 11%.
- For cars with CO_2 emissions of 95g/km to 99g/km the percentage is 12%.
- Cars with CO_2 emissions of 100g/km have a percentage charge of 13% and thereafter the charge increases by 1% for every complete 5g/km to a maximum of 35% (emissions of 210g/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 (£21,700 for 2014/2015) e.g. car emission 100g/km = 13% on car benefit scale. 13% of £21,700 = £2,821.

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

	2013/2014 Rates	2014/2015 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

	2013/2014	2014/2015
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£250,000	£500,000
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 2014 (Corporation Tax) or 06 April 2014 (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

CORPORATION TAX

	2013/2014	2014/2015
Full rate	23%	21%
Small companies rate	20%	20%
Small companies limit	£300,000	£300,000
Effective marginal rate	23.75%	21.25%
Upper marginal limit	£1,500,000	£1,500,000

VALUE ADDED TAX

	2013/2014	2014/2015
Standard rate	20%	20%
Annual registration threshold	£79,000	£81,000
Deregistration threshold	£77,000	£79,000

MAIN SOCIAL SECURITY BENEFITS

		2013/2014	2014/2015
		£	£
Child Benefit	First child	20.30	20.50
	Subsequent children	13.40	13.55
	Guardian's allowance	15.90	16.35
Employment and Support Allowance	Assessment Phase		
	Age 16 – 24	Up to 56.80	Up to 57.35
	Aged 25 or over	Up to 71.70	Up to 72.40
	Main Phase		
	Work Related Activity Group	Up to 100.15	Up to 101.15
	Support Group	Up to 106.50	Up to 108.15
Attendance Allowance	Lower rate	53.00	54.45
	Higher rate	79.15	81.30
Retirement Pension	Single	110.15	113.10
	Married	176.15	180.90
Pension Credit	Single person standard minimum guarantee	145.40	148.35
	Married couple standard minimum guarantee	222.05	226.50
	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		108.30	111.20
Jobseekers Allowance	Age 16 - 24	56.80	57.35
	Age 25 or over	71.70	72.40
Statutory Maternity, Paternity and Adoption Pay		136.78	138.18