Chartered Insurance Institute

# AF1

## Advanced Diploma in Financial Planning

### Unit AF1 – Personal tax and trust planning

### April 2019 Examination Guide

**SPECIAL NOTICES**

**Candidates entered for the October 2019 examination should study this examination guide carefully in order to prepare themselves for the examination.**

**Practice in answering the questions is highly desirable and should be considered a critical part of a properly planned programme of examination preparation.**

# AF1 – Personal tax and trust planning

## Contents



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# IMPORTANT GUIDANCE FOR CANDIDATES

## Introduction

The purpose of this Examination Guide is to help you understand how examiners assess candidates' knowledge and their ability to apply this to a case study scenario. You can then use this understanding to help you in your preparation for the examination.

## Before the examination

**Study the syllabus carefully**
This is available online at www.cii.co.uk. All the questions in the examination are based directly on the syllabus. *You will be tested on the syllabus alone,* so it is vital that you are familiar with it.

There are books specifically produced to support your studies that provide coverage of all the syllabus areas, however you should be prepared to read around the subject. This is important particularly if you feel that further information is required to fully understand a topic or an alternative viewpoint is sought. The reading list which can be found with the syllabus provides valuable suggestions.

**Note the assumed knowledge**
For the Advanced Diploma in Financial Planning, candidates are assumed to have studied the relevant units of the Diploma in Financial Planning or the equivalent. This knowledge is set out on the relevant syllabus.

**Read widely**
If you do not have experience in advising clients whose financial needs are relatively sophisticated, *it is quite unrealistic to expect that the study of a single textbook will be sufficient to meet all your requirements.* While books specifically produced to support your studies will provide coverage of all the syllabus areas, you should be prepared to read around the subject. This is important, particularly if you feel that further information is required to fully understand a topic or an alternative viewpoint is sought. It is vital that your knowledge is widened beyond the scope of one book. The reading list which can be found with the syllabus provides valuable suggestions.

**Make full use of the Examination Guide**
This Examination Guide contains a full examination paper and model answers. The model answers show the types of responses the examiners are looking for and which would achieve maximum marks, *however, you should note that there are alternative answers to some question parts which would also gain high marks.* For the sake of clarity and brevity not all of these alternative answers are shown.

This guide and previous Examination Guides can be treated as 'mock' examination papers. Attempting them under examination conditions as far as possible, and then comparing your answers to the model ones, should be seen as an essential part of your exam preparation. The examiner's comments on candidates' actual performance in each question provide further valuable guidance. You can obtain copies of the two most recent examination guides free of charge at www.cii.co.uk.

**Know the layout of the tax tables**
Familiarise yourself with the information contained within the tax tables printed at the back of each Examination Guide. These tax tables will be provided to candidates as part of the examination paper. The tax tables enable you to concentrate on answering the questions without having to worry about remembering all the information. *Please note that you are not allowed to take your own tax tables into the examination.*

**Know the structure of the examination**
Assessment is by means of a three-hour written paper in two sections. All questions are compulsory:

**Section A** consists of one case study, worth 80 marks. You will be expected to carry out a variety of tasks, after analysing the information provided.

**Section B** consists of two shorter case studies worth a total of 80 marks. Again you will be expected to carry out a variety of tasks based upon the information provided.

Each question part will clearly show the maximum marks which can be earned.

**Appreciate the standard of the examination**
Candidates must demonstrate that they are capable of advising clients *whose overall levels of income and capital require a more sophisticated scheme of investment* than is normally prepared by a level 4 qualified adviser. These clients require a critical appraisal of the various financial planning options available to them.

**Read the Assessment information and Exam policies for candidates**
The details of administrative arrangements and the regulations which form the basis of your examination entry are available online at www.cii.co.uk/qualifications/assessment-information/introduction/. This is *essential reading* for all candidates.

# In the examination

## The following will help:

**Spend your time in accordance with the allocation of marks:**

- The marks allocated to each question part are shown on the paper;
- If a question has just two marks allocated, there are likely to be only one or two points for which the examiner is looking for, so a long answer is wasting valuable time.
- Conversely, if a question has 12 marks allocated, a couple of lines will not be an adequate answer. Always remember that if the paper is not completed, your chances of passing will be reduced considerably.
- Do not spend excessive time on any one question; if the time allocation for that question has been used up, leave some space, go on to the next question and return to the incomplete question after you have completed the rest of the paper, if you have time.

**Take great care to answer the question that has been set.**

- Many candidates leave the examination room confident that they have written a 'good' paper, only to be surprised when they receive a disappointing result. Often, the explanation for this lies in a failure to think carefully about what the examiner requires before putting pen to paper.
- Highlighting key words and phrases is a technique many candidates find useful.
- The model answers provided in this Examination Guide would gain full marks. Alternative answers that cover the same points and therefore answer the question that has been asked would also gain full marks.

**Tackling questions**

Tackle the three questions in whatever order feels most comfortable. Generally, it is better to leave any questions which you find challenging until you have attempted the questions you are confident about. Candidates' should avoid mixing question parts, (for example, 1(a)(i) and (ii) followed by 2(b)(ii) followed by 1(e)(i)) as this often leads to candidates unintentionally failing to fully complete the examination paper. This can make the difference between achieving a pass or a narrow fail.

It is vital to label all parts of your answer correctly as many question have multiple parts to them (for example, question 1(a) may have parts (i), (ii) and (iii)). Failure to fully distinguish between the separate question parts may mean that full credit cannot be awarded. It is also important to note that a full answer must be given to each question part and candidates should not include notes such as 'refer to answer given in 1(b)(i)'.

**Answer format**

Unless the question requires you to produce an answer in a particular format, such as a letter or a report, you should use 'bullet points' or short paragraphs. The model answers indicate what is acceptable for the different types of question.

Where you are asked to perform a calculation it is important to show **all** the steps in your answer. The majority of the marks will be allocated for demonstrating the correct method of calculation.

Provided handwriting is legible, candidates will **not** lose marks if it is 'untidy'. Similarly, marks are not lost due to poor spelling or grammar.

**Calculators**

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 alphabetical or numerical data and/or formulae is prohibited. You may use a financial or scientific calculator, provided it meets these requirements. The majority of the marks will be allocated for demonstrating the correct method of calculation.

# EXAMINERS' COMMENTS

**Candidates overall performance**

Overall candidates performed fairly consistently.

Candidates performed solidly on the calculation questions and in particular high marks were achieved on the Income Tax question in Section A. This clearly demonstrated that candidates had practised this type of calculation including the layout.

The Capital Gains Tax calculation in question two included assets which have particular rules regarding their treatment; this did cause problems for the less prepared candidate, however a pleasing number did achieve high marks, again demonstrating they had not only practised this type of calculation but had ensured the layout was correct.

Question 2 part (c), on Powers of Attorney, was not well answered, particularly part (ii). Many candidates wrote pages of what they knew about Lasting Power of Attorneys (LPAs) without their answers referring to Stanley. Candidates should remember that answers in advanced financial planning papers should relate back to the information that is given in the case study. It is stated that Stanley would like Mabel to manage his finances and if she is unable to then he would like their son to take over. Very few candidates mentioned that their son could be included as a replacement attorney.

Question 3 part (a)(i) and (a)(ii) tested the tax position of a non-domiciled UK resident. Some candidates gave very good answers and performed well. However, in the main this area still stands out as one where candidates perform poorly. This is a key part of the syllabus, so future candidates should ensure they cover it in full in their revision.

**Question 1**

Part (a) was answered well. If candidates went wrong, it was generally by including the group income protection policy premiums which are not treated as a benefit-in-kind and taking a pension contribution from Amy's salary when this was a personal contribution into her self-invested personal pension (SIPP). Most candidates did however correctly treat the Venture Capital Trust (VCT) tax relief as a tax reducer and a pleasing number also correctly extended the basic rate tax band by the amount of Amy's gross personal pension contribution.

In part (b) answers generally, did not provide sufficient detail to gain high marks. The better candidates did realise that during her career break Amy may not have received National Insurance credits unless she had been claiming child benefit.

Part (c) tested knowledge on salary sacrifice and again the answers provided by candidates generally did not include the detail that was needed to gain full marks.

In part (d) interest free employer loans were tested, and this was generally answered well by candidates.

In part (e) many candidates were able to give some correct detail on disclaimers as they equally apply to deeds of variation. However, the key differences were missed by many, in that Carol must not have already accepted the inheritance and that it will pass back into the residue of the estate. Better prepared candidates were able to relate the question to the case study and by doing so gained marks for making the comment that the disclaimed inheritance will go to Amy and not Carol's children as she wanted.

Part (f) was not answered well by the majority of candidates. A few candidates even confused offshore funds with offshore bonds. A few well prepared candidates did however answer part (ii) well and gave very good explanations of the differences in reporting fund and non-reporting fund tax treatment.

Part (g) tested taxation of investment bonds not as a calculation but as an explanation and a few candidates gave comprehensive answers that were awarded high marks. Where candidates did use correct figures to explain the treatment, credit was also given.

In part (h) which tested Individual Voluntary Arrangements (IVAs), varying levels of knowledge was demonstrated by candidates. Some candidates answered as if they had been asked about the bankruptcy process. Better answers were given for part (h)(ii) which asked for the advantages for Ian using an IVA compared with him being made bankrupt.

**Question 2**

In part (a) the Capital Gains Tax (CGT) calculation included a holiday flat, a painting, silverware and Mabel also had registered losses. Some candidates gave excellent answers to the question which clearly demonstrated they had studied this area well and had practiced laying out their workings.

Others were not so well prepared and did not realise that as a chattel the silverware was exempt as the sale value was below £6,000 and for the painting, as the sale price was over £6,000, the chargeable gain cannot exceed 5/3 of the excess proceeds over £6,000; this meant two calculations were required to see which gave the lower amount. Candidates needed to use the information in the case study to then finish the calculation, in particular the fact that Mabel had a State Pension which was fully covered by her personal allowance. It was disappointing that a number of candidates thought that her remaining unused personal allowance for Income Tax could be used against her capital gains. This is not the case. The better candidates understood that losses and the annual exempt amount can be used against the asset that is taxed at the highest rate which in this scenario was the holiday flat.

Part (b) asked how HM Revenue & Customs might treat a failure to report accurately a capital gain. Most candidates correctly identified that a penalty or fine might apply. Few candidates were able to provide enough information to gain high marks.

Powers of Attorney feature in most exam papers in one way or another. In Part (c) candidates were asked why an Ordinary Power of Attorney would not suit the clients' needs and why the clients should make and register both types of LPA. In the majority of cases candidates did not give enough detail to perform well.

Part (d) tested the circumstances in which an attorney can be removed and this was answered very well; high marks were achieved by many candidates.

**Question 3**

Part (a) covered residence and domicile. Elize was domiciled in Iceland and resident in the UK and the questions asked how her Iceland investments and rental income would be taxed if she stayed domiciled in Iceland as well as if she elected to be UK domiciled. Some candidates gave excellent answers explaining both the arising basis and remittance basis in sufficient detail to gain high marks.

Part (b) was answered very well with a pleasing number of candidates demonstrating good knowledge of holdover relief.

Part (c) was also well answered by the majority of candidates, although some gave the general duties of trustees whereas the question had specifically asked for the investment duties.

Part (d) asked for two calculations; the periodic charge and the exit charge on the discretionary trust. Some candidates performed very well in part (i) and correctly deducted the Nil Rate Band (NRB) from the trust fund value and taxed the remaining £125,000 at 6% to give an effective rate of 1.67%. However, very few candidates then used the effective rate to work out the periodic charge.

Some candidates incorrectly used the NRB when calculating the exit charge, but many correctly calculated that the number of complete quarters since the last periodic charge was one.

Part (e) was well answered although some candidates are still not relating their answers to the case study to pick out relevant factors. The case study clearly states that John would like an income from the fund to help with potential university costs for his children so candidates would have gained higher marks if they had made some mention of this in their answer.

Chartered Insurance Institute

# AF1

# Advanced Diploma in Financial Planning

## Unit AF1 – Personal tax and trust planning

### April 2019 examination

**SPECIAL NOTICES**

**All questions in this paper are based on English law and practice applicable in the tax year 2018/2019, 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 AF1 – Personal tax and trust planning

## 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 as follows:

- Section A: 80 marks
- Section B: 80 marks

- You are advised to spend approximately 90 minutes on Section A and 90 minutes on Section B.

- 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.

- 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.**

## SECTION A

**This question is compulsory and carries 80 marks**

**Question 1**

**Read carefully all information provided in the case study before attempting the questions. Your answers should take into account the client's circumstances as set out in the case study. Please carry out ALL of the tasks (a), (b), (c), (d), (e), (f), (g) and (h) which follow.**

Amy, aged 53, lives with Ian, aged 48 and her three adult children. They all live in a house which is owned solely by Amy. Ian has little in the way of savings or assets in his own name.

Amy is an accountant and although she took a career break of eight years when her children were infants, she is now a director for an advertising company. Her basic salary is £105,000 per annum with an annual bonus of 20%. Amy's employer provides private medical insurance (PMI) and group income protection, paying the premiums per annum of £1,200 for the PMI and £1,800 for the group income protection. Amy contributes 5% gross of her basic salary into her existing self-invested personal pension (SIPP) into which her employer pays 8%. She also receives £1,200 per month maintenance payments from her ex-husband.

Amy's mother died nine months ago. Amy and her sister Carol are the beneficiaries of the estate awaiting grant of probate. Carol has stated that she has sufficient assets for her needs and so would like to re-direct her share of her mother's estate to her children.

Ian has run his own business as a recruitment consultant for the last 20 years but recently business has declined, and no profits have been made in the last six months. He would like to re-train and Amy is considering helping him by arranging an interest free loan from her employer.

In the 2018/2019 tax year Amy invested £35,000 into newly issued shares of a Venture Capital Trust. She also holds the following savings and investments:

| Investment | Current Value | Income received in 2018/2019 |
|---|---|---|
| Stocks and Shares ISA - UK equity funds | £32,000 | £1,280 |
| Current account | £12,000 | 0 |
| Deposit account | £35,000 | £350 |
| F & D Offshore Corporate Bond | £59,000 | £2,950 |
| Portfolio of directly held FTSE 100 shares | £50,000 | £3,000 |
| Onshore single premium assurance bond – commencing 1st June 2009 with an investment of £50,000 | £91,000 | Amy has taken 5% per annum on each policy anniversary since inception - except for the 1 June 2015 when she made a withdrawal of £10,000 |

Ian has been borrowing on credit cards to keep his business afloat. The current outstanding balances total £40,000. Ian is becoming increasingly concerned that he will not be able to meet the monthly repayments.

**Questions**

*To gain maximum marks for calculations you **must** show **all** your workings and express your answers to **two** decimal places.*

**(a)** Calculate, **showing all your workings**, Amy's Income Tax liability for the 2018/2019 tax year. **(15)**

**(b)** Describe in detail Amy's entitlement to State retirement benefits. **(8)**

**(c)** Explain to Amy, **using figures where appropriate**, the financial impact of sacrificing her annual bonus from her employer for an additional pension contribution to her SIPP. **(6)**

**(d)** Explain to Amy how an interest-free employer loan is treated for Income Tax purposes, should she decide to take this to help Ian re-train. *No calculation is required.* **(4)**

**(e)** **(i)** State the conditions that need to apply to enable Carol to use a disclaimer on her share of her mother's estate. **(8)**

**(ii)** State how a deed of variation will help Carol achieve her objective compared with using a disclaimer. **(2)**

**(f)** **(i)** Explain briefly how offshore funds acquire and maintain reporting status. **(3)**

**(ii)** Compare the taxation treatment of a reporting fund with a non-reporting fund. **(8)**

**(g)** Explain in full how Amy's investment bond will be taxed assuming she fully encashes it in May 2019. *Assume her total income in 2019/2020 is the same as she received in 2018/2019*. **(12)**

**(h)** Ian is concerned about being made bankrupt. Explain to him:

**(i)** the process for establishing an Individual Voluntary Arrangement (IVA); **(9)**

**(ii)** the **advantages** of using an IVA compared with bankruptcy. **(5)**

**Total marks for this question: 80**

**SECTION B**

**Both questions in this section are compulsory and carry an overall total of 80 marks**

**Question 2**

**Read carefully all information provided in the case study before attempting the questions. Your answers should take into account the client's circumstances as set out in the case study. Please carry out ALL of the tasks (a), (b), (c) and (d) which follow.**

Stanley, aged 75, is married to Mabel, aged 71. Stanley was recently diagnosed with the early stages of Alzheimer's. Mabel is in excellent health for her age.

In the 2018/2019 tax year Stanley received pension income of £56,000. Mabel received a State Pension of £7,850.

Mabel has £5,000 of registered capital losses from previous tax years. During the 2018/2019 tax year the couple sold the following assets:

| Asset | Acquisition value | Sale price | Costs | Notes |
|---|---|---|---|---|
| Holiday Flat | £30,000 | £91,000 | £8,500 | Property was inherited by Mabel and has always been held in her sole name. The property has never been the couple's principle residence. |
| Painting | £5,900 | £12,500 | £500 | Inherited by Stanley. Transferred into Mabel's sole name ten years ago when painting was valued at £9,800. |
| Silverware | £400 | £5,700 | £250 | Owned jointly until shortly before sale when Stanley transferred his share to Mabel. |

Stanley would like Mabel to manage his finances formally as soon as possible. In the event that Mabel is unable to act in this capacity Stanley would like their son to take responsibility for both of them.

**Questions**

*To gain maximum marks for calculations you **must** show **all** your workings and express your answers to **two** decimal places.*

**(a)** Calculate, **showing all your workings**, Mabel's Capital Gains Tax (CGT) liability for the 2018/2019 tax year. **(12)**

**(b)** Explain how HM Revenue & Customs may treat a failure to report accurately a capital gain. **(6)**

**(c)** Explain in detail why:

**(i)** an Ordinary Power of Attorney would not meet their needs; **(4)**

**(ii)** Stanley should make and register both types of Lasting Power of Attorney. **(7)**

**(d)** Outline the circumstances in which Mabel could be removed as an attorney under one or both types of Lasting Power of Attorney. **(11)**

**Total marks available for this question: 40**

**Question 3**

**Read carefully all information provided in the case study before attempting the questions. Your answers should take into account the client's circumstances as set out in the case study. Please carry out ALL of the tasks (a), (b), (c), (d) and (e) which follow.**

John, aged 48, is UK resident and UK domiciled. He and his minor children from a previous relationship recently returned to the UK from Iceland. While abroad, John married Elize, who is domiciled in Iceland but now resident in the UK. Elize has no children.

In Iceland Elize has a portfolio of shares worth £100,000 and her former home which is privately rented.

On 1 July 2009 John's mother, Susan, gifted £200,000 into a discretionary trust with John and his children as potential beneficiaries. Susan will shortly transfer a portfolio of unit trusts worth £160,000 into this trust.

John is a trustee of the trust with no real investment experience. He would like to generate an income in the future to help with potential university costs for the children. John is keen to understand his responsibilities and how the trust is treated for tax purposes.

**Questions**

*To gain maximum marks for calculations you **must** show **all** your workings and express your answers to **two** decimal places.*

**(a)** Describe to Elize how her Iceland investments and rental income will be taxed for Income Tax and Capital Gains Tax (CGT):

**(i)** if she remains domiciled in Iceland; **(6)**

**(ii)** if she elects to be UK domiciled. **(2)**

**(b)** Explain to Susan and John the CGT implications of transferring the portfolio of unit trusts into the discretionary trust and subsequently to a beneficiary. **(7)**

**(c)** Outline to John the investment duties as a trustee. **(7)**

**(d)** **(i)** Calculate, **showing all your workings**, the periodic charge at the $10^{th}$ anniversary of the discretionary trust. *Assume the value at that time is £450,000.* **(7)**

**(ii)** State and calculate, **showing all your workings**, the Inheritance Tax charge on final distribution of the discretionary trust. *Assume the trust comes to an end in November 2019 when the fund is worth £455,000*. **(5)**

**(e)** State the relevant factors that could cause John as trustee to review the investment policy of the discretionary trust. **(6)**

**Total marks for this question: 40**

**NOTE ON MODEL ANSWERS**
**The model answers given are those which would achieve maximum marks. However, there are alternative answers to some question parts which would also gain high marks. For the sake of clarity and brevity not all of these alternative answers are shown. An oblique (/) indicates an equally acceptable alternative answer.**

**Model answer for Question 1**

**(a)**

| | **Non Savings £** | **Savings £** | **Dividends £** |
|---|---|---|---|
| Salary | 105,000 | | |
| Bonus | 21,000 | | |
| P11D benefit - PMI | 1,200 | | |
| Bank interest | | 350 | |
| Offshore corporate bond fund - interest distribution | | 2,950 | |
| Dividends from portfolio | | | 3,000 |
| | 127,200 | 3,300 | 3,000 |

Group Income Protection (IP) - not treated as a benefit-in-kind.
Maintenance payments - not taxable.

Total income = £133,500 so Amy has no personal allowance.

Basic rate band extended by pension contribution - £105,000 x 5% = £5,250

**Tax payable**

**Non Savings**
£39,750 x 20% = £7,950
£87,450 x 40% = £34,980

**Savings**
£3,300 - £500
= £2,800 x 40% = £1,120

**Dividends**
£3,000 - £2,000
= £1,000 x 32.5% = £325

Total = £44,375

Less income tax relief on the Venture Capital Trust; £35,000 x 30% = £10,500
= £33,875

**(b)** *Candidates would have gained full marks for any eight of the following:*

- Amy will receive the new/single tier State Pension/£164.35.
- At age 67.
- She will get the full amount if she has paid or been credited with 35 years' worth of National Insurance contributions (NICs).
- No State Pension is available unless 10 years of credits/payments made.
- During her career break she may not have received National Insurance (NI) credits;
- unless she claimed Child Benefit;
- until the youngest child was age 12.
- The credits are automatically added to her NIC record.
- Credit can be obtained by making voluntary contributions/Class 3.

**(c)**

- Amy and her employer both save NICs.
- Amy = £21,000 x 2% = £420.
- Her employer = £21,000 x 13.8% = £2,898.
- Employer may or may not choose to pass on the NIC savings to Amy;
- increasing the amount being paid into Amy's pension by £420/£3,318.
- £5,600 of her personal allowance will be reinstated.

**(d)**

- Amy will be taxed on the benefit she receives/treated as benefit-in-kind.
- Based upon official rate given by HM Revenue & Customs;
- as Amy will not pay any interest she will be taxed on the amount borrowed at 2.5%.
- If the loan does not exceed £10,000 it is not taxable.

**(e)** **(i)**

- Carol must not have already accepted the inheritance/agree to forgo.
- Carol has 15 months to do so (must be done within two years of death).
- There must be no consideration for money or money's worth.
- Carol must sign the disclaimer.
- It must contain a statement that the disclaimer affects Inheritance Tax as if the disclaimed benefit had never been conferred.
- The disclaimer is not treated as a transfer of value.
- The property is not treated as passing to Carol and passes back into the residue of the estate.
- The disclaimed inheritance will go to Amy and not Carol's children.

**(ii)**

- By using a deed of variation Carol can control where the estate goes.
- With a disclaimer she cannot control where the property goes.

**(f)** **(i)**
- Funds must apply to HM Revenue & Customs for reporting fund status.
- This will be granted where funds report details of all its income to HM Revenue & Customs.
- A fund retains reporting status as long as it complies with the reporting fund rules.

**(ii)** **Reporting fund**
- Subject to Income Tax on any income arising whether distributed or not.
- Dividends are treated in the same way as UK based funds/use of dividend allowance/tax rates.
- Interest is treated in the same way as UK based funds.
- Any capital gains on sale are subject to the usual Capital Gains Tax (CGT) rules.

**Non-reporting fund**
- Gains on disposal, which includes accumulated income, calculated on CGT principles.
- But the annual exempt amount is not available.
- The gain is taxed as income at 20%, 40% or 45%.
- The starting rate for savings income, the dividend allowance and the Personal Savings Allowance are not available.

**(g)**
- A full surrender in May 2019 will be a chargeable event.
- The final encashment value is £91,000.
- To this add all the previous withdrawals of £32,500 (9 years x £2,500 + £10,000 in June 2015).
- From this (£123,500) we deduct the original investment (of £50,000);
- and deduct the chargeable gain of £7,500 in June 2015.
- (£91,000 + £32,500) - (£50,000 + £7,500) = £66,000;
- £66,000 is added to her total income in 2019/2020 (assume the same as 2018/2019) £133,500;
- as this pushes her into additional rate tax, she can use top slicing.
- The gain is divided by 9 full years (£66,000 / 9 = £7,333.33).
- None of the top slice falls into additional rate tax (£133,500 + £7,333.33 = £140,833.33);
- so £66,000 is taxed at the difference between basic and higher rate (x 20% = £13,200);
- as basic rate is deemed to have been paid in the fund.

**(h)** **(i)**

- Ian makes a formal proposal to his creditors that he will repay part or all of the debt.
- Ian must apply to the court;
- and must be helped by an Insolvency practitioner.
- Creditors' meeting held and if 75% of creditors by value agree proposals are accepted.
- All creditors are then legally bound by the Individual Voluntary Arrangement (IVA).
- The insolvency practitioner oversees repayments/supervises him.
- Ian may apply to the court for the grant of an interim order;
- this prevents creditors from proceeding with a bankruptcy petition.
- An IVA usually lasts five years.

**(ii)**

- Ian is closely involved in the process.
- It costs less than bankruptcy.
- The restrictions of bankruptcy are avoided.
- He will be able to act as a director.
- Ian avoids the stigma of being made bankrupt.

**Model answer for Question 2**

**(a)** **Flat**
£91,000 - (£30,000 + £8,500) = £52,500

**Painting**
Gain on painting is the lesser of:
Actual gain: £12,500 - (£5,900 + 500) = £6,100 and
£6,500 x 5/3 = £10,833.33
Where proceeds are more than £6,000 the chargeable gain on disposal cannot exceed 5/3 of the excess over £6,000 so the figure of £6,500 is used (£12,500 - £6,000) multiplied by 5/3) - the gain used is therefore £6,100 as this is the lower of the two figures.

**Silverware**
Exempt as a chattel and disposal is less than £6,000

**Exemption and losses deducted from flat**
£52,500 - (£11,700 + £5,000) = £35,800

**Basic rate tax band available**
£34,500

Flat: £34,500 x 18% = £6,210
£1,300 @ 28% = £364
Painting: £6,100 x 20% = £1,220

**Total**
£6,210 + £364 + £1,220 = £7,794

**(b)** *Candidates would have gained full marks for any six of the following:*

- May charge a penalty/fine;
- if they believe the inaccurate reporting is due to lack of reasonable care.
- The penalty will be a percentage of the correct/tax due;
- and will be increased if they believe the inaccurate reporting was deliberate.
- Penalty may be reduced/waived if the individual concerned tells HM Revenue & Customs about the error;
- and cooperates with HM Revenue & Customs in establishing the correct tax payable.
- The tax due must be paid.

**(c)** **(i)**

- An Ordinary Power of Attorney can only be used in respect of financial decisions/ cannot be used for health care decisions;
- and can only be used whilst Stanley is mentally competent.
- If Mabel wishes to continue to act for him once competence is lost, she would have to apply to the Court of Protection;
- which takes time/is costly/unlikely to grant her the powers that a Lasting Power of Attorney (LPA) would.

**(ii)**

- They are not valid until they are registered.
- With a financial LPA Stanley can give permission for Mabel to act for him whilst he is mentally competent;
- and can continue once he loses competence.
- A Health and Welfare LPA can only be used once Stanley has lost competence.

- Mabel can be shown as the only attorney;
- and their son can be included as a replacement attorney;
- ensuring the LPAs remain in force if Mabel is unable to act.

**(d)**

- Whilst Stanley is mentally competent;
- he could effect a deed of revocation to remove Mabel as an attorney.

- If they divorce, she will be unable to act;
- unless it is explicitly stated otherwise in the LPA.

- If Mabel becomes bankrupt/applies for a debt relief order;
- she can no longer act as an attorney under the financial LPA;
- but can continue under the Health and Welfare LPA.

- Mabel will be removed in the event she loses mental competence/or dies.

- If Mabel is shown to be abusing her power;
- the Office of the Public Guardian can remove her.

- Mabel can resign or refuse to act.

**Model answer for Question 3**

**(a)** **(i)** *Candidates would have gained full marks for any six of the following:*

- UK resident non-domiciles have two options: the arising basis;
- or Elize can apply for the remittance basis;
- where her overseas income and gains are £2,000 or more.
- Only income then brought into the UK will be taxable in the UK;
- but she will lose any personal allowance/CGT annual exempt amount.
- Remittance basis charge will apply once she has been resident for seven of the previous nine tax years = £30,000.
- If she is resident for 12 of the previous 14 tax years this increases to £60,000.

**(ii)**

- Elize's worldwide income and capital gains would be subject to UK Income Tax and CGT.
- She will no longer be entitled to use the remittance basis in respect of investment income in Iceland.

**(b)** *Candidates would have gained full marks for any seven of the following:*

- Transferring unit trusts to a discretionary trust is a disposal for CGT purposes on the settlor;
- taxed at their marginal rate of either 10% or 20%.
- A settlor can elect for holdover relief;
- because the gift is into a discretionary trust/is a chargeable lifetime transfer.
- CGT is then deferred until the donee disposes of the assets.
- The trustees would be liable to CGT at 20% unless;
- they elect for holdover relief on the transfer out of the trust;
- with the beneficiaries agreement.

**(c)**

- Obtain and consider proper advice.
- Duty of care to act appropriately/invest assets as if they are his own/acting in the best interests of beneficiaries.
- Monitor investments regularly/review.
- Take note of the standard investment criteria.
- Consider suitability of the investment/attitude to risk.
- Need for diversification.
- Make changes to investments if appropriate/rebalancing.

**(d)** **(i)** £450,000 - £325,000 = £125,000

£125,000 x 6% (30% x 20%) = £7,500

Effective rate of tax = £7,500 / £450,000 = 1.67%

£450,000 x 1.67% = £7,515

**(ii)**
- The trust will be subject to an exit charge.
- £455,000 x the number of complete quarters since the last periodic charge;
- = 1/40;
- Multiplied by the effective rate used at the last periodic charge - 1.67%
- Exit charge is £189.96

**(e)**
- Commencement of university fees or living costs for the children.
- Death or illness of a beneficiary.
- Change of circumstances for potential beneficiaries e.g. marriage.
- Where investment performance has not been as expected.
- Economic or legislative changes.
- Change in tax position of beneficiary/suitability/attitude to risk.

**All questions in the October 2019 paper will be based on English law and practice applicable in the tax year 2019/2020, unless stated otherwise and should be answered accordingly.**

**The Tax Tables which follow are applicable to the October 2018 and April 2019 examinations.**

# INCOME TAX

| RATES OF TAX | 2017/2018 | 2018/2019 |
|---|---|---|
| Starting rate for savings* | 0% | 0% |
| Basic rate | 20% | 20% |
| Higher rate | 40% | 40% |
| Additional rate | 45% | 45% |
| Starting-rate limit | £5,000* | £5,000* |
| Threshold of taxable income above which higher rate applies | £33,500 | £34,500 |
| Threshold of taxable income above which additional rate applies | £150,000 | £150,000 |
| Child benefit charge: | | |
| 1% of benefit for every £100 of income over | £50,000 | £50,000 |

**not applicable if taxable non-savings income exceeds the starting rate band.*

| | |
|---|---|
| Dividend Allowance | £2,000 |
| Dividend tax rates | |
| Basic rate | 7.5% |
| Higher rate | 32.5% |
| Additional rate | 38.1% |
| Trusts | |
| Standard rate band | £1,000 |
| Rate applicable to trusts | |
| - dividends | 38.1% |
| - other income | 45% |

| MAIN PERSONAL ALLOWANCES AND RELIEFS | 2017/2018 | 2018/2019 |
|---|---|---|
| Income limit for Personal Allowance § | £100,000 | £100,000 |
| Personal Allowance (basic) | £11,500 | £11,850 |
| Married/civil partners (minimum) at 10% † | £3,260 | £3,360 |
| Married/civil partners at 10% † | £8,445 | £8,695 |
| Transferable tax allowance for married couples/civil partners | £1,150 | £1,190 |
| Income limit for Married couple's allowance† | £28,000 | £28,900 |
| Rent a Room relief | £7,500 | £7,500 |
| Blind Person's Allowance | £2,320 | £2,390 |
| Enterprise Investment Scheme relief limit on £1,000,000 max** | 30% | 30% |
| Seed Enterprise Investment relief limit on £100,000 max | 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.*
*** maximum for 'standard' investment but for 'knowledge intensive' investment, the limit is £2,000,000.*

| | 2017/2018 | 2018/2019 |
|---|---|---|
| Child Tax Credit (CTC) | | |
| - Child element per child (maximum) | £2,780 | £2,780 |
| - family element | £545 | £545 |
| Threshold for tapered withdrawal of CTC | £16,105 | £16,105 |

# NATIONAL INSURANCE CONTRIBUTIONS

| Class 1 Employee | Weekly |
|---|---|
| Lower Earnings Limit (LEL) | £116 |
| Primary threshold | £162 |
| Upper Earnings Limit (UEL) | £892 |

| Total earnings £ per week | CLASS 1 EMPLOYEE CONTRIBUTIONS |
|---|---|
| Up to 162.00***** | Nil |
| 162.01 – 892.00 | 12% |
| Above 892.00 | 2% |

**This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £116 per week. This £116 to £162 band is a zero-rate band introduced in order to protect lower earners' rights to contributory State benefits e.g. the new State Pension.*

| Total earnings £ per week | CLASS 1 EMPLOYER CONTRIBUTIONS |
|---|---|
| Below 162.00** | Nil |
| 162.01 – 892 | 13.8% |
| Excess over 892.00 | 13.8% |

*** Secondary earnings threshold.*

| | |
|---|---|
| **Class 2 (self-employed)** | Flat rate per week £2.95 where profits exceed £6,205 per annum. |
| **Class 3 (voluntary)** | Flat rate per week £14.65. |
| **Class 4 (self-employed)** | 9% on profits between £8,424 - £46,350.<br>2% on profits above £46,350. |

# PENSIONS

| TAX YEAR | LIFETIME ALLOWANCE |
|---|---|
| 2006/2007 | £1,500,000 |
| 2007/2008 | £1,600,000 |
| 2008/2009 | £1,650,000 |
| 2009/2010 | £1,750,000 |
| 2010/2011 | £1,800,000 |
| 2011/2012 | £1,800,000 |
| 2012/2013 | £1,500,000 |
| 2013/2014 | £1,500,000 |
| 2014/2015 | £1,250,000 |
| 2015/2016 | £1,250,000 |
| 2016/2017 | £1,000,000 |
| 2017/2018 | £1,000,000 |
| 2018/2019 | £1,030,000 |

## 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.

## ANNUAL ALLOWANCE

| TAX YEAR | ANNUAL ALLOWANCE |
|---|---|
| 2011/2012 | £50,000 |
| 2012/2013 | £50,000 |
| 2013/2014 | £50,000 |
| 2014/2015 | £40,000 |
| 2015/2016 | £40,000~ |
| 2016/2017 | £40,000* |
| 2017/2018 | £40,000* |
| 2018/2019 | £40,000* |

*~ increased to £80,000 for pension input between April - 8 July 2015. If not used, can be carried forward to pension input period of 9 July 2015 - 6 April 2016, subject to a maximum of £40,000.*

**tapered at a rate of £1 for every £2 of adjusted income in excess of £150,000 where threshold income exceeds £110,000.*

| MONEY PURCHASE ANNUAL ALLOWANCE | 2017/2018 | 2018/2019 |
|---|---|---|
| | £4,000 | £4,000 |

## ANNUAL ALLOWANCE CHARGE

20% - 45% determined by the member's taxable income and the amount of total pension input in excess of the annual allowance or money purchase annual allowance.

# CAPITAL GAINS TAX

| EXEMPTIONS | 2017/2018 | 2018/2019 |
|---|---|---|
| Individuals, estates etc | £11,300 | £11,700 |
| Trusts generally | £5,650 | £5,850 |
| Chattels proceeds (restricted to five thirds of proceeds exceeding limit) | £6,000 | £6,000 |

| TAX RATES | | |
|---|---|---|
| Individuals: | | |
| Up to basic rate limit | 10% | 10% |
| Above basic rate limit | 20% | 20% |
| Surcharge for residential property and carried interest | 8% | 8% |
| Trustees and Personal Representatives | 20% | 20% |
| 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 TRANSFERS | 2017/2018 | 2018/2019 |
|---|---|---|
| Transfers made on death after 5 April 2015 | | |
| - Up to £325,000 | Nil | Nil |
| - Excess over £325,000 | 40% | 40% |
| Transfers made after 5 April 2015 | | |
| - Lifetime transfers to and from certain trusts | 20% | 20% |

*A lower rate of 36% applies where at least 10% of deceased's net estate is left to a registered 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 |
| - main residence nil rate band* | £100,000 | £125,000 |
| - UK-registered charities | No limit | No limit |

**Available for estates up to £2,000,000 and then tapered at the rate of £1 for every £2 in excess until fully extinguished*

| | | |
|---|---|---|
| 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/bride and/or groom | £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% |

Quick succession relief:

| | | | | | |
|---|---|---|---|---|---|
| - Years since IHT paid | 0-1 | 1-2 | 2-3 | 3-4 | 4-5 |
| - Inheritance Tax relief | 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 2018/2019:**

- The percentage charge is 13% of the car's list price for $CO_2$ emissions of 50g/km or less.
- For cars with $CO_2$ emissions of 51g/km to 75g/km the percentage is 16%.
- For cars with $CO_2$ emissions of 76g/km to 94g/km the percentage is 19%.
- Cars with $CO_2$ emissions of 95g/km have a percentage charge of 20% and thereafter the charge increases by 1% for every complete 5g/km to a maximum of 37% (emissions of 190g/km and above).

There is an additional 4% supplement for diesel cars not meeting Euro IV emission standards. However, the maximum charge remains 37% 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 (£23,400 for 2018/2019) e.g. car emission 90g/km = 19% on car benefit scale. 19% of £23,400 = £4,446.

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 contribution's (Class 1A) of 13.8%.

# PRIVATE VEHICLES USED FOR WORK

| | 2017/2018 Rates | 2018/2019 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

| | 2017/2018 | 2018/2019 |
|---|---|---|
| Plant & machinery (excluding cars) 100% annual investment allowance (first year) | £200,000 | £200,000 |
| 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 2016 (Corporation Tax) or 06 April 2016 (Income Tax)

| | | | |
|---|---|---|---|
| $CO_2$ emissions of g/km: | 50 or less* | 51-110 | 111 or more |
| Capital allowance: | 100% first year | 18% reducing balance | 8% reducing balance |

**If new*

# MAIN SOCIAL SECURITY BENEFITS

| | | 2017/2018 | 2018/2019 |
|---|---|---|---|
| | | £ | £ |
| Child Benefit | First child | 20.70 | 20.70 |
| | Subsequent children | 13.70 | 13.70 |
| | Guardian's allowance | 16.70 | 17.20 |
| Employment and Support Allowance | Assessment Phase | | |
| | Age 16 – 24 | Up to 57.90 | Up to 57.90 |
| | Aged 25 or over | Up to 73.10 | Up to 73.10 |
| | Main Phase | | |
| | Work Related Activity Group | Up to 102.15 | Up to 102.15 |
| | Support Group | Up to 109.65 | Up to 110.75 |
| Attendance Allowance | Lower rate | 55.65 | 57.30 |
| | Higher rate | 83.10 | 85.60 |
| basic State Pension | Single | 122.30 | 125.95 |
| | Married | 195.60 | 201.45 |
| new State Pension | Single | 159.55 | 164.35 |
| Pension Credit | Single person standard minimum guarantee | 159.35 | 163.00 |
| | Married couple standard minimum guarantee | 243.25 | 248.80 |
| | Maximum savings ignored in calculating income | 10,000.00 | 10,000.00 |
| Bereavement Payment* | | 2,000.00 | 2,000.00 |
| Bereavement Support Payment** | Higher rate - First payment | 3,500.00 | 3,500.00 |
| | Higher rate - monthly payment | 350.00 | 350.00 |
| | Lower rate – First payment | 2,500.00 | 2,500.00 |
| | Lower rate – monthly payment | 100.00 | 100.00 |
| Jobseekers Allowance | Age 18 - 24 | 57.90 | 57.90 |
| | Age 25 or over | 73.10 | 73.10 |
| Statutory Maternity, Paternity and Adoption Pay | | 140.98 | 145.18 |

**Only applicable where spouse or civil partner died before 6 April 2017.*
*** Only applicable where spouse or civil partner died on or after 6 April 2017.*

# CORPORATION TAX

| | 2017/2018 | 2018/2019 |
|---|---|---|
| Standard rate | 19% | 19% |

# VALUE ADDED TAX

| | 2017/2018 | 2018/2019 |
|---|---|---|
| Standard rate | 20% | 20% |
| Annual registration threshold | £85,000 | £85,000 |
| Deregistration threshold | £83,000 | £83,000 |

# STAMP DUTY LAND TAX

| | Residential |
|---|---|
| Value up to £125,000 | 0% |
| £125,001 - £250,000 | 2% |
| £250,001 and £925,000 | 5% |
| £925,001 and £1,500,000 | 10% |
| £1,500,001 and over | 12% |

*Stamp Duty Land Tax (SDLT) is payable in England and Northern Ireland only. Land Transaction Tax (LTT) is payable in Wales and Land and Buildings Transaction Tax (LBTT) is payable in Scotland. The rates for LTT and LBTT are different to the rates shown above.*

*Additional SDLT of 3% may apply to the purchase of additional residential properties purchased for £40,000 or greater.*

*SDLT is charged at 15% on interests in residential dwellings costing more than £500,000 purchased by certain corporate bodies or non-natural persons.*

*First-time buyers benefit from SDLT relief on purchases up to £500,000 when purchasing their main residence. On purchases up to £300,000, no SDLT is payable. On purchases between £300,000 and £500,000, a flat rate of 5% is charged on the balance above £300,000.*