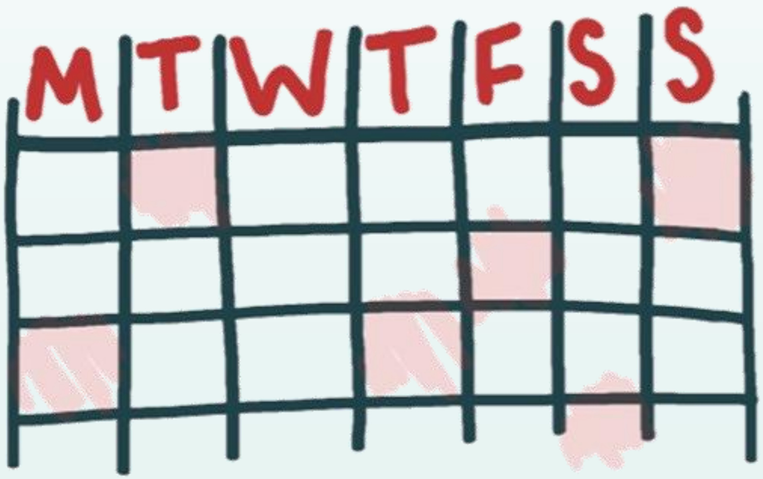
CeMAP 1

Online course

Agenda

- The examination and exam techniques
- Unit 1
    - Topics 1 - 16
- Unit 2
    - Topics 17 - 25



The examination

Computer based exam

Two units in CeMAP 1,

i.e. two separate exams

- 50 multi-choice questions in each unit
- 70% pass mark
- 60 minutes per unit
- Able to flag questions and return to them later

Given tax tables in the exam

Only have to retake units you fail

Examination technique

- Know the exam and do the study
- Answer all of the questions
- Read the full question, and answer the question you are given
- Take your time, and don’t panic
- Don’t change your answer – unless you are sure
- Use the three pass technique

CeMAP One

UNIT 1

Introducing the financial services industry

Function of Financial Services

- Money - medium of exchange and unit of account
- Must be:
  1. Sufficient in quantity
  2. Generally acceptable to all parties in a transaction
  3. Divisible into small units
  4. Portable
- Intermediation
  - geographic location, maturity transformation, aggregation, risk transformation RM – INSURANCE
- Financial institutions
  - retail/wholesale, proprietary/mutual
- Role of the Bank of England

Disintermediation

Cutting out the middleman’s profit

E.G. Companies raising shares to raise funds from the public.

- Recently Banks, Building Societies and such like.

Economic policy and financial regulation

Economic policy

Most governments aim to achieve 4 key economic objectives:

1. Price stability
2. Low unemployment
3. Satisfactory economic growth
4. Balance of payments equilibrium

Inflation / Disinflation / Deflation

Economic Cycle

Phase	Activity
Recovery and expansion	Interest rates, inflation and unemployment are low. Consumers have money to spend. Demand for goods and services rises, pushing prices up. Share prices improve as businesses flourish.
Boom	To prevent the economy from overheating, the Bank of England may intervene by putting up interest rates to control consumer spending and dampen inflation.
Contraction or slowdown	Once the interest rate rises start to bite, consumer spending falls. Demand for goods and services falls, profits fall (as do share prices) and unemployment rises. Inflation slows down.
Recession	A significant decline in economic activity (measured by gross domestic product (GDP)) over 2 consecutive quarters. The Bank of England may intervene to reduce interest rates in a bid to stimulate demand and set the economy on the path back to recovery.

Monetary policy

Inflation target

- 2% measured by CPI
- BoE has responsibility for achievement of target

Interest rates

- Set by MPC of BoE
- Impact of interest rate changes
- LIBOR / SONIA

Fiscal Policy

- Influences the money supply through manipulation of public sector finances
  - central government , local authorities, public corporations
- Balanced budget / Budget surplus / Budget deficit

Regulatory Oversight in UK

!st Level

Acts of Parliament e.g. FSMA 2000

2nd Level

Regulatory Bodies e.g. FCA, PRA

3rd Level

Policies and practices of the financial institution e.g. A bank's own procedures

4th Level

Arbitration Schemes e.g. FOS

UK Taxation 1

Residence and domicile

Residence in the UK for tax purposes

- **resident** if in UK for **183**+ days in any tax year
- **statutory resident test is applied** if not resident for at least 183 days in a tax year
- if resident in UK then liable to UK **income tax or CGT** on worldwide income and gains
- double taxation agreements

Domicile

- domicile of **origin**
- domicile of **choice**
- **deemed** domicile
- if UK domiciled then liable to **IHT** on worldwide assets
  - if not UK domiciled, still liable to IHT on UK assets

Income Tax

- What income is taxable/non-taxable?
- PAYE and self-assessment
- Allowances (tax tables) & allowance reductions
- Personal savings allowance / Dividend allowance /savings starting rate
- Order of taxation (income, savings, dividends)
- Calculations

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INCOME TAX

Tax year 6th April – 5th April

Income from work & pensions (earned)

- Employed – PAYE
- Self employed – direct to HMRC

Savings Income (unearned)

- Investment income
- Interest / Dividend

SELF ASSESSMENT DATES

Self Employed

- Self Assessment completion
  - 31st October – paper form
  - 31st January – online
- Failure
  - Fine £100
- Payment Dates
  - 31st January and 31st July

Personal allowance reduction

- If an individual earns in excess of £100,000, their PA will be reduced by half the excess over £100,000
- E.g. If income was £110,000, this exceeds £100,000 by £10,000 so their personal allowance would be reduced by £5,000 making it £7,500

Benefits in kind

- Taxable ‘perks’ provided by employer to employee e.g. company car / private medical insurance

- Each of these Benefits In Kind has a taxable value

- The taxable value is deducted from your personal allowance

  - e.g. James had a company car as a BIK with a taxable value of £3,000. His P/A would be:

    £12,570 - £3,000 = £9,570

Personal savings & dividend allowances

- PSA – from 6/4/16
  - BRT can earn up to £1,000 in savings income tax free
  - HRT can earn up to £500 in savings income tax free
  - ART has no PSA

- Since 6/4/17 banks and building societies have stopped deducting tax from savings

- ISA interest does not count towards PSA as it is already tax free

- **Dividend Allowance – income from dividends of up £1,000 is tax free regardless of amount of other income**

Income tax calculation 1

- Single person aged 35 has gross earnings of £14,000. Calculate their income tax liability.

Answer to calculation 1

Earnings	£14,000
Personal Allowance	<u>£12,570</u>
Taxable Pay	£ 1,430

£1,430 x 20% = £286 Tax Liability

Income tax calculation 2

- Still single aged 36 just got a pay rise! Gross earnings now £51,000. Now what is their income tax liability.

Answer to calculation 2

Earnings	£51,000
Personal Allowance	<u>£12,570</u>
Taxable Pay	£38,430

Taxable pay <u>above</u> £37,700 <u>**is liable for**</u> HRT!

£37,700 @ 20%	=	£ 7,540
£ 730 @ 40%	=	<u>£ 292</u>
		£ 7,832 Tax Liability

Income tax calculation 3

Bill is single and aged 27. He has earned income of £27,000 and a company car with a taxable value of £3,500.

What is his income tax liability?

Answer to calculation 3

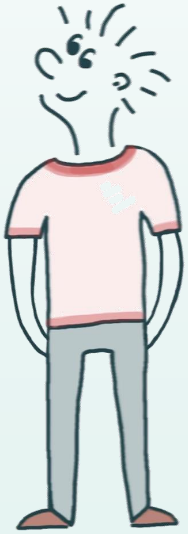
Earnings	£27,000
Personal Allowance (normal allowance LESS Value of company car)	£ 9,070
Taxable Pay	£17,930

£17,930 @ 20% = £ 3,586 Tax Liability

Income tax calculation 4

Bob is single and aged 49. He has earned income of £106,000.

What is his income tax liability?



Answer to calculation 4

His income exceeds £100,000 so we need to see how this will affect his personal allowance.

£106,000 - £100,000 = £6,000

£6,000 / 2 = £3,000 **deducted** from his personal allowance

Earnings	£106,000
Personal Allowance	£ 9,570
Taxable Pay	£ 96,430

£37,700 @ 20%	=	£ 7,540
£58,730 @ 40%	=	£ 23,492
		£ 31,032 Tax Liability

Income tax calculation 5

Jenny has earned income of £19,000. She also receives interest from her savings of £1,250 and dividend income of £3,100.

What is her income tax liability?

Answer to calculation 5

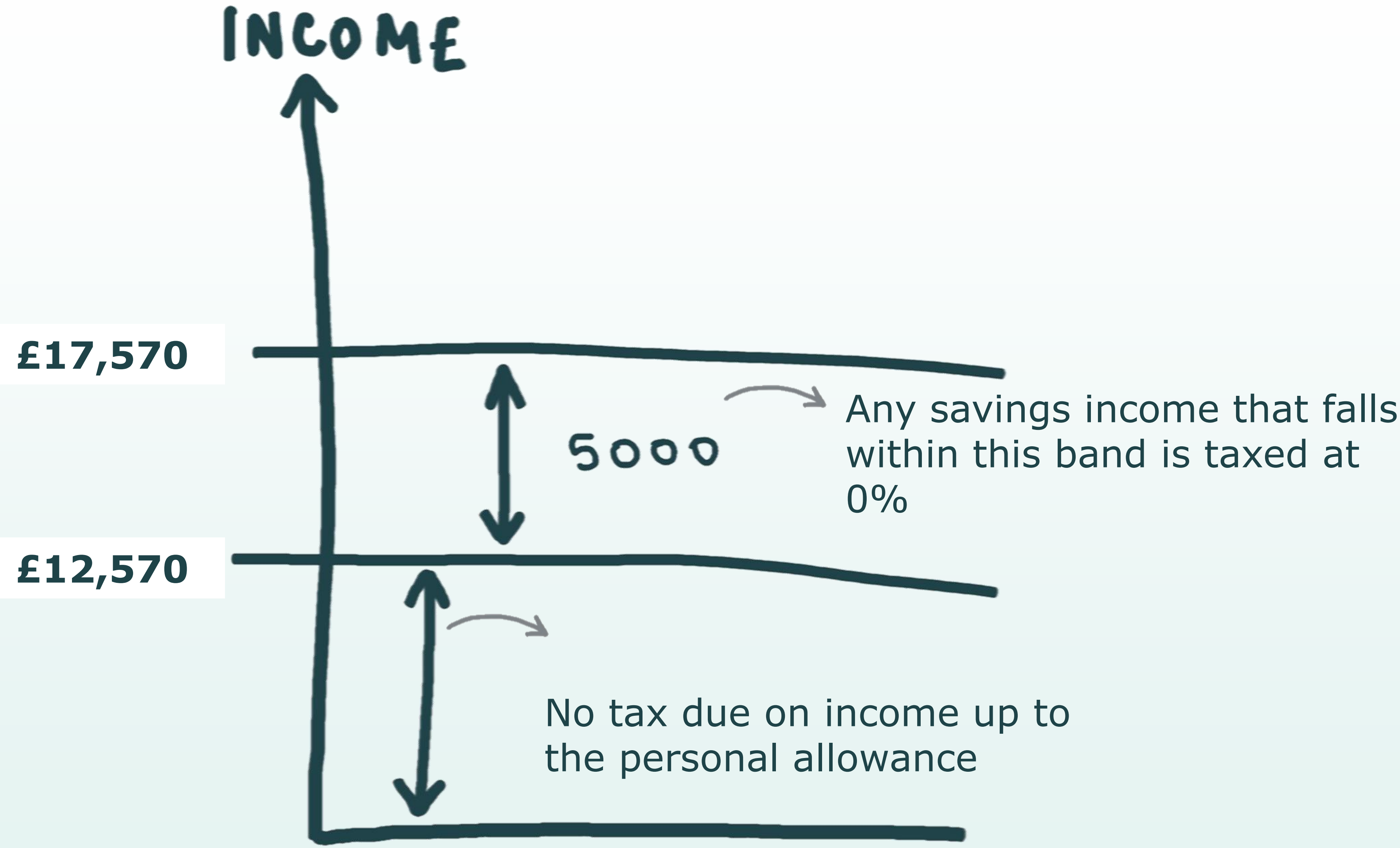
Earnings	£19,000
Personal Allowance	£12,570
Taxable Earned Income	£ 6,430
Interest	£ 1,250
Personal Savings Allowance	£ 1,000
Taxable Interest	£ 250
Dividends	£ 3,100
Dividend Allowance	**£ 1,000**
Taxable Dividends	**£ 2,100**

Answer to calculation 5

Earned income	£6,430 @ 20% =	£1,286
Savings income	£ 250 @ 20% =	£ 50
Dividends	**£2,100 @ 8.75% =**	**£ 183.75**
		£1519.75
		Tax Liability

Income Tax

How the Savings Starting Rate Band works



Income tax calculation 6

Moira has earned income of £12,900 and she also receives savings interest of £6,000 **= £18,900**.

What is her income tax liability?

Answer to calculation 6

Earnings	**£12,900**
Personal Allowance	**£12,570**
Taxable earned income	**£ 330**

- **This uses up £330 of her savings starting rate band of £5,000 so she still has £4,670 of her savings that fall within this band and will be taxed at 0%.**
- Moira is also a BRT so she will have her full £1,000 PSA to offset against her savings income.

Answer to calculation 6

Savings interest	£6,000
Savings Starting Rate Band	£4,670
PSA	£1,000
Taxable interest	£ 330
Taxable Earned inc. £330 @ 20% =	£ 66
Taxable Savings inc. **£330 @ 20% =**	**£ 66**
	£ 132 Tax Liability

Charitable Giving

- Gift Aid
- Payroll Giving

National Insurance

- Form of taxation on income
- Eligibility for social security benefits
- Class 1 – Employers & Employees
- Class 2 – Flat rate for self-employed
- Class 3 – Flat rate voluntary
- Class 4 – Additional self-employed contributions based on profits.

UK Taxation 2

Capital gains tax

- Tax payable if profit made on disposal of assets

- Tax rate
  - 10% (gain falling into BRT band) / 20% (gain falling into HRT or ART band)
  - For residential properties (BTL / 2nd home) it is 18% (gain falling into BRT band) / 28% (gain falling into HRT or ART band)

- Exemptions & Allowances

Exemption 5/3rds for chattels

e.g. Mary bought a vase at auction 6 years ago for £2,000. She sold it today for £8,000. **She has already used her annual exemption of £6,000 on another disposal**. Calculate the gain for CGT purposes.

The gain will be the LOWER of:

Actual Gain	5/3rd of the excess over £6,000 (but less than £15,000)
Selling price £8,000 Purchase price £2,000 GAIN = **£6,000**	Selling price £8,000 Less £6,000 Excess = £2,000 (5/3) x £2,000 = **£3333.33**

The gain for tax purposes will be £3333.33

CGT – Capital losses

Capital losses - Carried forward indefinitely

e.g. Mary made a gain this tax year of £12,500 and she also made a loss this year of £13,800. How much loss can she carry forward?

Tax year **2023/24**

Loss £13,800 – Gain £12,500 =

£0 gain so no CGT

£1,300 loss to carry forward to future years

CGT – Capital losses

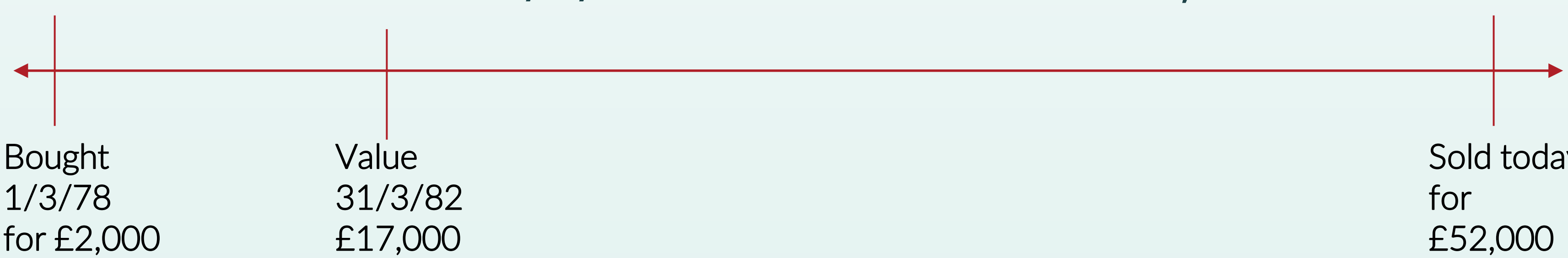
e.g. Let’s say Mary’s loss was made in a previous tax year. What difference does this make?

- Because the loss was made in a previous tax year we only need to offset enough to bring the gain this year down to the annual allowance figure
- **£12,500 gain - £6,000 (annual allowance) =**
- **£6,500 loss used**
- So we have no CGT to pay this year
- **And £13,800 - £6,500 = £7,300 loss to carry forward to future years**

Capital gains tax

- Reductions allowable to calculate gain
  - Acquisitions costs (i.e. value on date of acquisition if a price is not paid for the asset)
  - Buying & selling costs
  - Cost of enhancement (NOT maintenance)

- 31st March 1982 baseline – known as Rebasing
  - e.g. below - gain would be based on difference in value between 31/3/82 and sale date = £35,000



Capital gains tax

- Collection of CGT
  - Tax due on any gain on 31st January in the year following the tax year the gain was made e.g. if gain made in **2021/22, tax due must be paid by 31st January 2023**

- Private residence, roll-over, holdover and Business Asset Disposal relief

CGT

Roll-over Relief

1 year

3 years

Sell with gain of £280,000

CGT on 1st sale deferred until final disposal

Invest proceeds including whole gain

Business Asset Disposal Relief

- CGT = 10 % applied to a lifetime limit of £1,000,000 of cumulative gains arising from the disposal of trading businesses and from certain disposals of shares in trading companies.

- To claim Business Asset Disposal relief:
    - the individual must generally own min. 5% share capital of business
    - have min. 5% of the voting rights in that company
    - be entitled to min. 5% of the distributable profits and net assets of the company.
- Most property letting businesses do not qualify for Business Asset Disposal relief.

- Business Asset Disposal relief also applies to gains resulting from investment into unlisted companies.

Capital gains tax - calculation

- George bought an antique at auction. He paid £10,000 and the auction costs were £500.
- He sold it for £26,000. The selling costs were £600.
- George's taxable income is £14,000
- Calculate the CGT payable.

Answer to CGT calculation

Selling Price	£26,000
Less Purchase Price	£10,000
Less Buying Costs	£ 500
Less Selling Costs	£ 600
Total Gain	£14,900
Less CGT Exemption	**£ 6,000**
Taxable Gain =	**£ 8,900 x 10%**
CGT liability	**£890**

Inheritance tax

- Levied on estate on death
- Exemptions – tax tables
- Nil rate band / Residence Nil Rate Band
- Transferable Nil Rate Band

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Transferable nil rate band & residence NRB

Transferable NRB

- Transfer any unused **<u>% of</u>** nil rate band between spouses/civil partnerships

RNRB

- £175,000 (2022/23) as long as main residence is left to direct descendant
- Transferable between spouses and civil partners on death, much like the standard NRB. It is the unused % of the RNRB from the estate of the first to die which can be claimed on the second death.

Transferable nil rate band

e.g. Robert & Marion are married and each have an estate valued at £375,000. They have no direct descendants. Marion died in December 2007 when the NRB was £300,000 and left everything to Robert.

Calculate the potential inheritance tax liability if Robert died today with a total estate of £750,000 (including the inheritance from Marion)

IHT transferable NRB answer

On Robert's death

Total estate	=	£750,000
- nil rate band (NRB)	=	£325,000
- carried forward 100% NRB	=	£325,000
Taxable estate	=	£100,000
		x 40%
		£40,000 IHT

Potentially Exempt Transfers

- IHT may also be payable on gifts made during a person's lifetime – they are called potentially exempt transfers (PETs)
- No tax due at the time of transfer
- If the donor dies within **seven years** of making the gift, they are added back into the estate in full (in chronological order) for IHT calculation purposes
- These PET's may use up some / all of the deceased's NRB. If they exceed the NRB, IHT will be due from the recipient of the gift
- Taper relief may be used to reduce the tax payable

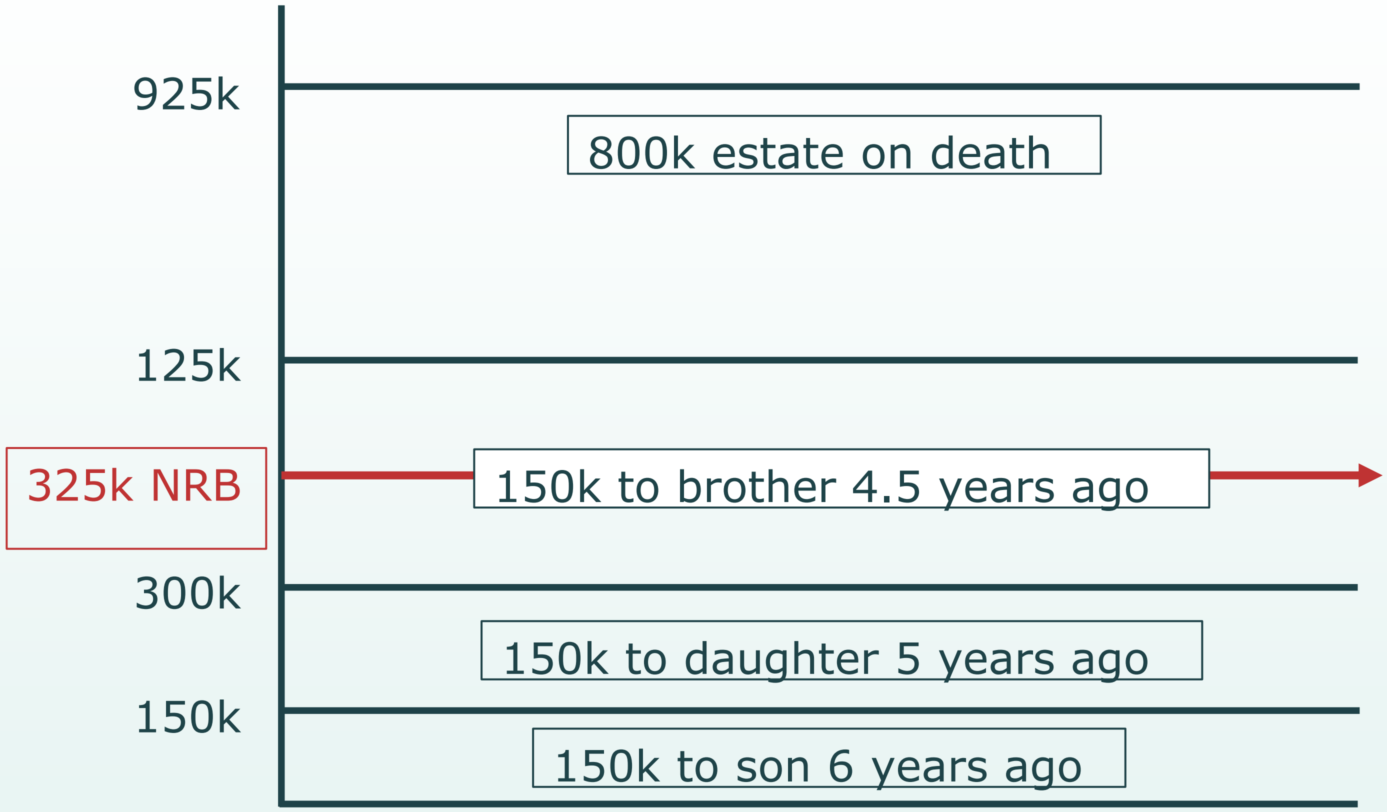
Example Question -
Effect of potentially exempt transfers on IHT

Bert died today with an estate valued at £800k – he did not own his property so there is no amount in the estate included for a residence.

On top of this £800k, Bert gifted:

- £100k to his sister 9 years ago
- £150k to his son 6 years ago
- £150k to his daughter 5 years ago
- £150k to his brother 4.5 years ago.

What IHT is due on Bert's estate and who must pay it?


925k
800k estate on death
125k
325k NRB
150k to brother 4.5 years ago
300k
150k to daughter 5 years ago
150k
150k to son 6 years ago

Example Answer -
Effect of potentially exempt transfers on IHT

- The £100k to the sister is exempt as Bert survived more than 7 years after gifting it. The other gifts however (because they were given within the 7 years prior to Bert's death) fall back into the estate in chronological order (starting with the one that was gifted earliest).

- The £150k given to his son 6 years ago uses up the 1st £150k of Bert's nil rate band (NRB) so there is no IHT payable on this.

- The £150k to his daughter 5 years ago uses up the next £150k of the NRB (making a total of £300k of the £325k NRB used) so there is no IHT payable on this.

Example Answer – cont'd

Effect of potentially exempt transfers on IHT

- Next we have the £150k he gave to his brother 4.5 years ago. There is only £25k of the NRB left so £125k of the £150k gift will exceed the NRB. This £125k is taxed as normal at 40% which = £50,000 however, we now go to the taper relief tables at the bottom of the IHT section of our tax tables. This gift was given 4.5 years before Bert's death so from the taper relief table we can see that only 60% of the tax due is payable so £50k x 60% = £30k. It is the responsibility of the brother to pay this £30k bill.

- Finally we also have the £800k estate which is all taxable at 40% which = £320,000. It is the responsibility of Bert's personal representatives to ensure this is paid before the estate funds will be released.

Chargeable lifetime transfers

- John had never made a CLT before.
  He then made the following CLT's:

	Funds placed into CLT's	Cumulative total over 7 years
2013/14	£100,000	£100,000
2014/15	-	
2015/16	£100,000	£200,000
2016/17	-	
2017/18	£100,000	£300,000
2018/19	-	
2019/20	£100,000	£400,000
2020/21	????	????

- It was only in 2019/20 that the total placed into CLT's over the 7 successive years exceeded the NRB of £325,000
- In 2019/20 he will be liable to IHT at 20% on the amount that exceeds the NRB i.e. £75,000 x 20% = £15,000 IHT

Stamp Duty

- Stamp Duty Land Tax (SDLT) – extra 3% added to rates if property purchased is an additional residential property. Relief available for multiple purchases in linked transactions. No SDLT was liable on 1st £500,000 P/P on residential property from 8/7/20 – 31/3/21.

- Stamp Duty Reserve Tax (SDRT) @ 0.5% on electronic share purchases (rounded up or down to nearest penny)

- SDRT @ 0.5% on paper share purchases of more than £1,000 (rounded up to nearest £5)

SDLT Calculation 1

Joe sold his house and bought a new property to live in on 5th May 2023.

The purchase price was £350,000. How much stamp duty would Joe pay?

On the purchase price up to £250,000K	**£ 0**
£250,000 - £350,000 (£100,000) @ 5%	**£5,000**
TOTAL stamp duty	**£5,000**

SDLT Calculation 2

James bought his first home for £450,000 on 15th June **2023**. How much stamp duty will he have to pay on this?

On the purchase price up to **£425K** **£0**

425,000 to 450,000 (£25,000) @ 5% £1,250

TOTAL stamp duty £1,250

SDLT Calculation 3

John bought a holiday home for £560,000. How much stamp duty will he have to pay on this?

0 to £250,000 @ 3%	**£ 7,500**
£250k to £560k (£310,000) @ 8%	**£24,800**
TOTAL stamp duty	**£32,300**

VAT & Witholding Tax

Value added tax (VAT)

- Indirect tax
- Registration compulsory when annual TURNOVER exceeds **£85,000**
  - General rate 20%
  - Some goods zero rated / exempt, 5% on domestic heating

Witholding Tax

- Paid at source before income is received

Corporation Tax

- Payable on profits of limited companies / clubs / societies / associations e.g. trade or housing associations
- Profits = Trading profit less allowable expenses; capital gains; income from letting; interest on deposits
- Due 9 months after end of relevant accounting period for companies with profits up to £1.5M
- For companies with profits exceeding £1.5M corporation tax is due quarterly

State Benefits & HMRC Tax Credits

Social Security Benefits

Retirement

- Basic State Pension
- Additional State Pension
  - Graduated State Pension (1961 – 1975)
  - SERPS (1978 – 2002)
  - S2P (2002 – 2016)
- New State Pension
  - 66
  - 67 by 2028,
  - **68 between 2037 & 2039**

Unemployed or low income

- Universal credit
- Working Tax Credit
- Income Support
- Jobseeker’s Allowance
- Support for Mortgage Interest (SMI)

Social Security Benefits

Maternity and children

- Statutory Maternity Pay
- Maternity Allowance
- Child Benefit
- Child Tax Credit

Sickness or disability

- Statutory Sick Pay
- Employment & Support Allowance
- Attendance Allowance
- Disability Living Allowance & Personal Independence Payment
- Carer’s Allowance

TOPIC 6

Direct Investments: cash and fixed-interest securities

Main Asset classes

1. Cash deposits

2. Fixed interest securities

3. Equities

4. Property

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Cash

- Deposits
- Interest paid
- Different accounts – current / savings
- Most cash deposit account savings interest is paid gross.
- If deposit interest exceeds the personal savings allowance and the 0% starting rate of savings tax, individuals must inform HMRC and have the tax deducted via their tax code / pay via self-assessment

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Gilts

Tradable loans to government

Issued by the Debt Management Office

Short, medium, long, undated

Pay a fixed rate of interest – **coupon**

Par value paid back at **redemption date**

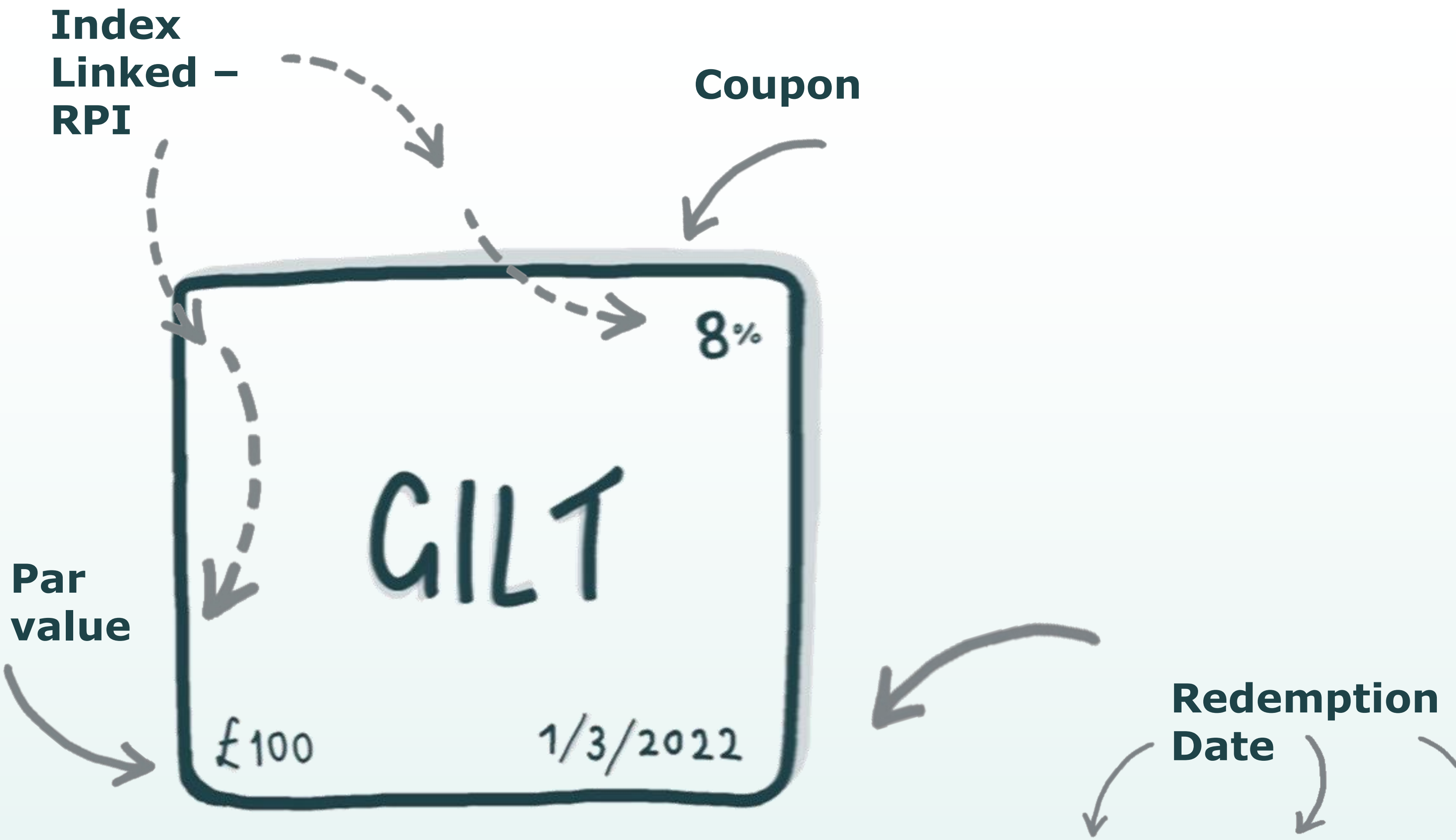
Interest paid gross and taxed as savings income

No CGT

Index linked - RPI

Cum/Ex-dividend

Running yield



Selling on = cum/ex-dividend

	Short	Medium	Long
Press	0-5	5-15	15+
D.M.O	0-7	7-15	15+

Local Authority / Corporate bonds & PIBS

- Tradable loans to **local authorities** / **commercial organisations**
- Fixed redemption date/value and interest
- **Higher risk** than gilts therefore **higher yields**
- Interest paid **gross**

- **PIBS** – Building Societies - Interest paid gross and taxed as savings income

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TOPIC 7

Other Direct Investments

Equities

- On ‘issue’, a way for firms to raise funds
- Secondary market on stock exchanges – LSE /AIM
- Have certain rights – voting and share of profits
- Income tax (**dividends**) and possible capital gains tax
- **Dividend allowance £1,000**
- **Ordinary shares** and **preference shares**
- **Warrants -** the right to buy ordinary shares at a fixed price on a future date
- Earnings per share, dividend cover, price earnings ratio
- Cum dividend and ex-dividend
- Rights issues / Scrip issues

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Property

Advantages

- Acceptable form of security for borrowing
- UK property market well developed
- Regular and increasing income stream & potential for capital growth
- Ease of access to ancillary services e.g. property management services

Disadvantages

- High investment cost e.g. purchase price / SDLT / legal fees
- Ongoing costs e.g. loan/mortgage, management & maintenance
- Illiquid investment
- Void periods
- Capital loss
- Legal fees to remove unsatisfactory tenants

Money Market Instruments

Treasury Bills – short term (normally 91 days) redeemable securities issued by DMO at less than par value. As such, no interest is paid but investors will receive more than they paid at the end of the term.

Certificates of Deposit – Issued by banks and building societies for normal terms of 3 or 6 months. They are receipts to confirm that a deposit (normally £50K+) has been made for a specified period at a fixed rate of interest.

Commercial Paper – A form of company borrowing from (mainly) large institutions over a period of 5 – 45 days. In exchange for funds they issue a commercial paper for more than the amount borrowed. This amount will be repaid at the end of the term.

Collective Investment schemes

Collective Investments

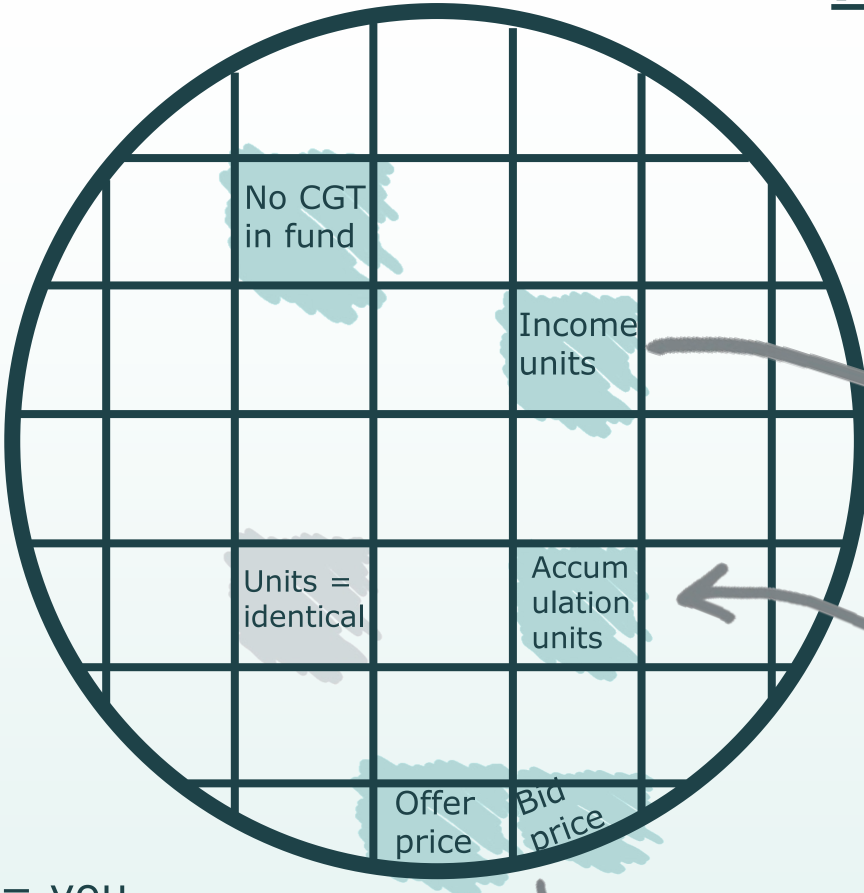
Main forms:

- Unit Trusts
- Investment Trusts
- OEICs
- Investment Bonds

Key Advantages:

- Investment Manager
- Diversification
- Reduced dealing costs
- Wide choice of funds

Unit Trust



Annual Management Charge

0.5 – 1.5%

Income out

Income stays in

= you purchase units

= you sell units

3→5% difference

Taxation

60% Assets interest bearing = interest

<60% Assets interest bearing = dividends

CGT liable on disposal

Unit trusts

- Open ended
- Unit price directly linked to fund value
- Bid / offer price (3-5%) covers Initial Charge
- Cancellation price
- Annual management charge 0.5 – 1.5%
- Distribution/Income or accumulation units
- Role of trustee
- Funds exempt from tax on gains
- Investors taxed per the underlying assets of the fund. Interest if min 60% of assets are in interest bearing assets e.g. gilts and corporate bonds / Equity if not.
- Dividends received as taxed as per normal share dividends / Interest received is paid gross
- Calculations – income (interest) and dividend (equities) tax.

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Unit trust – Taxation of dividends calculation

e.g. Stephen has earned income of £32,000 and receives a unit trust dividend of £12,450. He has his full personal allowance available to him.

How much tax will Stephen pay on his unit trust dividend?

Unit trust – Taxation of dividends - Answer

Income	£32,000
Less P/A	<u>£12,570</u>
Taxable	£19,430

Stephen still has £18,270 of his BRT band remaining which all of the £12,450 dividend falls within.

£1,000 @ 0% (D/A)	£0
£11,450 @ 8.75%	**£1,001.87**
TAX DUE	**£1,001.87**

Unit trust – Taxation of interest calc

Kirsty has earned income of £29,000 and receives interest from a fixed-interest unit trust of £17,000 in 2022/23.

How much tax will Kirsty pay on her unit trust interest?

Unit trust – Taxation of interest - Answer

Income	£29,000
Less P/A	£12,570
Taxable	£16,430

Kirsty still has £21,270 of her BRT band remaining which all of the £16,430 interest falls within.

£1,000 @ 0% (PSA)	£0
£16,430 @ 20%	£3,286
TAX DUE	**£3,286**

Investment trusts

- Closed ended investment companies
- Income through dividends
- Capital growth depends on demand for shares
- Net Asset Value (NAV) discount or premium
- Allowed to borrow (**gearing**)
- AMC = 0.5 – 1.5%
- Dealing fees added to any purchase and deducted from any sale
- May have limited life (split-capital trusts)
- No tax in fund on gains so investor may be liable on encashment
- Min 85% of income received must be distributed as dividends to shareholders - taxed as equities

OEICs

- Share characteristics with unit trusts and investment trusts
- Limited liability company with variable capital
- Issue shares in the company
- Independent Depositary
- Authorised Corporate Director
- Single priced
- Charges
    - initial = 3-5%
    - AMC = 0.5 – 1.5%
- Taxed as per unit trusts unless non-reporting fund based offshore

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Investment Bonds

- A single-premium, unit linked (i.e. collective investment), whole of life assurance policy
- If the life assured dies, the policy ceases and 101% of the bid value on the date of death is paid out
- Fund is subject to CGT at 20%
- For policy proceeds:
  - BRT – no further tax
  - HRT – further 20%
  - ART – further 25%
- Normally no income provided by way of dividends / distributions, however, 5% of initial investment can be withdrawn p/a without any IMMEDIATE tax liability

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Tax Wrappers

Tax Wrappers

The investment products we have looked at can be held within different tax wrappers. These are mainly:

- ISAs
- CTFs and Junior ISAs
- Venture Capital Trusts (VCTs)
- Enterprise Investment Schemes (EIS)

ISA

Main types:

- Cash (min age 16)
- Stocks and Shares (min age 18)
- Innovative Finance (min age 18)

Limit:

- **2023/24** = £20,000 combined
- Additional Permitted Subscriptions - applies when spouse/civil partner dies
- Right to make APS applies for LATER of 3 years from date of death / 180 days after administration of estate is complete. Just the 180 day rule for S&S ISAs.

- No income tax or CGT payable

Child Trust Funds and Junior ISAs

CTF

- **No longer available**
- CTF accounts were (deposit / share based / stakeholder) types
- Account remains in force until child reaches age 18 (child can manage account from age 16)
- Can be converted to Junior ISA

Junior ISA **(2023/2024 Max. annual** contribution £9,000)

- Stocks and Shares / Cash JISA available from 1/11/11 for children without a CTF
- Account remains in force until child reaches age 18 (child can manage account from age 16)
- **At age 18 the JISA becomes a conventional ISA**

Venture Capital Trusts (VCTs)

- Type of collective investment
- Must meet approval conditions and be approved by HMRC
- Purchase shares in the VCT on the stock exchange
- Run by investment manager
- Spreads money raised from investors across a range of different companies
- High risk
- No CGT
- 30% income tax relief on investments of up to £200,000 p/a
- Dividends from the £200,000 investment are paid tax free

Enterprise Investment Schemes (EIS)

- Involves direct investment in a company that is eligible for the EIS
- High risk
- No CGT on gains
- 30% income tax relief on investments of up to £1,000,000 p/a

Pensions

Pensions

- Contribution limits **2023/24**
  - **Annual £60,000 (reduced to a minimum of £10,000** if annual income is more than £260,000)
    - e.g. Cary's earned **£266,000 in 2023/24**
    - Her pension annual allowance would be reduced by:
    - £266,000 – **£260,000 = £6,000 / 2 = £3,000**
    - So she would have a pension annual allowance of:
    - **£60,000 - £3,000 = £57,000**
  - Lifetime £1,073,100
    - Excess taxed at 55% if taken as lump sum / 25% if taken as income
- Tax relief
- Carry forward – unused annual from the previous 3 tax years

Pensions

- Money Purchase Annual Allowance - £10,000
- Age to draw benefits
- Defined Benefit Schemes
- Defined Contribution Schemes
- AVCs / PPPs and FSAVCs

Pensions

- Workplace Pensions
- Stakeholder pensions
- How can benefits be taken?
  - Scheme pension & up to PCLS (D B schemes)
  - Up to 25% tax free
  - Annuity purchase
  - Flexi-access drawdown
  - Uncrystallised Funds Pension Lump Sum (UFPLS)

Life Assurance

Term assurance

- Level term
- Decreasing term (gift inter-vivos)
- Increasing term
- Convertible term
- Renewable term
- Family "income" benefit

Whole-of-life assurance

Single / joint life

Joint life 2nd death

Life of Another

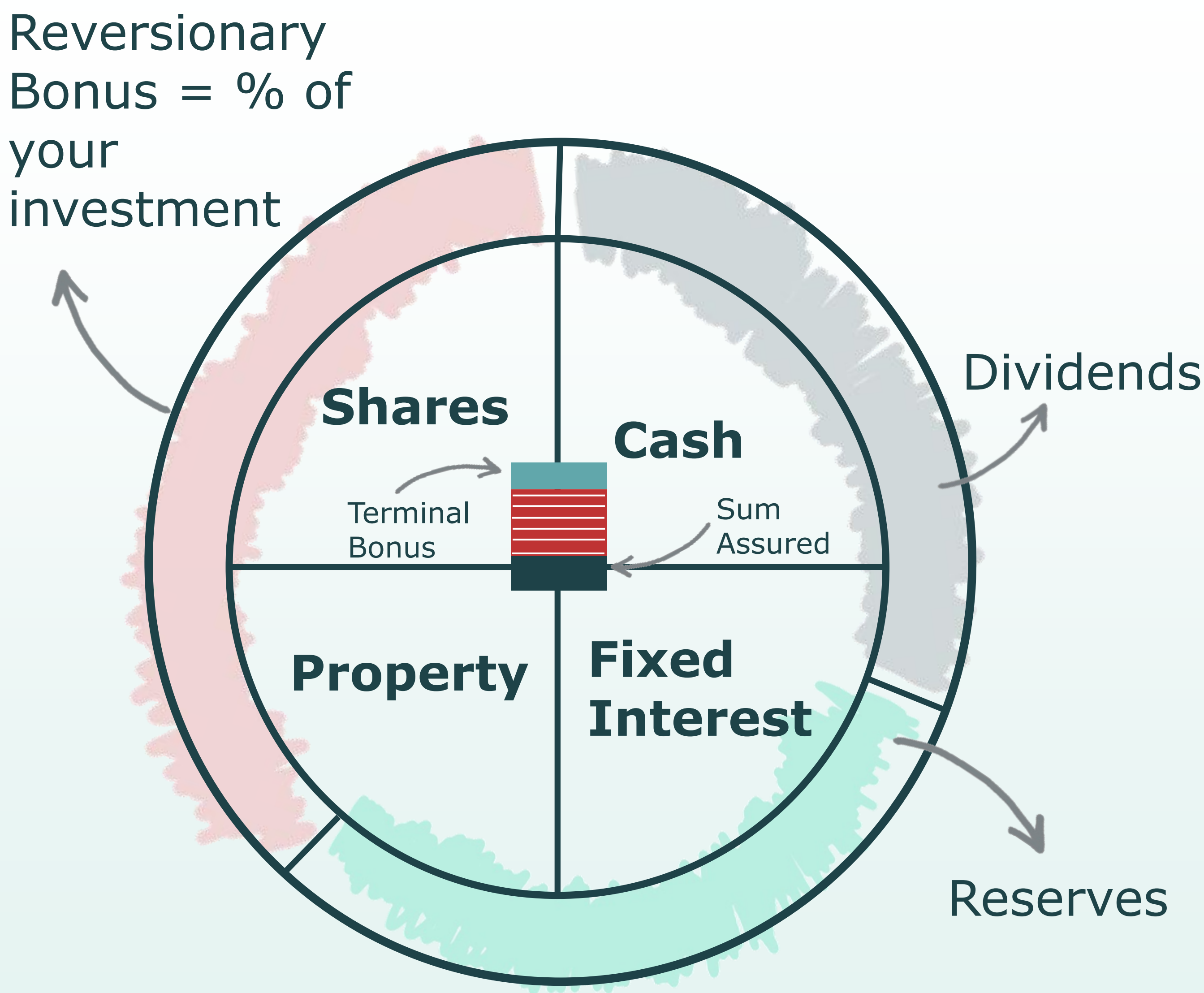
Types:

- Non profit / with profit / unitised with profit
- Unit linked
- Low cost
- Flexible whole of life
- Universal whole of life

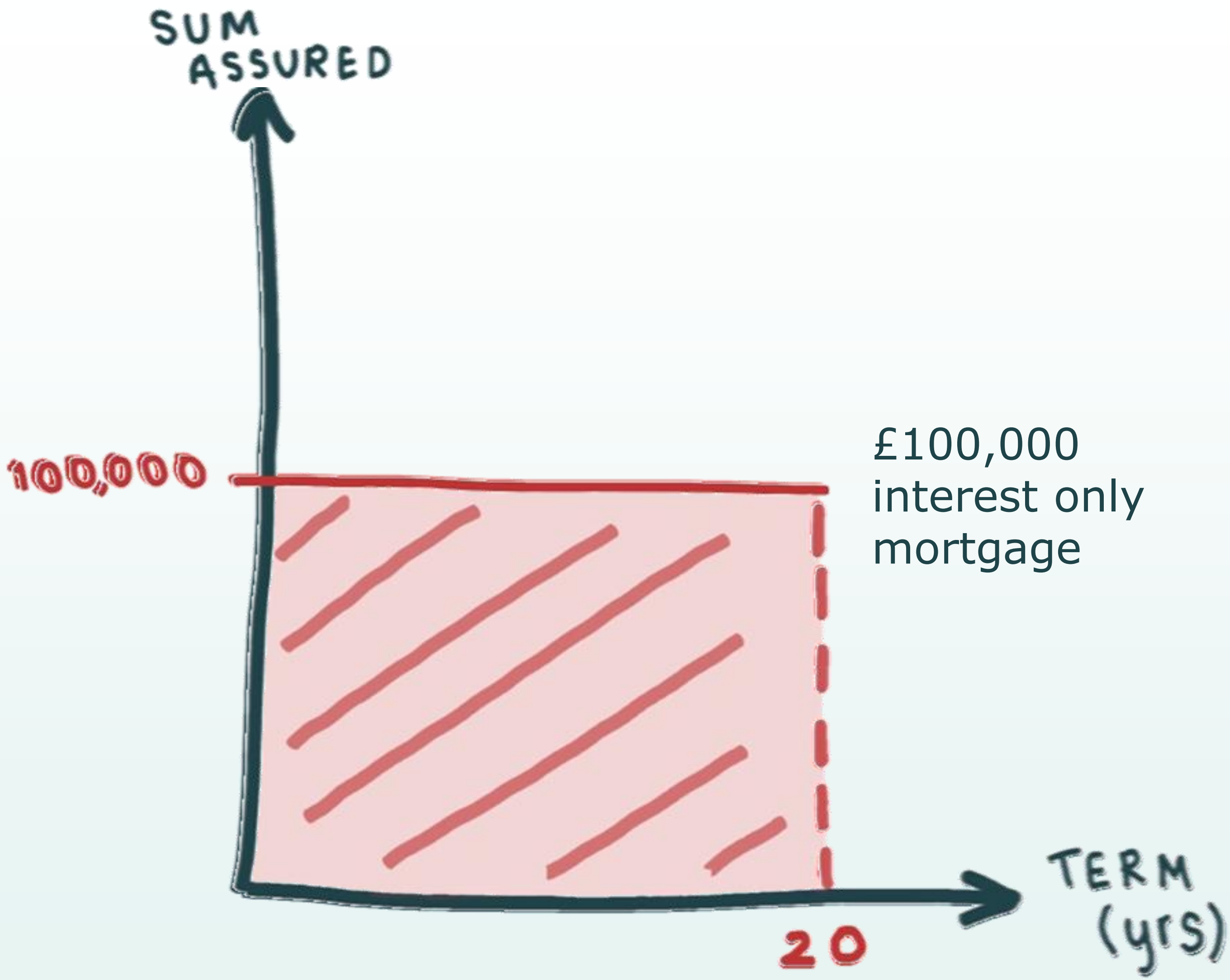
Endowment Policies

- Non-profit
- Full with –profit
- Low-cost with-profit
- Unit-linked
- Unitised with-profit

With Profit Fund

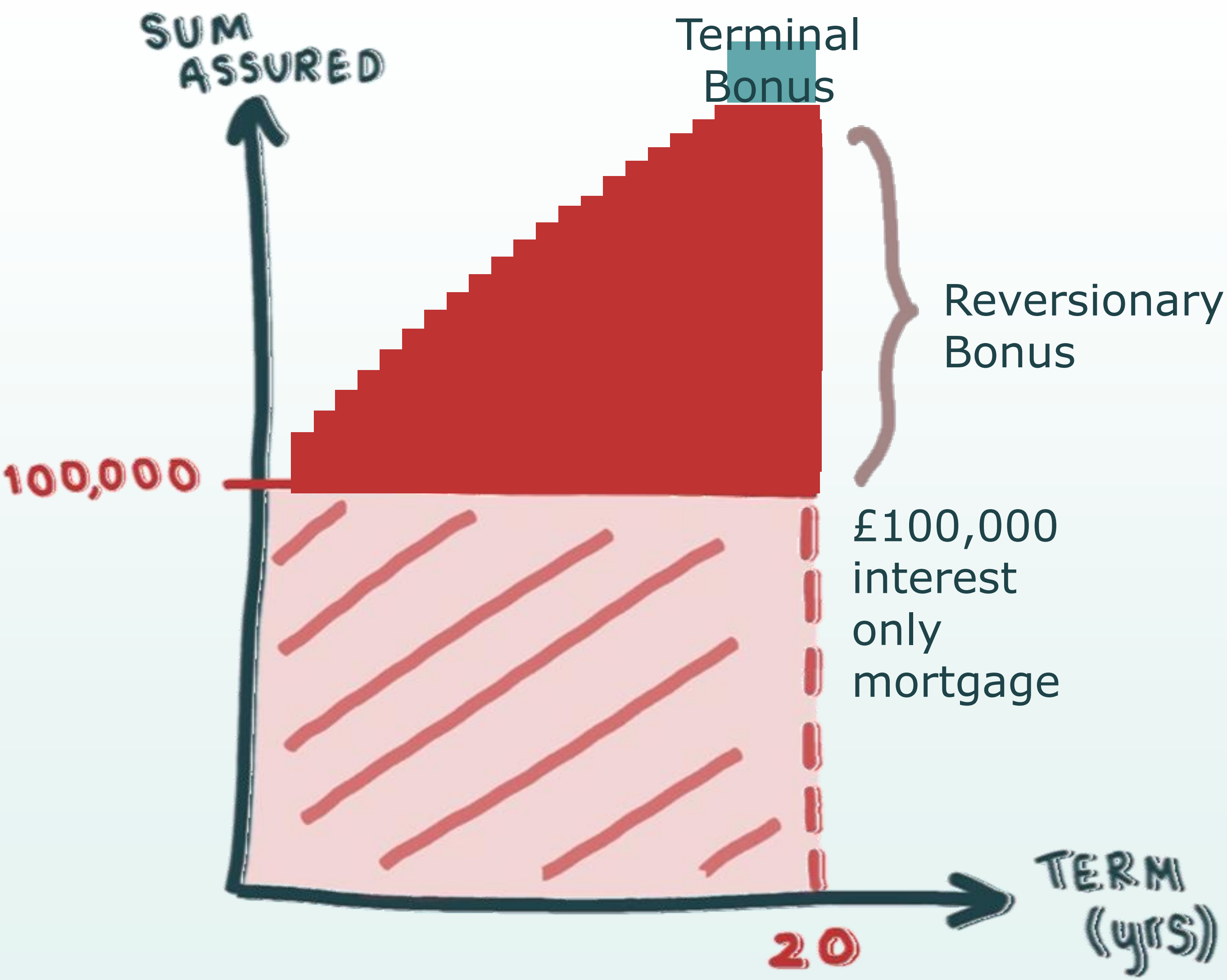


Non-Profit Endowment

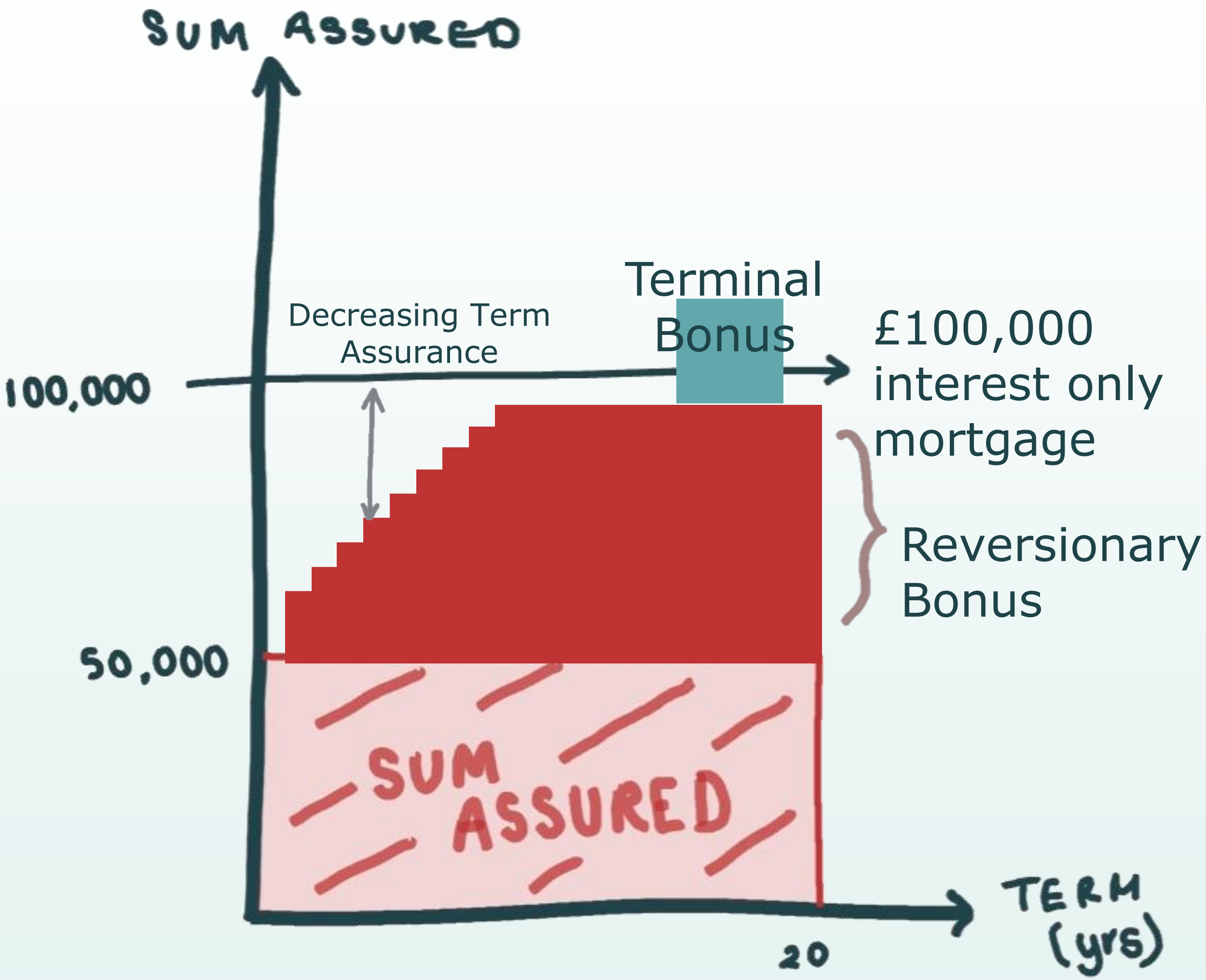


£100,000 interest only mortgage

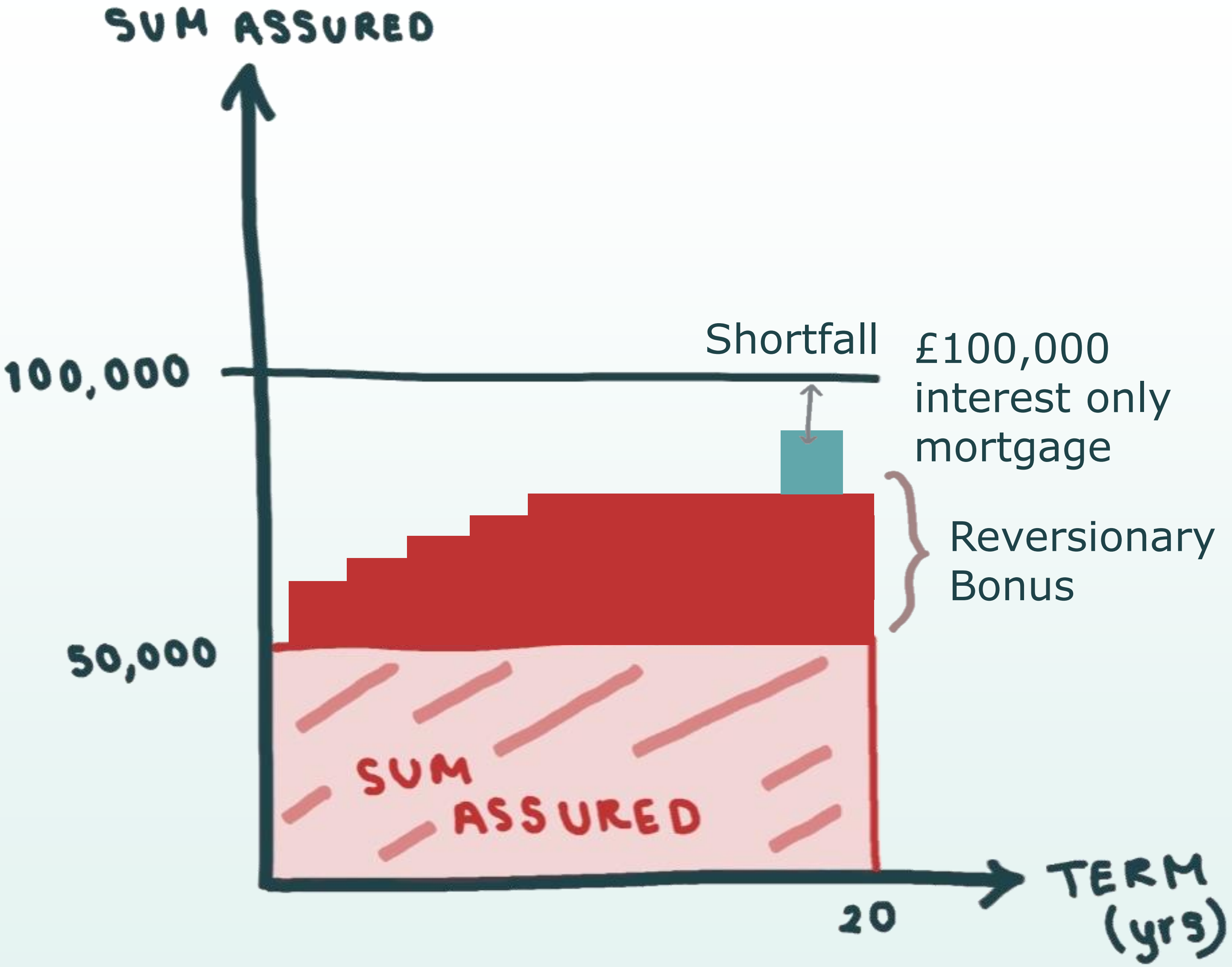
Full With-Profit Endowment



Low-cost with Profit Endowment



Low Cost With Profit Endowment



Unit Linked Endowment

£100,000 interest only mortgage

Health and General Insurance

Ill health insurance

Critical Illness Cover (CIC)

- tax-free **lump sum** on diagnosis of specific illnesses
- **ABI state it must cover cancer, heart attack and stroke**

Income Protection Insurance (IPI)

- pays an **income** (normally max 50-75% of pre-disability income) when the insured is unable to work through illness or accident

- Premiums may be guaranteed / reviewable / renewable
  - **higher premiums** for: risky occupations; older people; cover required; deferred period; current + past health
  - **permanent** in sense that insurer cannot cancel cover due to numerous claims
- may be index-linked
  - **individual** policies – income paid **tax-free**
  - group policies **taxed as earned income** (employer gets tax relief)

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Ill health insurance

Accident, sickness and unemployment

- **short-term** income replacement (usually **2 years** max) covering accident, sickness or **redundancy**
- typically covers mortgage repayments
- also pays lump sum on certain events (e.g.. loss of limb)
- **tax-free** benefits

- Reviewable annually at the discretion of the insurer

Private medical insurance

- provides private medical cover quicker and with greater choice than NHS cover
- existing conditions likely to be excluded
- subject to **IPT** but benefits **tax-free**

- Factors affecting the cost – location, type of hospital, standard of accommodation

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Ill health insurance

Long term care insurance

- if set up via an **immediate needs annuity** then benefits are tax-free and paid directly to care provider
- can also be paid for with income from ordinary purchased life annuity but will not be paid tax free

- a **deferred needs plan** is another option.
- It is an investment designed to build up funds that can be drawn upon to pay for care needs as and when required.
- Benefits paid tax free when the insured is unable to carry out a number of **activities of daily living** (ADLs)

General insurance

- Buildings insurance
- Contents insurance
- All risks insurance
- Motor
  - 3rd party; 3rd party, fire and theft; comp
- Travel insurance
- Payment Protection Insurance
- Insurance premium tax

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General insurance - Principle of Averaging

$$\left[\frac{\text{Amount you are insured for}}{\text{Amount you should be insured for}}\right] \times \text{CLAIM}$$

e.g. Martin was insured for £20,000 but should have been insured for £25,000. He made a claim for £10,000 and his excess is £500. What will he receive?

(£20,000 / £25,000) x £10,000 = £8,000 - £500 (excess)

= £7,500 insurance payout

TOPIC 13

Secured and Unsecured Lending

Unsecured Lending

- Personal loans
- Overdrafts
- Credit Cards - Revolving Credit

Secured lending - Mortgages

- Mortgagor / Mortgagee
- Repayment / Interest only (repayment vehicles – Endowment / Pension / ISA)
- Interest rate options – variable / discounted / fixed / capped /BRT / low start / deferred interest
- Flexible / Offset mortgages
- Cashback
- Shared ownership
- Equity release – Lifetime mortgage / Home reversion plan

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Lifetime Mortgage

Sold

Fixed Rate Interest Only Mortgage. Maximum 55% of property value dependent on age.

Mortgage and Interest repaid

e.g. Age 60 = Max. 25% so £100,000

Remainder = estate

Lump Sum Tax Free

Income

Draw Down

Make no repayments to lender whilst alive

Interest rolls up and is added to outstanding capital

If interest = 7% it would double your debt in 10 years

On death/move to residential care home

Home Reversion Plan

Sold

Sell all or part of house at discount to Reversion Company

The younger you are the bigger the discount, e.g. Age 65 = 50%

Receive lump sum tax free

Remain in house for life/ until move to permanent residential care

Pay £1plm/£12pla "Rent" to reversion company

On death/move into care

Reversion Co. to keep their % of the sale proceeds

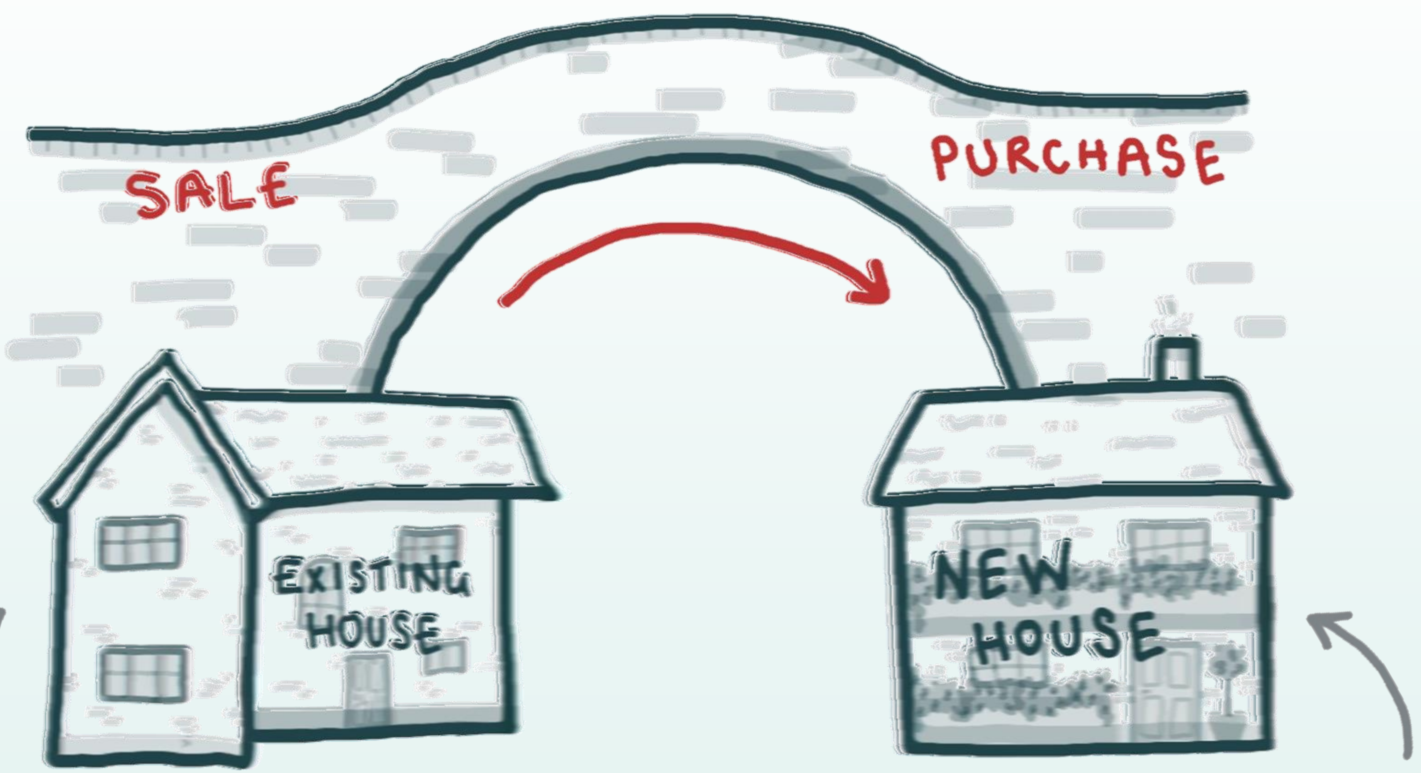
Remainder = estate

Second Charges/Second Mortgages

1st Charge
= Main Mortgage
Provider

2nd Charge
= Secured Loan
1/3/18

Bridging Finance



Sale not completed yet

Due to complete next week

Understanding and Satisfying Customer Needs

Financial lifecycle

- Children
- Students (16-20)
- Young adults in employment (20-30)
- Young families (30-40)
- Established families (40-50)
- Mature households (50-60)
- Retirement (60+)

Financial advice process

- Identify and agree needs and objectives
- Agree order of priority
- Recommend solutions
  - put the **right amount of money**
  - in the **right form**
  - in the **right hands**
  - at the **right time**
- Areas to consider: state benefits / existing arrangements / affordability / taxation / risk / timescale / flexibility
- Ensure the solution is implemented
  - present the recommendation
  - handle objections and obtain commitment
  - Documentation, after-sales care & servicing

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Fact-find information

Made up of Hard and Soft facts

Personal and family details

- name and address; date/place of birth; marital status; family details and dependants

Financial situation

- employment details; income and expenditure; assets and liabilities

Plans, needs and objectives

- client preferences, attitudes (inc. attitude to risk), capacity for loss, willingness to take action

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Common issues include …

- Inadequate life cover (e.g.. rely on mortgage cover)
- All investments in a deposit account
- Ineffective spread of investments within a married couple
- Non-taxpayers in investments where tax cannot be reclaimed
- Lack of pension provision
- Failure to make a valid will

The Main Advice Areas

Main areas of financial advice

- Budgeting
- Protection
- Borrowing & debt
- Saving & investment
- Retirement
- Estate planning
- Tax planning

Budgeting

Having sufficient funds to purchase necessities.

Planning for other purchases

Planning for emergencies

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Protection

- Family protection
  - against death
  - against sickness or disability or unemployment
- Business protection
  - death or sickness of a key employee or business partner
  - automatic accrual, buy and sell, cross-option
- Self-employed protection

Borrowing and debt

- Avoiding unnecessary debt
- Keeping repayments to a minimum
  - balancing cheapness and flexibility
- Using the most appropriate form of borrowing
  - mortgages, credit card, further advance, unsecured loan etc.

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Saving and investment

- Purpose – income or capital growth?
- Regular saving or lump sum
- Attitude to risk
- Accessibility
- Taxation
- Effects of inflation

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Retirement planning

- State pension benefits insufficient to meet most people's aims for retirement
- Occupational pensions important supplement
- People may need to make alternative arrangements
  - tax advantageous pension provision
  - alternative provision

Estate Planning

Inheritance tax levied at 40% on estates over £325,000

Estate planning options
- minimise the size of the estate
- insurance provision to pay the IHT bill

Tax planning

Tax is **always a consideration** in advice, but **never the main** reason for a recommendation

Consider tax efficient products/schemes

Consider reallocating assets between a couple to minimise tax bill

Key Legal Concepts

Law of contract

Requirements for a binding contract:

- offer and acceptance
- consideration
- capacity to contract
- terms must be certain, complete and free from doubt
- must be for a legal purpose / object must be legal
- must have entered into the contract freely i.e. not have been entered into due to misrepresentation or duress
- must be an intention to create a legal relationship

Consumer Insurance (Disclosure & Representations) Act 2012

- It is the duty of consumers to take **reasonable care** not to make a misrepresentation to the insurer.

Law of Agency

- Agent
- Principal
- Apparent authority
- Ratification

Power of attorney

Donor and donee (or attorney)

Power of attorney ceases if a person becomes mentally incapacitated

Lasting powers of attorney (LPA) are made whilst a person is mentally well and come into operation when they are incapacitated – 2 types

- Health and welfare
- Property and Financial Affairs

LPAs registered with the **Office of the Public Guardian**

If mental incapacity occurs and there is no LPA in place – the **Court of Protection** will appoint a deputy

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Wills

If valid will then **executors** of the will obtain a **'grant of probate'**

To be valid a will must be:

- in writing by someone 18 or over
- Properly executed

- It also must be signed by the testator in the presence of two witnesses. Witnesses **cannot** be beneficiaries (or their spouses)
- It will automatically be revoked on (re)marriage / civil partnership - unless 'written in contemplation of (re)marriage'
- It can be modified at any time – recorded in a **codicil** document
- **Deed of variation** can be completed by beneficiaries, to alter terms of will after testator's death

Intestacy

If there is no valid will then the person dies intestate

The **administrator** of the deceased persons estate must:

- obtain a **'grant of letters of administration'**
- administer the estate as per the rules of intestacy

Intestacy rules

- **If leave both spouse and children** - spouse gets personal chattels, the first £270K plus half the balance outright. Children immediately get the other half of the balance in equal measure
- **If leave spouse and no children** - spouse gets everything
- **If leave children and no spouse -** children get everything in equal measure.
- **Neither spouse nor children** - nearest living relative otherwise Crown

Trusts

- Trust Deed

Document that sets out how the trust is to be managed, by whom and for whose benefit.

- Settlor

Person who creates the trust and who originally owned the asset(s) held within it.

- Trustee(s)

Person(s) named in the trust deed who have legal responsibility of the trust property and must distribute the trust property as per the deed.

- Beneficiary(ies)

People or organisations who will benefit from the trust property.

Insolvency and bankruptcy

Insolvency means:

- person's liabilities exceed assets or
- cannot meet liabilities within reasonable time

Bankruptcy:

- is where insolvency is formalised by a **county court**
- can be for debts of **£5,000**
- order remains in force for **12 months** during which time person is an undischarged bankrupt
- official receiver appointed by court to identify and distribute assets and investigate reasons for the bankruptcy

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IVAs & CVAs

Individual voluntary arrangements (IVAs):

- Insolvency practitioner arranges for debts to be rescheduled
- must gain agreement of creditors owed at least **75%** of debt

Company Voluntary Arrangements (CVAs):

- Company equivalent to an IVA
- Can proposed by Directors or appointed liquidator
- Creditors representing **75%** of the company's debt must agree
- Aim is to avoid the company going into administration

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CeMAP One

UNIT 2

TOPIC 17

The FCA’s aims and activities

UK regulatory structure

- The FSA ceased to exist in 2014 with much of its responsibility passing back to the **Bank of England (BOE)** who are now responsible for protecting and enhancing financial stability.
- The **Financial Policy Committee (FPC)** – a committee of the BOE who look at the economy in more broad terms to identify and address risks that may threaten the stability of the economy.
- The **Prudential Regulatory Authority (PRA)** – a subsidiary of the BOE who have responsibility for the day-to-day prudential supervision of banks and other financial institutions.
- The **Financial Conduct Authority (FCA)** - has responsibility for the conduct of all retail and wholesale financial firms as well as prudential regulation of firms not regulated by the PRA.

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UK Regulation Structure

Bank of England

Prudential Regulation Committee (PRC)

Financial Policy Committee (FPC)

Monetary Policy Committee (MPC)

BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY

FCA FINANCIAL CONDUCT AUTHORITY

Sets interest rates

Prudential regulation
significant firms, deposit takers, insurance and inv firms

Conduct or Prudential & Conduct regulation
Investment firms, exchanges and other financial providers

PRA objectives

1. Promote the safety and soundness of the firms it regulates.

2. Secure an appropriate degree of protection for insurance policyholders.

3. Facilitate effective competition.

FCA operational objectives

1. Protect and enhance the integrity of the UK financial system

2. Securing an appropriate level of protection for customers

3. Promote effective competition in the interest of the consumer

Role of the FCA

- Setting standards
- Developing rules and regulations
- Supervising their implementation
- Authorises firms
- Approves individuals
- Enforces discipline
- Provides training and guidance
- Financial Services Compensation Scheme (FSCS) /Financial Ombudsman Service (FOS).

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Powers of the FCA

- Competition powers – to open up competition, carry out market studies and make referrals to the Competition and Markets Authority (CMA)

- Product Intervention Powers – to ban or restrict financial products.

- Power of Disclosure – to publish details of warning notices issued and disciplinary action taken.

- Power to take formal action – against misleading financial promotions.

FCA Handbook

- Made up of Rules & Guidance
- High level standards – apply to all firms and authorised individuals
- Prudential standards – deal with financial soundness and management
- Business standards – COBS / Market conduct / Client assets
- Regulatory processes – inc. rules and guidance for firms looking to seek authorisation
- Redress – complaints and compensation
- Specialist sourcebooks – inc. arrangements for credit unions, solicitors and accountants and collective investments

Principles for business

1. Integrity
2. Skill, care and diligence
3. Management and control
4. Financial prudence
5. Market conduct
6. Customers' interests – fair treatment of customers

Principles for business (cont.)

7. Communications should be clear, fair and not misleading
8. Conflicts of interest
9. Customers: relationships of trust
10. Protect clients assets
11. Regulations - be open and co-operative with the regulator
12. **<u>Consumer Duty</u>**

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Fair treatment of customers – the 6 outcomes

1. Consumers can be confident that they are dealing with firms where the fair treatment of customers

2. Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly

3. Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale

Fair treatment of customers – the 6 outcomes

4. Where consumers receive advice, the advice is suitable and takes account of their circumstances

5. Consumers are provided with products that perform as firms have led them to expect, and the associated service is both of an acceptable standard and as they have been led to expect

6. Consumers do not face unreasonable post-sale barriers imposed by firms to change product, switch provider, submit a claim or make a complaint

Regulating Firms & Individuals

Regulated Activities

- Accepting deposits
- Effecting/carrying out insurance contracts
- Dealing/arranging deals in investments
- Managing investments
- Setting up/operating collective investments
- Establishing stakeholder pensions
- Advising on investments
- Mortgage lending, admin, advising, arranging
- Advising and arranging general insurance
- Entering into or exercising rights under a regulated consumer credit agreement

Regulated investments

- Deposits
- Electronic money
- Insurance contracts (inc. funeral plans)
- Shares, corporate bonds, warrants
- Gilts and local authority stock
- Units in collective investments
- Stakeholder pensions
- Options and futures
- Mortgage contracts

Senior Managers & Certification Regime (SMCR)

- Replaced Approved Persons Regime
- Introduced 7th March 2016 for Banks, building societies and credit unions (had until 7/3/17 to certify existing staff)
- FCA extended the SMCR regime to FCA solo-regulated financial services firms from 9 December 2019.

Senior Managers Certification Regime

3 tiers under the SMCR:

- **Core regime** – firms in this tier will have to comply with the baseline requirements. It applies to the majority of firms, and will consist of three key elements:
  - The Senior Managers Regime (SMR).
  - Certification Regime (CR).
  - Code of Conduct.

- **Enhanced** – only the firms representing the greatest risk to consumers or markets will be classed as enhanced firms. These firms will have additional requirements.

- **Limited scope** – this will apply to firms that are already exempt under the approved persons regime. They will be exempt from some baseline requirements and will generally have fewer senior management functions.

Senior Managers Regime (SMR)

- Focuses on individuals in key roles in relevant firms
- FCA list a number of senior management functions for **core** firms i.e. functions they feel pose the greatest risk to either customers or market integrity if the person conducting them is not fit to do so
- FCA also list prescribed responsibilities which must be allocated amongst the senior managers of a business
- Firms must ensure the ongoing fitness and propriety of their senior managers.
- If an individual applies for a senior management role or moves to a different senior manager role that is materially different from their current one:
    - they must be pre-approved by the regulator and
    - their application must be accompanied by a 'statement of responsibilities'

Senior Managers Regime (SMR)

- Enhanced firms have two additional requirements:
  - Maintain a responsibilities map – details the way responsibilities are allocated between the senior management. Helps FCA identify who in senior management is responsible should things go wrong
  - Ensure that each activity, business area and management function is allocated a senior manager with overall responsibility
- Penalties – maximum **7 years in prison &/or unlimited fine** for senior manager whose action or inaction has led their business to fail, through 'reckless misconduct'.

Certification Regime (CR)

- The FCA have defined a number of 'significant harm' functions e.g mortgage advisers, financial advisers, investment managers……
- Individuals carrying out one of these functions are not required to secure direct approval from FCA but **THE FIRM** must certify their fitness and propriety to carry out their role.
- No employee should carry out a role requiring certification until assessed as **fit and proper** to do so.
- Their continued fitness and propriety should be assessed **at least annually**.

Code of Conduct

- The FCA make rules of conduct that apply to senior managers, certified persons and other employees.
- These rules set expectations about standards of behaviour for those employed in firms covered by the Senior Managers Regime.
- Firms must:
  - make individuals who are subject to the rules aware that this is the case, and provide training on how the rules apply to them
  - take effective action where staff fall below required standards
- Reporting
  - The FCA requires firms to report to it within **7 days** if they take disciplinary action against a senior manager as a result of a breach of one or more rules of conduct.
  - All other staff = **annual** report

Responsibilities of Senior Managers

- Take responsibility for a firm's compliance with FCA regulations
- Produce relevant management information to demonstrate that their advisers give quality advice and Treat Customers Fairly in 3 particular ways:
    1. Firm embodies a compliance culture with senior management using MI to drive forward their fair treatment of customers and the quality of their advice process
    2. All staff have clearly defined responsibilities and are monitored appropriately
    3. Monitoring and compliance procedures are regularly reviewed and updated

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Proportionate supervision

- FCA seeks to identify risks to it meeting its statutory objectives

- It assesses the risk firms present based on:
  - the potential impact on the FCA's objectives

- Fixed and flexible portfolio

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FINANCIAL CONDUCT AUTHORITY

3 Pillars:
Prudential supervision:

P1 Proactive	P2 Event Driven	P3 Issues & Products
Pre-emptive identification of harm through review and assessment of firms and portfolios: this includes business model analysis and reviewing the drivers of culture	Dealing with issues that are emerging or have happened to prevent harm growing	Wider diagnostic or remedy work where there is actual or potential harm across a number of firms

Enforcement

- Variation of a firm’s permissions
- Withdrawal of approval
- Injunction
- Restitution
- Redress
- Disciplinary action - Private warning, public censure, fine
- Disclosure
- Enhanced supervision

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TOPIC 19

Prudential Supervision

Capital adequacy requirements

Ensuring firms finances are prudently managed

Banks

- min solvency ratio 10.5% of risk weighted assets by 2019

- Additional requirements for the 30 banks identified globally as being 'too big to fail'

- From 1 January 2019, the minimum **Total Loss Absorbing Capacity (TLAC)** requirement for G-Sibs will be at least 16% of the resolution group's risk-weighted assets, increasing to at least 18% from 1 January 2022.
- TLAC will be formally implemented in 2019

Investment companies

- varies from min. €50K - €125K - €730K depending on type of dealer

Life assurance companies

- The solvency capital requirement is set at a level to ensure that insurers and reinsurers can meet their obligations to policy holders and beneficiaries

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Conduct of Business Requirements (1)

Types of client

- Retail client
- Professional client
  - De facto or elective
- Eligible counterparty

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Status of financial advisers

- **Independent Adviser**
  can call themselves independent if they offer recommendations which are 'unrestricted and unbiased' and consider a sufficient range of products which are sufficiently diverse in terms of both type and provider to suitable meet a client's objectives.

- **Restricted Adviser**
  - **does not fulfil independent requirements OR generally focuses on a limited selection of products or providers**
  - **basic advice e.g. stakeholder products**

- Execution only

- Basic advice

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Advertising & financial promotions

- “invitation or inducement to engage in an investment activity”
- Communicated only when prepared or approved by an authorised person
- Real time/Non-real time
- Unsolicited promotions
- Principle: fair, clear and not misleading:
  - - accurate
  - - understandable by the ‘average’ person it is aimed at
  - - not obscure important phrases or warnings
  - - contain the name of the FCA for direct offer advertisements

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Disclosure documents

On **first meeting** a customer and **before** any business is discussed, the adviser will issue an initial disclosure document which contains:

- Firms name and contact information
- How to communicate with the firm
- Authorisation details
- Advice type
- Investment management
- If they are authorised to hold client money
- Charging Structure & charges payable
- Details of FOS & FSCS

May also be a Client Agreement for investment clients

- Often discretionary management
- Not usual for packaged products

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Suitability requirements

Can't give advice until fully identified client's relevant financial and personal circumstances – fact find

Take all reasonable steps to ensure the client understands product risks
- base this on the client's knowledge and experience
- identify risk profile & capacity for loss

Suitability report

- Explains why a product was recommended and how it matched customer needs – most suitable
- Identifies potential disadvantages
- Written in plain English
- Suitability reports required for:

  - life policies
  - pensions policies
  - unit trusts, OEICs, investment trusts
  - pension transfers and opt-outs

Suitability report

- Timings:
  - For **investment advice / life policies** = suitability report issued before the transaction is concluded
  - If **life policy is sold over the telephone** = suitability report must be provided immediately after the conclusion of the life policy
  - **Personal pension or stakeholder pension**, where cancellation rights apply = the report must be sent no later than the 14th day after the contract is concluded
  - **All other cases** = report should be provided when or as soon as possible after the transaction is effected or executed

Product disclosure

- Key Features Document
- For packaged products e.g. life/pension policies, Unit Trusts and Investment Trusts
- Must be issued **before the sale completed**
- Produced by provider but given by adviser
- Document contents:
    - product aims
    - how it works
    - key terms of contract
    - material risks involved
    - complaint handling procedures
    - compensation available from FSCS
    - right to withdraw / cancel inc. terms and conditions for this

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Key Information Documents (KID)

- From 1/1/18 must be provided if customer is buying a product where the amount repayable can be affected by market fluctuations

- Document must be no longer that 3 sides of A4 and language used must be plain, concise and easy to understand.

- Document contents:
  - Product and provider names
  - Main features
  - Any possible risks
  - Any return that could be gained by investing
  - Costs & charges
  - Details of complaints procedure

Cooling off, cancellation & reflective periods

- Statutory cancellation notice
  - reminds client of cancellation rights
  - starts from when the client received the notice

Product	Timescale
Life and pension policies, contracts of insurance that either are or have elements of pure protection contract or payment protection.	30 days
Investments, deposits, other insurances	14 days
Binding mortgage offers	7 day reflection period

- Can withdraw during that time without commitment or loss
  - exception of a lump sum unit-linked investment where the value has fallen
  - would not suffer bid/offer spread though

TOPIC 21

Conduct of Business Requirements (2)

Regulation of mortgages

MCOB covers loans taken out which are subject to

1st/2nd charge secured on the borrower's property or are deemed 'consumer buy to let' (CBTL)

- must be in the EEA and either residential (40% family occupation) or CBTL
- must be to an individual/trustee
- must have completed on/after 31/10/2004

- Covers home improvements, debt consolidation; and equity release i.e. lifetime mortgages and home reversion plans.

Covers: lending; administration; arranging and advice

Only 2 levels of service can be provided: either Advice or Execution Only

Lenders must be authorised by the FCA and PRA

Does NOT Cover:

Business buy to let, corporate lending or lending overseas

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Mortgage Market Review

- April 2014
- Income verification - no non-status loans
- Lender to demonstrate affordability (on a repayment basis)
- For interest only mortgages, the lender must be satisfied that there is a clear and credible source of capital repayment in place.
- And "stress test" applications
- Right To Buy customers to receive advice
- Lenders to adhere to a "responsible" lending policy
- All interactive sales treated as "advised sales"
- Limitation of costs charged to those in arrears

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Regulation of general insurance

- Insurance Conduct Of Business - covers the sale of non-investment insurance to retail and commercial customers e.g. general insurance, protection, LTC, income protection & critical illness.
- Rules applicable to intermediaries who sell, administer or advise on general insurance are contained in ICOBs.
- **Firm** must provide consumer with information below before the conclusion of an initial contract of insurance and, if necessary, on its amendment or renewal:
    - its identity, address and whether it is an insurance intermediary or an insurance undertaking
    - whether it provides a personal recommendation about the insurance products offered
    - the procedures for making complaints to the firm and the FOS or, if the FOS does not apply, information about the out-of-court complaint and redress procedures available for the settlement of disputes.

Regulation of general insurance

- An **insurance intermediary** must also provide the customer with the following information:
    - the fact that it is included in the FCA Register and the means for verifying this
    - whether it has a direct or indirect holding representing 10 per cent or more of the voting rights or capital in a given insurance undertaking (that is not a pure reinsurer)
    - whether a given insurance undertaking (that is not a pure reinsurer) or its parent undertaking has a direct or indirect holding representing 10 per cent or more of the voting rights or capital in the firm
    - whether it is representing the customer or is acting for and on behalf of the insurer.

Regulation of general insurance

Product disclosure

Customer must be given an **Insurance Product Information Document** (IPID) outlining main features and significant limitations/exclusions.

Intermediary must provide product info to customer but the IPID is drawn up by the manufacturer of the policy.

A firm should provide evidence of cover promptly after the inception of a policy.

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Regulation of general insurance

Cancellation

General insurance = 14 days

Pure protection or payment protection = 30 days

Insurer can deduct reasonable and genuinely incurred costs (but cannot turn a profit)

On receipt of cancellation notice, all premiums paid must be returned within **30 days** and the contract is terminated

NO right to cancel for:

- travel policies of < 1 mth
- completed policies
- general ins sold by an unauthorised intermediary
- pure protection policies of < 6 mths
- pure protection policies from an occupational pension scheme for the benefit of employees
- a connected contract which is not a distance contract

TOPIC 22

Consumer Credit

Consumer credit

Consumer Credit Act 2006

Regulates **all** loans unless exempt (i.e. Regulated mortgages and further advances / High Net Worth borrowers)

Main provisions:

- licensing of lenders and no misleading marketing
- copy of loan agreement and cooling off period
- credit reference agency disclosure requirement
- definition of APR* (and typical APR quoted)

* Mortgage Credit Directive established (from 21/3/16) a new annual percentage rate charge called APRC which applies to 1st and 2nd charge mortgage lending. APR still applies to personal loans, credit cards and HP agreements.

Consumer credit

- **FCA** took over responsibility for consumer credit regulation from OFT on 1/4/14
- Their rules on consumer credit are contained in the Consumer Credit Sourcebook (CONC)
- Consumer credit firms must be authorised by the FCA who keep a register of firms who have been granted a consumer credit licence
- FCA conduct rules apply e.g. high-level Principles for Business
- High-Cost Short-Term credit (i.e. payday lenders) – FCA has introduced a cap on credit from 2/1/15:
  - Interest and fees charged must not exceed the amount borrowed
  - Must carry the following message: 'Warning: Late repayments can cause you serious money problems. For help, go to moneyadviceservice.org.uk'

Anti-money laundering

Proceeds of Crime Act 2002

- Regulated sectors:
  - Deposit taking
  - Money changing
  - Dealing, arranging or advising on investments
  - Long term insurance
- Offences:
  - Concealing / Arranging / Acquiring / Tipping off / Failure to Disclose (Disclosure to National Crime Agency (NCA) / Money Laundering Reporting Officer (MLRO)) / Recklessly making a false or misleading statement in context of Money Laundering (ML)
- Penalties include imprisonment, fines or both
  - Concealing / Arranging / Acquiring = Up to 14 years plus unlimited fine
  - Tipping off / Failure to Disclose = Up to 5 years plus unlimited fine
  - Partner/Director who fails to comply with ML regulations / Recklessly making a false or misleading statement in context of ML = Up to 2 years

Money Laundering Regulations 2017

- Emphasis is on adoption of RISK BASED approach by regulated firms to carrying out their ML obligations
- Guidance on the interpretation of the Regulations is provided by the Joint ML Steering Group (JMLSG)
- Wider range of businesses now covered which inc. Credit and Financial Institutions, Auditors, Accountants, Tax Advisers, Insolvency Practitioners & Estate Agents
- Suspicions must be reported to MLRO (who must be based in UK) who will decide whether they should be escalated to National Crime Agency

Financial Action Task Force (FATF)

- International governmental organisation who co-ordinate the international fight against ML
- It is a policy making body rather than getting involved in law enforcement
- Keeps list of countries / territories who it feels do not have adequate anti-ML measures
- Work of FATF falls into 3 areas:
    1. Sets standards for national anti-ML programmes
    2. Evaluates extent to which individual countries have implemented these standards
    3. ID's trends in ML methods

Money Laundering Regulations

- Policies & procedures
- Customer due diligence
- On-going monitoring
- Identification procedures
- Staff awareness & training
- Enforcement
- Suspicious activity reporting
- Record keeping

Other regulation affecting the advice process

General Data Protection Regulation

- Information Commissioner responsible for overseeing the application of the GDPR
- Applies to personal data
- Register with Public Register Of Data Controllers – maintained by Information Commissioner's Office
- 6 Data Protection Principles
- Right to see records
- Personal data
- Sensitive data
- Businesses established in >1 EU country

Criminal Offences under GDPR

1. Data controller failing to comply with an information/enforcement notice
2. Failing to make proper notification to the Information Commissioner
3. Processing data without authorisation from the Commissioner
4. Intentionally or recklessly re-identifying individuals from pseudonymised or anonymised data

Max Penalty: Higher of £17.5m / 4% of organisation's **worldwide** turnover, whichever is higher

Rules on Occupational pensions

Pensions regulator aims to ensure that OPS are run well. It has the power to:
- investigate schemes
- put things right (enforce actions, fines, trustee disqualifications, recover unpaid contributions)
- act against avoidance

Pension Protection Fund (PPF)
- protects members of schemes where employer & scheme has become insolvent
- compensation of 100% for existing pensioners and 90% for pre-retired
- compensated pensions will increase by RPI subject to maximum of 2.5%

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EU directives and regulations

EU directives are **binding as to the result** to be achieved (unless exemption negotiated), but the **choice of how** to do this is left to each country

EU regulations are **binding and are directly applicable** (i.e. no choice as to how they are implemented) and must usually be achieved within stated timetable

Electronic Money Regulations 2011 – introduced new requirements for all e-money issuers, new authorisation/regulation and prudential standards for e-money institutions.

Markets in Financial Instruments Directive (MiFID) – covers most tradeable financial instruments inc. shares, bonds, units in collective investments and derivatives. Life assurance, pensions and mortgages are outside the scope of MiFID.

EU directives and regulations

Undertakings for Collective Investment in Transferable Securities (UCITS) – applies to regulated investment funds that can be sold to the general public throughout the EU.

Consolidated Life Directive (2002) – sets the framework for the regulation of life assurance in the EU.

3rd Non-Life Directive – lays down the rules for cross-frontier non-life insurance that balances the needs of freedom and service and consumer protection.

Directive on Insurance Mediation –

- established the freedom for insurance intermediaries to provide services in all states throughout the EU. A key aim was to regulate the sales and standards of insurance brokers and intermediaries.
- The Directive also requires insurance intermediaries to hold PII of min €1M per case and €1.5M in total per annum. They should also have financial capacity of an amount equal to 4% of premiums received p/a subject to a minimum of €15,000.

Oversight Groups

- Auditors
  - Internal
  - External
- Trustees
- Compliance Officers

Consumer Rights, Complaints & Compensation

The role of government departments

HM Treasury

Department for Work & Pensions

HM Revenue & Customs

Ministry of Justice

The Claims Management Regulator

NCA National Crime Agency

The role of guidance services

- The Money and Pensions Service (MAPS)
  - Has created 1 organisation from three existing providers of government guidance:
    - The Money Advice Service
    - The Pensions Advisory Service
    - Pension Wise
- 5 core functions:
  - Pensions guidance
  - Money guidance
  - Debt advice
  - Consumer protection
  - Strategy

The role of guidance services

- Which?
  - Campaigns to protect consumers' rights, reviews products and services, and offers independent advice on a variety of subjects (including financial services).

- Citizens Advice
  - Available online, via telephone and face-to-face
  - Provides free, confidential and independent advice to help people overcome their problems.

Complaints – firms’ procedures

What is a complaint?

Firms must:

- have written procedures to appropriately handle complaints and try to come to settle the complaint
- report back to the FCA on complaints every six months
- If they receive 500+ complaints in 6 months, publish their complaints information.

keep records of complaints for 3 years from the date received / collective portfolio management services for a UCITS scheme **(Undertakings for Collective Investment in Transferable** Securities) = 5 years / MiFID business =no minimum retention period

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Complaints – firms' procedures

- Acknowledge the complaint promptly & in writing
- Endeavour to get final response to complainant within 8 weeks (and keep the informed in the meantime)
- If no final response at 8 weeks then must tell the customer they can contact FOS immediately if not satisfied
- Since Jan 2018, payment services providers must give a full response to a complaint within 15 days (35 days in exceptional circumstances)
- in final response remind them of FOS and the deadline to contact FOS of 6 months after receiving that letter

Financial Ombudsman Service (FOS)

- Independent arbiter on complaints
- FREE to customers
- Must be **eligible complainant**
- FOS only involved after firms' procedures have been exhausted
- Complaints must be made to FOS within:
  - 6 months from receipt of final response
  - 6 years of the event **OR**
  - 3 years of customer becoming aware

Financial Ombudsman Service (FOS)

- Maximum FOS award aimed to put claimant back in same financial position:
  - **From 1 April 2023 = £415,000 plus interest and the complainant's reasonable costs**
  - **For acts or omissions by firms between 1 April 2022 and 31 March 2023 that are referred to the FOS in that time, the limit will be £375,000**
- Awards are binding on the firm but not the complainant
- Include Consumer Credit Act disputes

Financial Services Compensation Scheme (FSCS)

- Default of **insurance** company or **Insurance intermediaries** :
  - 100% of claim if insurance is compulsory
  - 90% of claim if insurance is non-compulsory
- Insolvency of **regulated investment** firm or claim re. **mortgage** advice and arrangement:
  - 100% of first £85,000
- **Deposit** loss on default of bank or BS:
  - 100% of first £85,000 (£1M temporary high balance for max 6 months)
- Customer money held by **debt management** firms that fail:
  - up to £85,000

Pensions Ombudsman

- Decides on disputes of **running** of schemes, not sales
- Also covers state pensions
- Process for these complaints:

  - The scheme
  - The Pensions Advisory Service (TPAS) for arbitration
  - Only then the Pensions Ombudsman

- Complaints should be made within three years of the event
- Decision binding on the firm <u>and</u> complainant

Revision and Consolidation

Main areas of concern?

Practice!

MOCK EXAMs