Chartered Insurance Institute

AF1

Advanced Diploma in Financial Planning

Unit AF1 – Personal tax and trust planning

September 2022 Examination Guide

SPECIAL NOTICES

Candidates entered for the February 2023 examination should study this examination guide carefully in order to prepare themselves for the examination.

Practice in answering the questions is highly desirable and should be considered a critical part of a properly planned programme of examination preparation.

AF1 – Personal tax and trust planning

Contents

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IMPORTANT GUIDANCE FOR CANDIDATES

Introduction

The purpose of this Examination Guide is to help you understand how examiners assess candidates' knowledge and their ability to apply this to a case study scenario. You can then use this understanding to help you in your preparation for the examination.

Before the examination

Study the syllabus carefully

This is available online at www.cii.co.uk. All the questions in the examination are based directly on the syllabus. *You will be tested on the syllabus alone,* so it is vital that you are familiar with it.

There are books specifically produced to support your studies that provide coverage of all the syllabus areas, however you should be prepared to **read around the subject**. This is important particularly if you feel that further information is required to fully understand a topic or an alternative viewpoint is sought. The reading list which can be found with the syllabus provides valuable suggestions.

Note the assumed knowledge

For the Advanced Diploma in Financial Planning, candidates are assumed to have studied the relevant units of the Diploma in Financial Planning or the equivalent. This knowledge is set out on the relevant syllabus.

Read widely

If you do not have experience in advising clients whose financial needs are relatively sophisticated, *it is quite unrealistic to expect that the study of a single textbook will be sufficient to meet all your requirements.* While books specifically produced to support your studies will provide coverage of all the syllabus areas, you should be prepared to read around the subject. This is important, particularly if you feel that further information is required to fully understand a topic, or an alternative viewpoint is sought. It is vital that your knowledge is widened beyond the scope of one book. The reading list which can be found with the syllabus provides valuable suggestions.

Make full use of the Examination Guide
This Examination Guide contains a full examination paper and model answers. The model answers show the types of responses the examiners are looking for and which would achieve maximum marks, *however, you should note that there are alternative answers to some question parts which would also gain high marks.* For the sake of clarity and brevity not all of these alternative answers are shown.

This guide and previous Examination Guides can be treated as 'mock' examination papers. Attempting them under examination conditions as far as possible, and then comparing your answers to the model ones, should be seen as an essential part of your exam preparation. The examiner's comments on candidates' actual performance in each question provide further valuable guidance. You can obtain copies of the two most recent examination guides free of charge at www.cii.co.uk.

Know the layout of the tax tables
Familiarise yourself with the information contained within the tax tables printed at the back of each Examination Guide. These tax tables will be provided to candidates as part of the examination. 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, these are provided in the portal as you sit the exam (see page 6).*

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.

On-screen written exam demonstration (Demo 1)

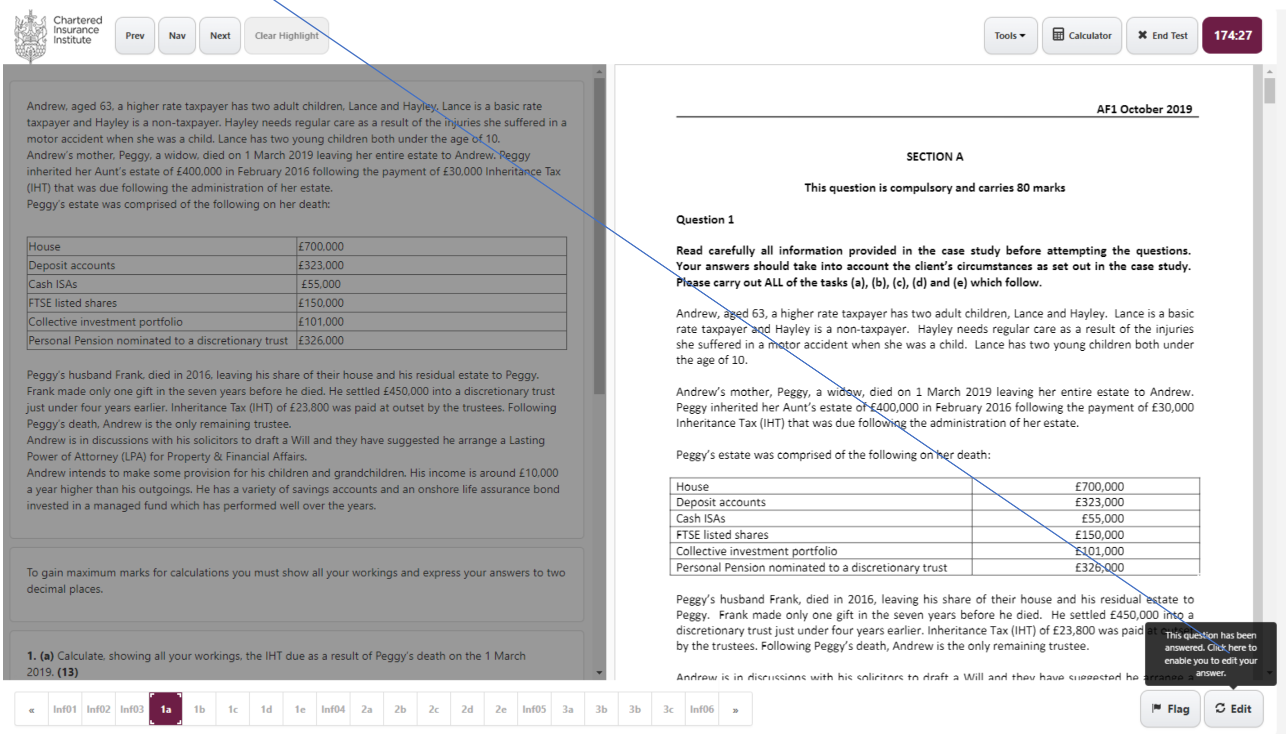
The familiarisation test allows you to experience using the assessment platform before your exam. You can try the familiarisation test at any time

https://www.cii.co.uk/learning/qualifications/assessment-information/on-screen-written-exams-by-remote-invigilation/exam-familiarisation/

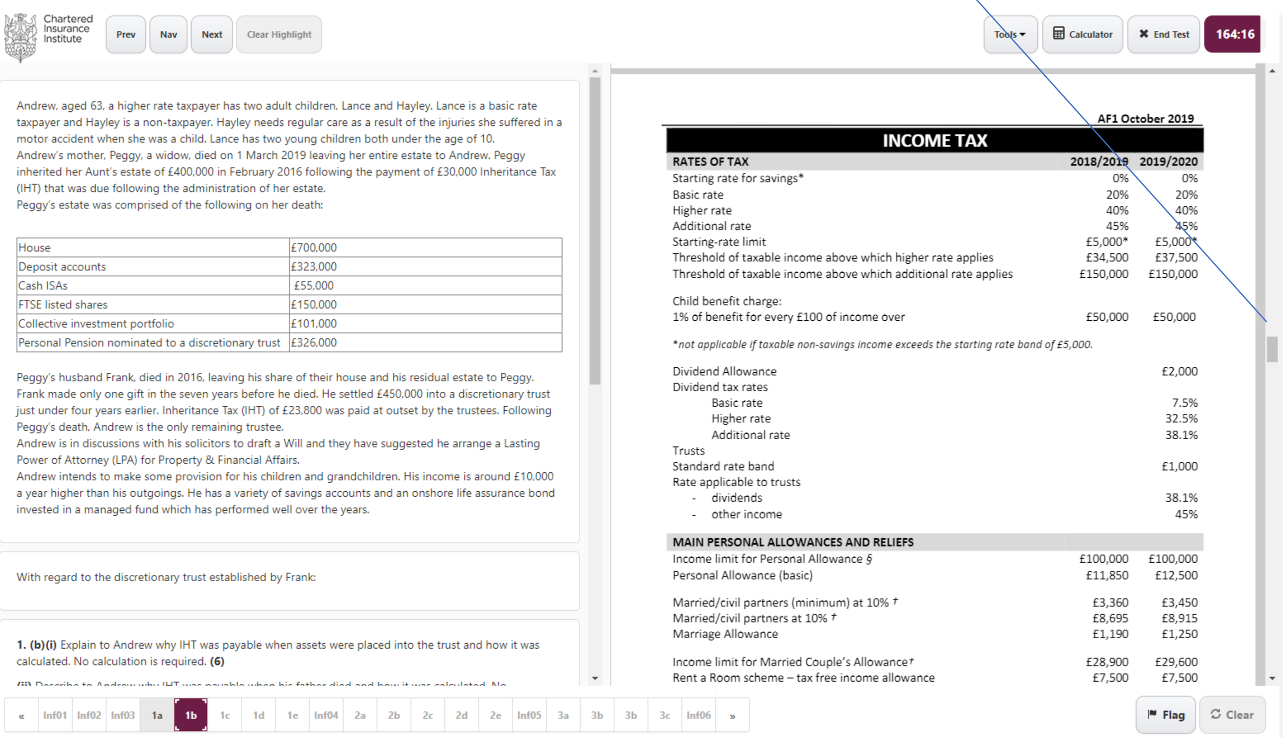
Please note, although based on AF1, this example test is designed for all candidates and while there might be slight differences in layout it will give you a good idea of how to navigate and use the platform functionality.

The demonstration test is designed to allow you before the day to go through the end-to-end process from logging in to answering test questions. **We strongly advise you try the demonstration test once you have received your login details and well in advance of the exam to help pre-empt any potential exam day issues.**

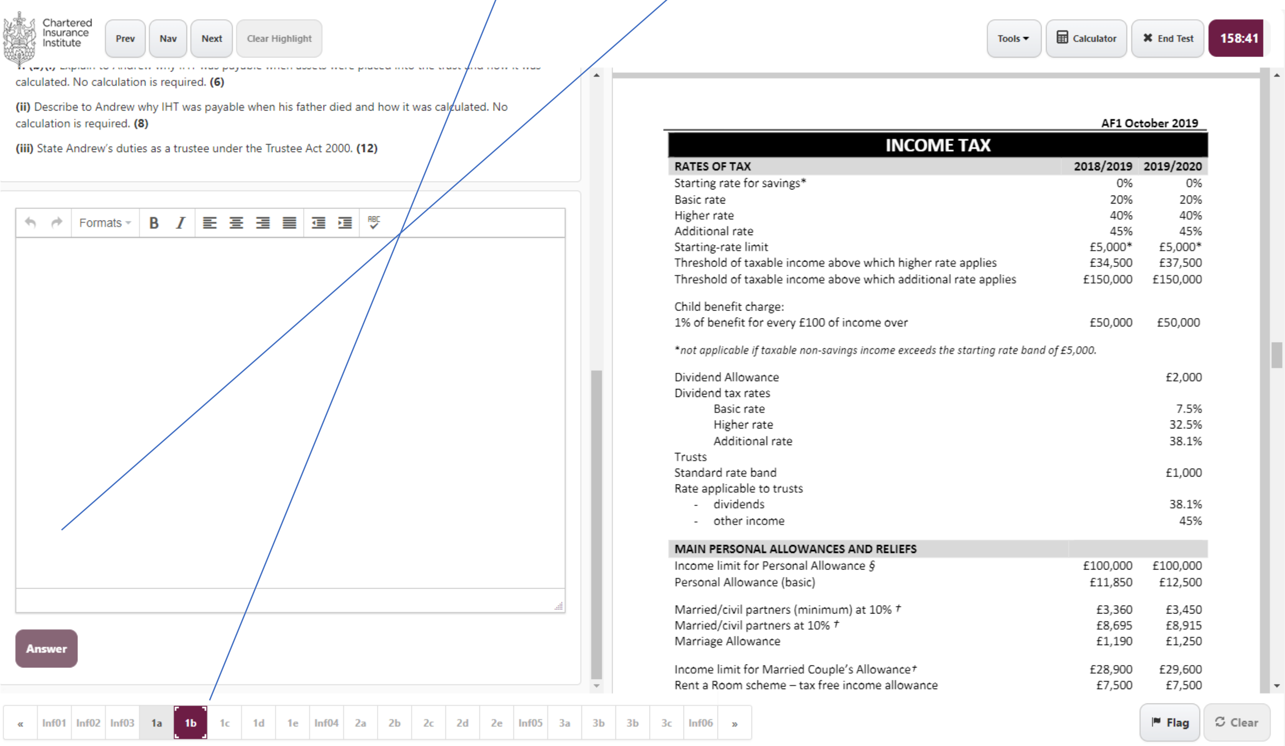
1. From the AF1 demonstration test, ensure you can scroll right and see the whole screen. Ensure your screen resolution shows all the features including the button to return back to your answers to **edit** them. To return to edit any answer you have already typed, you must press ‘Answer’ for the question you are already in otherwise it will not let you select a previous question you have answered to edit.



2. Tax tables are provided at the right-hand side of the interface after the question paper for candidates to use which is different to the CIIs multiple choice exams. Please do not bring your own copies into the exam. Scroll up and down using the navigation bar.



3. Once you have typed in your answer ensure you click the red '**Answer**' box, this will save your answer and move you onto the next question. Unless you press 'Answer', you will not be permitted to move onto other questions. Furthermore, please do not type all of your answers for every question into the answer space for Q1a. You should familiarise yourself with all questions prior to starting the exam.



4. On the day of the AF1 exam, please click on the AF1 Personal tax and trust planning:

AF1 Personal tax and trust planning

on-screen written exam demonstration (Demo 1)

5. The above screenshot shows the point before the exam has started; you wish to take a moment at this screen to jot down any notes on paper that may assist you during the exam. Please note the exam timer will not start until you click the exam titled: **AF1 Personal tax and trust planning.**

In the examination

The following will help:

Spend your time in accordance with the allocation of marks:

- The marks allocated to each question part are shown on the paper.
- If a question has just two marks allocated, there are likely to be only one or two points for which the examiner is looking for, so a long answer is wasting valuable time.
- Conversely, if a question has 12 marks allocated, a couple of lines will not be an adequate answer. Always remember that if the paper is not completed, your chances of passing will be reduced considerably.
- Do not spend excessive time on any one question; if the time allocation for that question has been used up, leave some space, go on to the next question and return to the incomplete question after you have completed the rest of the paper, if you have time.

Take great care to answer the question that has been set.

- Many candidates leave the examination room confident that they have written a 'good' paper, only to be surprised when they receive a disappointing result. Often, the explanation for this lies in a failure to think carefully about what the examiner requires before putting pen to paper.
- Highlighting key words and phrases is a technique many candidates find useful.
- The model answers provided in this Examination Guide would gain full marks. Alternative answers that cover the same points and therefore answer the question that has been asked would also gain full marks.

Tackling questions

Tackle the three questions in whatever order feels most comfortable. Generally, it is better to leave any questions which you find challenging until you have attempted the questions you are confident about. Candidates should avoid mixing question parts, (for example, 1(a)(i) and (ii) followed by 2(b)(ii) followed by 1(e)(i)) as this often leads to candidates unintentionally failing to fully complete the examination paper. This can make the difference between achieving a pass or a narrow fail.

It is vital to label all parts of your answer correctly as many questions have multiple parts to them (for example, question 1(a) may have parts (i), (ii) and (iii)). Failure to fully distinguish between the separate question parts may mean that full credit cannot be awarded. It is also important to note that a full answer must be given to each question part and candidates should not include notes such as 'refer to answer given in 1(b)(i)'.

Answer format

Unless the question requires you to produce an answer in a particular format, such as a letter or a report, you should use 'bullet points' or short paragraphs. The model answers indicate what is acceptable for the different types of question.

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 in your answer, even if you have used a calculator. You are permitted to use your own calculator.

Tips for laying out calculations in on-screen written 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 does not 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 bands, tax rates used in £ terms.
- Use subtotals where appropriate. For example:
    - Total assets - £1,500,000
    - Nil rate band (NRB) – (£325,000)
    - Residence nil rate band (RNRB) – (£175,000)
    - Assets after allowances - £1,000,000
- Show all your workings. This could include:
    - 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.

EXAMINERS' COMMENTS

Candidates' overall performance

It was disappointing that candidates did not perform as well in the September 2022 AF1 examination when compared to the sittings earlier this year in February and April.

The performance of candidates was generally less consistent and fewer candidates managed to achieve high marks.

Candidates who had not prepared well for the exam struggled with some of the core areas of the syllabus, including the responsibilities for the reporting and payment of Inheritance Tax (IHT), the implications of divorce on a Will/benefits of making a new Will and Lasting Powers of Attorney (LPA).

This demonstrates a clear gap in level 4 knowledge and it is recommended candidates study the areas covered in the J02 syllabus thoroughly before entering the AF1 exam.

Candidates should also be reminded to ensure they are up to date with industry changes and hot topics. It was particularly disappointing that many candidates performed poorly on questions relating to the Trust Registration Service (TRS) and National Insurance Contributions (NICs).

Question 1

Part (a) asked candidates to calculate the total IHT payable following Aled's death. In this question candidates were required to calculate the tax payable on the failed potentially exempt transfer (PET) Aled had made in December 2017 and the tax payable on his estate. Few candidates achieved full marks, however, candidates who had prepared well for the exam made a good attempt at calculating the two elements to this question. Candidates that did not perform so well either incorrectly included the PET when calculating the tax liability on the estate or concluded there was no tax payable on the PET, as they did not realise the Chargeable Lifetime transfer (CLT) made in 2012 used up part of the nil rate band (NRB).

In part (b), candidates had to explain who is responsible for the reporting and payment of IHT and when this must be done to avoid any penalties. This is a commonly tested question in AF1 and it was disappointing to see candidates perform poorly overall. Few candidates correctly identified Annabelle/the donee is responsible for paying the tax on the PET and that the personal representatives of the estate would be liable to pay the tax if not paid by Annabelle/the donee.

Part (c) tested candidates on the taxation of Aled's onshore investment bond following his death.

In part (c)(i), candidates were asked to explain briefly the Income Tax position of the bond when he died. It was disappointing that many candidates failed to identify that as Aled was not a life assured, the bond did not come to an end when he died, so there was no chargeable event.

Part (c)(ii) required candidates to describe the Income Tax treatment of the gain when the bond was surrendered. This question was very poorly answered and many candidates incorrectly stated the gain would be assessed as Aled's income, with some confusing the question with the taxation of a bond held under a discretionary trust, where the gain would be assessed as the settlor's income in the tax year of death.

Part (c)(iii), which asked candidates to explain how the taxation of the gain would have differed if the bond had been assigned to Annabelle and Gethin prior to surrender, was answered better than parts (c)(i) and (c)(ii), although the answers given by candidates generally lacked the detail required to score full marks as they did not use the information provided to them in the case study that Annabelle and Gethin were basic rate tax (BRT) payers.

In part (d)(i), candidates had to state who is responsible for registering the Discretionary Will Trust with the Trust Registration Service (TRS) and when it must be done. This is a particularly relevant question in the industry at present and although most candidates correctly identified the trustees must register the trust with the TRS, few were able to state when this must be done, with many candidates incorrectly providing answers based on the requirement to register non-taxable trusts within 90 days of the creation of the trust or by 1 September 2022 if later.

Part (d)(ii), in which candidates were asked to state the factors the trustees should consider when investing the cash held within the Discretionary Will Trust, was generally well answered.

Part (e) required candidates to describe how any exit charge would be calculated if capital distributions are made within the first 10 years of the Discretionary Will Trust being created. Exit charges have been frequently tested in AF1 as a calculation, however, this question was poorly answered, with candidates generally struggling to describe the method for calculating the charge. It was also disappointing that most candidates were unable to correctly identify any distributions within 2 years of the date of Aled's death would not be subject to an exit charge.

Part (f) was a straight-forward question asking candidates to explain the Stamp Duty Land Tax (SDLT) payable by Gethin on the purchase of Rose Cottage and when this must be paid. It was disappointing that some candidates were not able to state the correct SDLT rates and bands as these can be found in the tax tables provided to candidates in the examination.

In part (g)(i), candidates were required to explain the tax advantages if Gethin uses Rose Cottage as a qualifying furnished holiday let (FHL) when compared to a buy-to-let and this was reasonably well answered. It should be noted candidates were only awarded a mark for stating IHT Business Relief may be available after 2 years if they stated if '<u>additional services' were provided</u>. This has been subject to much coverage in the industry/media and we would expect candidates studying at this level to keep up to date with such developments.

Part (g)(ii), in which candidates had to state the conditions which must be met for Rose Cottage to qualify as an FHL, is a question that has been frequently tested in AF1 and was answered well by candidates who had studied thoroughly for the exam.

In part (g)(iii), candidates were asked how Gethin could benefit from an averaging election if he uses Rose Cottage as an FHL. This question has not been tested previously in AF1 and it was pleasing to see well prepared candidates achieve high marks.

Question 2

Part (a), which was a calculation of Chloe's Income Tax liability for the 2022/2023 tax year, was generally well answered, with many candidates achieving full marks.

Part (b) was a calculation of the total employee National Insurance Contributions (NICs) payable by Chloe in the 2022/2023 tax year. It was disappointing many candidates did not factor into their calculation the increase in the primary threshold from £190 to £242 from 5 July 2022, instead providing a calculation based on 52 weeks at £242. It was also a disappointment that some candidates incorrectly provided answers on the basis Chloe would pay class 2 and class 4 NICs.

Part (c)(i) asked candidates to explain the implications of divorce on Chloe's Will and part (c)(ii) asked candidates to explain briefly the benefits for Chloe of making a new Will. This is level 4 knowledge and it was disappointing to see many candidates underperform on this question.

Part (d) was a test of candidates' knowledge of Child Trust Funds (CTF), which remain relevant, as although CTFs were closed to children born after 2 January 2011, the first CTF's did not start to mature until 1 September 2020.

In part (d)(i), candidates were asked to explain the options the CTF provider has if Ben does not take control of his CTF upon reaching age 18. This was not well answered although many candidates correctly identified the CTF could be moved to a cash or stocks and shares ISA.

Part (d)(ii), in which candidates were required to explain Ben's options if he does take control of his CTF at age 18, was answered better, with many candidates stating Ben could encash the account or transfer it to an ISA.

Question 3

Part (a) asked candidates to calculate the Capital Gains Tax (CGT) payable if Tom disposes of half of his shares before he leaves the UK. This was generally well answered although a common mistake made by candidates who did not achieve full marks was the failure in their calculation to extend the basic rate band by Tom's gross pension contribution of £10,000.

Parts (b)(i) and (b)(ii) required candidates to explain the conditions that would need to apply for Tom to be able to sell the remainder of his shares whilst abroad and not be subject to CGT and to explain the consequences if he sold his shares whilst he was abroad but returned to the UK after 4 years. Both questions were answered poorly with candidates continuing to demonstrate a lack of knowledge of residency rules. Residency is frequently tested in AF1 and candidates should study this area thoroughly before entering the exam.

Part (c) asked candidates to describe the implications of Tom moving abroad on his stocks and shares ISA. Many candidates correctly identified the ISA could remain open and well-prepared candidates were able to correctly state he would still get UK tax relief on the funds, but cannot put money into the ISA after the tax year he moves abroad.

Candidates should expect to be tested on Powers of Attorney in AF1 and the exam concluded with a three-part question on Lasting Powers of Attorney (LPA).

In part (d)(i), candidates had to explain the consequences of Arnold losing mental capacity with no LPA in place. The majority of candidates correctly identified an application to the Court of Protection would be required although answers generally demonstrated a lack of knowledge in this area.

Part (d)(ii), which required candidates to describe the advantages of Arnold setting up a health and welfare LPA before he loses mental capacity, was also not well answered, although many candidates correctly stated Arnold can specify who he wants as attorneys and that the attorneys only have the power to make decisions once Arnold loses mental capacity.

In part (d)(iii), candidates were asked to explain the differences if Tom and Betty are appointed to act as attorneys jointly or jointly and severally. A similar question was asked in the April 2022 AF1 examination and although there was an improvement in the answers provided in the September 2022 exam, some candidates still mixed up their answers, incorrectly stating joint attorneys could act independently of one another and attorneys appointed to act jointly and severally could only make decisions together.

Overall in part (d), it was extremely disappointing to see candidates perform poorly in this area of the syllabus and candidates should ensure they have studied and have a solid understanding of Powers of Attorney before sitting an AF1 exam.

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 2022/2023, 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.

If you are sitting via remote invigilation 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.**
- Show your ID to the camera now, if you did not do so during the ID checks.
- Show the edge of your screen with a mirror, if you did not do this during the room scan.
- Show any blank sheets of paper for notes, if you did not show both sides to the camera during the room scan.

If you are sitting in a test centre and encounter a problem, please alert the invigilator.

For candidates sitting via remote invigilation or at a test centre

- **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 in your answer, even if you have used a calculator.
- **Tax tables are provided at the right-hand side of the interface after the question paper, this is different to the multiple choice exams**.
- 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. No watches are permitted**
- Please familiarise yourself with **all** questions before starting the exam.

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

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

Question 1

Aled died on 1 May 2022. He was widowed and left two children, Annabelle aged 30 and Gethin aged 28. He has four grandchildren, aged between 5 and 13.

Aled's wife, Branwen, died three years ago, leaving £162,500 each to Annabelle and Gethin and the remainder of her estate to Aled.

On 1 February 2012 Aled made a gift of £175,000 into a discretionary trust and on 1 December 2017 he made a gift of £250,000 to Annabelle. He had made no other lifetime gifts.

His estate comprised of the following assets:

Asset	Value at date of death (£)
Main residence	550,000
AIM Share Portfolio – purchased 1 September 2018	85,000
Cash ISA	200,000
Onshore Investment Bond	130,000
Current Account	25,000

Aled directed £300,000 of his estate into a Discretionary Will Trust, with the remaining estate split between Annabelle and Gethin, who are both basic-rate taxpayers.

Annabelle and Gethin were the executors of Aled's estate. During the administration of the estate, they surrendered Aled's Onshore Investment Bond on 1 June 2022. The Investment Bond was set up on 31 January 2015, on Annabelle and Gethin's joint lives, with an initial investment of £80,000. The final surrender value was £130,000 and no withdrawals had been taken.

Annabelle and Gethin are the trustees of the Discretionary Will Trust. The trust is currently comprised entirely of cash, which they would like to invest for the benefit of their children until they are aged 18, whilst also retaining the option to access funds earlier for education purposes.

Gethin used part of the inheritance from his father as a deposit towards the purchase of a second investment property, Rose Cottage, in England. The purchase was made on 1 August 2022 and the purchase price was £275,000.

Gethin is considering whether to use the cottage as a buy-to-let or as a furnished holiday let (FHL), although he is concerned the qualifying conditions may not be met in the first few years of letting the property. Gethin already owns an established qualifying FHL which has confirmed bookings totalling 165 days in the 2022/2023 tax year.

PLEASE ENSURE YOU ANSWER EACH QUESTION IN THE CORRECT ANSWER BOX.

Questions

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

(a) Calculate, **showing all your workings**, the **total** Inheritance Tax (IHT) payable following Aled's death on 1 May 2022. **(16)**

(b) Explain who is responsible for the reporting and payment of IHT and when this must be done to avoid any penalties. **(6)**

(c) **(i)** Explain briefly the Income Tax position of Aled's Onshore Investment Bond when he died. **(2)**

(ii) Describe the Income Tax treatment of the gain when the Onshore Investment Bond was surrendered on 1 June 2022. ***No calculations are required.*** **(9)**

(iii) Explain how the taxation of the gain would have differed if the Onshore Investment Bond had been assigned to Annabelle and Gethin prior to surrender. ***No calculations are required.*** **(5)**

(d) **(i)** State who is responsible for registering the Discretionary Will Trust with the Trustee Registration Service (TRS) and when it must be done. **(5)**

(ii) State the factors the trustees should consider when investing the cash held within the Discretionary Will Trust. **(5)**

(e) Describe how any exit charge would be calculated if capital distributions are made within the first ten years of the Discretionary Will Trust being created. ***No calculations are required.*** **(10)**

(f) Explain, **using figures where appropriate**, the Stamp Duty Land Tax (SDLT) payable by Gethin on the purchase of Rose Cottage and when this must be paid. **(5)**

(g) **(i)** Explain the tax advantages if Gethin uses Rose Cottage as a qualifying furnished holiday let (FHL) when compared to a buy-to-let. **(6)**

(ii) State the conditions which must be met for Rose Cottage to qualify as an FHL. **(7)**

(iii) Explain briefly how Gethin could benefit from an 'averaging election' if he uses Rose Cottage as an FHL. **(4)**

Total marks for this question: 80

SECTION B

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

Question 2

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

Chloe, aged 48, is divorced. She lives with her partner, Ewan, and her son, Ben, who will soon be 18.

Chloe is the sole director of a company providing flower arrangements for weddings and corporate events. She takes a salary of £45,000 per year which is paid as a regular monthly amount and dividends of £7,500 per year.

Her other income in the 2022/2023 tax year will be interest of £120 from a cash ISA, interest of £765 from unit trusts and dividends of £2,300 from a Venture Capital Trust (VCT).

When the government introduced Child Trust Funds (CTFs), Chloe invested the initial voucher and some cash in a CTF for her son, but she has since forgotten about it and Ben does not know about it either.

Chloe made a mirror Will before Ben was born. It has not been reviewed since. Her ex-husband is named as the executor and sole beneficiary.

PLEASE ENSURE YOU ANSWER EACH QUESTION IN THE CORRECT ANSWER BOX.

Questions

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

(a) Calculate, **showing all your workings**, Chloe's Income Tax liability in the 2022/2023 tax year. **(13)**

(b) Calculate, **showing all your workings**, the total employee National Insurance contributions (NICs) payable by Chloe in the 2022/2023 tax year. ***You should calculate this on a weekly basis.*** **(9)**

(c) **(i)** Explain the implications of divorce on Chloe's Will. **(5)**

(ii) Explain briefly the benefits for Chloe of making a new Will. **(4)**

(d) **(i)** Explain the options the Child Trust Fund (CTF) provider has if Ben **does not** take control of his CTF upon reaching age 18. **(5)**

(ii) Explain Ben's options if he **does** take control of his CTF at age 18. **(4)**

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

Tom, aged 50, is single and UK domiciled.

Tom has worked for his current employer for 15 years. He has recently been promoted and is required to work overseas for an initial period of 4 years, but this could be extended. He will leave the UK on 1 October 2022.

During his period abroad, Tom will rent out his house. He does not intend to return to the UK at any time during the next 4 years.

Tom will receive a salary of £60,000 in the 2022/2023 tax year. On 1 September 2022 he made a net contribution into his personal pension of £8,000.

Tom has a share portfolio with a current value of £75,000 which he bought 10 years ago for £20,000. He now plans to sell half of his shareholding before he leaves the UK. He intends to sell the remaining half of his shareholding whilst he is abroad as he understands he can do this without paying any tax.

Tom also uses his ISA allowance each year, making the maximum contribution into a stocks and shares ISA.

Arnold and Betty, Tom's parents, are in their late 70's and his father is showing signs of age related memory loss. Tom fears this could rapidly lead to full dementia and loss of mental capacity. He is considering setting up Lasting Powers of Attorney for both parents.

PLEASE ENSURE YOU ANSWER EACH QUESTION IN THE CORRECT ANSWER BOX.

Questions

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

(a) Calculate, **showing all your workings**, the Capital Gains Tax (CGT) payable if Tom disposes of half of his shares before he leaves the UK. **(10)**

(b) **(i)** Explain the conditions that would need to apply for Tom to be able to sell the remainder of his shares whilst abroad and **not** be subject to CGT on the disposal. **(5)**

(ii) Explain the consequences if Tom sold his shares whilst he was abroad but returned to the UK after 4 years. **(4)**

(c) Describe the implications of Tom moving abroad on his stocks and shares ISA. **(5)**

(d) **(i)** Explain the consequences of Arnold losing mental capacity with no Lasting Powers of Attorney in place. **(5)**

(ii) Describe the advantages of Arnold setting up a health and welfare Lasting Power of Attorney before he loses mental capacity with Tom and Betty as attorneys. **(6)**

(iii) Explain the differences if Tom and Betty are appointed to act as attorneys jointly **or** jointly and severally. **(5)**

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) **Tax payable on failed Potentially Exempt Transfer (PET)**

CLT in February 2012	£175,000 - £6,000 = £169,000
+ PET in December 2017	£250,000 - £6,000 = £244,000
less nil rate band (NRB)	=£325,000
excess over NRB	£88,000
x 40%	£35,200
x 60% taper relief	
Tax payable on PET	**£21,120**

<u>**Tax payable on estate**</u>
Chargeable Lifetime Transfer (CLT) does not reduce NRB when calculating tax on the estate as more than seven years ago.

NRB available to estate	£325,000 - £244,000 = £81,000
Main residence	£550,000
AIM share portfolio	£85,000
Cash ISA	£200,000
Onshore Investment Bond	£130,000
Current Account	£25,000

Less IHT business relief for AIM share portfolio (£85,000)

Total	**£905,000**
Less NRB	£81,000
Less residence nil rate band (RNRB) x 2	£350,000
Taxable estate	**£474,000**
x 40%	
Tax payable on estate	**£189,600**
Total Inheritance Tax (IHT) payable	**£21,120 + £189,600 = £210,720**

(b)

- The personal representatives of Aled's estate must make an IHT return to HM Revenue & Customs
- within 12 months of Aled's death.

- The personal representatives are responsible for paying the tax on the estate.
- Annabelle/the donee is responsible for paying the tax on the PET.

- IHT must be paid by the end of the 6th month after Aled died.
- The personal representatives will be liable to pay the tax on the PET if not paid by Annabelle/the donee.

(c) **(i)**

- There was no chargeable event when Aled died
- as the bond did not come to an end/Aled was not a life assured.

(ii)

- As the bond was surrendered during the period of the administration of the estate
- the personal representatives/Annabelle and Gethin are liable to Income Tax
- on the gain
- at the rate applicable to personal representatives/20%
- which is covered by the 20% tax credit.

- The gain will be taxed as estate income when distributed to the beneficiaries
- and taxed at the beneficiaries' marginal rate
- less a credit for tax paid by the personal representatives.
- Top slicing relief is not available.

(iii)

- The personal representatives are not liable to tax as the assignment to beneficiaries is not a chargeable event.
- The beneficiaries would be liable to tax on the gain
- and as they are basic rate taxpayers
- they would benefit from top slicing relief
- which would reduce or eliminate any liability to tax at the higher rate.

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

- The Will trust is excluded from registration for a period of 2 years from the date of Aled's death/1 May 2024.
- The trustees must register the trust with TRS
- 2 years after the date of Aled's death
- if the trust still exists/has not been wound up
- or earlier if the trust accepts additional assets
- or if it becomes a taxable trust.

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

- Trust provisions/rules.
- Tax position of the trust/beneficiaries.
- Timescales/age of beneficiaries.
- Income/capital requirements.
- Attitude to risk (ATR).
- Trustee Act 2000/standard investment criteria/diversification.
- Ethical preferences.
- Economic/market conditions.

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

- Any distributions within 2 years
- of the date of Aled's death
- will not be subject to an exit charge.

- An exit charge will be payable on any distributions after 2 years of the date of Aled's death.
- The effective rate of tax is calculated first
- on the basis of 30%
- of the lifetime rate/20%
- charged on a hypothetical transfer on the date of death
- taking into account the failed PET on 1 September 2017.

- The exit charge is the amount of the distribution multiplied by the effective rate of tax
- reduced by the number of quarters since the trust was created.

(f) 3% on the first £125,000/£3,750
5% between £125,001 and £250,000/£6,250
8% between £250,001 and £275,000/£2,000

- The tax must be paid within 14 days
- of the completion date.

(g) **(i)**

- Full mortgage interest relief available for FHL
- compared to buy to let (BTL) which is limited to a basic rate deduction.

- Profits count as UK relevant earnings when making pension contributions.
- CGT rollover relief/holdover relief may be available.
- Business asset disposal relief may be available on disposal.
- IHT Business Relief (BR) may be available after 2 years if 'additional services' are provided.

(ii)

- It will qualify as a FHL if it is furnished,
- it is available to let for at least 210 days
- in the tax year
- on a commercial basis to the public
- and was actually let for more than 105 days in the tax year.

- The cottage can be let for more than 31 days
- but these periods must not total more than 155 days in the tax year.

(iii)

- If Rose Cottage does not meet the letting condition of 105 days
- then as Gethin already owns another FHL
- an average number of days can be taken over both properties
- which may enable both to meet the qualifying conditions.

Model answer for Question 2

(a) **Taxable income**

£45,000 salary + £7,500 dividends + £765 interest = £53,265

Non-savings
£12,570 x 0% = £0
£32,430
X 20% = £6,486

Savings
£500 PSA x 0% = £0
£265 x 20% = £53

Dividends
£2,000 x 0% = £0
£2,505 x 8.75% = £219.19
£2,995 x 33.75% = £1,010.81

Total £6,486 + £53 + £219.19 + £1,010.81 = £7,769

(b) Salary per week £45,000/52 = £865.38

6 April 2022 – 5 July 2022 (13 weeks)
Up to £190 – nil
£865.38 - £190 = £675.38
@13.25%
= £89.49
x 13 weeks = £1,163.37

6 July 2022 – 5 April 2023 (39 weeks)
Up to £242 – nil
£865.38 - £242 = £623.38 @13.25%
= £82.60
x 39 weeks = £3,221.40

Total NICs £1,163.37 + £3,221.40 = £4,384.77

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

- On divorce, Chloe's Will remains valid.
- However, as her ex-husband will be treated as if he had died on the date the marriage legally ended
- he will not be able to benefit from the Will
- unless there were express clauses that stated otherwise.

- The estate will be distributed via the rules of intestacy.
- The ex-husband will not be able to be an executor.

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

- Chloe can leave her estate to who she wishes/avoids intestacy rules
- she could make provision for Ewan
- and she could specify when the beneficiaries receive their share/avoids Ben benefitting at age 18.
- She could appoint a new executor
- and a legal guardian for Ben until he reaches 18.

(d) **(i)**
- The CTF provider must place the CTF into a protected account
- with a tax advantaged status.
- This can be a matured CTF account or a cash or stocks and shares ISA
- offered by the original CTF provider.
- No new subscriptions can be accepted into the account.

(ii)
- Ben can encash the account
- or transfer the account to an ISA
- and the transfer amount will be disregarded for the ISA subscription limit
- unless the transfer is made to a Lifetime ISA, in which case the LISA limits are kept.

Model answer for Question 3

(a)

Pension contribution extends basic rate band by gross contribution
£8,000/0.8 = £10,000
Basic rate band £37,700 + £10,000 = £47,700

Basic rate band remaining
Taxable income £60,000 - £12,570 = £47,430
Extended BR band £47,700 – taxable income £47,430
= £270

Taxable gain
Sale proceeds £75,000/2 = £37,500
Less acquisition cost £20,000/2 = £10,000
= £27,500

Less annual exempt amount (AEA) £12,300
= £15,200

£270 x 10% = £27
£14,930 x 20% = £2,986

CGT payable = £3,013

(b) **(i)**

- He would need to sell the shares in the next tax year
- as he would then be non-UK resident for tax purposes.

- He would have to be non-UK resident for 5 years
- starting from 6th April 2023
- to avoid paying CGT on the shares.

(ii)

- He will be caught by the temporary non-residence rules
- as he would not have five years of non-residence
- and will be liable for CGT on the gain
- in the tax year he resumes UK residence.

(c)

- He can keep the ISA open.
- He will still get UK tax relief on the funds.
- Tom cannot put money into his ISA after the tax year that he moves abroad.
- He can pay into the ISA once he is UK resident again.
- He must tell his ISA provider as soon as he stops being a UK resident.

(d) **(i)**
- It would not be possible to set up new LPAs for Arnold once he has lost mental capacity.
- There would be no one who had legal rights to make decisions about his financial affairs or health and welfare.
- If Tom/Betty wished to make decisions about Arnold's financial affairs or health and welfare they would have to apply to the Court of Protection (COP) for the power to make decisions.
- The COP will grant a financial affairs deputyship
- but is unlikely to grant a wide-ranging health and welfare deputyship/may only grant a limited health and welfare deputyship/they would need to keep applying to the COP to extend the range of health and welfare deputyship.

(ii)
- The LPA would be valid/could not be challenged on grounds of capacity.
- Arnold can specify who he wants as attorneys
- Arnold can state any instructions/restrictions that he wished to place on the attorneys.
- The attorneys would have a legal right to make health and welfare decisions for him provided they were legal.
- The attorneys only have the power to make decisions once Arnold loses mental capacity,
- safeguarding his father.

(iii)
- If the attorneys were to act jointly, they must both make unanimous decisions together.
- The LPA would be invalid if either attorney dies/loses capacity as the attorneys must act jointly.
- Decisions could be delayed if Tom had to return to the UK while working abroad/if Tom out of the country unable to make decisions.

- If the attorneys act jointly and severally, either attorney could make a decision
- and the LPA would still be valid on death/incapacity of an attorney.

Glossary of terms

Some abbreviations candidates can use in on-screen written exams:

1. ATR – Attitude to risk
2. BRT – Basic rate taxpayer
3. BIK – Benefit in kind
4. CLT – Chargeable lifetime transfer
5. CFL – Capacity for loss
6. CGT – Capital Gains Tax
7. COP – Court of Protection
8. DOV – Deed of variation
9. DIS – Death-in-Service
10. DFM – Discretionary Fund Manager
11. EIS – Enterprise Investment Scheme
12. ESG – Environmental, Social and Governance
13. EPT – Excluded property trust
14. EPA – Enduring power of attorney
15. ERC – Early repayment charges
16. FAD – Flexi-access drawdown
17. FSCS – Financial Services Compensation Scheme
18. FOS – Financial Ombudsman Service
19. GAR – Guaranteed annuity rate
20. HRT – Higher rate taxpayer
21. IHT – Inheritance Tax
22. IT – Income Tax
23. IVA – Individual Voluntary Arrangement
24. LPA – Lasting power of attorney
25. LTA – Lifetime allowance
26. MVR – Market value reduction
27. MPAA – Money purchase annual allowance
28. NICs – National Insurance Contributions
29. NPA – Normal pension age
30. NRA – Normal retirement age
31. NRB – Nil rate band
32. OPG – Office of the Public Guardian
33. OEIC – Open ended investment company
34. PAYE – Pay As you Earn
35. PPP – Personal pension plan
36. PCLS – Pension commencement lump sum
37. PA – Personal allowance
38. PSA – Personal savings allowance
39. RAC – Retirement annuity contract
40. RNRB – Residence nil rate band
41. SIPP – Self-invested personal pension plan
42. SEIS – Seed Enterprise Investment Scheme
43. UFPLS – Uncrystallised fund pension lump sum
44. VCT – Venture capital trust

All questions in the February 2023 paper will be based on English law and practice applicable in the tax year 2022/2023, unless stated otherwise and should be answered accordingly.

The Tax Tables which follow are applicable to the September 2022 and February 2023 examinations.

INCOME TAX

RATES OF TAX	2021/2022	2022/2023
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	£37,700	£37,700
Threshold of taxable income above which additional rate applies	£150,000	£150,000

Child benefit charge:
1% of benefit per £100 of adjusted net income between £50,000 – £60,000

**Only applicable to savings income that falls within the first £5,000 of income in excess of the personal allowance*

Dividend Allowance	£2,000	£2,000
Dividend tax rates		
Basic rate	7.5%	8.75%
Higher rate	32.5%	33.75%
Additional rate	38.1%	39.35%
Trusts		
Standard rate band	£1,000	£1,000
Rate applicable to trusts		
- dividends	38.1%	39.35%
- other income	45%	45%

MAIN PERSONAL ALLOWANCES AND RELIEFS		
Income limit for Personal Allowance §	£100,000	£100,000
Personal Allowance (basic) §	£12,570	£12,570
Married/civil partners (minimum) at 10% †	£3,530	£3,640
Married/civil partners at 10% †	£9,125	£9,415
Marriage Allowance	£1,260	£1,260
Income limit for Married Couple's Allowance†	£30,400	£31,400
Rent a Room scheme – tax free income allowance	£7,500	£7,500
Blind Person's Allowance	£2,520	£2,600
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)	£2,845	£2,935
- family element	£545	£545
Threshold for tapered withdrawal of CTC	£16,480	£17,005

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 Employee	**Weekly**
Lower Earnings Limit (LEL)	£123
Primary threshold	£242*
Upper Earnings Limit (UEL)	£967

Total earnings £ per week	**CLASS 1 EMPLOYEE CONTRIBUTIONS**
Up to 242.00**	Nil
242.00* – 967.00	13.25%
Above 967.00	3.25%

**£190 per week/£9,880 per annum before 6 July 2022.*
***This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £123 per week. This £123 to £242* 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 175.00***	Nil
175.00 – 967.00	15.05%
Excess over 967.00	N/A

**** Secondary earnings threshold.*

Class 2 (self-employed)	Flat rate per week £3.15 where profits exceed £6,725 per annum.
Class 3 (voluntary)	Flat rate per week £15.85.
Class 4 (self-employed)	10.25% on profits between £11,908 – £50,270. 3.25% on profits above £50,270.

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 & 2013/2014	£1,500,000
2014/2015 & 2015/2016	£1,250,000
2016/2017 & 2017/2018	£1,000,000
2018/2019	£1,030,000
2019/2020	£1,055,000
2020/2021 – 2022/2023	£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
2014/2015 – 2022/2023	£40,000*

**Reducing 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	2021/2022	2022/2023
	£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	2021/2022	2022/2023
Individuals, estates etc	£12,300	£12,300
Trusts generally	£6,150	£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%
Business Asset Disposal Relief* – Gains taxed at:	10%	10%
Lifetime limit	£1,000,000	£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	2021/2022	2022/2023
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 EXEMPTION		
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*	£175,000	£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

	2021/2022 Rates	2022/2023 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
Motorcycles	24p per mile	24p per mile
Bicycles	20p per mile	20p per mile

MAIN CAPITAL AND OTHER ALLOWANCES

	2021/2022	2022/2023
Plant & machinery (excluding cars) 100% annual investment allowance (first year)	£1,000,000	£1,000,000
Plant & machinery* first year allowance for companies to 31/3/2023:	Super-deduction	130%
	Special rate	50%
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 1 April 2016 (Corporation Tax) or 6 April 2016 (Income Tax)

CO_2 emissions of g/km:	0*	1-50	Over 50
Capital allowance:	100% first year	18% reducing balance	6% reducing balance

**If new and unused*

MAIN SOCIAL SECURITY BENEFITS

		2021/2022	2022/2023
		£	£
Child Benefit	First child	21.15	21.80
	Subsequent children	14.00	14.45
	Guardian's allowance	18.00	18.55
Employment and Support Allowance	Assessment Phase		
	Age 16 - 24	Up to 59.20	Up to £61.05
	Aged 25 or over	Up to 74.70	Up to £77.00
	Main Phase		
	Work Related Activity Group	Up to 104.40	Up to 107.60
	Support Group	Up to 114.10	Up to 117.60
Attendance Allowance	Lower rate	60.00	61.85
	Higher rate	89.60	92.40
Basic State Pension	Single	137.60	141.85
	Married	275.20	283.70
New State Pension	Single	179.60	185.15
Pension Credit	Single person standard minimum guarantee	177.10	182.60
	Married couple standard minimum guarantee	270.30	278.70
	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	59.20	61.05
	Age 25 or over	74.70	77.00
Statutory Maternity, Paternity and Adoption Pay		151.97	156.66

CORPORATION TAX

	2021/2022	2022/2023
Standard rate	19%	19%

VALUE ADDED TAX

	2021/2022	2022/2023
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 - £925,000	5%
£925,001 - £1,500,000	10%
£1,500,001 and over	12%

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%