

AF5

Advanced Diploma in Financial Planning

Unit AF5 – Financial planning process

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 in the question, 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 AF5 – Financial planning process

Instructions to candidates

Read the instructions below before answering any questions

- **Three hours** are allowed for this paper which carries a total of 160 marks.
- You are strongly advised to attempt **all** tasks to gain maximum possible marks. The number of marks allocated to each task is given next to the task and you should spend your time in accordance with that allocation.
- **In this examination you should use the fresh copy of the fact-find provided. You are not allowed to bring into the examination the pre-released copy of the fact-find.**
- **Client objectives are provided overleaf and you should read them carefully before attempting the tasks.**
- Read carefully all tasks and information provided before starting to answer. Your answer will be marked strictly in accordance with the task 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 task on a new page and leave six lines blank after each task.

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.

CLIENTS' FINANCIAL OBJECTIVES

You have now been able to determine from the information in the fact-find that your clients have the following financial objectives:

Immediate objectives

- To invest Jason's pension commencement lump sum to provide tax efficient income and growth.
- To invest £50,000 in a suitable trust to help towards the possible future university fees for their grandchildren.
- To reduce Jason's and Carrie's administration and personal involvement in the management of their investments.

Longer-term objectives

- To mitigate Jason's and Carrie's Inheritance Tax liability whilst maximising the value of the estate passed to their children.
- To review Jason's and Carrie's existing investment portfolio to maximise the overall ongoing tax efficiency.
- To realise the full value of Carrie's shares on her death or serious illness for the benefit of her surviving family.

Attempt ALL tasks**Time: 3 hours**

1. Identify the additional information you would need to discuss with Jason and Carrie in order to advise them on how to meet their:
 - (a) immediate financial objectives; (15)
 - (b) longer-term financial objectives. (15)

2. Jason would like to know more about the risks associated with his investments and pension.
 - (a) Excluding market risk, identify and explain briefly the key risks that apply to Jason's AIM shares. (12)
 - (b) Explain briefly how the Pension Protection Fund (PPF) would apply to Jason's pension after he retired at age 65 in the event that FTT Engineering Ltd suffered a qualifying insolvency event and the pension scheme qualified for the PPF. (6)

3. Jason wants to invest some of his pension commencement lump sum to provide tax efficient income and growth.

Candidates will be rewarded for supporting their recommendations with relevant evidence and demonstrating how their recommendations work holistically to meet their clients' objectives.

 - (a) Detail and justify why a Venture Capital Trust may be a suitable recommendation for Jason to achieve this objective. (12)
 - (b) Describe the Income Tax and Capital Gains Tax advantages that apply to an Enterprise Investment Scheme (EIS). *Base your answer on an EIS and not a Seed EIS.* (10)

QUESTIONS CONTINUE OVER THE PAGE

4. Jason and Carrie want to review their existing investment portfolio.
- (a) Comment on the tax efficiency of Jason's and Carrie's current savings and investments and how they could improve this. *Ignore Inheritance Tax in your answer.* (14)
 - (b) Identify **six** benefits and **six** drawbacks of investment trusts. (12)
 - (c) State **six** benefits of using a discretionary fund manager for Jason and Carrie's open-ended investment company (OEICs), unit trusts and NISAs. (6)
 - (d) State **six** benefits of using a wrap/platform for their OEICs, unit trusts and NISAs. (6)
5. Jason and Carrie want to maximise the value of the estate passed to their children. They are concerned about the potential Inheritance Tax (IHT) liability payable on Carrie's death assuming Jason dies first.
- Comment on their current situation and identify any weaknesses in their existing investment and pension arrangements with regards to their IHT planning objective. *No calculation required.* (12)
6. Carrie wants to protect the full value of her shares in Myers Ltd should she suffer a serious illness, and for her family to receive the full value on her death in an IHT efficient manner. She intends to set up a first event, life and critical illness policy on her own life, written to her own normal retirement age to help achieve this.
- Candidates will be rewarded for supporting their recommendations with relevant evidence and demonstrating how their recommendations work holistically to meet their clients' objectives.*
- Recommend and justify how Carrie could set up a suitable shareholder agreement in order to meet this objective. (14)

7. With regards to Jason and Carrie's longer-term financial objectives:

Candidates will be rewarded for supporting their recommendations with relevant evidence and demonstrating how their recommendations work holistically to meet their clients' objectives.

(a) Detail and justify why recommending Jason and Carrie place £150,000 from their existing portfolio of OEICs, unit trusts and investment trusts into a discretionary trust may be suitable to meet their Inheritance Tax (IHT) planning objectives. (10)

(b) Explain how using a spousal bypass trust for Carrie's existing personal pension can help to mitigate any future IHT liability. (9)

8. Identify **seven** areas that should be taken into account at future reviews for their investment portfolio. (7)

The tax tables can be found on pages 9 – 15

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 | |
| | | <i>Final salary</i> | <i>Money purchase</i> |
| 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 (CO₂) emissions. There is no reduction for high business mileage users.

For 2014/2015:

- Cars that cannot emit CO₂ have a 0% charge.
- The percentage charge is 5% of the car's list price for CO₂ emissions of 75g/km or less.
- For cars with CO₂ emissions of 76g/km to 94g/km the percentage is 11%.
- For cars with CO₂ emissions of 95g/km to 99g/km the percentage is 12%.
- Cars with CO₂ 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 CO₂ 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% | 18% | 8% |
| | first year | reducing balance | 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 |

BLANK PAGE

BLANK PAGE

BLANK PAGE

