AF1

Advanced Diploma in Financial Planning

Unit AF1 – Personal tax and trust planning

February 2021 Examination Guide

SPECIAL NOTICES

Candidates entered for the April 2021 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

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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. 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.

Marks are not lost due to poor spelling or grammar.

You are able to flag questions and then go back to them.

Calculators
The calculator is in a pop-up box on the right-hand side of the interface. It is important to show all steps in a calculation, even if you have used a calculator.

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Tips for laying out calculations in on-screen exams
Where you are asked to perform a calculation, it is important to show **all the steps** in your answer. Most of the marks will be allocated for demonstrating the correct method of calculation.

While there are no marks for presentation, laying the calculation out well will make it easier for the examiner to identify all of the marks you have achieved. It doesn't matter how long the calculation is, if it is well set out. There is no preferred format but following the below guidelines is often helpful:

- Set out each stage of your calculation on a separate line.
- Label the values used i.e. in an IHT calculation:
    - Main residence £500k,
    - Onshore Bond £100k.
- Identify all allowances, exemptions, tax rate bands, tax rates used in £ terms.
- Use subtotals, where appropriate: i.e.:
    - Total assets - £1,500,000
    - Nil rate band – (£325,000)
    - Residence nil rate band – (£175,000)
    - Assets after allowances - £1,000,000
- Show all your workings. This includes:
    - grossing up of pension contributions,
    - how you work out the allowances if they are not standard,
- Make notes where appropriate. For example:
    - Bond loss is excluded
    - ISA income ignored
- Double check all of your figures, specifically:
    - That you have calculated each section correctly.
    - That you have added up all of your figures correctly.

EXAMINERS' COMMENTS

Candidates overall performance

This exam paper covered a variety of subject areas and overall performance was good from those candidates that were well prepared.

Many candidates seemed to have taken on board comments from previous exam guides and the quality and structure of answers seems to have improved, which was lovely to see.

As is often the case, to get maximum marks on certain questions, a candidate needed to provide lots of detail in their answers. As a general rule, the number of marks available should give an idea of how much detail is required. Therefore, it is advisable to add more in-depth answers to the questions that offer the highest marks.

Question 1

Part (a)(i) was well-answered with most candidates scoring high marks. Occasionally candidates would not include all of the relevant assets which lost them a mark at the start – it would be worth double checking the case study for this part of the calculation to make sure relatively straightforward marks are not missed. The more difficult elements of this question were that the Will Trust would form part of the estate for IHT, as it was a qualifying IIP. Another common mistake was either missing or incorrectly calculating the Business Relief on the business assets.

Part (a)(ii) was generally well-answered but only by the candidates who had identified that the Will Trust formed part of the estate. Where this was missed in the first part of the question, candidates generally did not perform well in (a)(ii).

Part (a)(iii) should have been a relatively well-answered question; however, some candidates did not spot the client's objective to not give up any capital. This meant that some candidates spent time detailing options that would not be appropriate i.e. outright gifting, bare and discretionary trust, using annual gift exemptions.

Part (b) was a challenging question and many candidates struggled to provide enough detail to gain full marks.

In particular, part (b)(i) required candidates to show understanding of the fact that the distribution of the estate would change depending on whether he died before, or after, marrying Sophia. Only candidates who detailed how this would work in both scenarios gained high marks on this question.

Part (b)(ii) was not particularly well answered. Some candidates detailed that a spousal exemption would be available but did not explain this fully. Confusingly, the spousal exemption is limited to £325,000 which is the same as the nil rate band. Better prepared candidates identified that this exemption is in addition to the nil rate band.

Many candidates gained some marks on part (b)(iii) but few provided enough detail to their answers. The question needed a candidate to look at both how to make the election and what the financial impact of this would be. This is quite a wide question and, as you will see from the model answer, there were lots of marks available. It would be good practice for candidates to refer back to the question before moving to the next to ensure they have answered the full question asked.

Part (c) was well answered and many candidates picked up the first four marks relating to which business would qualify based on how long they have been trading. Few candidates went further with their answer to set out the qualifying rules which would have gained them extra marks.

Part (d)(i) and (ii) focussed on the Will Trust which was an Immediate Post Death Interest (IPDI) which is classed as a qualifying Interest in Possession (IIP) trust. This type of trust is treated differently to a standard IIP trust and this was a challenge for many candidates. It should be noted that it is very common for this type of trust to appear in a Will so it is a very important area for candidates to revise. Candidates who described the tax treatment of a standard IIP trust did not perform well in this question, unfortunately.

Part (e)(i) and (ii) is often tested and candidates scored well, particularly in part (i). However, some candidates did not gain full marks in part (ii) as they missed the fact that benefits could be appointed absolutely out of a discretionary trust within two years, which could bring the Residence nil rate band back into play.

Part (f) focussed on the taxation of chargeable events within an investment bond. This area has historically been poorly answered. Happily, this trend appears to be reversing and more candidates showed better understanding of the updated five step process.

Question 2

Part (a) required candidates to apply their understanding of the Business Asset Disposal Relief rules to the individuals in the case study. A few candidates confused this with Business Relief so their answers gained much fewer marks. It is worth noting the updated names for each relief and how they differ. However, this was a generally well-answered question.

Part (b) was also well-answered, although few candidates provided enough detail to gain all five marks. The additional detail of which assets would attract relief and why, linking back to the case study, were required to achieve the last two marks.

The quality of answers to part (c) was mixed. There are two methods of calculating CGT on shares sold from a share pool and marks were given for either method. Well-prepared candidates scored full or nearly full marks on this question. Some candidates got a little lost and struggled to calculate the correct acquisition cost.

Part (d) related to the reporting and payment of CGT. Some candidates are still not showing an understanding of the ability to submit CGT returns using the real time service. In (d)(ii), many candidates scored poorly as they detailed fines for late reporting, rather than the fines for late payment of the CGT. It is important to read the question carefully and answer the question asked.

Part (e) was not particularly well-answered. In this particular case study, candidates needed to consider both Private Residence Relief and Lettings Relief in their answer. It is important to understand how these reliefs interact and the rules that apply to each.

Question 3

Part (a)(i) was a relatively straight-forward income Tax calculation and many candidates scored full marks. The more challenging aspects related to calculating the correct basic rate band and grossing up the pension and charity contributions.

Part (a)(ii) was less well answered. The question was looking for candidates to identify that Sadie's income was between £50,000 and £60,000. This means that she would be subject to the high-income tax charge, but she would still receive a net benefit after this tax is considered. Many candidates listed the general rules around Child benefit but did not go far enough to apply this to Sadie's specific circumstances.

Part (b)(i) and (ii) was looking for candidates to detail the difference between how a charitable contribution and a pension contribution would affect the tax treatment of Lorenzo's bond gain. Many candidates correctly identified that a pension contribution extends the basic rate band and could reduce the tax. Fewer candidates understood that this is not the case for charitable contributions.

Part (c) was answered very well, with candidates giving highly detailed answers on how different types of income are taxed.

Part (d) is often tested and candidates clearly know this area well. One point that was often missed is that not only could Vera specify who the attorneys are, but she can also set out the specific powers they have.

The exam closed with an area of the syllabus that candidates often avoid or do not revise particularly well – the rules around residency. In this case we were looking at what makes an individual automatically not UK resident. Few candidates scored highly here as not enough detail was given or incorrect days and years were used.

Unit AF1 – Personal tax and trust planning

Instructions to candidates

Read the instructions below before answering any questions

All questions in this examination 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.

- **Please write down the following number +44 (0)80 8273 9244 this is the number to use if your system freezes or you get forced out of your exam. It is fine to phone it if you have these issues.**
- **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.
- The calculator is in a pop-up box on the right-hand side of the interface. 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.
- For each answer, please type in the full question number you are answering e.g. **1a**
- **Please note each answer must be typed in the correct corresponding answer box.**
- **If you are wearing headset, earphones, smart watch please take them off.**
- Have you shown your ID during the ID check? If not, show it to the camera now please.
- Did you show the edge of your screen with a mirror during the room scan? If not, use a mirror to show it now please.
- If you have blank paper for notes, did you show both sides to the camera? If not, show both sides to the camera now please.

Subject to providing sufficient detail you are advised to be as brief and concise as possible, using note format and short sentences.

SECTION A

This question is compulsory and carries 80 marks

Question 1

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

Jonah, aged 57, is UK domiciled and has two minor children. He is engaged to Sophia, who has Italian domicile, she is a UK resident and has lived in the UK since 2016 after moving from Rome.

Jonah is the sole director and shareholder of both XYZ Software Engineers Ltd, which was established in January 2015 and Great Programming Ltd, established in January 2020. Both businesses are profitable and Jonah has no plans to sell.

Jonah and Sophia manage their finances separately and do not hold any assets jointly. Most of Sophia's assets are UK based but she still owns a large property in Italy.

When Jonah's mother died in 2010, a trust was established by her Will ('The Bennett Family Trust'). Jonah is the life tenant, and his children are the remaindermen, absolutely, in equal shares. The trust provides dividend income of £4,000 a year which is paid directly to Jonah.

Jonah's Will currently divides his estate equally between his children. However, he would now like to include Sophia as a beneficiary.

Jonah likes the idea of gifting his home into a discretionary trust for the future benefit of his children and is considering updating his Will to reflect this. On 23 February 2021, his home was valued at £750,000 and he had a repayment mortgage with an outstanding balance of £200,000.

On 23 February 2021 the value of Jonah's other assets were as follows:

	Value (£)
XYZ Software Engineers Ltd	100,000
Great Programming Ltd	150,000
The Bennett Family Trust	200,000
Onshore Life Assurance Bond	90,000
ISAs	50,000

To ensure his mortgage would be repaid in the event of his death, Jonah arranged a decreasing term life assurance policy to coincide with the term of his mortgage. The current sum assured is £200,000. He pays premiums of £25 a month based on his excellent health.

Jonah wants to reduce the potential Inheritance Tax liability on his death but does not want to give up access to any of his capital.

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 Inheritance Tax that would be due if Jonah had died on 23 February 2021.
You should assume he has not amended his Will. **(9)**

(ii) Explain briefly who will pay the Inheritance Tax due on Jonah's death and in what proportion. *No calculations are required.* **(4)**

(iii) Describe briefly some of the actions Jonah could take, during his lifetime, to reduce his Inheritance Tax liability taking into account his objectives. **(5)**

(b) **(i)** Explain briefly how the distribution of Jonah's estate would change, if he amends his Will to include Sophia, prior to their wedding. **(4)**

(ii) Describe how the Inheritance Tax calculation would differ, assuming Jonah had married Sophia and decided to leave **his entire estate** to her on his death. **(6)**

(iii) Explain how Sophia could elect to be treated as domiciled in the UK for Inheritance Tax purposes and the financial impact of this. **(10)**

(c) Explain in detail the extent to which Jonah's estate would qualify for Business Relief if he died on 23 February 2021. **(7)**

(d) **(i)** State how the trust established by Jonah's mother would be categorised by HM Revenue & Customs and describe how Income Tax and Inheritance Tax would be applied. **(7)**

(ii) Explain how the tax treatment of the trust would change following Jonah's death. **(5)**

(e) **(i)** Outline the conditions that need to be met for Jonah's estate to qualify for the residence nil rate band. **(4)**

(ii) Explain the implications on the qualification for the residence nil rate band if Jonah created a trust in his Will. **(6)**

(f) Jonah is considering surrendering his life assurance Bond.

(i) Describe briefly how any chargeable gain would be calculated on full surrender. **(4)**

(ii) Explain how any tax payable on full surrender would be calculated.
No calculations are required. **(9)**

Total marks for this question: 80

SECTION B

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

Question 2

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

Atique, aged 54, is the sole director of the building company he established in 2010. He owns 90% of the ordinary shares in the company and is entitled to 90% of the voting rights. In the tax year 2020/2021 he will receive salary and dividends totalling £65,000.

Guy is employed as a site manager and owns 4% of the ordinary shares in the company with the remaining 6% of ordinary shares held by a former employee Millicent.

A recent valuation of the business detailed the assets to be comprised of a large workshop, various pieces of specialist equipment, building materials and goodwill. Atique also personally owns a warehouse valued at £200,000 which is let to another business.

Atique plans to retire when he reaches age 55, in August 2021. His accountant has calculated he will realise a capital gain of £400,000 on the sale of his ordinary shares. Guy and Millicent will sell their shares at the same time.

Atique is a keen investor and has bought shares over the years in a company called Genplan plc. The purchases are shown in the following table:

Date of purchase	Number of shares bought	Purchase price (£)
July 2012	4,000	6,000
September 2014	2,000	3,600
March 2018	1,000	2,000

In October 2020 Atique sold 4,000 shares in Genplan plc at a price of £3.20 per share. At the same time, he sold qualifying shares in an Enterprise Investment Scheme that he had held for two years making a gain of £15,000. He also sold a qualifying corporate bond that he had held for four years making a loss of £4,000.

Atique has a lodger who rents a bedroom in his home which amounts to 10% of his property. When he retires, in August 2021, Atique plans to downsize. He bought the property for £200,000 and expects to sell for £310,000. He has just finished redecorating which cost £5,000. Sale costs are expected to be £10,000.

Questions

(a) Explain the extent to which the shareholders of the company will qualify for Business Asset Disposal Relief, on disposal of their ordinary shares in the company. **(9)**

(b) Explain how the gain will be treated and taxed when Atique sells the ordinary shares in his company. *No calculations are required.* **(5)**

(c) Calculate, **showing all your workings**, the Capital Gains Tax (CGT) liability for Atique on the sale of his investments in the 2020/2021 tax year. **(12)**

(d) In relation to the sale of investments in the 2020/2021 tax year:

(i) State how Atique could report any CGT he owes to HM Revenue & Customs. **(2)**

(ii) Explain the penalties that HM Revenue & Customs could impose if any CGT due is not paid on time. **(6)**

(e) Explain how the gain realised from selling his home in **2021/2022** will be treated for CGT purposes. *No calculations are required.* **(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), (c), (d) and (e) which follow.

Sadie, aged 48, and Lorenzo, aged 50, are married. They live with their two children, Oscar, aged 19, Liliana, aged 14, and Lorenzo's mother Vera, aged 85.

Sadie is an architect. She has worked for her employer for the past seven years and earns an annual salary of £57,000. She currently makes a personal monthly contribution of £250 net into a personal pension after opting out of her employers auto-enrolment pension scheme. She has also opted out of receiving any child benefit for her two children.

Lorenzo runs a catering business on a self-employed basis and realised profits of £50,000 last year. Oscar has been working for the business on a part-time basis since leaving school a year ago, although he has recently been offered a teaching position in France.

Lorenzo surrendered an onshore life assurance Bond in January 2021. He made a gain of £18,000 after holding the bond for twelve and a half years. He is considering reinvesting some of the proceeds from the bond and would like to discuss his options.

The couple made a gift aid donation of £4,000 from their joint bank account in November 2020.

They received the following investment income in 2020/2021:

Owner	**Investment**	**Income received in 2020/2021 (£)**
Joint	Deposit account	1,720
Lorenzo	Cash ISA	180
Sadie	Cash ISA	720
Sadie	UK equities	5,600

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 Income Tax payable by Sadie in the 2020/2021 tax year. **(11)**

(ii) State the factors Sadie needs to consider if she decides to opt back into receiving child benefit in a future tax year. **(4)**

(b) **(i)** State the tax treatment of Lorenzo's bond gain and the effect of the gift aid donation. **(3)**

(ii) Explain briefly the difference in the tax treatment of the bond gain if Lorenzo had made a pension contribution of the same amount instead of a gift aid donation. **(4)**

(c) Describe the personal tax treatment of any interest and dividend income if Lorenzo invests in both equity and non-equity Unit Trusts. **(6)**

(d) Explain the benefits of Vera establishing a full Lasting Power of Attorney whilst she is mentally capable. **(6)**

(e) Outline the circumstances in which Oscar would be treated as **automatically** non-resident in the UK if he moves to France. **(6)**

Total marks for this question: 40

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

Model answer for Question 1

(a)(i) Jonah's free estate

Main residence	£750,000
Onshore Insurance Bond	£90,000
ISAs	£50,000
XYZ Software Engineers Ltd	£100,000
Great Programming Ltd	£150,000
Term assurance	£200,000
Mortgage	(£200,000)
	£1,140,000
Business Relief (XYZ Software Engineers Ltd)	(£100,000)
No Business relief on Great Programming as not held for two years.	
Total free estate	**£1,040,000**
Will Trust	£200,000
Total chargeable estate	**£1,240,000**
Nil rate band	(£325,000)
Residence nil rate band	(£175,000)
Taxable estate	£740,000
Inheritance Tax (IHT) at 40%	**£296,000**

(ii)
- The IHT would be apportioned between the tax relating to the free estate and the tax relating to the Will trust.
- Jonah's executors will pay IHT on assets forming part of the free estate.
- The tax on the Will Trust would be payable by the trustees.

(iii) *Candidates would have scored full marks for any five of the following:*

- Put the term assurance policy into trust.
- Use money from ISA to invest in IHT qualifying AIM ISA/invest in a Business relief (BR) qualifying investment.
- Give up his interest in possession/rights to Will trust.
- Hold the assets in his Great Programming for 2 years to qualify for BR.
- Get married.
- Gifts out of surplus income.
- Flexible reversionary or loan trust.
- Leave some of his estate to charity on death.
- Save some of his money into a pension.

(b) **(i)**

- If he dies prior to the wedding, the estate would be distributed in line with the Will/his estate goes to his children and Sophia.
- Marriage invalidates the Will. / If he dies after the wedding, the amended Will would no longer be valid; and the estate would be distributed in line with Intestacy rules.
- However, if the amended Will had been made in contemplation of the marriage, it would be distributed in line with the Will.

(ii)

- Sophia is not UK domiciled so:
- the spouse exemption would be limited to the nil rate band at time of transfer (£325,000),
- less the value of any previous transfers which have been made to her.
- This would reduce the taxable estate and IHT liability
- The spouse exemption can be used in addition to the standard nil rate band.

(iii)

- She would need to make the election to HM Revenue & Customs (there is no specific form for this).
- It would take effect from the date of making it,
- but can be backdated by up to seven years or the date of their marriage, if later.
- She could also make the election after Jonah's death, provided it is within two years.
- Once the election is made, the spouse exemption will be unlimited and the estate passes to her free of IHT.
- She can also benefit from the transferrable nil rate band.
- Her worldwide assets would become liable to IHT.
- In her case, this may increase their overall liability to IHT.
- Once made, the election cannot be revoked.

(c)

- The estate cannot apply Business Relief to the value of Great Programming Ltd as he has not owned it for more than two years.

- The estate can apply 100% Business Relief on the value of XYZ Software Engineers Ltd as:

- Jonah has owned it for more than two years before his death.
- The business does not deal wholly or mainly with securities, stocks or shares, land or buildings or in the making or holding of investments.
- the business is trading.
- It is a commercial business.
- it is not being sold or wound up.

(d) (i)

- There was an immediate post-death interest (IPDI).
- The trust is therefore a **qualifying Interest in Possession trust. This is not a relevant property trust.**
- There are no periodic or exit charges.
- The entire value of the trust would remain inside Jonah's estate for IHT.
- Income is classed as dividends and not as trust income
- Income is taxed on Jonah at his own rates of Income Tax.
- Jonah can use his own personal allowance and dividend allowance.

(ii)

- Jonah's children would become absolutely entitled to the trust.
- The money would form part of their estates for IHT purposes.
- The money would stay in trust for them while they are minors.
- Any income generated by the trust would belong to the children and would be taxed on them, using their allowances.

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

- He must have owned a property that was his main residence at some point during his lifetime.
- There is no minimum period of occupation.
- The property needs to be inherited by a direct descendant i.e. Jonah's children.
- The value of his estate, immediately before death, must not exceed the £2m taper threshold to receive the full Residence Nil Rate band (RNRB)/must not exceed £2.35 million to receive any RNRB.
- Where the estate exceeds £2m, the RNRB is reduced by £1 for every £2 of value by which the estate exceeds the taper threshold.

(ii)

- As the trustees would have discretion over who ultimately receives the benefit this means that the property is not being inherited by a direct descendant.
- The RNRB could be lost.

- However, if the property is appointed to the children absolutely,
- within two years of death,
- the RNRB could be claimed.

(f) **(i)**
- Surrender value;
- plus all previous withdrawals;
- Minus the total amount invested;
- and any previous chargeable gains/excesses over the accumulated 5% allowances.

(ii) *Candidates would have scored full marks for any nine of the following:*
- The full amount of chargeable gain is added to other income
- calculate how much of the gain falls within the Personal Savings Allowance (PSA)/(starting rate/basic/higher/additional rate bands for tax).
- Calculate the total tax due on the gain across all tax bands.
- Deduct the basic rate tax credit/20%.

- Calculate the annual equivalent/top slice of the gain by dividing by number of years.
- Add this to Jonah's income to check whether the personal allowance will be restricted.

- Calculate the tax on the annual equivalent/top slice.
- Deduct the Basic rate tax credit (20%) on the annual equivalent;
- multiply by number of years;
- This is the relieved liability.

- the relieved liability is deducted from his overall tax liability.

Model answer for Question 2

(a)

- Atique will qualify for Business Asset Disposal Relief because:
- The company is a trading company.
- He will have owned the shares for two years before the sale.
- He is a director of the company.

- Millicent does not qualify for Business Asset Disposal Relief
- as she is not an employee/director.

- Guy does not qualify for Business Asset Disposal Relief
- as he owns less than 5% of the ordinary shares/voting rights.

(b)

- The whole gain will be taxed at 10%.
- The lifetime gains eligible for Business Asset Disposal Relief is £1m.
- He can use his annual exempt amount (£12,300), if this is available.

- Relief is only available on gains from assets used in his business.
- The warehouse will not qualify for Business Asset Disposal Relief.

(c)

Share Pool	Number of shares	Cost
July 2012	4,000	£6,000
September 2014	2,000	£3,600
March 2018	1,000	£2,000
Total	**7,000**	**£11,600**

There are two methods of calculating this, both with slightly different answers. We have set out both for your reference.

Please note that figures should be set out to 2 decimal places

<u>Method 1</u>

Acquisition cost
Shares sold £4,000
/total shares held £7,000
x total cost of shares £11,600
= £6,628.57

Sale proceeds
4,000 x sale price £3.20= £12,800

Gain
Proceeds £12,800 – Acquisition cost £6,628.57
= gain of £6,171.43

Because Atique has not held the Enterprise Investment scheme (EIS) for 3 years the £15,000 gain is fully taxable.

£6,171.43 + EIS gain £15,000 = total gain £21,171.43

Taxable gain
- annual exempt amount £12,300
= £8,871.43

Tax payable
x 20% as higher rate taxpayer.
= £1,774.29

The qualifying corporate bond is exempt from CGT, so the loss cannot be offset.

Method 2

Acquisition cost
total cost of shares £11,600
/total shares held 7,000
= £1.66 per share

£1.66 x shares sold 4000
= £6,640

Sale proceeds
4,000 x sale price £3.20 = £12,800

Gain
Proceeds £12,800 – Acquisition cost £6,6640
= gain of £6,160

Because Atique has not held the Enterprise Investment scheme (EIS) for 3 years the £15,000 gain is fully taxable.

£6,160 + EIS gain £15,000 = Total gain £21,160

Taxable gain
- annual exempt amount £12,300
= £8,860

Tax payable
x 20% as higher rate taxpayer.
= £1,772

The qualifying corporate bond is exempt from CGT, so the loss cannot be offset.

(d) **(i)**
- Immediately using the 'real time' CGT service.
- Annually in a self-assessment tax return.

(ii) *Candidates would have scored full marks for any six of the following:*
- HM Revenue Customs may charge a 5% penalty
- if the CGT is not paid within 30 days
- of the 31st January 2022, where gain made in 2020/2021.

- There may be a further 5% penalty
- if the CGT due is not paid within 5 months of penalty date/31 July 2022.

- There may be a further 5% penalty
- if the CGT due is not paid within 11 months of penalty date/31 January 2023.

- These penalties are in addition to the interest that also will be charged on all outstanding amounts including unpaid penalties, until payment is received.

(e)
- As 10% of his home is let he will only get Private Residence Relief (PRR) on £90,000 (90% of gain).

- Atique will be entitled to lettings relief of £10,000
- This is calculated as the **lowest** of:
    - the amount of Private Residence Relief (PRR),
    - £40,000; and
    - the gain made whilst letting out part of his home.
- He can claim lettings relief because he has lived in the home at the same time as his tenant.

- Due to the reliefs mentioned above, he will not be liable for CGT on the sale of his home.

Model answer for Question 3

(a) **(i)** £57,000 salary + £860 interest + £5,600 dividends

Basic rate band extended by total gross pension contribution
£250 x 12 months x 100/80 = £3,750

Basic rate band extended by gift aid donation
£2,000 x 100/80 = £2,500

Non-Savings
£12,500 x 0% = £0
£43,750 x 20% = **£8,750**
£750 x 40% = **£300**

Savings
£500 x 0% = 0
£360 x 40% = **£144**

Dividends
£2,000 x 0% = £0
£3,600 x 32.5% = **£1,170**

Total (£8,750 + £300 + £144 + £1,170)
= **£10,364**

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

- She would have to pay the high-income child benefit tax charge
- of 1% for every £100 of net income over £50,000.
- The tax charge is payable by self-assessment.
- However, Sadie would still receive some benefit (after tax)
- as her adjusted net income is less than £60,000.

(b) **(i)**

- The gift aid donation **would not** extend the basic rate band when calculating top slice relief.

- Lorenzo will pay higher rate tax (40%) on the whole gain
- less a 20% tax credit.

(ii)

- A pension contribution **would** extend the basic rate band
- by the amount of the gross contribution.

- Due to this, the top sliced gain would not exceed the extended higher rate threshold
- so there would be no further tax to pay on the gain.

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

- Interest and dividends from the trust would potentially be subject to Income Tax.
- Both are paid gross.

- Interest can use any available Personal Savings allowance (PSA)/starting rate for savings band.
- Any amount in excess of the PSA will be taxed at Lorenzo's marginal rate (0%/20%/40%/45%).

- The first £2,000 of dividends (the dividend allowance) is tax free.
- Any amount in excess of the dividend allowance is taxed at Lorenzo's marginal rate (7.5%/32.5%/38.1%).

- Tax is payable even if income is accumulated/reinvested.

(d) *Candidates would have scored full marks for any six of the following:*

- Vera would be able to choose her attorney(s).
- Vera can specify the **powers** her attorney(s) would have if she loses capacity.

- The LPA could apply to financial affairs and/or personal welfare

- Setting up an LPA avoids her family needing to apply to the Court of Protection to appoint a Deputy.
- which is costly
- and time consuming.

- It also avoids Vera's assets becoming inaccessible until a Deputy is appointed.

(e) *Candidates would have scored full marks for any six of the following:*

If Oscar:

- Spends fewer than 16 days in the UK in the tax year
- and was UK resident for one or more of the previous three tax years.

- Spends fewer than 46 days in the UK in the tax year
- and was not UK resident for any of the three previous tax years.

- Is working full time overseas
- spending fewer than 91 days in the UK
- and less than 31 days working in the UK.

All questions in the April 2021 paper will be based on English law and practice applicable in the tax year 2020/2021, unless stated otherwise and should be answered accordingly.

The Tax Tables which follow are applicable to the February 2021 and April 2021 examinations.

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:

- 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%

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% first year	18% reducing balance	6% 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%