THE CHARTERED INSURANCE INSTITUTE

R06

Diploma in Regulated Financial Planning

Unit 6 – Financial planning practice

April 2014 examination

SPECIAL NOTICES

All questions in this paper are based on English law and practice applicable in the tax year 2013/2014, unless stated otherwise and should be answered accordingly.

It should be assumed that all individuals are domiciled and resident in the UK unless otherwise stated.

Candidates should answer based on the legislative position immediately BEFORE the 2014 budget.

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 R06 – Financial planning practice

Instructions to candidates

Read the instructions below before answering any questions

- **Three hours** are allowed for this paper.
- This paper consists of **two** case studies and carries a total of 150 marks.
- You are advised to spend approximately 90 minutes on the questions for each case study. You are strongly advised to attempt **all** parts of each question in order to gain maximum possible marks for each question. 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.

Attempt ALL questions for each case study

Time: 3 hours

Case study 1

Tim, aged 32 and Emma, aged 31, are married. They have two children, Charlotte aged two and Harry aged six months.

Tim is employed in the legal department of a major public limited company and receives a gross salary of £60,000 per annum. He is a member of his employer's comprehensive private medical insurance scheme, which also covers his family. If Tim is unable to work through accident or sickness, his employer will pay his full salary for one year and then 75% of his salary until he reaches the age of 65.

Tim is a member of his employer's defined contribution pension scheme. He pays 5% per annum gross of his salary and his employer pays 10% of his gross salary into the scheme. Tim's fund value is currently £205,000. He is also a member of his employer's death-in-service scheme which provides a lump sum of four times annual salary.

Emma has been a self-employed website designer since 2006 and her taxable net profits are £20,000 per annum. She expects her business to be more profitable once Harry starts school and estimates that her taxable net profits will then be approximately £35,000 per annum. Emma has a personal pension plan valued at £85,000 but has not made contributions to the plan since 2012.

Tim and Emma live in a property as joint tenants, valued at £300,000. They have a repayment mortgage of £200,000 with an outstanding term of 25 years. Their interest rate is fixed at 3.8% for the next 10 years. They have a 25 year joint life, first death mortgage protection policy for £200,000. They have no other protection policies.

Emma has recently inherited a portfolio of shares valued at £210,000, following her grandfather's death. She has been informed that the shares have a standard deviation of 4%.

Tim and Emma's only savings are in the form of cash ISAs, with Tim's valued at £19,250 and Emma's valued at £17,450, and a jointly-held bank savings account of £22,000.

Tim and Emma have a low to medium attitude to risk. They have never used a financial adviser as they have always felt that they are capable of making their own financial decisions.

Their financial aims are to:

- ensure they are financially secure in the event of death or illness;
- make the best use of the shares inherited by Emma;
- ensure they have sufficient income in retirement.

Questions

(a) Explain the potential **benefits** for Tim and Emma if they decide to receive and act on advice received from a qualified financial adviser. **(8)**

(b) Tim and Emma would like information about how any financial advice they receive from an adviser will be paid for. Outline **two** benefits and **two** drawbacks to Tim and Emma of an adviser using:

(i) fixed fees; **(4)**

(ii) time-based charging. **(4)**

(c) State the additional information an adviser would require to advise Tim and Emma on their retirement planning objective. **(14)**

(d) When considering Tim and Emma's current protection arrangements and their stated objectives:

(i) Outline the areas where further protection planning is necessary for Tim and Emma. **(4)**

(ii) State the factors an adviser should take into account when constructing a plan to meet the needs identified in part **(d)(i)** above. **(12)**

(iii) Recommend and justify a suitable product for Emma to receive an income, if she was unable to work due to long-term illness. **(12)**

(e) Emma has been informed that the standard deviation of the share portfolio is 4%. Explain what this means in terms Emma and Tim will understand. **(5)**

(f) Tim and Emma are considering selling the shares to repay their mortgage. Outline **four** benefits and **four** drawbacks of this proposed course of action. **(8)**

Total marks available for this question: 71

Questions continue over the page

Case study 2

George, aged 66, is married to Ann, aged 65. They have two children who are both financially independent and three grandchildren.

George is employed by a small engineering firm. He receives a gross salary of £65,000 per annum, and receives no benefits-in-kind. He is a member of his employer's group personal pension scheme. George makes a contribution of 3% of basic salary via salary sacrifice and his employer contributes 3% of basic salary to the scheme.

George's pension is invested in a managed fund and valued at £900,000. He is considering taking the scheme benefits and working part-time. He has deferred his State Pension.

Ann has been helping to raise the grandchildren for the past ten years and has not been in paid employment during that time. She currently receives a State Pension of £5,200 gross per annum. This is her only source of income.

George has a medium to high attitude to risk and Ann has a cautious attitude to risk. They have mirror Wills leaving everything to each other. Neither George nor Ann has made any previous gifts.

They have the following assets:

Owner	Asset	Amount (£)
Joint Tenancy	Family Home	750,000
Joint	Bank savings account	90,000
Ann	Stocks and Shares ISAs	125,000
George	Cash ISAs	40,000
George	Stocks and Shares ISAs	70,000
Joint	Onshore Investment Bond	120,000
George	UK Equity Unit Trusts	150,000

The total value of any other assets they have, including chattels and cars, is £110,000. They have no mortgage or other debts.

There financial aims are to:

- ensure they have sufficient income in retirement;
- maximise tax efficiency;
- pass as much of their estate to their children as possible.

Questions

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

(a) **(i)** State the process an adviser should follow to advise George and Ann on their investment planning. **(8)**

(ii) Identify the reasons why an adviser should not solely rely on a risk profiling tool to clarify George and Ann's attitude to risk. **(6)**

(b) **(i)** Explain why George could consider using a capped drawdown pension to provide an income from his pension fund rather than purchase an annuity. **(6)**

(ii) State **five** benefits and **five** drawbacks of a salary sacrifice pension arrangement. **(10)**

(iii) State the reasons why a spousal bypass trust is suitable to receive any death benefits paid from George's pension fund to minimise any future Inheritance Tax (IHT) liability. **(8)**

(c) State the factors an adviser should take into account when advising George on whether to continue to defer his State Pension. **(7)**

(d) **(i)** Calculate, **showing all your workings**, George and Ann's immediate IHT liability on second death. *Ignore the value of George's personal pension and State Pension in your calculation.* **(5)**

(ii) Recommend and justify ways in which George and Ann could immediately reduce the IHT liability that would be payable on either death. **(9)**

Questions continue over the page

(e) Recommend and justify the actions that could be taken to maximise tax efficiency of George and Ann's assets. *Ignore any IHT liability.* **(12)**

(f) State the factors an adviser should take into account when reviewing George and Ann's investments at their next annual review. **(8)**

Total marks available for this question: 79

The tax tables can be found on pages 10 - 16

INCOME TAX

RATES OF TAX	2012/2013	2013/20[illegible]
Starting rate for savings*	10%	10%
Basic rate	20%	20%
Higher rate	40%	40%
Additional rate	50%	45%
Starting-rate limit	£2,710*	£2,790*
Threshold of taxable income above which higher rate applies	£34,370	£32,010
Threshold of taxable income above which additional rate applies	£150,000	£150,000
Child benefit charge from 7 January 2013:		
1% of benefit for every £100 of income over	£50,000	£50,000

**Restricted to savings income only and not available if taxable non-savings income exceeds starting rate band.*

MAIN PERSONAL ALLOWANCES AND RELIEFS

Income limit for Personal Allowance §	£100,000	£100,000
Personal Allowance (basic if born after 5 April 1948) §	£8,105	£9,440
Personal Allowance (if born between 6 April 1938 and 5 April 1948) §	£10,500	£10,500
Personal Allowance (if born before 6 April 1938) §	£10,660	£10,660
Married/civil partners (minimum) (if born before 6 April 1935) at 10% †	£2,960	£3,040
Married/civil partners (if born before 6 April 1935) at 10% †	£7,705	£7,915
Income limit for age-related allowances	£25,400	£26,100
Blind Person's Allowance	£2,100	£2,160
Enterprise Investment Scheme relief limit on £1,000,000 max	30%	30%
Seed Enterprise Investment relief limit on £100,000	50%	50%
Venture Capital Trust relief limit on £200,000 max	30%	30%

§ the Personal Allowance reduces by £1 for every £2 of income above the income limit irrespective of age (under the income threshold).
† where at least one spouse/civil partner was born before 6 April 1935.

Child Tax Credit (CTC)		
- Child element per child (maximum)	£2,690	£2,720
- family element	£545	£545
Threshold for tapered withdrawal of CTC	£15,860	£15,910

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	Weekly	Monthly	Yearly
Lower Earnings Limit (LEL)	£109	£473	£5,668
Primary threshold	£149	£646	£7,755
Upper Accrual Point	£770	£3,337	£40,040
Upper Earnings Limit (UEL)	£797	£3,454	£41,450

Total earnings £ per week	CLASS 1 EMPLOYEE CONTRIBUTIONS	
	Contracted-in rate/contracted-out (money purchase)	Contracted-out rate (final salary)
Up to 149.00*	Nil	Nil
149.01 – 770.00	12%	10.6%
770.01 – 797.00	12%	12%
Above 797.00	2%	2%

**This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £109 per week. This £109 to £149 band is a zero rate band introduced in order to protect lower earners' rights to contributory State benefits e.g. Basic State Pension.*

Total earnings £ per week	CLASS 1 EMPLOYER CONTRIBUTIONS		
	Contracted-in rate	Contracted-out rate	
		Final salary	*Money purchase*
Below 148.00**	Nil	Nil	Nil
148.01 – 770.00	13.8%	10.4%	13.8%
770.01 – 797.00	13.8%	13.8%	13.8%
Excess over 797.00	13.8%	13.8%	13.8%

*** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £2.70 where earnings exceed £5,725 per annum.
Class 3 (voluntary)	Flat rate per week £13.55.
Class 4 (self-employed)	9% on profits between £7,755 - £41,450 2% on profits above £41,450.

PENSIONS

TAX YEAR	LIFETIME ALLOWANCE	ANNUAL ALLOWANCE
2006/2007	£1,500,000	£215,000
2007/2008	£1,600,000	£225,000
2008/2009	£1,650,000	£235,000
2009/2010	£1,750,000	£245,000
2010/2011	£1,800,000	£255,000
2011/2012	£1,800,000	£50,000
2012/2013	£1,500,000	£50,000
2013/2014	£1,500,000	£50,000

ANNUAL ALLOWANCE CHARGE

20% - 45% member's tax charge on the amount of total pension input in excess of the annual allowance.

LIFETIME ALLOWANCE CHARGE

55% of excess over lifetime allowance if taken as a lump sum.

25% of excess over lifetime allowance if taken in the form of income, which is subsequently taxed under PAYE.

CAPITAL GAINS TAX

EXEMPTIONS	2012/2013	2013/2014
Individuals, estates etc	£10,600	£10,900
Trusts generally	£5,300	£5,450
Chattels proceeds (restricted to five thirds of proceeds exceeding limit)	£6,000	£6,000

TAX RATES		
Individuals:		
Up to basic rate limit	18%	18%
Above basic rate limit	28%	28%
Trustees and Personal Representatives	28%	28%
Entrepreneurs' Relief* – Gains taxed at:	10%	10%
Lifetime limit	£10,000,000	£10,000,000

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

INHERITANCE TAX

RATES OF TAX ON DEATH TRANSFERS	2012/2013	2013/20
Transfers made after 5 April 2013		
- Up to £325,000	Nil	Nil
- Excess over £325,000	40%	40%
- Lifetime transfers to and from certain trusts	20%	20%

**For deaths after 5 April 2013, a lower rate of 36% applies where at least 10% of deceased's net estate is left to charity.*

MAIN EXEMPTIONS

Transfers to		
- UK-domiciled spouse/civil partner	No limit	No limit
- non-UK-domiciled spouse/civil partner (from UK-domiciled spouse)	£55,000	£325,000
- UK-registered charities	No limit	No limit
Lifetime transfers		
- Annual exemption per donor	£3,000	£3,000
- Small gifts exemption	£250	£250
Wedding/civil partnership gifts by		
- parent	£5,000	£5,000
- grandparent	£2,500	£2,500
- other person	£1,000	£1,000

100% relief: businesses, unlisted/AIM companies, certain farmland/building
50% relief: certain other business assets

Reduced tax charge on gifts within 7 years of death:

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

CAR BENEFIT FOR EMPLOYEES

The charge for company car benefits is based on the carbon dioxide (CO_2) emissions. There is no reduction for high business mileage users.

For 2013/2014:

- Cars that cannot emit CO_2 have a 0% charge.
- The percentage charge is 5% of the car's list price for CO_2 emissions of 75g/km or less.
- For cars with CO_2 emissions of 76g/km to 94g/km the percentage is 10%.
- For cars with CO_2 emissions of 95g/km to 99g/km the percentage is 11%.
- Cars with CO_2 emissions of 100g/km have a percentage charge of 12% and thereafter the charge increases by 1% for every complete 5g/km to a maximum of 35% (emissions of 215g/km and above).

There is an additional 3% supplement for diesel cars not meeting Euro IV emission standards. However, the maximum charge remains 35% of the car's list price.

Car fuel The benefit is calculated as the CO_2 emissions % relevant to the car and that % applied to a set figure (£21,100 for 2013/2014) e.g. car emission 100g/km = 12% on car benefit scale. 12% of £21,100 = £2,532.

1. **Accessories** are, in most cases, included in the list price on which the benefit is calculated.
2. **List price** is reduced for capital contributions made by the employee up to £5,000.
3. **Car benefit** is reduced by the amount of employee's contributions towards running costs.
4. **Fuel scale** is reduced only if the employee makes good **all** the fuel used for private journeys.
5. **All car and fuel benefits** are subject to employers National Insurance Contributions (Class 1A) of 13.8%.

PRIVATE VEHICLES USED FOR WORK

	2012/2013 Rates	2013/2014 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

	2012/2013	2013/2014
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£25,000	£250,000
Plant & machinery (reducing balance) per annum	18%	18%
Patent rights & know-how (reducing balance) per annum	25%	25%
Certain long-life assets, integral features of buildings (reducing balance) per annum	8%	8%
Energy & water-efficient equipment	100%	100%
Zero emission goods vehicles (new)	100%	100%
Qualifying flat conversions, business premises & renovations	100%	100%

Motor cars: Expenditure on or after 01 April 2013 (Corporation Tax) or 06 April 2013 (Income Tax)

CO_2 emissions of g/km:	95 or less*	96-130	131 or more
Capital allowance:	100% first year	18% reducing balance	8% reducing balance

*If new

Research & Development:	Capital expenditure	100%

CORPORATION TAX

	2012/2013	2013/2014
Full rate	24%	23%
Small companies rate	20%	20%
Small companies limit	£300,000	£300,000
Effective marginal rate	25%	23.75%
Upper marginal limit	£1,500,000	£1,500,000

VALUE ADDED TAX

	2012/2013	2013/2014
Standard rate	20%	20%
Annual registration threshold	£77,000	£79,000
Deregistration threshold	£75,000	£77,000

MAIN SOCIAL SECURITY BENEFITS

		2012/2013 £	2013/2 £
Child Benefit	First child	20.30	20.30
	Subsequent children	13.40	13.40
	Guardian's allowance	15.55	15.90
Employment and Support Allowance	Assessment Phase		
	Age 16 – 24	Up to 56.25	Up to 56.80
	Aged 25 or over	Up to 71.00	Up to 71.70
	Main Phase		
	Work Related Activity Group	Up to 99.15	Up to 100.15
	Support Group	Up to 105.05	Up to 106.50
Attendance Allowance	Lower rate	51.85	53.00
	Higher rate	77.45	79.15
Retirement Pension	Single	107.45	110.15
	Married	171.85	176.15
Pension Credit	Single person standard minimum guarantee	142.70	145.40
	Married couple standard minimum guarantee	217.90	222.05
	Maximum savings ignored in calculating income	10,000.00	10,000.00
Bereavement Payment (lump sum)		2,000.00	2,000.00
Widowed Parent's Allowance		105.95	108.30
Jobseekers Allowance	Age 16 - 24	56.25	56.80
	Age 25 or over	71.00	71.70
Statutory Maternity, Paternity and Adoption Pay		135.45	136.78

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