



Chartered
Insurance
Institute

AF1

Advanced Diploma in Financial Planning

Unit AF1 – Personal tax and trust planning

October 2020 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2020/2021, 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.

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, **both questions are compulsory**.
- 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.
- It is important to show all steps in a calculation, even if you have used a calculator.
- Tax tables are provided at the right-hand side of the interface.

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.

Ralph aged 56 is married to Nicky aged 54. They have one daughter, Bethany, aged 24 who has a child of her own, Lucas aged 5.

Ralph is a self-employed architect. In the 2019/2020 tax year Ralph's total tax bill was £16,000. In the 2020/2021 tax year he expects to make a gross profit of £95,000 with total allowable business expenditure of £20,000. Ralph has been making contributions into a personal pension of £300 per month since 2015.

Ralph and Nicky receive income from the following savings and investments:

	Owner	Income (£)
Open ended investment company (OEIC) - UK equity fund	Ralph	4,300 per annum
M & D PLC corporate bond 5.56% 2035	Ralph	1,100 per annum
Seed Enterprise Investment Scheme (SEIS)	Ralph	0
Cash on deposit	Joint	430 per annum
Stocks and shares ISA - UK small companies fund	Nicky	1,900 per annum
Buy-to-let property	Nicky	750 per month

In the 2020/2021 tax year Ralph sold a portfolio of shares making a gain of £30,000. He invested the whole gain into qualifying shares in a SEIS.

Nicky is an accountant and her salary for the 2020/2021 tax year will be £60,000. She owns a buy-to-let property on which she pays £300 per month on her interest-only mortgage. The property is let at £750 per month and the running costs of the property are estimated at £2,000 per year.

Nicky has been making contributions of £800 per month net for the last five years to a self-invested personal pension, the pension is currently worth £105,000.

Bethany lives in rented accommodation with her boyfriend, Hugo. Bethany works part-time as a hairdresser; her earnings are £10,000 per annum. She also receives Child Benefit for Lucas of £1,094.60 a year. Bethany has credit card debt of £19,000 and has been unable to make the monthly repayments for the last six months. She is considering the various options she has other than bankruptcy. Hugo works in marketing and has earnings of £65,000 per annum. He is not Lucas's father.

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**, Ralph's total Income Tax liability for the tax year 2020/2021. (13)
- (ii) Calculate, **showing all your workings**, the total National Insurance contributions (NICs) Ralph will pay for the tax year 2020/2021. (5)
- (iii) State when Ralph would need to make payments relating to his Income Tax and NICs for the tax year 2020/2021 and detail what these payments are based on. (7)
- (iv) Explain in detail why Ralph should contact HM Revenue & Customs regarding his Income Tax payments for the tax year 2020/2021. (6)
- (b) (i) Explain briefly the criteria a qualifying company must meet in order to be a suitable investment for a SEIS. (5)
- (ii) Explain, **using figures where appropriate**, how the gain Ralph has made on his portfolio of shares will be treated for Capital Gains Tax purposes. (6)
- (iii) State the **two** methods Ralph could use to report his capital gain. (2)
- (c) (i) Explain, **showing figures where appropriate**, the maximum tax relievable pension contribution Nicky can make in the 2020/2021 tax year. (9)
- (ii) Calculate, **showing all your workings**, the total profit Nicky will receive from her buy-to-let property. (8)
- (d) Describe the impact of Bethany living with Hugo on the Child Benefit payments she receives. (7)
- (e) (i) Outline the factors that must be taken into account before Bethany can apply for a debt relief order (DRO). (7)
- (ii) Explain briefly the advantages to Bethany of her entering into an Individual Voluntary Arrangement as an alternative to bankruptcy. (5)

Total marks for this question: 80

Section B questions can be found on pages 7 - 11

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) and (c) which follow.

Astrid, aged 54, married Ian, aged 57 on 6 February 2020. Astrid has always been domiciled in Norway and has been a UK resident since 2005. Ian is UK resident and UK domiciled. Both Ian and Astrid own UK-based businesses. In addition, Astrid has extensive business and property interests in Norway.

Astrid has claimed the remittance basis of taxation since she arrived in the UK.

Astrid owns a flat in Manchester where her and Ian's businesses are based. She purchased the property in her sole name in June 2018.

The couple have lived together since January 2019 and occupy Astrid's property during the week. Ian owns a property in Derbyshire where they spend every weekend.

They both intend to sell their businesses in the next two to three years, at which time they will decide where they will live in their retirement.

Astrid has £200,000 to invest for their retirement and she is considering the use of an offshore fund.

QUESTIONS CONTINUE OVER THE PAGE

Questions

- (a)** Astrid and Ian have been advised that they should contact HM Revenue & Customs and nominate one of their properties as their main residence.
- (i)** Explain briefly why Astrid and Ian must make this nomination. **(2)**
 - (ii)** State the factors they should take into account when selecting which of the properties to nominate. **(6)**
 - (iii)** Outline the conditions that must be met for the nomination to be successful. **(4)**
 - (iv)** In the event that they do not make a nomination, identify **eight** factors HM Revenue & Customs will take into account in determining which property they will regard as the couple's main residence. **(8)**
- (b)** Explain why Astrid will no longer be able to claim the remittance basis of taxation in subsequent years and, outline the impact of this change on her ongoing tax affairs. **(9)**
- (c)** Describe the tax treatment of reporting and non-reporting offshore funds should Astrid choose to use them for her investment. **(11)**

Total marks available for this question: 40

Question 3

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

Sasha, aged 48, is one of the trustees of a discretionary trust, created for the benefit of her nieces, Anna aged 16, and Becca aged 23. Anna is a non-taxpayer and Becca is a basic rate taxpayer.

The original settlor of the trust stated in a letter of wishes that they would like income from the trust to be used to support Anna and Becca's education, and then the capital to be used to help them get on the property ladder at some point in the future. This was the only trust established by the settlor.

The trust holds the following assets and receives the income detailed below:

	Current value (£)	Income (£)
Rental property	1,000,000	30,000 per annum
Portfolio of equities	300,000	9,000 per annum
Cash	10,000	Nil

Expenses of the trust amount to £5,000 a year.

The rental property was valued at £830,000 when it was gifted into the existing trust in 2015. Becca lived in the property until 2017 and the property has been let ever since. The original purchase price was £500,000. When the property was gifted, the settlor and the trustees elected for hold-over relief.

Becca has finished university and has found a house that she would like to buy. The trustees are considering selling the rental property to release capital to Becca for her to purchase a property.

Anna lives with her mother, Elsa. Elsa has asked for capital from the trust so that she can buy a property. Elsa is not a potential beneficiary of the trust.

Sasha is planning on going travelling for six months, in the near future and would like to give her brother authority to take care of her financial responsibilities while she is out of the country.

QUESTIONS CONTINUE OVER THE PAGE

Questions

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

- (a) With regard to the discretionary trust:
- (i) Explain the Income Tax treatment of the income received by the trustees. (8)
 - (ii) Explain how the trust expenses will be accounted for in the calculation of taxable income. (6)
 - (iii) Describe how Anna and Becca will be treated for Income Tax purposes if the trustees distribute income of £10,000 net to them both. (5)
- (b) Calculate, **showing all your workings**, the Capital Gains Tax liability assuming the rental property is sold in the 2020/2021 tax year. Assume that the costs of selling the property are £7,000. (6)
- (c) Explain the legal implications of Sasha and the other trustees appointing capital to Elsa to purchase a property. (7)
- (d) (i) Explain the benefits of Sasha giving her brother a general Power of Attorney to act on her behalf whilst she is away. (6)
- (ii) Explain briefly the limitations for Sasha of taking this course of action. (2)
- Total marks for this question: 40**

INCOME TAX

RATES OF TAX	2019/2020	2020/2021
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	£37,500	£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
*Only applicable to savings income that falls within the first £5,000 of income in excess of the personal allowance		
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) §	£12,500	£12,500
Married/civil partners (minimum) at 10% †	£3,450	£3,510
Married/civil partners at 10% †	£8,915	£9,075
Marriage Allowance	£1,250	£1,250
Income limit for Married Couple's Allowance †	£29,600	£30,200
Rent a Room scheme – tax free income allowance	£7,500	£7,500
Blind Person's Allowance	£2,450	£2,500
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	£2,830
- family element	£545	£545
Threshold for tapered withdrawal of CTC	£16,105	£16,385

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	Weekly
Lower Earnings Limit (LEL)	£120
Primary threshold	£183
Upper Earnings Limit (UEL)	£962

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS
Up to 183.00*	Nil
183.00 – 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 £120 per week. This £120 to £183 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 169.00**	Nil
169.00 – 962.00	13.8%
Excess over 962.00	13.8%

*** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £3.05 where profits exceed £6,475 per annum.
Class 3 (voluntary)	Flat rate per week £15.30.
Class 4 (self-employed)	9% on profits between £9,500 - £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
2020/2021	£1,073,100

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.

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*
2020/2021	£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 by £1 for every £2 of 'adjusted income' over £240,000 to a minimum of £4,000 if 'threshold income' is also over £200,000.

MONEY PURCHASE ANNUAL ALLOWANCE	2019/2020	2020/2021
	£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	2019/2020	2020/2021
Individuals, estates etc	£12,000	£12,300
Trusts generally	£6,000	£6,150
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%
	10%	10%
Business Asset Disposal Relief* – Gains taxed at:		
Lifetime limit	£10,000,000	£1,000,000

**For trading businesses and companies (minimum 5% employee or director shareholding) if held for at least two years.*

INHERITANCE TAX

RATES OF TAX ON TRANSFERS

	2019/2020	2020/2021
Transfers made on death		
- Up to £325,000	Nil	Nil
- Excess over £325,000	40%	40%
Transfers		
- 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*	£150,000	£175,000
- 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:

	0-3	3-4	4-5	5-6	6-7
- Years before death					
- Inheritance Tax payable	100%	80%	60%	40%	20%

Quick succession relief:

	0-1	1-2	2-3	3-4	4-5
- Years since IHT paid					
- Inheritance Tax relief	100%	80%	60%	40%	20%

PRIVATE VEHICLES USED FOR WORK

	2019/2020 Rates	2020/2021 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

	2019/2020	2020/2021	
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£1,000,000	£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	6%	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

		2019/2020	2020/2021
		£	£
Child Benefit	First child	20.70	21.05
	Subsequent children	13.70	13.95
	Guardian's allowance	17.20	17.90
Employment and Support Allowance	Assessment Phase		
	Age 16 - 24	Up to 57.90	Up to £58.90
	Aged 25 or over	Up to 73.10	Up to £74.35
	Main Phase		
	Work Related Activity Group	Up to 102.15	Up to 74.35
	Support Group	Up to 111.65	Up to 113.55
Attendance Allowance	Lower rate	58.70	59.70
	Higher rate	87.65	89.15
Basic State Pension	Single	129.20	134.25
	Married	201.45	268.50
Single Tier State Pension	Single	168.60	175.20
Pension Credit	Single person standard minimum guarantee	167.25	173.75
	Married couple standard minimum guarantee	255.25	265.20
	Maximum savings ignored in calculating income	10,000.00	10,000.00
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	58.90
	Age 25 or over	73.10	74.35
Statutory Maternity, Paternity and Adoption Pay		148.68	151.20

CORPORATION TAX

	2019/2020	2020/2021
Standard rate	19%	19%

VALUE ADDED TAX

	2019/2020	2020/2021
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%

Important note: For residential properties purchased between 8th July 2020 and 31st March 2021, Stamp Duty Land Tax does not apply up to £500,000. For purchases above £500,000, the band rates above apply as normal. Additional SDLT rules still apply as below.

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 may be 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%