Chartered Insurance Institute

AF4

Advanced Diploma in Financial Planning

Unit AF4 – Investment Planning

October 2019 Examination Guide

SPECIAL NOTICES

Candidates entered for the April 2020 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.

AF4 – Investment planning

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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. For further information contact Customer Service.

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 questions 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.

EXAMINER COMMENTS

Candidates' overall performance

Overall, candidates performed will in this paper. The paper presented candidates with a broad test across the syllabus and respective learning outcomes.

In terms of observations on areas where candidate performance could improve, candidates should be aware of the requirements of calculation questions, specifically the available marks and importance of showing all their workings. Where candidates showed all the respective stages of a calculation, they were able to gain most of the available marks. Candidates who did not show all their workings and/or did not use the correct formula were not able to attain the available marks. This was particularly evident in question 3 parts (a)(i) and (a)(ii).

Also, it was common for less well-prepared candidates to repeat some of their answers within a question-part, sometimes duplicating the same point several times. This was particularly evident in question 1 part (f).

Candidates answering with a succinct, bullet-point focused style were more effective, and this style of answer was more efficient in gaining marks than the longer, narrative style answer. Candidates should always be aware of the relationship between the number of available marks for a question-part and the number of distinct points required in their answer.

Question 1

In part (a) candidates performed very well. Almost all candidates gained the maximum marks available in parts (a)(i) and (a)(ii), although a reasonable number of candidates did not understand how to apply a negative variable.

Most candidates correctly identified the mark for 'UK equities' in part (a)(iii) although many of these candidates did not go on to achieve the mark for 'highest allocation', instead they tended to repeat '50%' from the case study. The vast majority of candidates performed well, which suggests there is a good level of revision around the core investment formulae, such as alpha and the Capital Asset Pricing Model (CAPM).

In part (b) candidates performed very well.

In part (c), candidates performed adequately. A surprisingly high proportion of candidates did not perform well because they applied either incorrect rates of Stamp Duty/Stamp Duty Reserve Tax or used the Stamp Duty Land Tax rates, leading to several totals in the high hundreds of pounds, even thousands of pounds.

Candidates performed well in part (d)(i) but performed less well in part (d)(ii). In part (d)(ii), a high number of candidates either thought that unlisted securities could not be held at all or believed that a much higher proportion of a fund's total assets could be unlisted, in many instances 20%-30%. These are high profile issues around unlisted securities within collective funds.

In part (e) candidates performed adequately. Most candidates performed well in part (e)(i). The model answer was based upon the main regulatory definition and it was pleasing to see many candidates having a good knowledge of this area. Those candidates who did not perform well generally defined attitude to risk or described risk profile.

In part (e)(ii) candidates performed adequately. In part (e)(iii), most candidates identified the relationship between long-term investment, short-term volatility and the need to consider a higher level of attitude to risk, to achieve an objective with a greater target value.
Better-prepared candidates also gained the mark for identifying that capacity for loss is also a factor.

In part (f) candidates performed adequately. Candidates who did not perform well generally did not gain the marks for 'maximum return' for 'a given/set risk' or its inverse. It is also important to highlight that candidates need to ensure they read the question carefully as some candidates gave answers, sometimes in great detail, related to the efficient market hypothesis (EMH) and not MPT.

In part (g) candidates performed adequately. In part (g)(i) many candidates compared the general characteristics of passive and active management and/or repeated elements of their answers from part (f) rather than specific reasons for using discretionary management. Candidates performed better in part (g)(ii), with a high number of candidates gaining the first quartile of the available marks.

In part (h) candidates performed well, with almost all candidates identifying two biases. Candidates who did not perform well generally did not gain the marks for identifying the reasons for the biases.

Question 2

In part (a) candidates performed adequately. Those candidates who did not perform well generally repeated terms around 'interest rate' and 'credit/default' marks, often duplicating each two or three times within their answer.

In part (b) candidates performed well. Most candidates identified at least two types of preference share and the respective characteristic. Almost all those candidates who did not perform well stated the characteristics of a normal preference share, such as fixed dividend and no voting rights. A small proportion of candidates stated general characteristics of equities and so were not able to gain any of the available marks.

In part (c) candidates performed well. Those candidates who did not perform well generally repeated information contained in the case study or stated general financial planning factors that were not aligned with the requirements of the question.

In part (d) candidates performed adequately. The majority of candidates gained more than half the available marks, with a good balance between benefits and drawbacks.

In part (e) candidates performed adequately. With benchmarks subject to greater scrutiny, including being the subject of regulatory review.

In part (f) candidates performed adequately. In part (f)(i) the majority of candidates identified the M0 and M4 terms but did not correctly describe the differences between them, often only stating their shared characteristics. Those candidates who did not perform well often omitted to define the M0 and M4 terms or defined them the wrong way around. In part (f)(ii), most candidates gained the marks for 'selling securities' and 'Interest rates rise' whereas candidates who did not perform well explained the inverse position and so were not able to gain any marks. In part (f)(iii), most candidates stated one correct reason.

Question 3

In part (a) candidates performed well. The price earnings (P/E) ratio is a core formula within the syllabus and is tested regularly, so it was not surprising to see the majority of candidates gain most of the available marks. However, as candidates were first required to calculate the earnings per share figure from the data contained in the case study, many candidates did not perform this stage correctly or omitted it from their workings. In addition, several candidates used an incorrect formula, with a very small number using the return on capital employed (ROCE) formula, which could not have been correct given it was tested in part (a)(ii), and so could not have gained any of the available marks.

In part (a)(ii), the majority of candidates knew the ROCE formula although those who did not perform well mainly subtracted the retained earnings and reserves from the share capital rather than added all these values.

In part (b) candidates performed well.

In part (c) candidates performed very well. Those candidates who did not perform well generally repeated themselves, e.g. duplicating 'profits growth', 'profits expectations' and 'profitability'. A good number of candidates identified the mark for 'inclusion/removal from index', which suggests candidates were correctly referring to the case study in order to evaluate any information contained therein that related to the question-part.

In part (d) candidates performed adequately. Too many candidates' answers were based upon a normal Enterprise Investment Scheme (EIS) rather than a Seed Enterprise Investment Scheme (SEIS). Candidates who performed well in part (d)(i) almost all then performed well in part (d)(ii), which one would expect if their level of knowledge of the product's features was detailed. As with part (d)(i), those candidates who did not perform well in part (d)(ii) mainly answered based upon an EIS rather than SEIS.

In part (e) candidates performed adequately. Only a small number of candidates identified the relative differences in time periods and the fact that a trend will eventually end. In part (e)(ii), those candidates who did not perform well mainly explained the value style of investing.

Chartered Insurance Institute

AF4

Advanced Diploma in Financial Planning

Unit AF4 – Investment planning

October 2019 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2019/2020, 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 AF4 – Investment 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.

Nicolas, aged 35, is a higher-rate and Alessandra, aged 33, is a basic-rate taxpayer. They have just inherited £200,000 and are seeking advice on investing for the long-term. Both have personal pensions but no other retirement provision. As a consequence, they understand their existing provision is unlikely to meet their retirement objectives in full and they are considering using some of their inheritance for this purpose.

Nicolas and Alessandra each have an ISA. Nicolas' ISA is invested in a multi-asset fund, the most recent one-year performance of which is set out in **Table 1** below:

Table 1

	UK Equities	Global Equities	Frontier Markets	Fixed Interest
Asset Allocation %	50	25	10	15
Fund Performance %	6	3.5	9	-3.5
Benchmark Performance %	7	4.5	5	-2

Alessandra has fully funded her ISA for the 2019/2020 tax year and is holding cash while she decides whether to make three investments, as per **Table 2** below:

Table 2

Asset	Purchase method	Investment amount
FTSE 100 listed equity	Paperless, via CREST	£11,000
FTSE SmallCap listed equity	Paper, via stock transfer	£3,850
FTSE All-Share Exchange Traded Fund (ETF)	Online platform	£5,150

There are no initial charges on the above investments other than a flat dealing fee of £9 per transaction.

Alessandra's previous tax year's ISA contributions are invested in a UK equity open-ended investment company (OEIC). The OEIC's factsheet states the fund invests on a very concentrated basis, employs a high conviction approach and holds unlisted securities. Nicolas and Alessandra have asked their adviser how these factors may affect the risk.

Their financial adviser is constructing an investment portfolio for the inheritance and is considering allocations to a range of passive index tracking funds together with a discretionary fund management (DFM) service. The adviser has mentioned to Nicolas and Alessandra that the overall portfolio will be constructed using the principles of Modern Portfolio Theory.

Questions

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

(a) **(i)** Calculate, **showing all your workings**, the overall benchmark return to which Nicolas' multi-asset fund is compared. **(5)**

(ii) Calculate, **showing all your workings**, the overall performance of Nicolas' multi-asset fund. **(5)**

(iii) Identify and explain briefly, the asset class that has made the greatest impact on performance of Nicolas' portfolio relative to the benchmark. **(3)**

(iv) Calculate, **showing all your workings**, the fund's alpha. **(6)**
*Assume a risk-free rate of return of 0.25% and a beta of 1.3. Use the market return and fund return figures from your answers in parts **(a)(i)** and **(a)(ii)** above*.

(b) State **three benefits** and **three drawbacks**, of using a stocks and shares ISA as a long-term investment vehicle for Nicolas and Alessandra's retirement, compared to a personal pension. **(6)**

(c) Calculate, **showing all your workings**, the total costs and levies payable upon the transactions set out in **Table 2** on page 4. **(8)**

(d) **(i)** Explain the diversification rules for a retail Undertakings for the Collective Investment of Transferable Securities (UCITS) OEIC, based upon the minimum number of permissible holdings and their respective percentages. **(5)**

(ii) State the maximum exposure a retail UCITS OEIC may hold in unlisted securities. **(2)**

(e) **(i)** Explain to Nicolas and Alessandra the term 'capacity for loss'. **(4)**

(ii) List the non-financial factors that can influence an investor's attitude to risk. **(6)**

(iii) Explain why Nicolas' attitude to risk may be higher for a personal pension compared to a stocks & shares ISA. **(5)**

(f) Describe the key principles of Modern Portfolio Theory, in respect of the construction of an investment portfolio. **(10)**

(g) **(i)** Outline to Nicolas and Alessandra why their financial adviser is considering using a discretionary fund manager (DFM) service as well as passive funds. **(5)**

(ii) State the potential risks of using a DFM service. **(6)**

(h) Alessandra's decision to hold cash within her ISA may be influenced by investor psychology.

State **two** reasons why she may be putting off the decision to invest, identifying **one** justification for **each** reason, from a behavioural finance perspective. **(4)**

Total marks available 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), (d), (e) and (f) which follow.

Efekan, aged 64, plans to retire during the next 12 months. He has accumulated £110,000 in a self-invested personal pension (SIPP) and £240,000 in a general investment account (GIA). The GIA is invested equally in UK fixed interest and UK equity collective funds.

Efekan has been recommended to an authorised advisory firm. As a result of an analysis of his financial position, Efekan's target income is £23,500 per annum gross from the overall portfolio after allowing for his State Pension and a deferred company pension. He has asked the financial adviser to assess the feasibility of generating income from his portfolio.

Efekan is aware that yields are low by historical standards but has read articles about alternative asset classes offering higher yields, such as aircraft leasing and leveraged loans. He is also interested in purchasing preference shares as an income producing asset within his SIPP.

Efekan has rarely reviewed the performance of his investments but is aware that most of the fund correspondence he receives mentions 'benchmarks' and 'over/under performance'. He also believes that the money supply can also be used as a benchmark and has asked the financial adviser to clarify this term.

The two existing products are held on a direct basis and the financial adviser is assessing the potential suitability of consolidating the SIPP and GIA onto a platform.

Questions

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

(a) State **five** main risks to which Efekan may be specifically exposed to if he invests in high yielding alternative income products. **(5)**

(b) State the **four** main types of preference share and identify the key characteristic for **each** type. **(8)**

(c) Identify **four** important considerations that could impact Efekan achieving his income objective in retirement. **(4)**

(d) State **five benefits** and **five drawbacks** to Efekan of transferring his existing assets to a platform, compared with holding them directly. **(10)**

(e) Identify the **three** main categories of benchmark used by fund managers. **(3)**

(f) **(i)** Describe the key differences between M0 and M4 as measures of money supply. **(4)**

(ii) Explain briefly how the Bank of England could reduce the money supply and state the effect on interest rates. **(4)**

(iii) State **two** reasons why the money supply is not suitable as a benchmark for Efekan's investment portfolio. **(2)**

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.

Kathryn is a retail client who is about to have a review meeting with her financial adviser. She has been a higher-rate taxpayer for several years and her main investment asset has been residential buy-to-let property. Following changes to the tax regime, she has been disposing of properties and is about to sell her last one. Upon completion, she will receive £320,000 sale proceeds and wishes to re-invest this amount.

As a result of the changes to the tax treatment of property investing, Kathryn is keen to access products with tax concessions, both to mitigate the tax liability arising from the property sale as well as upon any future disposal of the product(s).

Kathryn has heard about Seed Enterprise Investment Schemes (SEISs) and is keen to know more about them.

The financial adviser is aware that Kathryn has strong views on socially responsible investment and in advance of the meeting Kathryn sent her adviser details of a company listed on the FTSE-SmallCap Index: Waternova plc. The company invests in micro projects involving water technology.

Financial information for Waternova plc is set out in **Table 1** below:

Equity	Waternova plc
Share price	43p
Dividend per share	2.25p
Dividend cover	1.29x
Profit before interest and tax	£1,600,000
Share capital	£12,000,000
Retained earnings	£2,000,000
Reserves	£450,000

Kathryn has a small existing investment portfolio, which is invested in a manager of managers fund. The fund has just announced a change in manager for two of its UK equity mandates. One of the new managers invests on a contrarian style basis and the other on a momentum style basis.

Questions

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

(a) **(i)** Calculate, **showing all your workings**, the Price Earnings (P/E) ratio for Waternova plc. **(4)**

(ii) Calculate, **showing all your workings**, the return on capital employed (ROCE) for Waternova plc. **(7)**

(b) Describe the general limitations of using investment ratios, such as P/E or ROE/ROCE, when analysing a company's financial performance. ***Exclude** any limitations that are unique to a specific ratio.* **(5)**

(c) Identify **eight** main factors, **excluding** 'market movement' that could affect Watenova plc's share price. **(8)**

(d) **(i)** Explain briefly how Kathryn could use a Seed Enterprise Investment Scheme (SEIS) to mitigate her Capital Gains Tax liability. **(4)**

(ii) Explain briefly the initial Income Tax treatment of a new SEIS investment. **(4)**

(e) **(i)** Describe what is meant by a momentum investment style. **(4)**

(ii) Describe what is meant by a contrarian investment style. **(4)**

Total marks available 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) **(i)**

- UK Equities 50% x 7% = 3.5%
- Global Equities 25% x 4.5% = 1.125%
- Frontier Markets 10% x 5% = 0.5%
- Fixed Interest 15% x -2% = -0.3%

- Total = 4.83%

(ii)

- UK Equities 50% x 6% = 3%
- Global Equities 25% x 3.5% = 0.875%
- Frontier Markets 10% x 9% = 0.9%
- Fixed Interest 15% x -3.5% = -0.525%

- Total = 4.25%

(iii)

- UK equities.
- Negative contribution/underperformance.
- Highest allocation.

(iv)

- 4.25 - [0.25 + 1.3(4.83 - 0.25)]
- α = -1.95

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

Benefits

- Accessible at any time/open-ended/before age 55.
- Tax free on any withdrawals/income.
- Not subject to earnings/annual allowance.
- Not subject to lifetime allowance.

Candidates would have gained full marks for any three of the following:

Drawbacks

- No tax relief.
- £20,000/lower investment limit.
- Part of estate/cannot write under trust.
- Funds not ‘earmarked’ for retirement/temptation to access early.

(c) **FTSE 100 equity**

- £11,000 x 0.5% = £55
- Panel of Takeovers and Mergers levy £1 (*must be for FTSE 100 equity only)*

- **FTSE small cap equity**
  £3,850 x 0.5% = £19.25 rounded up to £20

ETF

- Dealing (£9 x 3) = £27
- **Total £103**

(d) **(i)**

- 16 holdings.
- Maximum 10%;
- in up to four companies.
- Maximum 5%;
- for rest/other companies.

(ii)

- 10%;
- of total assets/fund.

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

- The ability/degree/level/scope;
- to absorb/withstand;
- any negative investment event.
- Adverse effect/materially detrimental;
- on lifestyle/standard of living.

(ii)

- Previous experiences.
- Time horizon/age/state of health/dependants.
- Client objectives/ethical/religious views.
- Investor psychology/perception.
- Framing.
- Society/collective mood/political/economic environment.

(iii)

- Longer term investments/higher risk more likely to achieve objective.
- Impact of short-term volatility less.
- Not accessible till age 55.
- Effect of tax relief/employer contributions.
- Consideration given to capacity for loss different.

(f) *Candidates would have gained full marks for any ten of the following:*

- A diversified portfolio;
- of non/un/imperfectly correlated.
- Investors are risk adverse.
- Maximum return;
- for given/set risk.
- Efficient frontier;
- uses expected return of each asset.
- Standard deviation/normal distribution (of each asset);
- to produce optimal portfolio.
- Systematic risk cannot be removed/can be reduced.
- Non-systematic risk can be removed.
- Sensitivity to the market is expressed by beta is market risk.

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

- Active management/alpha.
- Wider range of asset/funds.
- Time markets/hold cash/speed of transaction.
- Bespoke.
- Influence asset allocation/core and satellite.
- Tax planning service.

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

- Financial Services Compensation Scheme (FSCS) limit exceeded/not available.
- Discretionary fund manager (DFM) uses unsuitable assets.
- Duplication with non-DFM portfolio.
- DFM acts outside its mandate/deviation from any benchmark/style drift.
- Regulatory issues.
- Overtrading/higher costs.
- Service may incur tax liability.
- Underperformance/negative alpha/does not add value.

(h) *Candidates would have gained full marks for any four of the following:*

- **Loss aversion**;
- fear of losing money on investments.

- **Overconfidence**;
- timing the market/convinced prices will fall.

- **Mental accounting**;
- compartmentalising each asset/not looking at overall position.

Model answer for Question 2

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

- Liquidity risk.
- Accessibility risk.
- Interest rate/gearing risk.
- Valuation risk.
- Diversification/correlation risk.
- Default/credit risk.

(b)

- Cumulative.
- Has right to any unpaid dividend/arrears carried over.

- Participating.
- Additional dividend linked to company profits.

- Redeemable.
- Repayable by company.

- Convertible.
- Convertible to ordinary shares on pre-set terms.

(c) *Candidates would have gained full marks for any four of the following:*

- Changes in health/life expectancy.
- Changes in taxation.
- Changes in inflation.
- Market volatility/returns.
- Sustainability of income.
- Other savings.

(d) *Candidates would have gained full marks for any five of the following:*

Benefits

- Everything in one place/consolidated valuations/reporting.
- Less admin/paperwork.
- Income flexibility.
- Pre-funding/cash account.
- Access to institutional/clean share classes.
- Access to tools.
- Discounted/lower fund charges.

Candidates would have gained full marks for any five of the following:

Drawbacks

- May pay exit charges.
- Additional platform charges/pay for services not used.
- Unnecessary functionality/too complex solution.
- May have to sell assets.
- Time out of market.
- Risk of platform failure/outage.
- Unable to hold alternative income products.

(e)

- Constraint;
- target;
- comparator.

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

- M4 includes deposits created by lending/all bank accounts.
- M0 includes operational deposits at the Bank of England.

- M4 is broad money.
- M0 is narrow money.

- M4 is indicator of economy.
- M0 is indicator of consumer spending/retail sales.

(ii)

- Selling securities;
- reduces velocity of money/increasing supply of securities;
- reduces purchasing power/prices of securities.
- Interest rate rise/higher yields.

(iii)

- Economic not financial/stock market and GDP different.
- Not a measure of return/performance.

Model answer for Question 3

(a) **(i)**
- 1.29 x 2.25 = 2.9025
- 43p/2.9025 = 14.81

(ii)
- £1,600,000 /
- (£12,000,000 + £2,000,000 + £450,000 = £14,450,000)
- x 100 = 11.0726 = 11.07%

(b) *Candidates would have gained full marks for any five of the following:*
- Credibility of the source of information/manipulation.
- Use different accounting policies/conventions/company may change accounting policy.
- Masked by exceptional/one-off items.
- Data may be obsolete/historical/not reflect current/future trading.
- Affected/masked by macro trends.
- Not considered in isolation/other factors.
- Can't compare across sectors.

(c) *Candidates would have gained full marks for any eight of the following:*
- Economic outlook.
- Political/changes in legislation/tax/regulation changes.
- Investor sentiment/broker or credit rating change/demand & supply.
- Takeover activity.
- Profit/earnings expectation.
- Capital event.
- Dividend expectation.
- Quality/change of management.
- Competitors.
- Fraud.
- Inclusion/removal from index.

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

- Invest up to £100,000 of the gain.
- Gain (on Seed Enterprise Investment Scheme SEIS) exempt from Capital Gains Tax (CGT);
- after three years.
- Reinvestment relief;
- 50% CGT exempt/property chargeable gain reduced by £50,000.
- Loss relief available.

(ii) *Candidates would have gained full marks for any four of the following:*

- 50% relief;
- up to £100,000;
- must be held for three years.
- Relief up to tax liability/paid in tax year;
- can go back one tax year.

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

Momentum

- Identify trend.
- Trend accelerating/continuing.
- Sell before trend ends.
- Ignores intrinsic value/fundamentals.
- Generally, short term.

(ii) *Candidates would have gained full marks for any four of the following:*

Contrarian

- Consensus usually wrong.
- Returns from going against the herd/ market sentiment.
- Positive when outlook negative/out of favour.
- Price less than intrinsic value/undervalued.
- Generally, long term.

All questions in the April 2020 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 2019 and April 2020 examinations.

INCOME TAX

RATES OF TAX	2018/2019	2019/2020
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	£34,500	£37,500
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 of £5,000.*

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		
Income limit for Personal Allowance §	£100,000	£100,000
Personal Allowance (basic)	£11,850	£12,500
Married/civil partners (minimum) at 10% †	£3,360	£3,450
Married/civil partners at 10% †	£8,695	£8,915
Marriage Allowance	£1,190	£1,250
Income limit for Married Couple's Allowance†	£28,900	£29,600
Rent a Room scheme – tax free income allowance	£7,500	£7,500
Blind Person's Allowance	£2,390	£2,450
Enterprise Investment Scheme relief limit on £2,000,000 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.
*** Investment above £1,000,000 must be in knowledge-intensive companies.*

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)	£118
Primary threshold	£166
Upper Earnings Limit (UEL)	£962

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS
Up to 166.00*	Nil
166.01 – 962.00	12%
Above 962.00	2%

**This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £118 per week. This £118 to £166 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 166.00**	Nil
166.01 – 962	13.8%
Excess over 962.00	13.8%

*** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £3.00 where profits exceed £6,365 per annum.
Class 3 (voluntary)	Flat rate per week £15.00.
Class 4 (self-employed)	9% on profits between £8,632 - £50,000. 2% on profits above £50,000.

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
2019/2020	£1,055,000

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
2015/2016	£40,000~
2016/2017	£40,000*
2017/2018	£40,000*
2018/2019	£40,000*
2019/2020	£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	2018/2019	2019/2020
	£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	2018/2019	2019/2020
Individuals, estates etc	£11,700	£12,000
Trusts generally	£5,850	£6,000
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 (2018/2019), two years (2019/2020).*

INHERITANCE TAX

RATES OF TAX ON TRANSFERS	2018/2019	2019/2020
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

	2018/2019	2019/2020
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*	£125,000	£150,000
- 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*

	2018/2019	2019/2020
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 2019/2020:

- The percentage charge is 16% 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 19%.
- For cars with CO_2 emissions of 76g/km to 94g/km the percentage is 22%.
- Cars with CO_2 emissions of 95g/km have a percentage charge of 23% and thereafter the charge increases by 1% for every complete 5g/km to a maximum of 37% (emissions of 165g/km and above).

There is an additional 4% supplement for diesel cars not meeting Euro 6 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 (£24,100 for 2019/2020) e.g. car emission 90g/km = 22% on car benefit scale. 22% of £24,100 = £5,302.

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

	2018/2019 Rates	2019/2020 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

	2018/2019	2019/2020
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£200,000	£1,000,000
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%	6%
Energy & water-efficient equipment	100%	100%
Zero emission goods vehicles (new)	100%	100%
Electric charging points	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%	18%	6%
	first year	reducing balance	reducing balance

**If new*

MAIN SOCIAL SECURITY BENEFITS

		2018/2019	2019/2020
		£	£
Child Benefit	First child	20.70	20.70
	Subsequent children	13.70	13.70
	Guardian's allowance	17.20	17.60
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 110.75	Up to 111.65
Attendance Allowance	Lower rate	57.30	58.70
	Higher rate	85.60	87.65
Basic State Pension	Single	125.95	129.20
	Married	201.45	201.45
Single Tier State Pension	Single	164.35	168.60
Pension Credit	Single person standard minimum guarantee	163.00	167.25
	Married couple standard minimum guarantee	248.80	255.25
	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
Jobseeker's Allowance	Age 18 - 24	57.90	57.90
	Age 25 or over	73.10	73.10
Statutory Maternity, Paternity and Adoption Pay		145.18	148.68

**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

	2018/2019	2019/2020
Standard rate	19%	19%

VALUE ADDED TAX

	2018/2019	2019/2020
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.

	Non residential
Value up to £150,000	0%
£150,001 and £250,000	2%
£250,001 and over	5%