Chartered Insurance Institute

# AF1

## Advanced Diploma in Financial Planning

### Unit AF1 – Personal tax and trust planning

### October 2019 Examination Guide

**SPECIAL NOTICES**

**Candidates entered for the July 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.**

# 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.

# EXAMINER COMMENTS

**Candidates overall performance**

Overall, candidates performed well across the main areas tested.

Once again, the calculation questions yielded high marks for most candidates, many of whom are structuring and showing their workings very well. Even with errors around some of the more technical points, high marks were still achieved for getting the rest of the calculation correct.

Some of the more technical aspects of the examination did cause problems for candidates, specifically temporary non-residence and the taxation of life assurance bonds. Candidates should make sure that they are keeping up to date with any and all changes.

While the performance of candidates as a whole was very encouraging, some are still struggling to relate their answers to the case study presented.

**Question 1**

The Inheritance Tax calculation in part (a) was generally well-answered. The majority of candidates structured the calculation well and received a good amount of marks. Most candidates correctly identified that Frank's unused Residential Nil Rate Band (RNRB) could be transferred to Peggy. However, the majority did not gain a mark for quoting the RNRB as £150,000 rather than £125,000. It should be noted that while the paper is based in the 2019/2020 tax year, the death had occurred in the previous tax year and therefore the band from that year should be used.

The most technical aspect of the calculation was the Quick Succession Relief element which was not well understood by many candidates. Often the taper percentage was quoted correctly, which gained a mark but was applied to the wrong amounts.

Part (b) related to the discretionary trust established by Frank. Candidates showed an in depth understanding of how discretionary trusts are taxed and generally achieved a high number of marks on trustee duties. Some candidates wrote at length in part (b)(iii) repeating the same principle but in different ways, only gaining one mark for that particular point. A mark that was consistently not given was where the candidate gave the answer "invest cash/invest cash promptly" without qualifying this with "if appropriate/taking into account any short-term cash needs".

Part (c) was not well answered by many candidates. Some confused the two parts of the question and gave the drawbacks in part (c)(i) rather than part (c)(ii) where it was required. A number of candidates thought that they could set up an LPA after mental capacity has been lost, which is not the case. Some went into great detail about how mental capacity is determined which did not answer the questions and did not gain any marks.

Part (d) focussed on gifting and trust taxation. Part (d)(i) was very well-answered with most candidates gaining high marks. Part (d)(ii) was less well-answered. It was looking for an explanation of how the parental settlement rules apply (or do not) to the case study and this was often missed.

Part (e) tested the new rules around the taxation of life assurances bonds and there was a clear divide between candidates who had revised this and those that had not. This posed a challenge for a number of candidates who did not fully describe the 5-stage process for calculating the tax on bond surrender comparing the unrelieved gain against the relieved gain. Candidates would have still obtained some marks for identifying how the gain is arrived at and that top-slicing could be available. While some marks were gained in both cases, the better-prepared candidate achieved higher marks.

**Question 2**

The Capital Gains Tax (CGT) calculation in part (a) was answered well by most candidates. Private residence relief (PRR) still posed a problem for some candidates. Candidates should note the format of the model answers as this will help them gain better marks in similar style questions. For example, the formula uses months and not years or quarters. Often candidates made simple errors in working out the months and did not gain all of the available marks.

Additionally, it is important for candidates to note the rules around lettings relief and the interactions between that and PRR, and that you can have both.

In part (a)(ii) few candidates described the no loss no gain disposal between the spouses or the fact that Kim would not be able to claim PRR. Many candidates assumed that the tax would be lower but the loss of the PRR and lettings relief on Kim’s portion of the gain would actually increase the tax payable, even with the additional CGT allowance.

Part (b) was not answered well by candidates, with only a handful gaining any of the marks available. This question was specifically looking for the tax treatment of capital gains for someone who is a temporarily non-resident and returns to the UK. Some candidates described the tax treatment of gains generally, which would not have been enough to achieve marks for this question.

Disappointingly, part (c) was not well answered. Many candidates noted the rate of increase wrongly and referred to the ability to take a lump sum, which is no longer an option.

Part (d) was generally well-answered although some candidates did not gain some marks as they used the incorrect bandings which are provided in the tax tables. This highlights the need for candidates to familiarise themselves with the tax tables (and exam guides) and refer back to them during the exam.

The rules around EIS and VCTs in part (e) was clearly well-studied as most candidates performed very well.

**Question 3**

The Income Tax calculation in part (a)(i) was well-answered by candidates. It is good to see that many candidates had studied the previous model answers and set out calculations in this way.

Most candidates are comfortable with the reduction in personal allowance and calculation of adjusted net income. Some struggled with the order of taxation, resulting in the wrong tax rates being used so it would be worth candidates reviewing this as part of their studies. The most common errors were around the taxation of the savings and the precedence of the starting rate savings band ahead of the Personal Savings Allowance (PSA). Another consistent error was the calculation of the remaining basic rate band – it should be noted that the dividend allowance forms part of this.

In part (a)(ii), some candidates confused employed and self-employed National Insurance contributions (NICs) and incorrectly stated that class 2 and 4 NICs would be payable. Additionally, some candidates did not gain marks where they were not specific enough in their answers. This is a fairly common structure of remuneration so it's important to understand how this works and the benefits.

Candidates generally performed well in part (b). Well-prepared candidates were able to give the higher-level detail around "wholly and exclusively" rules and the fact that company contributions are technically unlimited.

In part (c), most candidates understood the premise that marriage invalids a Will and that Caroline would be deemed to die intestate, but some did not give relevant detail. Some candidates did not gain marks as they did not identify that the discretionary trust would not be set up if the Will is invalid.

Chartered Insurance Institute

# AF1

# Advanced Diploma in Financial Planning

## Unit AF1 – Personal tax and trust 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 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) and (e) which follow.**

Andrew, aged 63, a higher rate taxpayer has two adult children, Lance and Hayley. Lance is a basic rate taxpayer and Hayley is a non-taxpayer. Hayley needs regular care as a result of the injuries she suffered in a motor accident when she was a child. Lance has two young children both under the age of 10.

Andrew's mother, Peggy, a widow, died on 1 March 2019 leaving her entire estate to Andrew. Peggy inherited her Aunt's estate of £400,000 in February 2016 following the payment of £30,000 Inheritance Tax (IHT) that was due following the administration of her estate.

Peggy's estate was comprised of the following on her death:

| | |
|---|---|
| House | £700,000 |
| Deposit accounts | £323,000 |
| Cash ISAs | £55,000 |
| FTSE listed shares | £150,000 |
| Collective investment portfolio | £101,000 |
| Personal Pension nominated to a discretionary trust | £326,000 |

Peggy's husband Frank, died in 2016, leaving his share of their house and his residual estate to Peggy. Frank made only one gift in the seven years before he died. He settled £450,000 into a discretionary trust just under four years earlier. Inheritance Tax (IHT) of £23,800 was paid at outset by the trustees. Following Peggy's death, Andrew is the only remaining trustee.

Andrew is in discussions with his solicitors to draft a Will and they have suggested he arrange a Lasting Power of Attorney (LPA) for Property & Financial Affairs.

Andrew intends to make some provision for his children and grandchildren. His income is around £10,000 a year higher than his outgoings. He has a variety of savings accounts and an onshore life assurance bond invested in a managed fund which has performed well over the years.

**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**, the IHT due as a result of Peggy's death on the 1 March 2019. **(13)**

**(b)** With regard to the discretionary trust established by Frank:

**(i)** Explain to Andrew why IHT was payable when assets were placed into the trust and how it was calculated. *No calculation is required.* **(6)**

**(ii)** Describe to Andrew why IHT was payable when his father died and how it was calculated. *No calculation is required.* **(8)**

**(iii)** State Andrew's duties as a trustee under the Trustee Act 2000. **(12)**

**(c)** If Andrew lost mental capacity without an LPA in place:

**(i)** Outline the process that would need to be followed to enable his family to manage his financial affairs. **(6)**

**(ii)** Explain the drawbacks to Andrew and his family of the approach outlined in your answer in **part (i)** above**.** **(7)**

**(d)** **(i)** Outline the exemptions and allowances that are available to Andrew when making gifts to his children and grandchildren. **(7)**

**(ii)** Explain why it would be more tax efficient for Andrew to establish an absolute trust for Lance's children, instead of Lance. **(4)**

**(iii)** Describe the ongoing income, capital gains and eventual Inheritance Tax treatment that would apply to a trust for Hayley's benefit if she qualifies as a vulnerable beneficiary. **(6)**

**(e)** Andrew would like to surrender the life assurance bond and gift the proceeds to Lance.

Explain in detail, the method used to calculate the tax payable on the surrender of the life assurance bond. *No calculation is required.* **(11)**

**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 clients' circumstances as set out in the case study. Please carry out ALL of the tasks (a), (b), (c), (d) and (e) which follow.**

Kim and Robert, both aged 65, have been married for 25 years and have three adult children. In the summer of 2016 on their retirement, they rented a property in France and have spent the last three years living there and travelling across Europe, returning to the UK for less than two weeks each year. Prior to this they had always lived and worked in the UK. They both receive income from private UK pensions and as a result pay tax at the higher rate.

In August 2019 they returned to their main residence in the UK when Robert's mother passed away. They recently inherited £500,000 from her estate and are now in the process of buying a freehold holiday home in the UK for £460,000.

Robert owned a flat prior to meeting Kim, which he lived in for five years before they married and bought their current main residence together. Robert bought the flat on 01 January 1989 for £48,000. He moved out on 1 January 1994 and the flat has been commercially let ever since. Robert completed the sale of the flat on 1 October 2019 for £280,000. Costs for sale of the property have been calculated as £3,800. Kim has never lived in the property.

Kim had a unit trust portfolio which she sold in July 2018 to assist with their costs while travelling. She had owned it for over 10 years and made a gain of £40,000.

Kim is now interested in investing in either an Enterprise Investment Scheme (EIS) or a Venture Capital Trust (VCT) and is keen to understand the taxation implications of both products.

Both Kim and Robert will be entitled to receive a State Pension at age 66. They do not think they will need the income available at that point and are considering deferring their entitlement.

**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 Capital Gains Tax (CGT) liability as a result of the sale of Robert's flat and state when it must be paid. **(12)**

**(ii)** Explain how the rented flat would have been subject to tax had Robert transferred ownership into their joint names before he sold it. *No calculation is required.* **(5)**

**(b)** Explain how Kim would account for any tax due on the sale of her unit trust portfolio in 2018. *No calculation is required.* **(4)**

**(c)** Explain how Kim and Robert would defer their State Pensions and what they would potentially receive in the future. **(3)**

**(d)** Calculate, **showing all your workings**, the Stamp Duty Land Tax due as a result of the purchase of the holiday home. **(4)**

**(e)** Explain the personal tax treatment for Kim were she to invest in:

**(i)** an EIS; **(6)**

**(ii)** a VCT. **(6)**

**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) and (c) which follow.**

Caroline, aged 58, is the sole shareholder of her own limited company. In the tax year 2019/2020, she will pay herself a salary of £8,632 and £94,000 in dividends. She has recently got engaged to Dominic and has two adult children, Eliza and Bethany, from her former marriage which ended in divorce seven years ago. Bethany has recently married and is expecting her first child.

Five years ago, Caroline invested £80,000 into an offshore life assurance bond from which she has been withdrawing £4,000 on each anniversary. She also has a joint account with her mother Anne, who does not pay tax.

Caroline's investments are:

| Owner | Investment | Current Value | Expected Income for 2019/2020 tax year |
|---|---|---|---|
| Joint | Instant Access Savings | £45,000 | £136 |
| Caroline | Cash ISA | £20,000 | £300 |
| Caroline | Portfolio of fixed interest unit trusts | £70,000 | £1,790 |
| Caroline | Portfolio of equity OEICs | £90,000 | £1,350 |
| Caroline | Offshore life assurance bond | £143,000 | - |

Caroline made a Will shortly after her divorce, naming her brother as an executor along with her solicitor. The Will makes provision for the establishment of a discretionary trust with her two daughters as beneficiaries.

**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**, Caroline's Income Tax liability in the tax year 2019/2020. **(12)**

**(ii)** Explain the benefits to Caroline's financial situation of structuring her salary and dividends as laid out in the case study. *No calculation is required.* **(9)**

**(b)** Caroline is considering making a pension contribution in the tax year 2019/2020.

Explain the taxation considerations and limitations of making:

**(i)** a personal contribution; **(4)**

**(ii)** a company contribution. **(4)**

**(c)** Explain the implications were Caroline to marry Dominic and die without making a new Will;

**(i)** in respect of her existing Will; **(5)**

**(ii)** for the distribution of her estate; **(4)**

**(iii)** if Bethany and her husband were to divorce after Caroline's death. **(2)**

**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)** £30,000 x (£400,000 - £30,000) / £400,000
= £27,750
Quick Succession Relief (QSR) = £27,750 x 40%
QSR = £11,100

Peggy's estate:

| | |
|---|---|
| House | £700,000 |
| Deposit accounts | £323,000 |
| Cash ISAs | £55,000 |
| FTSE listed shares | £150,000 |
| Collective investment portfolio | £101,000 |
| **Total** | **£1,329,000** |
| | |
| Nil rate band (NRB) | (£325,000) |
| *Late husband had used his NRB* | |
| Residence NRB | (£125,000) |
| Transferred Residence NRB | (£125,000) |
| *Inherited late husband's Residence NRB* | |
| | |
| Taxable estate | £754,000 |
| | |
| Inheritance Tax (IHT) at 40% | £301,600 |
| Less QSR | (£11,100) |
| **Total IHT payable** | **£290,500** |

**(b)** **(i)**

- The gift into trust was a chargeable lifetime transfer.
- The cumulative total value of gifts was in excess of his nil rate band.
- The excess was subject to Inheritance Tax (IHT) at the lifetime rate of 20% (half of 40%).

- Due to the amount of tax paid at outset (£23,800) he had not already used his annual gift allowances/chargeable amount reduced by £6,000.

**(ii)**

- IHT was payable as he died within seven years of making a chargeable lifetime transfer on the excess over the nil rate band

- Chargeable lifetime transfer is therefore £119,000 after a deduction of two annual gift allowances (£125,000 - £6,000);
- was subject to IHT at 40%;
- however taper relief applies/as more than three years since gift;
- reducing the IHT payable by 20%.
- Also, as there was a lifetime tax charge/tax at outset when the trust was set up;
- the IHT on death can be reduced by the tax paid/credit against further tax due.

**(iii)**

- Exercise reasonable care and diligence/duty of care/use care and skill that is reasonable/acting as a prudent businessperson.
- Ensure they are registered as the legal owners.
- Read and understand the trust deed/comply with terms of trust.
- Act impartially between the beneficiaries/in the best interests of all beneficiaries.
- Taking into account the tax position of the trust and the beneficiaries.
- Avoid conflicts of interest/keep own finances separate.

- Duty to invest any cash received into the trust appropriately, unless it is being paid out immediately.
- Invest trust money properly/standard investment criteria/taking advice/ diversifying.
- Monitor/review investments regularly.

- Keep proper accounts of all trust property/accurate records.
- Use the utmost diligence to avoid any loss/protect the trust property.
- Pay tax/self-assessment/tax enquiries/HM Revenue & Customs dealings.

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

- Application would need to be made to the Court of Protection (COP);
- via the office of the public guardian.
- A single order/court order will be granted/COP will make a judgment.
- If required hold a hearing in court/further investigation.
- Deputy appointed.
- Reviewed by the court on a regular basis.
- Deputy would usually need to provide a surety/security bond/insurance policy.
- Application and supervision fees will be payable. There may also be fees if a hearing is required.

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

- Applying to the Courts is time-consuming.
- Expensive. This could include application costs, supervision fee, hearing fees, surety bond.
- Andrew will have had no say in who will be responsible for his affairs and making decisions on his behalf.
- Andrew's assets will be inaccessible/no financial decisions can be made until the deputyship order is agreed;
- this means any costs during this time will need to be met by his family.
- A court-appointed deputy is subject to strict ongoing supervision.
- Decisions outside order will need permission of the court/can't make substantial gifts outside normal pattern/IHT planning is limited.
- Powers will be limited.

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

- Annual gift allowance – £3,000 per tax year.
- Unused allowances can be carried forward for one tax year (£6,000).
- Small gifts – £250 per person to any number of people.
- Cannot be linked to other gifts/exemptions in same tax year.
- Gifts in anticipation of marriage.
- Could gift his surplus income of £10,000;
- intended to be on a regular and habitual basis.
- And does not reduce his standard of living.
- Gifts for maintenance.

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

- A gift from Andrew would not be subject to the parental settlement rules.
- All income from the trust would be assessed as income of the grandchildren and taxed accordingly.

If Lance makes the gift:

- Parental settlement rules would apply;
- trust income is £100 or above;
- the whole amount would be taxed as income of Lance as the settlor parent.
- As the beneficiaries are minors and unmarried.

**(d)** **(iii)**

- Trustees can claim the difference between/tax reclaimed as Hayley is a non-taxpayer:
- The Income Tax that would have been paid normally/trust tax treatment and;
- the Income Tax that would have been paid if the trust income had been paid directly to Hayley/bare trust.

- The annual exempt amount for Capital Gains Tax (CGT) would be £12,000/personal rate rather than £6,000/trust rate.

- There are no periodic or exit charges for IHT.
- When Hayley dies, any assets held within the trust are treated as part of her estate and IHT may be charged.

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

- Establish if the bond has made a chargeable gain/this is a chargeable event;
- surrender value;
- plus all previous withdrawals;
- minus the total amount invested;
- and any previous chargeable gains/excesses over the accumulated 5% allowances.

- Add the full amount of the gain to Andrew's income.

- Consider the amount of taxable income for the year and identify how much of the gain falls within the Personal savings allowance/starting rate /basic/higher/additional rate for tax.
- Calculate the total tax due on the gain across all tax bands.
- Deduct the basic rate tax credit.

- Calculate the annual equivalent/top slice of the gain (divide by number of years).
- Calculate the tax on the top slice.
- Deduct the basic rate tax credit on the annual equivalent;
- multiplied by number of years;
- the relieved liability is deducted from his overall tax liability.

**Model answer for Question 2**

**(a)** **(i)**

- Disposal proceeds £280,000

- Less costs of disposal (£3,800)
- Less purchase price (£48,000)

- Less Private Residence Relief
- Period of ownership 1/01/1989 - 1/10/2019 = 369 months
- Principle residence 60 months
- + last 18 months = 78 months

- Proportion charged to Capital Gains Tax (CGT) £228,200 x 291 / 369

- Gain £179,962.60
- Less letting exemption (£40,000)

- Less annual exempt amount (£12,000)
- £127,962.60 x 28%
- = £35,829.53

- The CGT must be paid by 31 January 2021.

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

- There would have been no CGT on the transfer (treated as a no gain no loss disposal).
- Kim would have received half of the asset at Robert's original purchase price/gain spilt evenly.
- Half of the income would have been transferred to Kim.
- She could have used her own annual exempt amount of £12,000.
- Kim would not have been able to claim private residence relief or letting exemption.
- The transfer would have increased their overall CGT liability.

**(b)**

- Even though Kim was a non-UK resident in 2018 she will still be liable to CGT.
- She would have been classed as a temporary non-resident;
- as she was outside of the UK for fewer than five complete tax years.
- The gain made in 2018 is chargeable in 2019/2020 tax year when she resumed UK residence.

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

- They must defer their claim;
- for at least nine weeks to receive any increase.
- Rate of increase is 1% for every nine weeks deferred (5.8% a year).
- They cannot take the deferred amount as a lump sum.

**(d)** Purchase price = £460,000

- Up to £125,000 @ 3% = £3,750
- Above £125,000 and up to £250,000 @ 5% = £6,250
- Above £250,000 and up to £925,000 @ 8% = £16,800
- Total Stamp Duty Land Tax = £26,800

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

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

- Up to 30% income tax relief;
- on investments up to £1,000,000 in a tax year;
- £2,000,000 if £1,000,000 is in knowledge intensive companies;
- Given as an income tax reduction.
- Disposal exempt from CGT if held for three years.
- Deferral of CGT available.
- Basic Rate after two years ownership provided held on death.
- Dividends are subject to Income Tax.
- Loss relief against Income or Capital Gains Tax.

**(ii)** VCT

- Up to 30% income tax relief;
- on investment up to £200,000 per tax year.
- Given as an income tax reduction.
- Dividends are tax free.
- No CGT on disposal.
- Income tax relief withdrawn if held less than five years.

**Model answer for Question 3**

**(a)** **(i)** Taxable Income

| | Non Savings | Savings | Dividends |
|---|---|---|---|
| Salary | £8,632 | | |
| Bank Interest | | £68 | |
| Fixed interest Unit Trust | | £1,790 | |
| Equity OEICs | | | £1,350 |
| Dividends | | | £94,000 |
| **Total** | £8,632 | £1,858 | £95,350 |

Adjusted Net Income
£8,632 + £1,858 + £95,350 = £105,840

Personal Allowance Reduction
£105,840 - £100,000 / 2 = £2,920
(£12,500 - £2,920) = £9,580

Non-savings
£8,632 x 0% = 0 (within Personal Allowance)

Savings
£948 x 0% = 0 (within Personal Allowance)
£910 x 0% = 0 (within Starting Rate Savings Band)

Dividends
£2,000 x 0% = 0

£34,590 x 7.5% = £2,594.25
£58,760 x 32.5% = £19,097

Total = £21,691.25

**(ii)**
- No Income Tax is payable on the salary of £8,632.
- Salary is a deductible cost for corporation tax purposes.
- Dividends are not classed as earnings for National Insurance (NI) purposes.
- The salary is above the lower earnings limit (£118 per week)/enabling Caroline to qualify for State benefits (receive NI credits).
- Caroline does not need to pay employee/personal contributions (as her salary is not in excess of £166 per week).
- The company does not need to pay employer/company contributions (as her salary is not in excess of £166 per week).
- The £2,000 dividend allowance is available.
- Dividends are taxed at 7.5% (basic) and 32.5% (higher) rather;
- than 20% (basic) and 40% (higher) for earned income.

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

- Caroline could contribute £8,632 with tax relief/100% of salary;
- basic rate tax relief given at source.
- Her basic rate band would be extended by the gross pension contribution.
- Caroline would save 25% tax on the dividends that would fall into the extended band (32.5% less 7.5%).
- Caroline's personal allowance would be reinstated.

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

- Corporation tax relief for company;
- provided the contribution meets 'wholly and exclusively' rules.
- Companies can make unlimited pension contributions however tax relief is limited;
- contributions up to £40,000/limited to annual allowance;
- plus any available carry forward allowance.

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

- Marriage revokes the existing Will/is invalid;
- unless the Will was made in anticipation of marriage;
- otherwise Caroline is deemed to have died intestate.
- Brother will not be executor/administrators will need to be appointed;
- by the court.
- The trust will not be established.

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

- Dominic will be entitled to all personal chattels/jointly held assets;
- and a statutory legacy of £250,000;
- and half the residue of the estate absolutely.
- Eliza and Bethany will receive the other half absolutely.
- Savings account auto passes to Anne.

**(iii)**

- Bethany will receive her share of the estate absolutely.
- Husband may be entitled to claim a share of the inheritance.

**All questions in the July 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 July 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.<br>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

| | | |
|---|---|---|
| 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*

| | | |
|---|---|---|
| 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% first year | 18% reducing balance | 6% 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% |