The London Institute of Banking & Finance

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CeMAP 1 COURSE CONTENTS

PERFORMANCE TRACKER 1

Unit	Topic	1st Attempt %	2nd Attempt %	3rd Attempt %	4th Attempt %
1	1 & 2				
1	3				
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1	5				
1	6				
1	7				
1	8				
1	9 & 10				
1	11 & 12				
1	13				
1	14 & 15				
1	16				

Use the above tracker to identify your weakest units & sections and then prioritise your study in those areas

PERFORMANCE TRACKER 2

Unit	Topic	1st Attempt %	2nd Attempt %	3rd Attempt %
2	17			
2	18			
2	19 & 20			
2	21 & 22			
2	23			
2	24			
2	25			

Use the above tracker to identify your weakest units & sections and then prioritise your study in those areas

INTRODUCTION

Examination Format

- CeMAP 1 is a multiple choice examination with 4 possible answers being given from which you must select the correct answer.

- There are two units each with 50 questions and you have a maximum of 1 hour to complete each unit. If you finish one unit early you cannot carry over any surplus time into the next unit.

- You must pass both units to achieve an overall pass on CeMAP 1 which is a minimum of 35 out of 50 on both units (70%). If you fail one of the units you will be required to resit that unit only.

- The grade boundaries are as follows:

  - 90% 45 – 50 correct - Pass with Distinction
  - 80% 40 – 44 correct - Pass with Merit
  - 70% 35 – 39 correct - Pass

The Pearson Vue Electronic Exam

- All CeMAP exams use the Pearson electronic system. There are over 150 centres at which you can take the exam but you might have to wait a while if you want to take it at a specific centre.

- To book your exam, you need to register with the London Institute for Banking and Finance by calling on 01227 818609 or at www.libf.ac.uk We recommend that you take your exam within 14 days of completing this course if possible.

- On the day you will usually need to take a form of ID, which must be photo ID. You will be given a Taxation Table on the screen, calculator, mini whiteboard and pen for any rough working out.

- You will be allocated to a desktop computer which will usually be operated by mouse. Once the exam starts and the questions appear, you use your mouse to choose the correct letter. When the exam ends you will find out the result!!

CeMAP 1

Introduction to the Financial Services Environment and Products

Unit 1 – Topic 1

Introducing the financial services industry

Money

- Money provides a way of paying for products and services and has two main functions. It is a unit of account and a medium of exchange.

- To be a medium of exchange money must be:

    - acceptable to all parties
    - sufficient in quantity
    - divisible into small units
    - portable

- Money can be either in cash or held in a bank account or other savings product. Notes and coins are legal tender – they have the backing of the government and the central bank – Bank of England.

- Money also acts as a store of value. This means that it can be saved and used later to pay for products and services. To do this, money must retain its exchange value or purchasing power. Inflation can have a negative impact on the exchange value of money.

- The financial services industry provides different usages for money through different vehicles such as current accounts, mortgages & protection (insurance).

Intermediation

- The surplus sector comprises those who are cash rich e.g. they hold more money than they wish to spend. They want to lend out their surplus to earn more money.

- The deficit sector comprises those who don't have enough money and therefore they are prepared to borrow from anyone who will lend to them.

- A financial intermediary such as a bank or building society is an institution that borrows from the surplus sector at an agreed interest rate and then lends it to the deficit sector at a higher interest rate. The difference between the two rates represents the profit for the intermediary.

- Sometimes there is no need for an intermediary e.g. where the borrower goes direct to the lender. This is called **disintermediation.** An example of this would be 'crowdfunding' – where a business advertises on its website for investment from the general public.

- Intermediaries become necessary when:

    - **geographic location** make it difficult to find one another.

    - amount mismatch requires **aggregation** – match the amounts needed.

    - term mismatch requires **maturity transformation**- match the terms needed and required e.g. able to offer a wide range of accounts.

    - **risk transformation** – spreading the risk of default by either party, in other words not lending to just one client but to a wide variety of borrowers so that if a few fail to pay, the loss can be absorbed.

- Intermediaries bring together the lender and the borrower and include financial advisers and mortgage brokers who are regarded as 'product sales intermediaries'

Financial Institutions

Prior to the 1980s there were more clearly defined boundaries between different kinds of financial institutions. Today many of those distinctions have been blurred. Increasing numbers of mergers and takeovers have taken place which has increased the size and strength of some financial institutions and the term 'bancassurance' has been coined to describe banks who own insurance companies and vice versa.

The Bank of England

The Bank of England has a mission to promote and maintain monetary and financial stability and therefore its duties include:

- Banker to the banks – all major banks have an account with the BoE and the BoE has responsibility for setting the interest rates on these accounts held by the major banks.

- Issuer of banknotes – Bank of England is the central note issuing authority.

- Banker to the government – BoE is a central bank because it is banker to the government and covers any government deficits through automatic loans to the government.

- Set Interest Rates – Since May 1997 the Bank's Monetary Policy Committee (MPC) granted responsibility for the setting of the UK Bank of England Base rate.

- The Committee meets at least 8 times a year to decide the current base rate to help the government meet its inflation target. The government has set an official target of 2% inflation rate plus or minus 1%, or in other words the Government is happy if it is between 1-3%.

- Lender of last resort – duty to ensure a satisfactory supply of money remains in circulation and to make funds available if they are in short supply – to maintain confidence in the system. E.g. Northern Rock in 2007.

- Foreign exchange – manage the country's reserves of gold & foreign currency.

- The Financial Services Act 2012 became law in April 2013. This effectively ended the role of the FSA as the regulator of financial services. Under the new rules, the Prudential Regulatory Authority(PRA) which is a subsidiary of the Bank of England was established which meant that significant institutions such as banks, building societies, insurance companies would all fall under this new regulator.

- The FSA's former role in relation to behaviour and conduct, consumer protection and promoting competition within financial services was transferred to a new organisation called the Financial Conduct Authority (FCA).

- The Bank of England was also responsible initially for managing new issues of gilt edged securities but that role has now passed to the UK Debt Management Office within the Treasury. This is to avoid a conflict of interest that might arise from the Bank's responsibility for the setting of interest rates.

Proprietary & Mutual Organisations

- Proprietary Organisation – limited companies owned by shareholders e.g. RBS, HSBC.

- Mutual Organisation – not limited companies, no shareholders- owned by the members e.g. Building societies – also Friendly Societies and Credit Unions.

- Allowed building societies to demutualise and convert to a bank with the approval of its members.

- A Credit Union is a financial organisation run for the benefit of its members who are normally linked in some way e.g. club, church, area. A credit union is owned by the members and they offer simple savings and loans to its members.
- A unique feature is that members' savings and loan balances are covered by life assurance.

Retail Banking

- Provision of financial services to the public and to companies through a network of branches.

Wholesale Banking

- Money is raised wholesale by financial institutions from the wholesale money markets, often called the interbank market.

- Banks and other financial institutions will often borrow money wholesale from other banks and then lend it to the public retail which will give them a profit.

- Building Societies are now able to raise funds from the wholesale market up to a limit of 50% of their total liabilities.

- Subprime lenders raise their funds from the wholesale market.

- The rate of interest charged on the inter-bank market, which is known as the London Inter-Bank Offer Rate (LIBOR), is fixed daily and can have maturity dates from one day upwards. Money can be raised very quickly on the interbank market.

- LIBOR is often used as a rate for corporate lending which may be set as LIBOR plus a specified margin e.g. LIBOR + 2.5%.

- LIBOR is a rate that each bank submits or declares itself based on what they are paying or would expect to pay for borrowing from other banks. This is then averaged to give an overall LIBOR rate. However, in 2012 some banks were falsifying their LIBOR submission to perhaps give a false impression of their financial wellbeing.

- Responsibility for administering LIBOR is now with the Intercontinental Exchange Benchmark Administration.

- As a result of the 2012 LIBOR scandal, banks now have to base their LIBOR submissions on actual transactions as opposed to the bank's expectations regarding interest rates. The banks will also have to evidence the transactions that they are relying on and there are now criminal sanctions if there is any LIBOR rate manipulation.

Unit 1 – Topic 2

Economic policy and financial regulation

Economic and Monetary Policy

The long term objectives that the government are looking to achieve are often referred to as 'macroeconomic objectives'. This gives us a picture of the economy as a whole as opposed to 'microeconomics' which looks in detail at one small part of the economy.

- Managing the economy requires a number of things:

    - Price stability – keeping inflation on the low side. Inflation is defined as a general increase in prices and services. Disinflation is where prices are still rising but less quickly than before and Deflation is a general fall in prices and services eg -0% inflation rate.

    - Low unemployment – ensures a demand for goods & services and reduces the cost of state benefit

    - Balance of Payments equilibrium – import/export balance relationship

    - Satisfactory economic growth – economy is growing. This is sometimes measured by Gross Domestic Product (GDP) which is the measure of the value of the goods and services in a country over a specified period of time. If there is a significant decline in GDP over 2 successive quarters, this is defined as a 'recession'.

- Very difficult to achieve all of these at the same time. Any attempt to improve one of these could affect the other.

- The government's long term objective is to keep unemployment and inflation on the low side. So, they are happy to accept a 'trade off' of a low rate of inflation and a low rate of unemployment.

- The official measure of inflation is the Consumer Price Index (CPI). This is basically a basket of goods and services, the sorts of things that people buy on a regular basis. There is a very similar index called the Retail Prices Index (RPI) which is also based on a basket of goods and services, and is usually higher.

- The government has set an official target of 2% inflation rate plus or minus 1%, or in other words the Government is happy if it is between 1-3%.

- The main way that the authorities can influence whether this goal is to be achieved is through the setting of interest rates by the Monetary Policy Committee.

Monetarist View of Economics

- Monetarists believe that inflation is a man-made phenomenon and is caused by allowing credit and money to be easily made available – supply of money.

- Therefore inflation can be controlled by the government using the setting of high interest rates to discourage people taking on additional debt.

- In UK this is now the job of the MPC to set interest rates, although the Treasury does have the right to give instructions to the Bank of England should they wish to.

- If the base rate does rise, most lenders will follow suit although they do not have to and also vice versa.

Fiscal View of Economics

- Fiscal policy is concerned with government and public spending.

- The Government has a huge public sector responsibility in paying for health care, education and public safety and this money is raised through taxation.

- With regard to the public sector there are 3 possible outcomes:

    - **Balanced budget** – all revenue from taxation is invested in public spending.

    - **Budget surplus** – more is raised in taxation than is invested in public spending.

    - **Budget deficit** – public spending is greater than revenue from taxation.

- If a budget deficit exists there will be a need for the government to meet that shortfall. This is referred to as the Public Sector Net Cash Requirement (PSNCR).

- In practice, fiscal and monetary policy are not applied in isolation but are closely linked and governments generally use a combination of the two.

European Union

Although we are now in the process of exiting the European Union and Article 50 has been triggered, there is still some uncertainty at the time of writing regarding what is going to happen within the UK regarding their future relationship with Europe.

There are 2 main types of European law which apply to EU countries which are:

Regulations

- These are binding in their entirety as to what is to be achieved and how it is to be achieved.

- Directly applicable to all member states unless particular states have been granted a dispensation.

Directives

- Are binding upon each member state to which they are addressed as to the result to be achieved.

- Must be achieved within a certain timescale (2 years normally).

- However, the means by which they are to be achieved can be determined by each state. In other words, they are not binding in their entirety.

European Supervisory Authorities

As a result of the financial crisis, there was a need for reform of virtually every area of EU wide financial services.

In 2011 the EU set up three European Supervisory Authorities that have powers to make rules and decisions that are binding on regulators and firms which are:

- European Securities and Marketing Agency
- European Banking Authority
- European Insurance and Occupational Pensions Authority

The Single Supervisory Mechanism (SSM) is the name which indicates that the European Central Bank holds responsibility for the supervision and monitoring of banks in EU member states.

Five Tiers of UK Regulation

- First Level – European union regulations and directives.
- Second Level – Acts of Parliament e.g. Building Societies Act 1986
- Third Level – UK regulatory bodies such as the PRA and FCA.
- Fourth Level – compliance policies of individual financial institutions
- Fifth Level – rulings from arbitration and ombudsman schemes following customer complaints.

UNIT 1 – TOPICS 1 & 2 – UK FINANCIAL SERVICES			
Question	**Answer**	**Mark**	**Comments / Notes**
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	Result %		**Result % = (Total / 17) x 100**
NOW TRANSFER YOUR RESULT TO PERFORMANCE TRACKER 1			

Unit 1 – Topics 1 & 2 - Test

1 Financial intermediaries can provide maturity transformation because they:

A offer a wide range of deposit accounts to a wide range of depositors.
B aggregate many small deposits from a large number of clients.
C provide services to clients from many different geographical locations.
D reduce the risk of default or fraud by lending to a wide variety of borrowers.

2 A key difference between a mutual organisation and a proprietary organisation is that a mutual organisation:

A can issue shares on the stock market.
B is owned by members not shareholders.
C shares its profits in the form of dividends.
D is only allowed to lend to other financial institutions.

3 How can a bank involved in wholesale banking raise money quickly in order to finance business activities?

A By a further issue of shares
B By borrowing from the Bank of England
C From the interbank market
D By issuing gilts

4 What is the role of the Bank of England's Monetary Policy Committee?

A To veto undesirable takeovers
B To set capital adequacy levels
C To set the Bank of England Base Rate
D To set inflation targets

5 In order to be acceptable as a medium of exchange, money must have all EXCEPT which one of the following?

A It must be divisible into small units
B It must be generally acceptable to all parties in all transactions
C It must be free from the effects of inflation
D It must be sufficient in quantity

6 The Bank of England is a central bank because it:

A deposits money with the International Monetary Fund.
B has been approved by the Treasury and lends money direct to other banks.
C holds reserves of foreign currency for other banks and institutional investors.
D acts as banker to the government, supervises the economy and regulates the supply of money.

7 What means have large institutions in financial services markets predominantly used to achieve growth and diversification in recent years?

A Mergers and takeovers
B Focus on existing strengths
C Internally funded growth
D Additional share issues

8 Jon has notes and coins that are accepted as legal tender. This is because they have:

A been approved by the Treasury.
B the backing of the government and the central bank.
C been issued by a high street bank.
D the International Monetary Fund's backing and are issued by the government.

9 Which one of the following factors distinguishes building societies from other financial institutions?

A They are mutual institutions owned by their members
B They are owned by their shareholders
C They only lend for mortgage purposes
D They cannot make regulated loans

10 Up to what percentage of their liabilities may Building Societies raise funds on the wholesale market?

A 50%
B 25%
C 100%
D 40%

11 What is the target range of inflation that the government are hoping to achieve as measured by the Consumer Price Index?

A 3-5%
B 2-4%
C 1-3%
D 2.5-5%

12 The European Union has issued a new DIRECTIVE. This means that each member state:

A must implement the Directive in its entirety within the specified timescale.
B can choose whether or not to adopt the Directive.
C has the choice of how to meet the Directive's objectives.
D must implement the Directive, provided the member state is part of the Eurozone.

13 The regulatory framework for the financial services industry in the UK is a five tier process. Which one of the following bodies has taken over the activities in the third tier?

A The Financial Ombudsman Service
B The Building Societies Commission
C The PRA and FCA
D The Lenders Code

14 Which index does the government use to assess the inflation rate?

A Retail prices index
B Consumer prices index
C Construction and building prices index
D FTSE 100 index

15 Under what circumstances if any can a nation state opt out of a regulation laid down by the European Council and Council of Ministers?

A None
B Only if specific dispensation has been granted
C Only if an alternative approach has been agreed
D Only if the member has joined within the previous three years

16 Which type(s) of policy if any are used by governments to achieve their long term economic objectives?

A Fiscal only
B Monetary only
C Monetary and fiscal
D Neither monetary nor fiscal

17 What is gross domestic product? A measure of the value of:

A demand within a country over a specified period.
B goods and services within a country over a specified period of time.
C money supply within a country over a specified period of time.
D national average earnings within a country over a specified period of time.

Unit 1 – Topic 3

UK Taxation (Part 1) – Income Tax

Tax Legislation

- Following the 'Budget' which is now delivered in the Autumn, a Finance Bill is published which contains the taxation proposals that are to be debated in Parliament.

- If, following debate, the Finance Bill is approved and receives Royal Assent, it becomes the Finance Act.

Domicile

- Domicile refers to the country that a person treats as their permanent home or to which they plan to return.

- Domicile of origin is determined at birth as the domicile of the father or if they are unmarried, the mother.

- Domicile of choice is when a person chooses a new domicile by showing an intention to settle there permanently and severing their former connections. There is no specific process for this.

- Deemed domicile is when a person is not UK domiciled but has lived in the UK for 15 out of the last 20 years.

- If a person is either UK domiciled or deemed domiciled their estate for inheritance tax purposes includes all worldwide assets.

- If a person is neither UK domiciled or deemed domiciled at death the estate for inheritance tax purposes only includes assets held in the UK.

Residence

- This affects a person's liability to pay income tax and capital gains tax.

- If a person is classified as resident or ordinarily resident they are liable for income tax and capital gains tax on income and capital gains made worldwide.

- A person is classed as 'resident' if they:

    - Spend 183 days or more in UK during a tax year

Income Tax

Income tax is based on income received throughout the whole tax year 6 April-5 April.

- Income from employment/self-employment/pensions is often referred to as earned income.

- Income that hasn't come from your employment/self-employment e.g. interest from savings, dividends from shares, rental income, trust income is referred to as unearned income.

The following examples of income are all liable for income tax:

- Salary or wages, bonuses, commission, benefits in kind
- Tips
- Certain pension or retirement benefits
- Interest on bank/building society accounts not including ISAs
- Dividends from shares
- Income from gilts
- Trust income
- Property rental income
- Income from copyright and patent
- The value of benefits in kind such as company cars if total income including the value of benefits in kind exceeds £8,500

Some examples of income not liable for income tax are:

- The first £30,000 of redundancy payments
- Interest from National Savings Certificates & Premium Bonds
- Income from ISAs
- Educational grants
- Casual Gambling proceeds and lottery prizes
- Some social security benefits
- Benefits from Friendly Society Policies
- Covenanted or Gift Aid payments
- The proceeds from a qualifying life policy
- The capital element received from a purchased life annuity
- Certain grants from employers solely because an examination has been passed (certain criteria apply)

Who is liable for Income Tax?

- Everyone is regardless of age, even children potentially, if their income exceeds the personal allowance (see below)

- When a child receives income via a settlement from parents that will be treated as the parent's income for taxation purposes.

Personal Allowances (on taxation table)

- The personal allowance is the amount you can earn before tax becomes payable.

- **The amount of the personal allowance for this tax year is £12,500 for everyone. The 'income limit' to receive the full personal allowance is £100,000.**

- Note: If you are over the 'income limit', the allowance reduces by half of the amount (£1 for every £2) you have over that limit.

- If you earned £102,000 you would not be entitled to a personal allowance of £12,500 because you have an income which is £2,000 above the £100,000 limit, this means that you will only have a personal allowance of £11,500 e.g. it reduces by £1,000 because you are £2,000 above the limit.

- Taxpayers are allowed to make certain deductions from their gross income before assessing their tax liability including **pension contributions** and **allowable expenses incurred wholly for business reasons.**

    - Self-employed business expenses must be **wholly and exclusively for the trade**
    - Employed business expenses must be **wholly, exclusively and necessarily for the job.**

- Marriage allowance – it is possible for spouses and civil partners who are non-taxpayers and born after April 1935 to transfer up to 10% of their personal allowance to their spouse as long as the spouse is not a higher/additional rate taxpayer.

- Married couples have an additional allowance where at least one spouse was born before 6 April 1935. This could reduce their tax bill by between £345 and £891.50.

- There is also a Blind Person's Allowance (£2,450) if a person is registered as blind with a local authority. This allowance can be transferred to a spouse even if they are not blind.

- An allowance for property and trading income also now exists for people who supplement their main income with property or trading income. Each allowance is £1,000. The allowance applies to people who make small amounts of money on ebay or renting a room in their house or a parking space.

- After these deductions have been made, what is left is taxable income, which is then applied to the tax bands below.

Income Tax Bands on earned income (on taxation table)

Tax Band	Rate	From	To
Basic Rate	20%	£ 0	£ 37,500
Higher Rate	40%	£ 37,501	£ 150,000
Additional Rate	45%	£ 150,001	Upwards

Please note that these are the tax rates that apply once your total or gross income has had the personal allowance taken off. So if your gross income was £40,000 this would be reduced to taxable income of £27,500 which would then be taxed at 20%.

To be a higher rate taxpayer you need to be earning in excess of £50,000 gross.

Example

Tina earns £ 55,500 gross before allowances and no other income. Calculate her income tax liability for this year?

Deduct the personal allowance

55,500
12,500

£43,000 (taxable income)

This is the amount of taxable income that is left. This amount is more than £37,500 basic rate threshold, so you know that there will be some higher rate tax to pay.

£43,000 (**total taxable income**)

37,500	@	20%	=	£ 7,500
5,500	@	40%	=	£ 2,200
Total tax due				**£ 9,700**

Income Tax on interest from Savings

- For those on low incomes (less than £17,500), there is potentially a 0% starting rate on the first £5,000 of interest on savings.

- However, this rate does not apply where their income exceeds £17,500 which is the personal allowance of £12,500 plus the starting rate allowance of £5,000

- In other words, if their total income plus savings is less than £17,500 then the 0% starting rate can apply to the interest on their savings.

- Please note that if your income is above the personal allowance of £12,500 but less than £17,500, the £5,000 allowance reduces by £1 for each £1 of income above the personal allowance. (see example 1 below)

- Additionally, basic rate taxpayers receive an income tax free allowance of £1,000 on interest from savings. So, the first £1,000 on interest they receive on savings is tax free. Any interest received above £1,000 will have to be declared and the tax paid via self-assessment.

- For higher rate taxpayers, this allowance is £500. Any interest received above the £500 would have to be paid again via self-assessment.

- There is no income tax free allowance on interest from savings for additional rate taxpayers.

<u>Example 1</u>

Sara earns £14,500 gross before allowances and has savings income of £2,500. Calculate her income tax liability for this year?

As her income is below £17,500, Sara will be entitled to the 0% starting rate for savings interest.

As the earned income is above the personal allowance there would be some income tax to pay on the £14,500 earned income.

£14,500 – £12,500 perosnal allowance = £2,000 @ 20% = £400

As her income is £2,000 above the personal allowance, she will not be entitled to a £5,000 allowance on her savings – this will reduce by £2,000 to a £3,000 allowance.

2,500 savings income is still less than her interest savings allowance of £3,000:

2,500 @ 0% = £ 0 on the savings interest

Example 2

Joe earns £28,500 gross before allowances and has savings income of £2,500. Calculate his income tax liability for this year?

Deduct the personal allowance

28,500
12,500

16,000	@	20%	=	£3,200 income tax on earned income

2,500 (savings income + the £28,500 salary is above £17,500 so no 0% starting rate is available but is still within the basic rate band so:

£1,000	@	0%	= £ 0
£1,500	@	20%	= £300 savings tax via self-assessment

Income Tax on dividends

- Dividends, which is a distribution from a company's profits only to people who own shares in a company, are paid without deduction of income tax.

- Individuals who receive dividends, benefit from a £2,000 dividend allowance where no income tax is payable.

- Basic rate taxpayers – pay 7.5% income tax on dividends over and above the £2,000 allowance via self-assessment.

- Higher rate taxpayers pay 32.5% income tax via self-assessment.

- Additional rate taxpayers pay further 38.1% income tax via self-assessment.

Collecting Income Tax

Income taxed at source

- Where possible HMRC collects income tax at source e.g. from the person who makes the payment not the recipient (the individual).
- In this case, tax is usually deducted at the basic rate and any further liability is paid via the tax return e.g. self-assessment.

Employed

- If you are employed, income tax is paid by the employer at source under the PAYE scheme. HMRC will provide a tax code for each employee.

- A P60 is issued to each employee in April each year for the previous tax year showing all the tax and national insurance deducted.

- On leaving an employer, the employee should be provided with a P45 which you will need to give to your next employer.

Self Employed

- Sole traders and people in 'partnership' pay income tax directly to HMRC through declaring their **'net profit before tax** 'e.g. after deducting fixed and variable costs.

- These figures can be either submitted directly to HMRC who will calculate the tax liability or they can calculate the tax liability themselves and send it to HMRC for approval – 'self-assessment'.

- This needs to be done by 31st January following the end of that tax year. Self-employed people pay their income tax and their Class 4 national insurance in two equal instalments due on 31st of January and 31st July.

Please note that if a person's income comes from different sources it is taxed according to a set order of priority:

1 Earned income
2 Interest
3 Dividends

Charitable Giving

Making gifts to charity is beneficial for the charity and also reduces an individual's income tax liability by utilising a concept called gift aid. Employees who gift to charity from their salary also benefit from a reduction on their tax liability.

National Insurance Contributions (NIC)

There are four categories:

Class 1 – Employees' and employer's contributions
Class 2 – Self-employed flat rate contributions collected through self assessment
Class 3 – Voluntary contributions
Class 4 – Self-employed profit related contributions

Class 1 Employee and Employer Contributions

- Paid by employees at 12% who earn more than the primary threshold.
- There is a reduced level of 2% payable on earnings above an upper limit.
- Paid by employers at 13.8% on employees' earnings above a certain amount called the secondary threshold.

Class 2 NICs

- Flat rate contributions paid by the self-employed quoted as a weekly figure and collected through self-assessment.

Class 3 NICs

- Voluntary contributions that are made by people who may have fallen behind on their national insurance payments, e.g. career break or working abroad.
- By paying these it may give them entitlement to certain state benefits such as the basic state pension.

Class 4 NICs

- Self-employed have to pay additional NICs on their profits.
- For profits above the upper limit they have to pay a reduced additional rate.
- They are paid to HMRC in half yearly instalments along with income tax via self-assessment.

UNIT 1 – TOPIC 3 – INCOME TAX			
Question	**Answer**	**Mark**	**Comments / Notes**
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	Total		
	Result %		**Result % = (Total / 17) x 100**
NOW TRANSFER YOUR RESULT TO PERFORMANCE TRACKER 1			

Unit 1 – Topic 3 Test

1 Every year in the Autumn, a number of taxation measures are made in the budget. These then take effect as a result of the related:

A Income and Corporation Taxes Act
B Social Security Act
C Taxation Act
D Finance Act

2 Marco is a resident of the UK and this is also the country in which he usually lives, although his country of domicile is Italy. On which one of the following would he not be expected to pay UK tax?

A Income earned from renting his villa in Italy, but kept in an Italian bank
B Income earned from renting his villa, but brought back to the UK
C Tax on an inheritance left by his father in Italy
D Tax on capital gains from the sale of some shares on the New York stock exchange

3 When does a person acquire their domicile of origin?

A At birth
B At 18
C At 21
D At 16

4 Which one of the following payments will NOT be liable to income tax?

A Interest from a building society postal account
B Income from company dividends
C Interest from an Individual Savings Account
D Income from Government loan stocks

5 Where an employee receives a termination payment on becoming redundant, up to what amount will the payment be free from income tax?

A £20,000
B £25,000
C £30,000
D £35,000

6 Where a child receives an income from an arrangement made by his or her parents, how is this taxed?

A As the child's personal income
B It is tax-free
C The first £70 is always tax free
D It will normally be added to the parent's income

7 What does the term 'collecting income tax at source' actually mean?

A Recipient pays the tax to the Inland Revenue before using the money
B The tax is collected through the recipient's tax return
C The total income is automatically reduced by basic rate tax
D The collection is from those who make the payment, not the recipient

8 For income tax purposes, self-employed people are taxed on their:

A turnover
B gross profit
C net profit
D personal drawings

9 Which one of the following individuals would be most likely considered a UK resident for tax purposes?

A Sandra who normally lives in France but spends two months a year on a farm in Scotland.
B Luigi who has a nine month contract in Essex with a telecom company commencing in April.
C Dmitri who has a seven month business consultancy contract in London commencing in January.
D Bella who spends 180 days a year in the UK developing her Italian based design company.

10 What is the tax liability of a higher rate taxpayer on income earned from dividends after their allowance has been used?

A 32.5%
B 20%
C 40%
D 22.5%

11 Terence is aged 38, married and has a gross salary of £26,500 from his employment. If he had no taxable benefits in kind, how much income tax did he pay?

A £ 4,579.50 B £ 4,814.00 C £ 5,300.00 D £ 2,800.00

12 Steven (age 35) has a taxable income of £28,000. He receives NO other income of any sort during the tax year. As a single person, what is his tax liability?

A £ 4,914 B £ 5,600 C £ 3,100 D £ 5,195

13 **The profits of a sole trader are subject to which class of National Insurance contributions?**

A Class 4 B Class 3 C Class 2 D Class 1

14 **William is deemed to be resident in the UK for tax purposes in the previous tax year. What is the minimum number of days that he must have been in the UK in that tax year?**

A	1 day	B	183 days
C	90 days	D	365 days

15 **The precise definition of employee expenses that are used to reduce income tax liabilities is they MUST be specifically incurred wholly:**

A while doing the job
B and exclusively while doing the job
C and necessarily while doing the job
D exclusively and necessarily while doing the job

16 **Who is allowed to use expenses to reduce income tax liability?**

A Employees
B Employees, partners and sole traders
C Sole traders only
D Sole traders and partners only

17 **Jan has not worked for 5 years, which class of National Insurance contributions should she make to maximise her entitlement to state benefits:**

A Class 1 B Class 2 C Class 3 D Class 4

Unit 1 – Topic 4

UK Taxation (Part 2)

Capital Gains Tax

- This is a tax that is payable on gains or profit made on the disposal of certain assets.
- Limited companies are not specifically liable for this tax, although any gains they make would be dealt with via corporation tax.

Exempt assets

- Main private residence
- Ordinary private cars
- Personal belongings below £ 6,000
- Gifts to the nation
- Foreign currency for personal use
- Government stocks (gilts)
- Gains on qualifying life policies disposed of by the owner. The new owner of the policy will not be exempt.
- Assets acquired on death although Inheritance Tax may apply in this case
- National Savings Certificates
- ISAs

Notes

- Where assets are bought and sold in the course of a trade for instance an art dealer there is no liability for CGT but the profits are dealt with via income tax.
- Since April 2015, non UK residents are also potentially liable for gains made on UK residential property.

There has to be a Disposal (Sale)

- A gain is made when an asset is sold at a higher price than it was bought at
- A disposal can also include a transfer of ownership of an asset

Annual CGT Allowance

- Every person regardless of age has an annual CGT personal allowance where no tax is incurred of £12,000.

- The full allowance also applies to trustees of a disabled person and to personal representatives. It also applies to a bare trust which has a specified beneficiary who will have absolute entitlement to the assets at 18.

- Half the annual CGT allowance (£6,000) applies to most other types of trust.

- If this allowance is not used in a tax year it cannot be carried forward to future years.

Other Deductions – Allowable Expenses (Buying, Improving, Selling)

- The costs of acquiring or buying an asset can be deducted from the gain made
- The costs of improving an asset can also be deducted though not repair costs
- Costs incurred on disposing or selling an asset can also be deducted

- Capital gains made prior to 31 March 1982 are not taxed. Any assets acquired before 31 March 1982 will be assessed at their value on 31 March 1982.

Roll over relief

- Business assets are chargeable to CGT. However, if the business asset disposed of is replaced by other business assets **'roll over relief'** may be claimed on all chargeable gains realised by individuals. This means that the CGT is deferred until a final disposal is made.

- The replacement asset must be bought within a period of one year before and three years after the sale of the original asset.

Hold over relief

- Similarly, CGT on any gain arising on the gift of certain assets such as shares in a business or sale at an under value can normally be deferred until the recipient disposes of it.

Note

Please note that any shares or unit trusts that are disposed of and repurchased within a 30 day period are treated for CGT purposes as if those two transactions never took place.

Capital Losses

- If you suffer a loss on the disposal of an asset, that loss can be offset against capital gains achieved on other assets.
- Any such losses must first be offset against gains made in that tax year.
- Any losses still outstanding may then be offset against gains to be made in future years.

CGT Rates and Payment

- The **total** gain is the sale price minus the original purchase price.
- A gain that is made after the personal allowance has been applied is called the **'taxable gain'.**

  - For gains made on **residential property**, the taxable gain is then taxed at a rate of 18% for non-taxpayers and basic rate taxpayers or 28% for higher rate and additional rate taxpayers**.**

  - For gains made on anything other than property, for example on selling shares, the rate is 10% for basic rate taxpayers or 20% for higher rate or additional rate taxpayers.

  - A lower rate of 10% applies to the first £10m of cumulative gains arising from the disposal of trading businesses and disposals of shares in trading companies. This is known as 'entrepreneur's relief. In order to qualify, the individual must own at least 5% of the share capital and be entitled to 5% of the voting rights. Property letting companies do not normally qualify for this relief.

- CGT is normally payable on 31 January following the end of the tax year in which the gain is made.

<u>Calculation Example</u>

Alan, a higher rate taxpayer bought a unit trust for £ 50,000 in May 2003 and sold it for £ 80,000 in May 2019. At the same time he sold some shares for £ 10,000 that he had bought for £ 12,000.

What capital gains tax will he pay?

Step 1 Calculate the Total Gain

Sale Price – Purchase Price = Total Gain

80,000 – 50,000 = £30,000

Step 2&3 Deduct the annual allowance from the total gain and any losses b/fw

30,000
- 12,000 CGT allowance
- 2,000 losses from sale of shares

£16,000 @ 20% = £3,200

Inheritance Tax (IHT)

- IHT is potentially payable when a 'transfer of value' occurs usually on death at the rate of 40%.

- This is charged on the estate of the deceased individual at the rate of 40% on the amount of the estate that exceeds the nil rate band, currently £325,000.

- For IHT purposes the estate includes:

    - The value of all assets at death held solely in that person's name
    - Value of gifts made within 7 years of death
    - Some lifetime gifts – mainly to companies or clubs or societies

- If a person is **either** UK domiciled or deemed domiciled at death, the estate on which IHT is charged includes all assets, regardless of where they are in **the world.**

There is always a 'deemed transfer of a person's assets on death and these transfers will either be exempt, potentially exempt or chargeable.

Exempt Transfers

- **Spouse Exemption -** includes same sex couples under the Civil Partnership Act

    - The whole estate no matter how large can be passed to the spouse with no IHT liability

- Surviving spouses and civil partners can increase their own nil rate band by the proportion of unused nil rate band from the earlier death of their spouse/partner.

Example

If on the first death an estate of £200,000 was left entirely to the deceased's wife, the husband's nil rate band hasn't been used at all as the spouse exemption applies. Therefore, the unused proportion in this instance is 100%.

Therefore, if the wife was to die today, her nil rate band would be increased by 100% or doubled to £650,000.

Residence Nil Rate Band (RNRB)

- If part of the estate includes a residence, then an additional residence nil rate band can be applied. It is £150,000 this tax year but rises to £175,000 by 2020/21.

- From 2021/22 the RNRB will increase in line with the Consumer Price Index.

- Where the RNRB is unused on the first death, the unused proportion can be transferred for use by the surviving spouse.

- This means that in this tax year, for married couples who own a property, on the second death, they have an effective nil rate band of £950,000. eg 150,000 RNRB x 2 = £300,000 added to the £325,000 nil rate band x 2 = £650,000

- This also means that from the next tax year the maximum amount exempt from IHT for married couples will effectively be £1M.

- **Small Gifts Exemption**

    - Gifts of up to £250 per annum per person are exempt

- **Annual Gift Exemption**

    - Gifts totalling £3,000 in any one year which are not covered by other exemptions. If this is not used in a particular year it can be carried forward for one year only.

- **Marriage Gifts**

    - £5,000 from each parent, £2,500 from each grandparent, £1,000 from others

- **Other Exemptions**

    - Gifts to charities and political parties and to the nation.
    - Gifts that are made regularly out of income which do not affect the donor's standard of living.

Potentially Exempt Transfers (PETs)

- These are lifetime transfers made between individuals that may incur IHT

- If the person giving the gift dies within 7 years of making the gift, the value of that gift will be added onto the deceased's estate which could result in the estate having to pay IHT or a higher amount of IHT

- No IHT is payable at the time of the transfer

- The IHT rate applicable can be reduced by tapering relief.

Gift followed by death within	IHT Rate payable
0 – 3 years	100% of normal death rate = 40%
3 - 4 years	80% of normal death rate = 32%
4 – 5 years	60% of normal death rate = 24%
5 – 6 years	40% of normal death rate = 16%
6 – 7 years	20% of normal death rate = 8%

Chargeable Lifetime Transfers

- A chargeable lifetime transfer is one where an immediate charge to IHT is payable by the recipient of the gift if the total value of gifts made over the last 7 years is in excess of the nil rate band.

- They are usually gifts to a club or society.

- These transfers are charged at half the normal rate immediately – 20%.

- As with PETs if death occurs within 7 years the full balance of IHT becomes payable.

Other Issues

- Funeral expenses and settlement of bills can be deducted from the estate before calculating IHT liability.
- IHT is payable or charged against the estate of the deceased.

Value Added Tax (VAT)

- VAT is an indirect tax levied on the sale of certain goods and services
- There are normally two rates:

    - Zero rate
    - Standard rate 20%

- A person or company needs to register for VAT when its annual turnover exceeds a certain figure.

- If a business exceeds the annual registration limit, it must register for VAT unless the product or service is exempt.

- Businesses below that limit may decide to register.

Exempt Supplies

- Provision of insurance policies and the charging of commission.

- Supply of health and education services.

- Provision of credit services such as mortgages

- The supply of financial advice is not exempt and advisers who charge a fee for advice could be held liable to charge VAT for this advice as accountants or solicitors are.

Zero Rated Supplies

- Food but not restaurants or takeaways
- Books and newspapers
- Children's clothing
- Prescriptions
- Domestic water supply
- Domestic heating is charged at a reduced rate

Registration is not strictly necessary if that company is providing zero rated goods. However, registration would be necessary if they wanted to reclaim any VAT paid for goods coming into their business.

Advantages of Registration

- VAT paid out for your business can be reclaimed
- If turnover falls below a certain threshold, a business may de-register from VAT registration

Stamp Duty Reserve Tax (payable on buying shares)

HEADS OF CHARGE	CHARGED ON	RATE
Bearer Instruments	Market Value	1.5%
Purchase of shares	Market Value (only if market value of shares is greater than £1,000)	0.5%

- Bearer instruments are securities where the name of the owner is not recorded. Possession is the only proof of ownership and title passes by physical delivery.
- If the transaction is carried out through an electronic system called CREST the tax is deducted automatically, for other transactions the buyer has to notify HMRC and make the payment.

Stamp Duty Land Tax (SDLT) – on transfer of land

Up to £125,000	0%
On the value between £125,000 and £250,000	2%
On the value between £250,000 and £925,000	5%
On the value between £925,000 and £1.5M	10%
On the value above £1.5M	12%

So, if you bought land with a value of £275,000 the Stamp Duty Land Tax would be:

The first £125,000 @ 0% = £0

The next £125,000 @ 2% = £2,500
Then £25,000 @ 5% = £1,250

Therefore, SDLT in total = £3,750

Please note that there is a 3% addition to these rates if the property purchased is an additional residential property. E.g. buy to let.

Stamp Duty Land Tax and First Time Buyers

- There are new rules currently in place effective as of November 2017 specifically for first time buyers.
- If you are a first time buyer, buying a property for £300,000 or less then no stamp duty land tax is payable.
- If you are a first time buyer, buying a property for between £300,000 and £500,000 then there is a 5% charge on the excess above £300,000.

Corporation Tax

- This is a tax paid by limited companies on their profits.

- Companies are taxed on their profits based on their accounting period which they choose. A company with profits up to £1.5M has 9 months from the end of their accounting period to submit their accounts and pay the tax due.

- Companies with profits over £1.5M can pay their Corporation Tax in quarterly instalments.

- Companies resident in the UK pay tax on their worldwide profits.

Withholding Tax

- This phrase is normally associated to those people who are not residents of the UK but who earn income in the UK such as non-resident entertainers and sportsmen and women.

- The aim is to ensure that this income does not leave the country without being taxed. This is achieved by taxing their income at source at 20%.

- The UK has a 'double taxation' agreement with over 100 countries to ensure that the same income is not taxed twice.

UNIT 1 – TOPIC 4 – TAXATION PART 2			
Question	**Answer**	**Mark**	**Comments / Notes**
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Unit 1 – Topic 4 Test

1 Which one of the following is normally exempt from capital gains tax on disposal?

A A holiday home
B Shares in UK companies
C A unit trust
D An antique table worth £5,000

2 Which one of the following statements in respect of capital gains tax (CGT) is correct?

A Chargeable assets held within and outside the UK may be subject to CGT on disposal.
B Premium Bond and Lottery winnings are subject to CGT because they are classed as unearned income.
C The annual exemption allowance may be carried forward to be used in a later tax year.
D CGT may be payable on a deceased's estate in addition to inheritance tax.

3 Suzy bought an antique Chinese vase in 1985 and recently sold it at an auction at a profit. Which one of the following will she NOT be able to offset against any liability to capital gains tax'?

A The cost of acquiring the vase in 1985
B The cost of a repair to a hairline crack
C Advertising costs
D The auctioneer's commission for the sale

4 Matthew recently sold some unit trusts and made a taxable gain of £6,700. His taxable income for this tax year is £20,000. How much capital gains tax is he required to pay?

A £1,840
B £1,340
C £670
D Nil

5 Which one of the following transactions could be subject to capital gains tax?

A An antique bought by an individual for £20,000 and sold for a profit
B A painting bought by a self-employed dealer for £20,000 and sold for a profit
C An insurance bond bought for £20,000 and surrendered by the original investor at a profit
D Government stocks bought for £20,000 and sold at a profit

6 **Which one of the following disposals may incur a liability to capital gains tax at the time of disposal?**

A A UK resident selling his holiday home in Spain for a profit
B Transfers between spouses who are living together
C Disposals to recognised charities
D The deemed disposal of assets on an individual's death

7 **What exactly are 'allowable deductions' in the calculation of capital gains tax liability?**

A Government fixed allowances against capital gains tax liability
B The annual exemption limit only
C Costs incurred in acquiring, enhancing and disposing of an asset
D The annual exemption limit and the indexation allowance

8 **What is the position when a capital loss is made on disposal of an asset?**

A It is not relevant to capital gains tax calculations
B It must be carried forward to the next tax year to offset against future capital gains
C It can be offset initially against gains made in the year the loss occurred
D It should be carried back to the previous year

9 **A capital gains tax liability could arise in which of the following circumstances?**

A A corporation sells some of its investments
B A partnership's daily trading
C A public limited company's daily trading
D Disposal of assets upon the retirement of a sole trader

10 **Which of the following assets would be exempt from capital gains tax**

A A piece of personal jewellery valued at £20,000
B A Spanish property used for holiday visits
C Euros held for use on foreign holidays
D Shares purchased on the UK stock market

11 **In May 2016 Peter made a gift of £100,000 to his son Paul. Peter died in June 2019 leaving an estate of £350,000. Which IHT rate is applicable to the gift?**

A 0% B 24% C 32% D 40%

12 Julian died in May leaving an estate valued at £350,000. Having made NO gifts or transfers previously he now left half his estate to his son and half to his wife. What was the inheritance tax liability?

A Nil B £43,200 C £30,000 D £140,000

13 On which one of the following would inheritance tax be charged at 40%?

A The total value of the deceased's estate
B The amount of the chargeable estate above the threshold
C The full value of the estate after an individual domiciled in the UK dies intestate
D The value of the estate that remains after the proportion due to the deceased's spouse has been deducted

14 A potentially exempt transfer is best described as:

A a small gift not exceeding £250, made during an individual's lifetime.
B a transfer with deferred inheritance liability provided it is made more than 7 years before death.
C any transfer of any amount between spouses.
D a transfer that bears no immediate charge to inheritance tax irrespective of the amount of transfer.

15 When is the tax due to be paid following a 'chargeable lifetime transfer'?

A Immediately
B After 6 years
C After 7 years
D Following the death of the donor

16 If an individual is domiciled in the UK at the time of death, his estate for inheritance tax purposes would include all assets:

A in the UK only
B in the EC only
C in countries with a double taxation agreement with the UK only
D wherever situated

17 For VAT purposes, businesses that charge fees for giving advice on insurance and pensions contracts are:

A exempt
B zero rated
C subject to half the normal rate of VAT
D subject to the normal rate of VAT

18 Which one of the following is NOT zero-rated from VAT?

A Meals in restaurants
B Food in supermarkets
C Children's clothing
D Supplies of medicine

19 Which one of the following businesses does NOT have exemption from VAT on its supplies?

A Doctors
B Opticians
C Dentists
D Accountants

20 Robert bought some ordinary shares in August costing £100,000. How much stamp duty reserve tax did he have to pay?

A £2,000
B £1,500
C £500
D £1,000

21 What is the stamp duty reserve tax due on a purchase of bearer instruments with a market value of £100,000?

A £500
B £1,000
C £1,500
D £2,000

22 What rate of withholding tax is levied on non-resident entertainers and sportsmen and women in the UK?

A 22%
B 20%
C 40%
D 25%

23 In the event of a transfer on death, where will any liability for inheritance tax payment fall?

A On the donor
B On the deceased's spouse or next of kin
C On the deceased's estate
D On the deceased's life assurance company

24 **Assuming the current annual gift allowance for inheritance tax purposes remains at £3,000, what exemption would be allowed in year four if the individual did NOT make use of the exemption in the preceding three years?**

A None B £3,000 C £6,000 D £12,000

25 **Which one of the following would NOT be considered a liability when calculating an individual's estate at death?**

A	Mortgages	B	Loans
C	Hire purchase	D	Jointly held assets

Unit 1 – Topic 5

State Benefits

Universal Credit

- In an effort to simplify the benefit system, Universal Credit is set to replace much of the present benefits structure.

- This will bring together a range of working age benefits into a single streamlined payment. People claiming benefits will automatically be moved onto Universal Credit from 2013 and this is to be phased in by 2021.

- Benefits covered by universal credit include income support, income based Jobseekers allowance, income based Employment Support Allowance, Working and Child tax credit and housing benefit.

Working Tax Credit

- Purpose is to make work worthwhile for those on low incomes
- Have to be employed or self-employed working at least 16 hours per week

Income Support

- For those aged between 16 and the qualifying age for state pension credit with income below a certain level
- Working 16 hours a week or less, or even not working at all.
- Entitlement not dependent on an individual's NICs but is means tested on both income and savings.

Jobseeker's Allowance (JSA)

- For those who are unemployed but are actively seeking work.
- Must not be working or working less than 16 hours per week
- NIC credits are given for each week that the person receives JSA
- Can be contribution based or income based. Contribution based depends on having paid a certain amount of Class 1 NICs and is paid at a fixed rate irrespective of savings or partners' savings.
- If you don't qualify for contribution based you can get it on the income basis which is income support in all but name.
- Contribution based JSA is paid gross and paid irrespective of any partner's income or savings, but is taxable and paid for 6 months.

Support for Mortgage Interest (SMI)

- Those in receipt of Income Support, Jobseekers Allowance, Universal Credit or Pension Credit can apply for assistance to pay the interest on their mortgage.
- SMI will pay interest on a mortgage of up to £200,000 at a standard rate of interest and it pays direct to the lender.
- It does not cover associated mortgage costs such as insurance premiums, repayment of capital, arrears etc
- SMI is now treated as a loan secured on the property as a second charge and is subject to interest. The loan is repaid when the property is sold or ownership transferred.

Statutory Maternity Pay (SMP)

- Must have been with the same employer for at least 26 weeks including the qualifying week which is 15 weeks before the due date of birth
- Her earnings must not have been less than the lower earnings limit – the level at which NICs start to be payable
- Must have paid a minimum level of Class 1 NICs
- Payable for a maximum period of 39 weeks
- Earliest first payment is 11 weeks before the due date of birth
- Latest first payment is the due date of birth
- Weeks 1-6 - 90% of average weekly earnings paid
- Weeks 7-39 - lower of flat rate or 90% of average weekly earnings
- SMP is taxable and paid by the employer

Maternity Allowance

- For those who are unable to claim SMP such as the self-employed or someone who has recently changed jobs
- Payable for a maximum of 39 weeks
- Earliest payment and latest payment is the same as SMP
- Paid at a lower rate than SMP
- Paid by the Dept. for Work and Pensions and tax free.

Child Benefit

- Tax free benefit for those who have responsibility for bringing up children
- Payable for each child up to the age of 16 (19 if in full time education)
- Are two rates with a higher rate paid for the first child
- Benefit is not based on the claimant's NIC record
- This benefit is now means tested in the form of a tax charge if either partner earns more than £50,000. If the income exceeds £60,000 the tax charge effectively cancels out the benefit.

Child Tax Credit

- Available to the parent who has responsibility for the child’s care designed to help people who are on lower incomes.
- They do not need to be working to claim it.
- Eligibility and the amount awarded depends on personal circumstances.
- It is to be replaced by Universal Credit over the coming years.

Statutory Sick Pay (SSP)

- For employees who are off sick for 4 days or more
- Employers pay the employee and then reclaim from the DWP
- Paid for a maximum of 28 weeks
- Employees earnings have to be above the lower earnings threshold
- After 28 weeks, you may be able to apply for short term incapacity benefit
- Benefits are taxable

Employment and Support Allowance (ESA)

- This replaced Incapacity Benefit as the main long term sickness benefit from October 2008.
- It was intended to transfer all the people from Incapacity Benefit onto ESA by now, but this is still ongoing so some people may still be on incapacity benefit.
- There are two forms of ESA – Contribution based ESA also referred to as ‘new style’ ESA is dependent on NIC record. It is not means tested and the payments are taxable.
- By contrast, income based ESA does not depend on NICs, is means tested but not taxable.
- This new benefit introduced a 13 week assessment period and changes the emphasis by looking at what the claimant can do as opposed to what he cannot do.
- Following the assessment people will be given employment advice and support.
- During the 13 week period a benefit per week is payable.

Attendance Allowance – 65 and overs

- Short term rate – either day or night help. Long term rate – both day and night
- Not based on NIC record
- Not means tested and tax free

Disability Living Allowance/Personal Independence Payments– Under 65s

- Available to those whose disability started between the ages 16-64, but once given it can continue after 65.
- There is a care element and a mobility element
- From April 2013 this benefit is called Personal Independence Payment and those claiming under the old system are to be transferred over.

Carer's Allowance

- For those caring for a severely disabled person and must be between 16 and 65 giving at least 35 hours to the task
- Person being cared for must also be receiving Attendance Allowance or Disability Living Allowance
- Benefit not based on NIC record and are taxable

People in hospital or residential care or nursing home

- When people are in hospital some of the needs intended to be met by state benefits are instead met by the NHS.
- In general terms state benefits will continue to be paid when someone goes into hospital.
- However, in certain limited situations, this could cease after they have spent 52 weeks in hospital.

Basic State Pension

- Available for both men and women from age 65.
- From 2020, the state pension age will then increase to 66 and then to 67 by 2028. In future there will be regular reviews of state pension age, the principle being that people should spend a third of their life in retirement. The first review was in May 2017.
- Provides little more than subsistence
- State pension increases each year by the higher of any increase in National Average Earnings index or 2.5% or the Consumer Prices Index(CPI). This is referred to as the 'triple lock'
- There are additional state pensions – state earnings related pension (SERPs) which was replaced by the state second pension (S2P) but only for employees. Employees are automatically enrolled in this unless they contract out.
- These additional state pensions are only available for people who reached state pension age before April 2016.

Single Tier State Pension

- For people reaching retirement age on or after April 2016, a new state pension system has been introduced which will bring to an end the system of additional state pensions with a single benefit determined by national insurance contributions.
- The maximum benefit is given if you have 35 years' worth of NICs and no pension if you have less than 10 years NICs. This will gradually be phased in over a 5 year period from 2016.

Pension Credit

- Designed to top up an individual's pension entitlement up to a specified amount.

Benefits Cap

- The idea behind this is to have a maximum amount that people are able to claim in relation to state benefits which is to be the maximum level of the average UK wage.

UNIT 1 –TOPIC 5 - STATE BENEFITS			
Question	**Answer**	**Mark**	**Comments / Notes**
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11			
12			
Total			
Result %			**Result % = (Total / 12) x 100**

Unit 1 – Topic 5 Test

1 **Which one of the following client need areas do social security benefits NOT cater for?**

A Pension provision
B Savings
C Loss of income through sickness
D Accommodation

2 **Which one of the following social security benefits is means tested?**

A Attendance Allowance
B Income support
C Statutory maternity pay
D Statutory sick pay

3 **Contribution-based jobseeker's allowance depends on having paid national insurance contributions. Which class or classes of contributions must have been paid?**

A Class 1 or Class 4
B Class 1 or Class 3
C Class 1 only
D Class 4 only

4 **What is the maximum period for which Statutory Maternity Pay (SMP) can be claimed?**

A 11 weeks
B 15 weeks
C 18 weeks
D 39 weeks

5 **Mandy is pregnant with her first baby. She has been a full time self-employed graphic designer for the last two years. What benefit may Mandy be able to claim before her baby is born?**

A Statutory Maternity Pay
B Maternity Allowance
C Child Benefit
D Income Support Payments

6 **To which State benefit would a self-employed person be entitled?**

A Statutory Sick Pay
B Statutory Maternity Pay
C State Second Pension
D Basic State Pension

7 **Mrs. Turner is a lone parent earning £30,000 p.a. What would be the treatment of the Child Benefit she receives?**

A Tax free
B Taxable at the lower rate
C Taxable at the basic rate
D Taxable at Mrs. Turner's marginal rate

8 What is the MAXIMUM amount of time Statutory Sick Pay can be claimed?

A 26 weeks B 28 weeks C 30 weeks D 32 weeks

9 A tax-free weekly cash benefit for people disabled at or after age 65 who need a lot of looking after. Which Social Security benefit does this describe?

A Invalidity benefit
B Severe disablement allowance
C Attendance allowance
D Disability living allowance

10 Which one of the following statements in respect of Jobseeker's Allowance is correct?

A A claimant must be out of work or working less than 16 hours per week
B A male claimant must be between the ages of 16 and 60 to apply
C A claimant must have not more than £2000 in savings to be able to benefit
D A claimant must not be in receipt of earned income or investment income

11 What is the maximum period for which Maternity Allowance can be claimed?

A 11 weeks B 15 weeks
C 18 weeks D 39 weeks

12 Contribution-based jobseeker's allowance is payable for a MAXIMUM of:

A 3 months B 6 months
C 1 year D 2 years

Unit 1 – Topic 6

Direct Investments : Cash & fixed interest securities

Bank and Building Society Accounts

Banks and building societies offer accounts which fall into two main categories, current accounts and savings accounts:

Traditional Current Accounts

- For most people the main type of bank account that they would have. This type of account enables people to pay money in, take money out either electronically or via an ATM or by writing cheques. An automatic overdraft is often given by the bank as well.
- Some banks offer current accounts with additional benefit packages such as breakdown, travel insurance etc. for a monthly fee, called a packaged account.
- Interest can also be paid on current accounts.

Basic Bank Accounts

- For people who are on low incomes or have very poor credit history may be refused a normal current account but they will be able to take out a basic bank account.
- The major difference with these is that there is no overdraft facility and no chequebook.

Savings Accounts

- When a lump sum or capital is placed in a deposit account, its value is increased through interest.

- Inflation however will reduce the real value of this amount over time.

- A suitable account to have for short term, easy access savings and especially useful for an ‘emergency fund’ to cover an unforeseen problem – rainy day money.

- This sort of account is considered to be desirable for an individual who has spare money for the first time in his/her life.

- Interest - pays interest on a daily basis- credited monthly, quarterly, half yearly or annually. May be a notice period for the withdrawal e.g. 30 or 60 days – the notice could be waived but there would likely be a penalty equal to the amount of interest that would have been earned.

- Term accounts – the money may be locked away for a period of 1-5 years, sometimes in return for a fixed rate – the longer the term and/or higher the amount held, the higher the rate of interest.

- Fixed term bonds – offers a fixed rate of return if money is saved for a fixed term. Typically, there is no access at all during the period but again offer a higher rate of interest.

Offshore Deposits

- These accounts are based outside the UK in places such as the Channel Islands

- These offer the potential of a higher return but they are also higher risk. This is because they are not protected by the Financial Services Compensation Scheme (FSCS) and also due to currency movements.

- The FSCS protects up to a level of £85,000 per investor per provider should the UK bank or building society become insolvent.

- Overseas interest is taxable for UK residents so they are required to declare the income to HMRC and pay tax at their marginal rate, or in other words their highest rate of income tax.

- They may be able to claim relief from some or all of this, if it has been taxed at source overseas under the double taxation rules.

Cash ISAs

- Available to UK residents 16 and over and can only be held in a single name.

- Interest is paid tax free on the current investment limit of £20,000 per annum.

- There is no fixed term and withdrawals can be made at any time

National Savings & Investments

There are a range of these different accounts which are offered on behalf of the government. These are all low risk as the capital is not at risk.

NS&I – Direct Saver

- Available for individuals : aged 16 or over
- Minimum investment : £1
- Interest : variable
- Tax treatment : **interest** paid gross but taxable

NS&I - Investment Account

- Available for individuals : minimum age 16
- Interest : variable rate, tiered rates
- Investment : £20 to £1M
- Tax treatment **: interest paid gross but taxable**

NS&I - Income Bonds (regular monthly income)

- Available to individuals : over 16
- Investment : £500 minimum to £1M maximum
- Interest rate : variable
- Tax treatment **: interest paid gross but taxable**

NS&I – Guaranteed Income Bonds

- Term : 1 and 3 years
- Available for : aged 16 or over
- Investment : £500 to £1M
- Interest : fixed
- Tax treatment **: interest paid gross but taxable**

NS&I – Guaranteed Growth Bonds

- Term : 1 and 3 years
- Available for : aged 16 or over
- Investment : £500 to £1M (£2M joint)
- Interest : fixed rate of annual growth
- Tax treatment **: interest paid gross but taxable**

NS&I - Premium Bonds (tax free)

- Potential gain through a regular tax-free prize draw with prizes of up to £1million per month.
- Investment : £50,000 maximum
- Interest : no interest is paid

- Available : Anyone over 16 or can be bought for anyone under 16
- Withdrawal : anytime but 8 working days' notice should be given
- Tax : winnings are **TAX FREE**

Fixed Interest Securities

Gilts

- Issued by the government to raise money

- Low risk investment as the government will not default on the interest or the capital return

- Coupon – this is the rate of interest that will apply throughout the term

- Interest – paid half yearly on the par value of the gilt

- Redemption Date – this is the date the government will repay the capital

- Short Dated Gilts – from 0 to 5 years to run according to the financial press

- Medium Dated Gilts – from 5 to 15 years to run according to the financial press.

- Long Dated Gilts – over 15 years to run according to the financial press

- Undated gilts have no redemption date and need to be sold on the open market to recover the capital. The Government have the discretion but no obligation to redeem (repay) the capital at any point.

- Gilts are issued by the UK Debt Management Office who actually define short dated gilts as 0-7 years and medium dated as 7-15 years.

- As with shares gilts can be sold for amounts above or below their par value. Movements or anticipated movements in interest rates could affect the market value of that gilt as will the amount of time left on that gilt, and supply and demand.

    - If for example, a gilt was quoted as Treasury Stock 2020 @ 9%, then if interest rates at that time were low, then that guaranteed 9% rate could be attractive to other investors and they could be prepared to pay more than the face or par value of that gilt.

- When the redemption date is reached the government will only pay the par value of that gilt.

- Gilts can be fixed interest or index linked.

- If it is index linked BOTH the capital value and the interest rate will move in line with inflation.

- On sale of a gilt, they are quoted either:

  - Cum dividend – new purchaser receives the next interest payment
  - Ex-dividend – seller receives the next interest payment

- Gains made on the sale of a gilt are exempt from CGT

- Interest is paid gross, (although you can choose for the interest to be taxed at source) and then taxed as savings income so:

  - BRTP pay 20%
  - HRTP pay 40%
  - Additional Rate taxpayer pays 45%

Local Authority stocks/bonds

- Similar to gilts except they are from a local authority where your investment is secured on local authority assets.

- Term is fixed as is the rate of interest paid half yearly

- These are not negotiable and cannot be sold on the open market

- Not quite as risk free as gilts and no government guarantee is provided.

- Interest is paid net of income tax.

Permanent Interest Bearing Shares

- PIBS are from Building Societies to raise capital.

- Interest is fixed and paid half yearly.

- PIBS not covered by the Financial Services Compensation Scheme and therefore rank behind account holders in priority of payment should the building society become insolvent.

- Interest is paid gross.

Corporate Bonds

- Issued by companies to raise money.
- Fixed rate of interest, a fixed redemption date and a fixed return.
- Like gilts, they can be bought and sold for amounts above their 'face value'
- A much higher risk than gilts but potentially a higher reward
- The bonds may be secured or unsecured.
- If it is secured, it is referred to as a **debenture** and therefore a charge is made against the company's assets these are secured against the company's assets. Debenture holders have priority over other creditors on liquidation.
- If the corporate bond is unsecured, sometimes called loan stock, the investor ranks with the other ordinary creditors.
- The interest payment is paid net of income tax.
- Some corporate bonds give the holder the right to convert the loan to ordinary shares but there is no obligation to do so.
- Whether the bond is secured or not, the holders of these type of debt take priority over the shareholders on liquidation.

Eurobonds

- A Eurobond is a type of fixed interest investment that uses a different currency. E.g. a UK company night offer a Eurobond in Germany based in US dollars.

'Alternative Finance'

- Sometimes called 'peer to peer' lending (P2P), this involves a saver placing their money with a lender who will then lend out money to businesses that are seeking funding. E.g. Funding Circle.
- The returns can be very good but the risks are that the returns would reduce if repayments on the loan by the business are missed. Also, there is no Financial Services Compensation Scheme protection for these schemes.

UNIT 1 – TOPIC 6 – FIXED INTEREST			
Question	**Answer**	**Mark**	**Comments / Notes**
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	Result %		**Result % = (Total / 19) x 100**
NOW TRANSFER YOUR RESULT TO PERFORMANCE TRACKER 1			

Unit 1 – Topic 6 Test

1 Which one of the following client need areas are bank and building society accounts BEST equipped to provide for?

A Rainy day money
B Savings for those who want a guaranteed real return on their money
C Long term regular savings
D Pension provision

2 Which one of the following would be regarded as an advantage of a building society savings account?

A A high rate of interest reflecting the risks involved
B Regular interest payments and security of capital
C The potential for capital growth with high risk
D A tax-free return but no guarantee of performance

3 Income tax is not payable on which one of the following forms of income?

A Winnings on Premium Bonds
B Income from local authority stocks
C Tips
D Inventor's income from copyright or patent

4 A new gilt issue has been referred to as medium dated in the financial press, however the UK Debt Management Office has described it as short dated. It will therefore be for which of the following terms?

A Two years
B Four years
C Eight years
D Six years

5 Which type of investment would be MOST suitable for a non-taxpayer requiring monthly income with NO risk to capital?

A Gilts
B National Savings Income Bonds
C National Savings Certificates
D An annuity

6 What is the maximum total investment into Premium Bonds?

A £30,000
B £50,000
C £3,600
D £20,000

7 **Barry owns £5,000 of premium bonds. Which one of the following is FALSE?**

A His recent £1,000 winnings are tax-free
B He must give 3 months' notice if he wants to encash them
C He may purchase another £15,000 of bonds
D There is no interest rate paid on premium bonds

8 **Which of the following statements in respect of gilts and local authority stock is true?**

A Interest on local authority stock is subject to capital gains tax
B Local authority stocks are not negotiable and carry a government guarantee
C Interest on gilts is paid without deduction of income tax but is taxable
D Gilts are negotiable and any gain may be subject to capital gains tax

9 **Which one of the following is LEAST likely to affect the price of gilts?**

A The time outstanding until redemption date
B The length of time it has been held for
C Current market interest rates
D Anticipated changes in interest rates

10 **What rate of capital gains tax, if any, would a basic rate taxpayer be liable to on gains made from gilts?**

A 22% B 20%
C 18% D Nil

11 **Why would a client want to know the 'coupon' of a gilt?**

A It gives an indication of the total income and capital growth that can be expected
B It is the amount of capital that will be repaid
C It is the income payment that will be received
D It is the purchase price required

12 **According to the financial press, the term to run before redemption under a medium-dated gilt is between:**

A 3 and 5 years B 5 and 10 years
C 5 and 15 years D 10 and 15 years

13 **What is 'index-linked' on an index-linked gilt?**

A The coupon rate only
B The redemption price only
C The price throughout the term and the redemption price
D The coupon rate and the redemption price

14 What returns can be achieved on an investment into gilts?

A The capital will remain intact and interest will be added in line with prevailing interest rates
B A fixed rate of interest will be paid during the term and the investment can be sold at any time to realise capital
C There is potential for high capital and income growth but the value of both may fluctuate in the short term
D Both capital and income returns will accumulate and be payable free of all UK taxes

15 Which one of Belinda's needs would direct investment in gilts be UNABLE to satisfy?

A Fixed income
B Low risk investment
C Return free of capital gains tax
D Income free of higher rate income tax

16 Which one of the following organisations issues permanent interest bearing shares?

A Companies quoted on the London Stock Exchange
B Building societies
C Local authorities
D The Bank of England

17 Derek has invested in undated gilt-edged securities. This means that:

A the interest will be paid net of lower rate income tax.
B he will have to sell them on the open market to access his capital.
C the government will pay no interest until the holding is sold.
D the government will redeem the holding at anytime, if Derek requests it.

18 The principle difference between corporate bonds and gilts is that corporate bonds:

A usually pay variable rate interest
B are available for larger amounts
C normally have no specified redemption date
D are considered to be higher risk investments

19 A key difference between a debenture and a loan stock issued by a company is that a debenture:

A holder has the right to vote at the company's annual general meeting.
B is usually secured on the assets of the company.
C can be converted to ordinary shares in the company.
D pays a fixed rate of interest

Unit 1 – Topic 7

Other direct investments

Equities and Other Company Finance

Ordinary Shares

- People who hold ordinary shares have two main rights

    - To receive a share of the profits through dividends
    - To vote at shareholders' meetings

- Investment in shares is high risk as there is a danger of losing all your capital investment. This risk can be reduced through 'diversification' which involves spreading that risk among a number of companies.

The Stock Market

The Stock Exchange is the market for selling shares and is both a primary and secondary market.

- A primary market is when shares are created originally usually via a 'flotation'
- A secondary market is where investors buy and sell existing shares.

The Main Market

- A full listing is only available to very large companies able to meet certain requirements such as having at least 25% of the share capital in public hands and having been trading for at least 3 years.

The Alternative Investment Market

- This is for newer, smaller companies and the membership rules are less strict
- There is therefore greater growth potential in investing in these companies
- Investment in these companies is considered higher risk
- By joining the AIM the profile of these companies will be enhanced

Market Indices

It is easy to follow the overall performance of shares by following one or more of the various indices that are produced:

- FTSE 100 – top 100 companies measured by market value
- FTSE 250 – the next 250 companies in the list after FTSE 100
- FTSE 350 – combination of FTSE 100 and FTSE 250
- FTSE All Share – top 900 companies split into sectors.

Risk and Reward

- Shareholders have no liability for the debts of the company. The company itself is liable for those debts as it is a separate legal entity.

- The shareholder will lose what he has invested into that company if the company goes into liquidation

- Shares are considered high risk-high reward

- Over time however, shares and other asset backed investments have outperformed the deposit based investments

Financial Returns from Shares

There are 2 ways in which people are interested in investing in shares:

Income – in receiving an annual income through distribution of dividends

Capital – through seeing the growth of the share price leading to eventual encashment for a profit.

- Companies are not obliged to distribute dividends to shareholders. They may choose to do so in order to generate interest in that company by other prospective investors.
- When dividends are to be paid there are ways of judging the success of that investment:

    - Earnings per share – net profit divided by the number of shares

    - Dividend Cover – where a company pays 25% of its profits in dividends that dividend is said to be covered 4 times. Where a company pays 50% of its profits in dividends it is said to be covered 2 times. A dividend cover of 2.0 or more is considered acceptable. A dividend cover below 1.0 could be indicating that the company is paying dividends from profits from previous years from retained surpluses.

    - Price/Earnings Ratio – Share Price divided by Earnings per share. Shares with a low P/E Ratio (less than 4) have poor growth prospects. Shares with a P/E Ratio of 20 or more are considered growth stocks, so the indicators are showing that these shares with a high P/E ratio are likely to continue to rise.

- Gains made on the sale of shares are subject to CGT

- Dividends received from the profits of company to shareholders are paid without deduction of income tax and as discussed earlier, there is a £2,000 dividend allowance.

- If dividend income exceeds the allowance, further tax would have to be paid via self-assessment (see topic 3).

Rights Issue

- When a company issues more shares to existing shareholders at a discount. The existing shareholder does not have to take up the option. Stock Exchange rules require that when a company has shareholders and they are looking to raise capital by issuing more shares, those shares must be offered to existing shareholders first.

Scrip Issue/Bonus Issue/Capitalisation Issue

- Issue of new shares to existing shareholders for free. No additional capital is raised here. Effectively, the number of shares is increased and the share price is reduced. Often awarded to employees of a company.

Preference Shares

- They rank above ordinary shareholders when dividends are paid out and on liquidation

- Dividends are **generally** but not always fixed

- These shares do not usually carry voting rights but they could acquire them if dividends have been delayed

- Cumulative Preference – this means that if dividends are not paid, the entitlement is accumulated until they are paid.

Convertible Preference Shares

- These are traditionally corporate bonds issued by a company when they want to raise capital which carry the right to be converted at a later date to ordinary shares.

- However, in recent years they have been increasingly issued as convertible preference shares.

Warrants

- Warrants give the holder a right to buy the company's **ordinary** shares at a fixed price at an agreed future date.

- The attraction is that they give the holder the possibility of buying the shares at a fraction of their true worth on that agreed future date.

- The warrant confers the right to buy the shares at a **fixed price** on or before a specified date, i.e. **while the warrant is exercisable**. If the prevailing share price is higher than the warrant price at the time of the purchase, the warrant holder can realise a profit.

- If the share price on that future date is below the price offered by the warrant, then it will not be worth exercising the warrant and it will lapse.

Investment Property and Buy to Let (BTL) Mortgages

- Investment in property has become very popular for the following reasons:

    - Rents and house values tend to move in line and above the rate of inflation providing built in indexation
    - An acceptable form of security when borrowing money

- Some of the disadvantages are:

    - Periods without tenants
    - Recessions can make that property difficult to let
    - Investment costs can be high e.g. Stamp Duty, legal fees
    - Property may not be as easily marketable as other investments, or in other words it may take time to sell that property – 'illiquid'
    - As with shares, investment property could be seen as risky for the small investor. For those with smaller amounts of capital, property bonds might be appropriate whereby the fund is invested in a range of properties and shares in property companies which means you are spreading the risk.

- Income from property is subject to income tax after deduction of allowable expenses.

- On disposal, any gain is potentially subject to CGT

- Historically, lenders have viewed these as commercial loans and therefore there has usually been a higher interest rate

- The Government has introduced some measures that could limit the attractiveness of the buy to let market which include:

    - Second properties are now subject to a 3% stamp duty surcharge
    - The wear and tear allowance of 10% has been replaced. The rules only allows the actual cost of replacement of furnishings to be offset against profits
    - Previously, a BTL landlord could deduct the full cost of mortgage interest from the rental income when calculating profits. This has changed from 2017 with the new rules phased in over the next 3 years.

- There is also the option to invest in commercial property which is defined as any property that is not wholly residential.

- Commercial properties tend to provide reasonably high rental income with normally steady growth in capital value. However, interest rates may be higher than for residential loans.

Money Market Instruments

This is the generic term to describe a number of forms of short term investment. Interest is not normally paid during the term of the transaction, but there will be a form of interest in the difference between the amount invested and the amount repaid.

There are various types of these:

Treasury Bills

- Like gilts these are issued by the Treasury's Debt Management Office, but they differ from gilts in that:

    - They are for short terms normally 91 days
    - They are 'zero coupon' securities so no interest is paid and are instead issued as a discount to the par value.

- Like gilts, these are very low risk as the government will not default on the return
- These are usually purchased in very large amounts and therefore are of little interest to the small investor
- As with gilts, they can be bought and sold on the secondary market.

Certificates of Deposit

- These are short term investments typically for periods of 3-6 months for larger amounts of money usually in excess of £50,000.
- They are issued by banks and building societies on a fixed rate of interest which will be paid along with a return of capital at the end of the term.

Commercial Paper

- This is used by some businesses that are looking to raise money to get some working capital.
- The commercial paper is an unsecured ‘promissory note’ to repay the capital plus interest.
- The transactions are usually for very large amounts.
- There may well be a letter of credit from a bank which guarantees to make repayment if the borrower defaults.
- The term is usually up to 45 days

UNIT 1 – TOPIC 7 – OTHER DIRECT INVESTMENTS			
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Result %			**Result % = (Total / 16) x 100**
NOW TRANSFER YOUR RESULT TO PERFORMANCE TRACKER 1			

Unit 1 – Topic 7 Test

1 **If a company distributes 25% of its profits what would the dividend cover be?**

A 4 B 8 C 10 D 25

2 **Which one of the following is NOT a feature of ordinary shares? The shareholder:**

A has the right to vote at annual general meetings.
B has the right to receive a share of the profits.
C is liable for the debts of the company.
D ranks after preference shareholders.

3 **When considering investing in residential property, which one of the following characteristics is UNTRUE?**

A Costs associated with property investment are generally high
B Rental income provides a poor hedge against the impact of inflation
C There may be periods when suitable tenants are difficult to find
D The capital value of the property may fall

4 **Bank deposit accounts are NOT generally considered to be suitable vehicles for long term investment because they:**

A pay interest net of lower rate tax.
B have proven unattractive when compared with asset-backed investments.
C are generally only suitable for higher rate tax payers.
D normally have a maximum investment term.

5 **Which of the following types of share is most commonly a convertible over recent years?**

A Cumulative
B Ordinary
C Redeemable
D Preference

6 Which one of the following statements concerning preference shares is FALSE?

A They are a part of the share capital of the company
B They normally rank before ordinary shares for dividends
C The dividends are always fixed
D Convertible shares are a type of preference share

7 What is the main attraction of direct investment in the ordinary shares of quoted companies?

A Dealing costs are lower than those charged by unit trust fund managers
B Dividends are guaranteed to be paid and are tax-efficient for higher rate taxpayers
C Potential capital growth in the medium to long term
D The selling price of shares is usually the same as the purchase price, thus removing the bid/offer spread

8 Jon purchased a share when the price was very high. He was able to justify this because:

A the price earnings ratio was also high.
B the dividend cover was 0.80.
C the dividends had decreased.
D the price has increased by more than 25% in two years.

9 If Helen invests in shares, which are quoted in the Alternative Investment Market, her shares:

A are likely to be in new, small companies with growth potential.
B must be held by her for at least one year before they can be sold.
C have a minimum guaranteed capital value.
D will provide a fixed income for the first five years.

10 James has a residential property from which he generates a rental income. When he has to pay tax on the income he can:

A opt to pay a flat rate of tax on the gross income.
B offset any income tax due against any fall in the capital value of the property.
C deduct certain expenses to reduce the tax due.
D defer payment of any tax until the property is sold.

11 Why would an investor be interested in holding warrants issued by a company?

A Because investors can receive dividends without having to make any capital outlay
B Because investors can receive shares without having to make any capital outlay
C Because, if the value of the connected shares falls, the investor can claim a loss that can be offset against capital gains made elsewhere
D Because, if the price of the shares has increased at the time a warrant is exercisable, the holder will make a profit on their sale

12 Alec Enterprises intends to raise additional finance by issuing more shares. They are therefore obliged to:

A make a rights issue
B delay dividend payments
C guarantee no existing shareholder will be adversely affected
D make at least 25% more shares available

13 The risk of investment fluctuations can be reduced through which feature of the investment process?

A Clustering
B Dynamisation
C Diversification
D Gearing

14 Greg decided to invest in cumulative preference shares as he wanted to ensure:

A guaranteed security
B conversion to ordinary shares
C capital growth
D some certainty regarding future dividend payment

15 A right to buy shares at a specified price by a specified date is a:

A forward contract
B warrant
C put option
D future contract

16 A company is paying a dividend that has a dividend cover of 0.95. This primarily indicates that it:

A has reduced its payment compared with last year
B is highly profitable
C will be paid out of retained surpluses
D is quoted on the Alternative Investment Market

Unit 1 – Topic 8

Collective investments

Collective Investments

- Collective investments allow small investors to contribute to a large investment fund.
- This has many advantages:

    - A top class fund manager can be used with the cost shared by all investors
    - No research is needed by the investors- fund manager is an expert
    - The risk is spread through investment in a range of funds
    - Fund managers can negotiate reduced dealing costs
    - Wide choice of funds in which to invest

- Collective investments are categorised as having 'medium risk profile'.

- You can have actively managed funds where a fund manager is intervening and making individual decisions on a regular basis as to the buying and selling of assets.

- You can also have a passively managed fund which might be set up just to follow a stock market index such as the FTSE 100.

- You can have collective investments where the primary objective is capital growth at the expense of income or you can set up to produce a high level of income with modest capital growth or you could have a balance between the two.

Unit Trusts

- A pooled investment – large numbers of investors contribute to a large single fund

- A Trust Deed sets out the powers of the Trustees & fund manager

- Trust Deed places legal obligations on both trustees & fund manager

- The fund value is divided into units with the actual unit price being a small fraction of the total value in the fund

- Unit Trusts are **open ended** with the fund manager able to create more units in response to demand thereby increasing the size of the fund.

- Unit trusts can be equity unit trusts where the underlying investment is in shares and therefore any income that comes from the unit trust is treated as dividend income and therefore subject to dividend taxation rules.

- Or it could be categorised as a fixed interest unit trust, where the underlying investment is into interest bearing accounts and therefore any income is treated as interest and therefore subject to savings interest taxation rules.

Role of the Fund Manager

- Fund Manager is responsible to the trustees
- Manages the trust fund and values the assets
- Sets the price of the units
- Sells units to investors
- Buys back units from unit holders

The fund manager is obliged to buy back units from investors when the investor wants to sell.

Role of the Trustees

- Trustees are often high street banks and have a role to ensure fund managers comply with the Trust Deed.
- Trustees also have to ensure that there is sufficient investor protection in place in order to comply with the FCA.
- Approve marketing material and issue the certificates to investors.

Pricing of Units

- There are three important unit prices:

  - Offer Price – Fund Manager sells to investors at this price

  - Bid Price – Fund Manager buys back from unit holders at this price

    - The difference between the two prices (3-5%) represents the management charge for the fund manager – **bid/offer spread**

  - Cancellation Price – this is the minimum permitted bid price. When there are investors both buying and selling the bid price will generally be higher than this. If there are more people selling than buying the cancellation price may be used.

- Please note that some unit trusts are now being set up without a bid/offer price to avoid confusion with investors but there may be an exit charge with these, if they are sold within 3-5 years.

Historic and Forward Pricing

- Historic – units are sold at the previous day's valuation – rarely used

- Forward – units are sold at the next valuation (at the end of the day). This is the most common method.

Buying and Selling Units

- Fund Managers have to buy when the unit holders want to sell.

- Units can be bought over the phone or by writing

- Purchasers receive a Contract Note from the fund manager and a Unit Certificate from the trustee. The certificate is proof of ownership

- When selling, the unit holder signs the renunciation section on the back of the certificate and sends it to the fund manager.

Charges

- Bid/Offer Spread
- Annual Management Charge e.g. 0.5 to 1.5% - may be called a monthly charge

Unit Types

- Accumulation – where the objective is capital growth – any income is reinvested

- Distribution – designed to produce income through dividends to the investor

Taxation of Unit Trusts

- Income received from equity unit trusts is classed as dividend income and is subject to dividend taxation rules as discussed earlier.

- Taxation of income from a fixed interest unit trust sometimes referred to loosely as a non-equity unit trust will be classed as savings income and the interest is paid gross. If the interest exceeds the personal savings allowance, then tax is payable via self assessment at the appropriate rate according to your tax band.

- A fixed interest unit trust is defined as having at least 60% of the investment in interest bearing investments such as gilts, corporate bonds, interest accounts.

- Gains within the fund in the hands of the fund manager are exempt from CGT. However, when the unit holder sells the unit, they are subject to CGT.

- Whilst we can't say that unit trusts have no risk, because the investment is spread among between 30 and 150 companies the risk element is considered to be medium.

Investment Trusts

- These are not actually trusts at all but investment companies whose business is to invest in stocks and shares

- Investors buy shares in the investment trust company. The investment trust is not actually FCA authorised like a Unit Trust is, but must meet FCA requirements to be listed on the stock exchange.

- **The share price can sometimes be sold at a discount to its 'net asset value' (NAV) which gives the potential for greater returns.**

- As with all companies, the number of shares available remains constant so an investment trust is regarded as 'close ended' as opposed to unit trusts which are open ended.

- The other advantage they have is that investment trusts are able to benefit from **'gearing'** which is the ability to borrow to further investment aims. This gives the ability to enhance the growth potential in a rising market. However, in a falling market losses can be increased. This is not available to unit trusts except over shorter terms based on future cash inflows.

Investment trusts and Split capital investment trusts

- With investment trusts, the standard rule is that at least 85% of the income generated must be passed on to the shareholders as dividends. The exception to this rule is if it has been set up as a split capital investment trust.

- Split level trusts or split capital trusts or ‘splits’ are fixed term investment trusts offering two or more different types of share are offered. The most common are:

    - Income shares – receive the whole of the income generated but no capital growth.

    - Capital shares – receive no income but receive all the capital growth

- Real Estate Investment Trusts (REITs) allow private investors to invest more tax efficiently in property in the form of an investment trust without the risks associated with direct property investment.

    - They will pay no corporation tax provided that:

        - At least 75% of income is from rent
        - At least 90% of net profits go to the shareholders
        - No individual shareholder to own more than 10% of the shares

Taxation of Investment Trusts

- Investment Trusts from a dividend taxation point of view are treated in exactly the same way as Unit Trusts and stocks and shares.

- CGT would potentially apply on the sale of the shares in the normal way

Open Ended Investment Companies (OEICs)

- This is another type of collective investment

- Have similarities with Unit Trusts in particular

- Unable to ‘gear’ – borrow to further their investment aims

- Established under company law so not a trust

- They are overseen by the depositary which could be a bank as opposed to trustees

- The authorised corporate director performs the same role as the fund manager for a unit trust

- Can have different types of OEIC including income, capital growth, fixed interest, overseas and specialist markets

Investing and Pricing

- Investors buy shares in an OEIC which is open ended which means that more shares can be created to meet demand.

- The OEIC can invest in a variety of funds and switches between funds are common.

- **OEIC shares are single priced so no bid/offer spread.**

- OEIC shares tend to be priced on a ‘forward’ basis.

OEIC Charges

- Initial Charge – no bid/offer spread but a separate charge is taken between 3-6% of the investment.
- Annual Management Charge – 0.5% to 2%
- A dilution levy which is a potential cost when you sell.
- Other administration charges may also be deducted from income.

Taxation of OEICs

- Taxation of OEICs is identical to unit trusts and investment trusts. If the OEIC is based offshore a UK resident is still liable.

	UNIT TRUST	INVESTMENT TRUST	OEIC
KEY FEATURES	-Trustee oversees the trust. -Trust is open ended -Value of the fund is divided into units. -Fund Manager buys and sells the units . -No ability to gear up	-Investors purchase shares in the investment company -Not open ended -May be available at a discount. -Inv Trusts benefit from gearing	-Depositary oversees the OEIC. -Investors purchase shares -OEIC is open ended -No ability to gear up
TAXATION OF DIVIDENDS	Dividend taxation rules apply	Dividend taxation rules apply	Dividend taxation rules apply
CGT LIABILITY	Investor - YES	Investor - YES	Investor - YES

Non-mainstream pooled investments

- The previous examples of collective investments can be sold to the general public, if they adhere to the rules set out in the FCA handbook.

- There are, however, some unregulated collective investments (UCIS) that have the freedom to invest in non-traditional schemes such as wine, classic cars, crops etc.

- These are only considered suitable for a very small group of high net worth individuals.

Friendly Society Plans

- These are also collective investments and they do have tax advantages, but the maximum investment is £270 per year lump sum or £25 per month or £75 per quarter for a 10 year term. There is no tax on encashment.

Investment Bonds

- These are single premium, unit linked, non-qualifying whole of life policies

- In order to be qualifying, the policy must:

    - Premiums must be payable for at least 10 years or three quarters of the original term if less than 10 years.
    - The premium must be a regular premium, at the very least payable annually.
    - Premiums in any one year must not exceed twice the premiums in any other year.
    - The sum payable on death must be at least equal to 75% of the total premiums payable.

- An investment bond is non qualifying because it is a single premium.

- Premiums paid into a life assurance policy such as investment bonds are invested into different assets such as property, shares etc. All the benefits that come out of the policy are deemed to have already been taxed at 20% within the fund.

- If the policy was to be regarded as ‘qualifying’ this would mean that the pay out from these policies is tax free. Endowments and other life assurance policies are usually regarded as ‘qualifying’.

- An additional tax liability may arise if the policy is ‘non qualifying’ if the person is a higher rate taxpayer.

- Investment Bonds are therefore counted as non-qualifying.

- A single premium or lump sum purchases units in a specified fund or funds.

- This investment can be cashed in or surrendered for a value equal to the bid value at that time.

- If you die before surrender an enhanced amount is paid out, typically 101% of the bid value.

- Switching between funds is allowed without any penalty.

Taking an income from Investment Bonds

- These are intended for capital growth, but it is possible to take an income through ‘partial surrenders ‘of capital.

- Up to 5% of the original investment may be withdrawn each year up to a total of 20 years without incurring an immediate tax liability even for HRTPs. This is referred to as ‘tax deferred’.

- This tax deferred feature is attractive to HRTPs as they can defer that liability to retirement when they may then be a BRTP.

Taxation

Withdrawals

- Basic rate income tax at 20% is deemed to have been paid from the fund itself so there will be no further income tax liability for a NTP or BRTP on those ‘partial withdrawals’.

- If a HRTP or Additional Rate tax payer (ARTP) who took 5% income per year and deferred the tax liability to a later date, and they are still a HRTP or ARTP at that point, they will have to pay a further 20% or 25% respectively.

- The 5% allowance per year, if not used, can be carried forward and accumulated up to 100% of the original investment.

- If they were a HRTP/ARTP when they took the 5% withdrawals and they deferred the tax to a time when they are no longer a HRTP/ARTP, then there will be no further liability.

On sale or surrender

- As the tax is deemed to have been settled within the fund at 20%, therefore, when the bond is surrendered if the bond holder is a NTP or BRTP there will be no further liability.

- If however, the bond holder is a HRTP/ARTP there may be a charge of a further 20%/25% which is income tax not capital gains tax.

Structured Products

- The characteristic of these is that they offer an element of protection of the capital (up to 100%) while offering the chance to benefit from the growth in the stock market.

- They appeal to investors who are wary of the downside of the stock market but who would like to share in its growth possibilities. These are often called Non Structured Capital at Risk Products or (Non SCARPS).

- However, there are other types of structured products where the return of capital is not guaranteed if a stock market index such as the FTSE fell sharply, as happened in the last few years. These are called Structured Capital at Risk Products or (SCARPs).

UNIT 1 – TOPIC 8 – COLLECTIVE INVESTMENTS			
Question	**Answer**	**Mark**	**Comments / Notes**
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Total			**Result % = Total / 24 x 100**

Unit 1 – Topic 8 Test

1 When managing unit trusts what does the term 'open-ended' mean?

A That clients can buy more units
B That the fund manager can create more units
C That the fund manager does not need to value the units
D That there is flexibility in the taxation arrangements of units

2 Which of the following statements is correct in respect of a unit trust?

A Any gain made on the sale of units by an investor may be liable to capital gains tax
B The fund manager is able to borrow
C An investor who requires mainly capital growth will be best advised to purchase distribution units
D The price at which an investor purchases units in the fund is referred to as the bid price

3 Historically, charges on unit trusts have generally comprised:

A a bid offer spread only
B an annual management charge only
C an annual management charge and a policy fee
D a bid offer spread and an annual or monthly management charge

4 Which one of the following statements is FALSE of unit trusts?

A They can be used to provide a balance of regular income and capital growth
B They will always provide a high rate of return in the short term
C They should be viewed as a long-term investment
D They can be used to plan for school fees

5 What are the regular payments made out of investment trusts known as?

A Distributions
B Coupons
C Allocations
D Dividends

6 Under a unit trust what does the cancellation price represent?

A The maximum price at which a full encashment of the units may be made
B The minimum price at which investors may cash in their units
C The price applicable to investors if they cancel during the cooling off period
D The price at which the manager will buy back units if underlying assets do not have to be traded

7 Unit trusts are strictly governed by a set of terms. In what document are these terms defined?

A Trust Certificate
B Trust Deed
C Contract Letter
D Contract Note

8 Which one of the following is NOT the responsibility of a unit trust fund manager?

A To establish the cancellation price of units
B To buy back units from clients when they wish to sell
C To manage the trust fund's investments
D To ensure that the trustee complies with the trust deed

9 At what rate would capital gains tax be charged on gains made on the sale of a unit trust investment by a higher rate taxpayer?

A 10% B 18% C 22.5% D 20%

10 Who is responsible for paying capital gains tax from unit trusts to HMRC?

A The unit holder
B The trustees
C The unit trust company
D The fund managers

11 Which one of the following BEST describes an investment trust?

A A unit linked single premium non-qualifying whole-of-life policy investing solely in shares
B A trust which invests solely in shares in the Alternative Investment Market
C A company which invests in shares of other companies
D A partnership which invests in gilt-edged securities

12 What is the MAXIMUM amount, if any, that an individual can invest in an investment trust in any one tax year?

A £3,000
B £6,000
C £9,000
D Unlimited

13 Gains made within an investment trust are subject to what tax, if any, in the hands of the fund managers?

A Basic rate tax
B Capital gains tax
C Corporation tax
D None

14 If the shares of an investment trust stand at a discount below the net asset value per share, which one of the following is CORRECT?

A Capital growth is potentially higher than direct investment
B A minimum level of capital growth is guaranteed
C Capital growth will be negligible
D Income growth is forsaken for capital growth

15 Which one of the following is TRUE of open-ended investment companies (OEICS)?

A Switches are made on a mid-price basis
B Shares are bought and sold at the same price on any given day
C There is no initial charge
D The initial charge is included in the bid/offer spread

16 Which one of the following is NOT a feature of open-ended investment companies (OEICS)?

A Investments are pooled
B New funds are easily created
C The number of shares issued is restricted
D Many types of share may be included

17 Non Structured Capital at risk products normally provide a minimum return of:

A Nothing
B 85% of the initial capital invested
C 50% of the initial capital invested
D 100% of the initial capital invested

18 **Unit trusts, investment trusts and open ended investment company shares are suitable for which profile of investor?**

A A long-term investor who would still like reasonably easy access to funds
B A long-term investor who is happy to give notice to withdraw funds
C A low-risk investor who requires a guaranteed income
D A high-risk investor who likes to play the stock market

19 **Why does investment in a collective investment scheme carry a reduced risk when compared with direct investment in equities?**

A because collective investment schemes invest in a large number of different companies
B because fund managers can negotiate higher dividend payments
C collective investment schemes invest in equities that are not available to individuals
D Collective investments must guarantee as a minimum, the return of capital invested

20 **Which of the following is true in relation to the manager of an investment trust?**

A He cannot borrow funds
B He can borrow to improve income and capital growth
C He can issue more units or repurchase units according to demand
D he can cancel units if the fund grows sharply

21 **Dave has an investment bond issued by a life office, invested in their managed fund. At what rate is the provider's underlying fund taxed?**

A 18% B 20%
C 22% D 40%

22 **Which one of the following describes MOST investment bonds?**

A A single premium, unit linked, non-qualifying whole-of-life assurance
B A regular premium, unit linked, qualifying whole-of-life assurance
C A single premium, unit linked, qualifying whole-of-life assurance
D A regular premium, unit linked, non-qualifying whole-of-life assurance

23 **Tom, a higher rate taxpayer, has a single premium investment bond. How will any capital gains be treated?**

A Tom will pay inheritance tax at 20% on taxable gains that are made
B Tom will pay an extra 20% income tax on encashment of the bond
C The insurance company bears the entire capital gain tax burden
D The insurance company charges Tom for the gain

24 Jack is currently a higher rate taxpayer with 5 years to go before retirement. He has an investment bond that he is using to save for his retirement, when he expects his income to drop significantly. What feature of this product might he find especially useful when he has retired?

A The 5% annual allowance for withdrawals can be carried forward to future years.
B Withdrawals of any amount can be made free of tax, at any time
C He can switch investment funds within the bond at low or no cost
D He can split the bond into smaller policies for tax-free encashment at any stage

Unit 1 – Topic 9

Tax wrappers

Individual Savings Accounts (ISAs)

- This is the government's tax efficient savings schemes
- There is a cash ISA where your money is invested into an account with an interest rate
- There is also a stocks and shares ISA where your money is invested into different stocks and shares, but could also include gilts, corporate bonds, unit trusts, OEICs, investment trusts, life assurance policies
- Contributions are limited in each tax year to £20,000. Under the ISA rules, the £20,000 maximum can be split in any way between cash and stocks and shares per tax year.
- The ISA contribution limit normally increases each year in line with the Consumer Price Index (CPI)
- If you save in an ISA you are entitled to keep all that you earn and not pay any tax on it
- You can pay into your ISA whenever you want and you can stop making payments at any time
- They can only be established in a single name- joint ISAs are not possible and be a UK resident
- Must be 18 or over to invest in the equities element of an ISA and 16 or over for the cash ISA.
- There is also an Additional Permitted Subscriptions (APS) allowance where on the death of the ISA holder the deceased person's spouse or civil partner can pay additional amounts normally for a maximum period of 3 years.
- There is also a Help to Buy ISA whereby you deposit £1,200 initially and then up to £200 per month can be added. Each £200 deposited will be given a further £50 bonus (25%) which is paid when the house purchase completes. The maximum bonus overall is £3,000 so if you save £12,000, the government will add a £3,000 bonus.
- The amounts that you pay into the Help to Buy ISA still form part of your £20,000 ISA allowance.

- The property purchased via Help to Buy is a maximum of £450,000 in London and £250,000 elsewhere.

- The Help to Buy ISA is available until 30 November 2019.

Lifetime ISA

- This was introduced in April 2017 with the aim of encouraging people to save for their first home in the UK up to a value of £450,000 and/or for their retirement on reaching 60.

- A lifetime ISA can be opened by anyone between the ages of 18-40

- Savings made before the age of 50 attract a 25% bonus paid by the government which is now paid monthly so you can get interest on this.

- A maximum of £4,000 per year can be saved; there is no monthly savings limit

- Savings into a Lifetime ISA still forms part of your overall ISA allowance.

- The 25% bonus is lost and a penalty applied if funds are withdrawn for any other reason other than purchase of a first home, reaching 60 or the holder suffering a terminal illness.

- You can contribute to both a Help to Buy ISA and a Lifetime ISA but the bonus payment to purchase your first home can only come from one of them.

Advantages

- No liability to income tax or capital gains tax
- Flexible product
- On death of the account holder the ISA can be transferred to either a spouse or civil partner.

Child Trust Fund (CTF)

- This is a tax free savings account for children born on or after 1 September 2002 where the government provided an initial voucher of £250 to open an account.

- It was withdrawn in the 2010 emergency budget but existing accounts can continue although no further government contributions will be made. There are maximum contributions that apply.

- There are different types of CTF which are:

    - Deposit (like a cash ISA)
    - Stock and shares (similar to a stocks and shares ISA)
    - Stakeholder (also similar to stocks and shares ISA but slightly less risk and the charges for this one are limited to 1.5% of the fund)

- Junior ISAs became available in 2011 for all children who do not have a child trust fund account.

- At age 16 the holder of the junior ISA can become responsible for the ISA but they cannot access the fund until they become 18 and which point it turns into a normal adult ISA.

- Just as with normal ISAs, cash and stocks and shares elements can be combined.

Venture Capital Trusts (VCT)

- A VCT is a high risk investment in a listed company and you are buying shares in the VCT company who then manage the investments on your behalf and decide what companies to invest into.

- The VCT then uses the money raised to invest in a range of different companies often start-up companies.

- Due to the risk element and to make it more attractive, tax relief is awarded at 30% on up to £200,000 per tax year.

- There is no CGT on encashment and no tax on the first £200,000 of dividends

- The VCT needs to be approved by HMRC

Enterprise Investment Schemes (EIS)

- This is a similar scheme but the main difference here is that the investor is buying shares directly in one specific company, usually a start-up company.

- This is also high risk and therefore 30% tax relief is awarded on up to £1,000,000 per tax year.

- Investment in the EIS company are exempt from CGT.

Unit 1 - Topic 10

Pension products

Occupational Pension Schemes

- There are 2 main types

    - Money Purchase Scheme – Defined Contribution

        - Contributions invested to create a fund
        - Pension dependent on investment performance

    - Final Salary Scheme – Defined Benefit

        - A fraction of your final salary paid for every year of service up to a maximum of 40 years
        - If the fraction was $1/60^{th}$ your maximum pension is therefore $40/60^{th}$ or 2/3 of the employees' salary just before retirement.

Additional Voluntary Contributions (AVC)

- Employers who provide occupational schemes are obliged to also provide facilities such as AVCs to help employees increase their pension fund or buy added years on a defined benefit scheme.

Free Standing Additional Voluntary Contributions (FSAVC)

- Following the Finance Act 1987 employees can opt for FSAVCs provided by a different pension provider than the one the company uses.
- The advantage of this is that you are keeping this fund separate from your employer, the disadvantage is that it can be more expensive.
- No ability to buy 'added years' on a defined benefit scheme.

One of the main attractions of pension funds which include personal pension plans, stakeholder pension plans, AVCs and FSAVCs is that like an ISA the fund does not have to pay CGT whatsoever, no income tax on savings income and no higher rate or additional rate income tax on dividends.

The advantage that a pension has over an ISA is that a pension fund benefits from the tax relief given by the government to our pension contributions which is not available on an ISA. Therefore, the fund grows tax efficiently.

Workplace Pensions – Auto-Enrolment

- From October 2012 the rollout of workplace pensions commenced whereby larger employers had to automatically enrol their employees into a workplace pension and also contribute to the scheme.
- It applies to all employers for employees who are 22 or over and earn in excess of £10,000.
- The employee can choose to opt out but only after they have automatically been made a member.
- By April 2019, a minimum of 8% of the employee's salary will have to be paid into the scheme, which is split between 4% from the employee, 3% from the employer and 1% from the government in tax relief.
- As an alternative to auto enrolment the employer can meet its obligations by enrolling its employees into a trust based occupational scheme called the National Employment Savings Trust or NEST.

Personal Pension Plans (PPPs)

- These are money purchase arrangements so the pension achieved is dependent on the level of contributions and investment performance

- They cannot be arranged in joint names

- The main tax advantages are:

  - Contributions attract tax relief initially at the basic rate 20% even for a non-taxpayer
  - HRTP can claim an additional 20% through self-assessment so the HRTP gets tax relief at 40%
  - Additional rate taxpayers who pay tax at 45% can claim an additional 25% back through self-assessment so they get tax relief overall at 45%

- On retirement the plan holder can

  - Take up to 25% as tax free cash and use the remainder to buy an annuity which is buying a guaranteed income for life. The annuity income is taxable as earned income. Under the **open market option**, the individual at retirement to shop around to get the best annuity rates rather than just accept the deal offered by the pension provider.

  - Take the 25% tax free cash and then do 'flexi access drawdown' where the rest of the pension fund stays invested and you drawdown amounts from your fund subject to limits which are taxable. Once any benefits in excess of the 25% tax free cash are drawn down, a £4,000 annual allowance applies.

- Take the 25% tax free cash and then take the remainder of the pension fund as a taxable lump sum at your marginal rate – 'Uncrystallised Pension Fund Lump Sum' – available since April 2015.

Personal Pension Plan Rules

- Since April 2006 the maximum annual contribution which is the aggregate of all pension arrangements including occupational pensions is the higher of

    - Up to 100% of their UK earnings

      OR

    - £3,600

- There is however an overall maximum annual allowance which is currently £40,000. This can be exceeded but tax will be charged on the excess.

- If an individual has income in excess of £150,000 the annual allowance is reduced - £1 of the allowance is reduced for every £2 of income over £150,000 which could reduce the annual allowance down to a minimum of £10,000.

- There is also a lifetime allowance of £1,055,000. If the individual's total benefits exceed this at retirement there is a tax charge on the excess.

- These limits now apply to all pension arrangements whether taken together or individually

- Whether the individual has retired or not benefits can be taken at any time after age 55. This may rise to 57 by 2028.

- Contributions are paid net of basic rate tax, so an actual contribution of £100 into your pension fund would cost you £80. Higher rate taxpayers would be able to reclaim a further 20% through self-assessment.

- On death before retirement, a personal pension plan can be used to provide either income or a lump sum. On death after retirement, it can be used to provide benefits to spouse/civil partner or dependants of the deceased.

Stakeholder Pension

- Designed to encourage individuals to make pension provision and to particularly attract those on low earnings.

- They do have restrictions in terms of:

- Charges cannot exceed 1.5% of the fund value for the first 10 years and 1% thereafter
- Exit and entry charges are not allowed
- Minimum contribution required cannot be more than £20

Self-Invested Personal Pension (SIPP)

- A SIPP gives access to a wider range of funds than conventional pension schemes and also allow commercial property to be purchased.
- It gives the policy holder the ability to make their own decisions.

Group Personal Pension

- This a collection of individual personal pension plans arranged by an employer for their employees all administered by the same pension company.
- Each member has their own plan and the advantage of this is that they can take this plan with them if they were to leave that employer.

UNIT 1 – TOPIC 9 & 10 – TAX WRAPPERS & PENSIONS			
Question	**Answer**	**Mark**	**Comments / Notes**
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Total			**Result % = Total / 12 x 100**

Unit 1 – Topic 9 & 10 Test

1 Excluding any employer's contribution, what is the MAXIMUM percentage of UK earnings that an employee can contribute to a personal pension plan?

A 100%
B 78%
C 40%
D 25%

2 Which one of the following items would usually be used to calculate the maximum permitted contribution payable to a personal pension plan?

A Date of birth
B Employee's highest rate of income tax
C Class 1 NIC record
D UK earnings

3 What is the HIGHEST rate of tax relief in total that can be granted to personal pension contributions?

A 100%
B 20%
C 40%
D 45%

4 Which one of the following is TRUE of the tax relief available for an individual's contribution to a personal pension plan?

A They will receive tax relief up front at their marginal rate
B They will receive basic rate tax relief up front and any higher rate relief via self-assessment
C Relief is restricted to 10% for starting rate taxpayers
D Nil rate taxpayers cannot receive tax relief on contributions

5 After taking the tax-free cash sum, a personal pension plan holder would often use the balance of the fund to buy:

A an annuity
B A pension income bond
C a FSAVC
D Compulsory retirement contract

6 A client's personal pension plan fund at retirement is £150,000. What is the MAXIMUM available as a tax free cash sum?

A £24,000
B £32,000
C £40,000
D £37,500

7 The open market option enables the plan holder to:

A move his pension fund between providers in order to get the best investment return before retirement.
B move the accumulated fund at retirement to the provider which will provide the best annuity rate.
C have more than one personal pension plan with different providers, in order to get the best returns.
D accumulate his fund with one provider but get personal pension term assurance from another.

8 How is the income from a pension taxed in retirement?

A As earned income
B As unearned income
C As investment income
D It is tax free

9 If a customer is contributing to an occupational pension scheme and wishes to also start a stakeholder pension, what is the maximum amount of income per annum that they can have earned in the last year?

A £3,600
B £17,010
C £24,300
D No limit

10 Julia is a higher rate taxpayer. She understands that she pays her pension contributions net of tax relief to the product provider, and has to reclaim the remainder from HMRC. At what rate is this additional relief reclaimed from HMRC?

A 18%
B 22%
C 40%
D 20%

11 Which of these statements is INCORRECT in relation to an ISA?

A The maximum contribution per tax year is £20,000.
B Joint ISAs can now be taken under the new rules
C Growth of the fund is tax free in the hands of the investor
D Dividends paid into an ISA are paid without deduction of income tax

12 Colin is paying £100 per month to the cash element of an ISA in this tax year. He is considering using the equities element to the ISA. What is the maximum additional amount he can pay into the ISA this tax year?

A £18,800
B £20,000
C £3,600
D Nil

Unit 1 – Topic 11

Life assurance

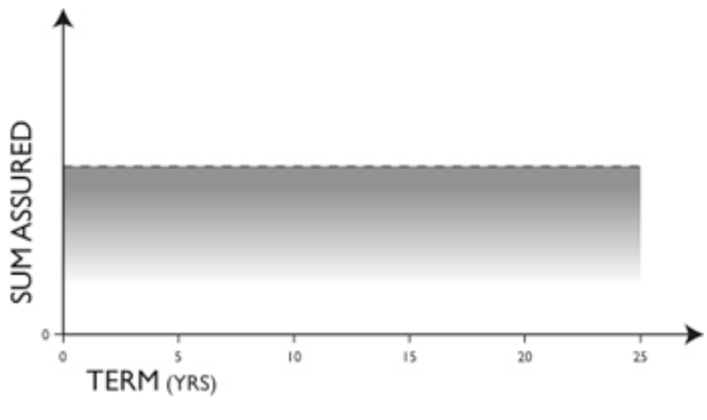
There are 2 main categories of life assurance – **Term Assurance and Whole of Life Assurance**

Term Assurance (in general)

- These differ from WOL policies in that there is only a pay out when death occurs during the term of the policy.
- If the assured survives the term there is no pay out and the policy ceases
- There is no investment element to these policies so they do not have a surrender value
- Premiums are usually paid monthly and are fixed at the outset
- Can be taken on a single or joint life basis

Level Term Assurance

- A fixed or level sum is paid on death during the term of the policy
- The sum assured is level throughout the term
- Premiums are also fixed throughout the term
- If the insured survives the term the policy ends
- Usually used in conjunction with an interest only mortgage



Decreasing Term Assurance

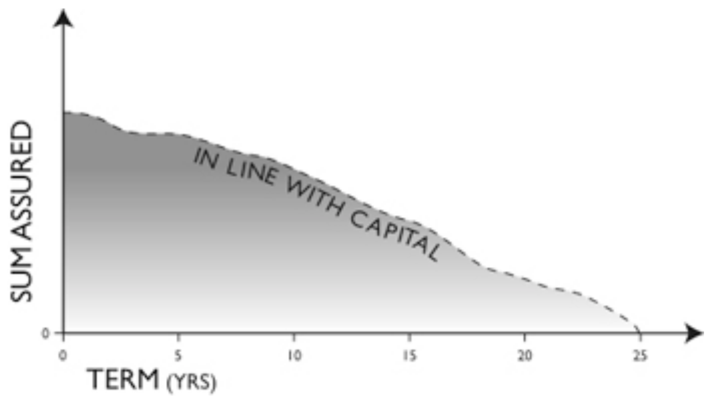
- Sometimes called a Mortgage Protection Policy or mortgage protection assurance

- Generally speaking, this repays the outstanding balance on a repayment mortgage

- Premiums will always be cheaper than a level term policy

- Premiums are level even though the amount of cover reduces over time

- Usually used in conjunction with a repayment mortgage



Gift Inter Vivos Cover

- This is a decreasing term assurance contract to cover a potentially exempt transfer (PET). It will provide an amount to pay the reducing IHT liability when a person dies within 7 years of making a gift. The cover will remain level for 3 years and then reduces each year after that until the policy ends at the end of year seven.

Increasing Term Assurance

- Sum assured increases each year by either a fixed amount or a certain percentage

- This feature ensures that the pay-out keeps pace with inflation

Convertible Term Assurance

- A special type of term assurance, (typically level) which includes an option to convert it to either an endowment or whole of life plan at any stage during the term.

- If a higher level of cover is required after conversion this additional sum is subject to normal underwriting.

- Due to its convertible status this costs around 10% more than term assurance.

- At the point of conversion there is no need for further medical evidence although the age of the assured will be taken into account at the point of conversion.

- The option can only be exercised while the convertible term assurance is in force.

- A useful policy for a couple with a young family who want the option to convert a plan when affordability is less of an issue.

Renewable Term Assurance

- This is a policy which is renewable at the end of the term without further medical evidence.

- The sum assured is the same but the premiums will take into account the age of the assured at the renewal stage.

Renewable and Increasing Term Assurance

- A renewable contract with the option to increase the level of cover at a specified date or when renewing it without further medical evidence

Family Income Benefit

- A form of decreasing term assurance which instead of paying out a lump sum, the contract will pay out a series of instalments starting from the date of death of the assured and ending at the end of the policy term.

- Payments can be converted to a lump sum but the total amount payable would be reduced if this were the case.

- FIB is not subject to income tax and policies can also be arranged with escalating benefit to combat the effects of inflation.

Pension Term Assurance (PTA)

- Life insurance taken in conjunction with a personal pension plan or a stakeholder plan

- Applications submitted prior to December 2006 qualified for tax relief on the premiums. This has now been withdrawn on new applications after December 2006.

- Plan holders who took this out prior to December 2006 are unaffected.

Whole of Life Assurance (WOL) in general

- Whole of Life Assurance pays out on the death of the assured whenever it occurs so there is a guaranteed pay out.
- Premiums are payable throughout life or up to a specified age
- As there is a guaranteed pay out these policies acquire an investment or surrender value although this will be very low in the early years, often less than the amount of premiums paid.
- Policies can be written on single or joint basis – payable on first or second death
- Mainly used to provide protection for dependents but can also be used to cover an IHT bill following death.

Types of Whole of Life

Flexible Whole of Life

- Issued on a unit linked basis and combine life cover with investment

- It is flexible in that you can cash in units at the bid price to buy life cover

- The policyholder selects the monthly premium according to affordability and the required level of life cover

- The higher the level of life cover, the larger the number of units that will need to be cashed in to pay for this

- If you require lower life cover, the more units you can purchase for investment which you can then use later in life if your circumstances change.

- These policies are very flexible and the balance between life cover and investment can be altered very easily

- Minimum Cover – low protection amount and a substantial investment element

  Balanced Cover –cover maintained throughout life based on stated sum assured

  Maximum Cover – level of cover guaranteed for a stated time (10 years) after which increased premiums will be needed if cover is to continue.

- Initial level of cover is usually guaranteed for 10 years. After this the life company has the right to increase premiums or decrease the cover.

Universal Whole of Life Policies

- This is an extension of a flexible WOL policy with a range of 'bolt ons.'
- In addition to life cover you can add any of the following:

  - Income Protection insurance
  - Critical Illness Cover (CIC)
  - Accidental death benefit
  - Total and permanent disability
  - Hospital benefits
  - Flexible premium levels
  - Waiver of premium (WOP) – allows the policy holder to stop paying premiums if they are unable to work due to sickness or disability.

- Any of these benefits are paid for by cashing in or cancelling units at the bid price

Uses of Whole of Life Policies

- Mainly used for protection – to protect dependents following the death of a breadwinner
- They can also be used to:

  - Cover funeral expenses following death
  - Provide funds to pay an IHT bill following death

- If the WOL policy is being used to cover an IHT liability it is common to set it up to pay out on **a joint life, second death basis** – known as a last survivor policy.

- It is usual to set up these policies in trust so that the proceeds are not paid to the estate but can be used instead to pay the IHT liability.

Unit 1 – Topic 12

Health and general insurance

Health Insurance

Critical Illness Cover (CIC)

- Gives a tax free lump sum on diagnosis of a list of specified illnesses
- Pre-existing conditions excluded
- Can be used to clear a mortgage balance
- Illnesses and conditions covered generally include:
  - Heart attack and coronary disease requiring surgery
  - Stroke
  - Most cancers – some exclusions with certain cancers
  - Kidney failure
  - Multiple sclerosis
  - Major organ transplant
- Other conditions that are sometimes covered are:
  - Paralysis
  - Blindness
  - Loss of limbs
- Many policies will pay out in the event of total and permanent disability but the definition varies between providers. Some providers take it as meaning the disability prevents them from doing any job suitable by virtue of their education, status and experience.
- Other companies have a tighter definition that requires that the disability has to prevent them from doing any job.

Income Protection Insurance

- Pays an income when the policy holder has suffered accident or sickness
- The amount claimed cannot generally be more than 50% to 75% of that person's income less state benefit.
- Housewives/homemakers may also be able to take out this sort of cover

- Policy term cannot exceed state retirement age

- The plan holder will select a deferred period – the longer the deferred period the cheaper the premiums will be. Deferred premiums are typically 4,13,26,52 or 104 weeks.
- The insurer cannot cancel the policy regardless of the number of claims made.

- A waiver of premium option can be chosen whereby if benefits are being paid on the policy, you wouldn't also have to pay the monthly premium.

- Some policies will allow the benefits to be indexed each year so the pay out each year could go up each year in line with inflation.

- If the illness means that a person can still work but can't do their previous job, then policies can allow payment to be paid on a proportionate basis eg might only be able to work part time or a lower paid job.

- The insurer could cancel the policy if hobbies or change in employment significantly increase the risk of a claim.

- Premium are either guaranteed or reviewable/renewable.

- Premiums are higher if in a high risk occupation.

- Class 1 - lowest risk – accountants, civil servants, clerical and admin. jobs
- Class 2 - low risk - hairdressers or pharmacists
- Class 3 – moderate risk – farmers or electricians
- Class 4 – highest risk – coal miners and industrial chemists

- Benefits are tax free if taken by an individual but if an employer provides the cover on a group basis the pay-out is usually taxable.

Exclusions

- Certain occupations would be excluded on the basis of being too high risk.

Accident, sickness, unemployment insurance (ASU)

- Covers a borrower's mortgage payments for a maximum of two years but can also include mortgage related costs
- The unemployment aspect only covers involuntary redundancy
- Can exclude unemployment cover if the borrower wishes
- Payments start after a deferred period e.g. 28 days
- Benefits are tax free. If provided by an employer as tax deductible expense for the company, it will still be treated as a taxable benefit in kind for the individual if you are earning more than £8,500

Exclusions and Restrictions

- Any redundancy known about will not be covered
- A person may have to be employed for a minimum period before they can take out this policy.
- For unemployment cover, no claim is considered for as long as 6 months after the policy is accepted
- There are additional requirements for self-employed claimants to be successful

Private Medical Insurance

- These policies provide cover for private medical treatment
- Benefits include:

    - Avoiding NHS waiting lists
    - Choice of hospital, consultant
    - Can pay daily rate of income if there is an overnight stay in NHS hospital
    - Choice of timing
    - Better quality room

- Covers in patient charges, outpatient charges and surgical and medical fees
- The premium will be influenced by age, quality of room required and the type of hospital

- General Exclusions

    - Pre-existing medical conditions
    - Routine eye and dental treatment
    - Self-inflicted problems
    - Cosmetic surgery
    - Alternative therapies

- Taxation

    - Premiums subject to Insurance Premium tax
    - For employers it is a deductible expense

Long Term Care Policies

- Provide funds to cover the cost of long term care

- There will be an assessment on the insured's ability to complete everyday tasks such as washing, dressing, feeding, toileting, mobility and food preparation.

- This is known as activities of daily living (ADL)

- The higher the ADL failure count, the greater the benefit available

- If benefits are paid to the organisation providing the care, they are tax free

General Insurance

- This includes all insurance that is not life assurance. There are 5 broad bands of general insurance:

    - Property loss – loss, theft or damage to objects
    - Liability loss – legal liability to 3rd parties e.g. personal injury
    - Personnel loss – injury, sickness or death of employees
    - Pecuniary loss – as a result of defaulting creditors
    - Interruption loss – business unable to operate due to fire for example

- In general terms the principle of **indemnity** applies – that is, if a person has suffered loss they should be restored to the same position they were in before that loss – neither better off or worse off.

- Therefore, if your car has been damaged by someone else and it's going to cost £1000 to repair it, the insurance pay out should be £1000.

The Principle of Averaging

- Occurs at the time of a claim when the insurer discovers that the property is under insured. This may be deliberate in order to keep the premiums low or it could be that inflation has increased the amount required
- The insurer may as a penalty for this, reduce the amount they pay out to the insured through 'averaging'
- In the event of a complete loss, for example, a house burning down, the amount paid out would be limited to the amount that the property is insured for.
- Many losses are only partial and in that instance 'averaging' can occur. In other words, someone who was under insured should not be indemnified in full. In this case, the claim is scaled down in the same proportion with regard to the premium paid to the premium that should have been paid.

Example

Adam has contents insurance for £10,000 when the true insurance value should have been £15,000.

If Adam made a claim for £300 for a damaged carpet, he would only get a pay-out of £200 as he was only insured for 2/3 of the amount that he should have been insured for.

Policy Excess

- Helps to keep premiums low whereby the insurer deducts a certain amount from each claim e.g. £100

Buildings Insurance

Standard Risks Covered

- Fire and smoke damage
- Lightning, earthquake and explosion
- Storm and flood
- Subsidence and heave
- Impact damage on the property
- Theft and attempted theft
- Damage caused by riot, strike or civil disturbance
- Leakage of water due to freezing or burst pipes
- Additional premiums may cover accidental breakage of fixed glass and sanitary fittings

- Some of the above will not be covered if the property is left unoccupied for more than 30 or 60 days including
    - Theft and attempted theft
    - Burst pipes
    - Riot, civil commotion or vandalism
    - Damage to glass

Contents Insurance

- Covers anything that you would take with you should the property be sold
- Could include accidental damage, damage to freezer contents and extended cover for items kept in a garden shed

All Risks Insurance

- Also known as extended contents cover
- Covers items regularly taken outside the home e.g. engagement rings, watches
- Unspecified items – each item has a value below a specified limit
- Specified items – items above that limit must be specifically listed and valued

Private Motor Insurance

- There are three levels of cover

    - Third party only
    - Third party, fire and theft
    - Comprehensive

Travel Insurance

- Cover can be arranged for individual journeys or on an annual basis.

- Cover usually includes:

    - Cancellation due to illness, injury
    - Missed flights due to transport failure
    - Delayed departures
    - Medical expenses
    - Personal accident
    - Loss of possessions
    - Personal liability
    - Legal expenses

Insurance Premium Tax

- This is only applicable to general insurance and is charged on premiums at the rate of 12%. The only exception is travel insurance which is charged at the normal VAT rate of 20%.

- There is no insurance premium tax on long term assurance such as life and protection insurances such as income protection insurance, critical illness.

UNIT 1 –TOPIC 11 & 12– LIFE ASSURANCE & GENERAL			
Question	**Answer**	**Mark**	**Comments / Notes**
1			
2			
3			
4			
5			
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18			
Total			**Result % = Total / 18 x 100**

Unit 1 – Topic 11 & 12 Test

1 The MAIN benefit of increasing term assurance is that it:

A qualifies for life assurance premium relief
B provides a hedge against inflation
C guarantees cover for the whole of the policyholder's life
D offers the possibility of a terminal bonus on death

2 What is the principal purpose of whole-of-life plans?

A Savings
B Investment
C Retirement planning
D Protection

3 How is life cover paid for on a flexible whole-of-life assurance?

A Via the bid offer spread
B Within the plan fee
C By cancellation of units
D As a direct deduction from the monthly premium

4 Flexible whole of life policies are best suited to which of the following scenarios?

A Primarily as a savings vehicle
B As a protection plan only
C As a protection plan with some allowance for savings
D As a way of including other forms of protection policy

5 For which one of the following situations might a joint whole-of-life policy be the most suitable recommendation?

A Ken and Sheila, a recently retired couple, wish to provide a tax-free legacy
B Simon and Lois, a middle aged couple who wish to maximise their savings
C Vince and Lucy, a married couple requiring a lump sum for their old age
D Bernard and Rita, a newly married couple seeking a mortgage

6 Stewart wants to start a whole-of-life assurance, which will also provide critical illness cover. Which specific type of plan should he choose?

A Flexible
B With-profit
C Universal
D Unit linked

7 What is the main difference between accident sickness and unemployment (ASU) policies and income protection insurance policies?

A ASU provides short-term cover only
B ASU does not have a deferred payment period
C ASU provides for other employment scenarios not just redundancy
D ASU provides total protection for all income

8 Benefits from a critical illness policy are usually payable as:

A a lump sum to the policyholder.
B regular income to the policyholder.
C a lump sum to the policyholder's estate.
D regular income to the policyholder's dependents.

9 Which one of the following illnesses would NOT normally result in benefits being paid out from a critical illness policy?

A Heart attack B Stroke
C Skin cancer D Kidney failure

10 What type of insurance policy can provide a daily rate of income if treatment involving an overnight stay in an NHS hospital is involved?

A Permanent health B Private medical
C Long-term care D Critical illness

11 Julian wishes to make sure that he can meet all of his essential outgoings if he is unable to work due to medium or long term illness. Which of the following insurance products would be most suitable?

A Accident and sickness
B Critical Illness
C Income Protection
D Private Medical

12 What is usually the MAXIMUM benefit payment period for accident, sickness and unemployment (ASU) policies?

A 1 year B 2 years C 5 years D 7 years

13 **Which of the following is normally regarded as a standard peril in the majority of buildings insurance policies?**

A Accidental damage
B Third party liability
C Riot or civil commotion
D Civil war or insurrection

14 **Which of the following statements is true in relation to either income protection insurance or critical illness cover?**

A There is no limit to the level of benefit that can be arranged under an income protection plan.
B Premiums on a critical illness policy qualify for tax relief for retired policyholders.
C Critical illness cover provides a taxable lump sum on diagnosis of a prescribed illness.
D There is no limit to the number of claims that can be made on an income protection insurance policy provided premiums are paid up-to-date.

15 **Matthew has been given various pieces of information regarding critical illness insurance. Which of the following is correct?**

A The monthly benefit received from a critical illness policy is taxed as income
B The lump sum benefit received under critical illness insurance is free from all UK taxes
C Premiums on a CIC plan attract tax relief at the policyholder's highest marginal rate
D Monthly benefit under a critical illness plan is limited to 60% of the policyholder's pre-disability monthly income

16 **Christopher is employed in an occupation that requires him to be fully active and physically fit. He is concerned that he will not be able to maintain his new mortgage if he were to suffer an illness that might force him to take lower paid employment. Which of the following products would provide him with a long-term income in such an event?**

A Critical illness cover
B Income Protection
C MPPI
D Whole of life plan

17 **When will benefit payments under a family income benefit plan stop?**

A Upon the death of the recipient
B State pension age
C At the end of the plan term
D After 10 years

18 What type of assurance is a family income benefit plan?

A Level term

B Decreasing term

C Whole-of-life

D Endowment

Unit 1 – Topic 13

Secured and unsecured lending

Mortgages

- There are actually only 2 mortgage repayment methods available – CAPITAL REPAYMENT and INTEREST ONLY.

- The parties involved in a mortgage are:

    - The lender sometimes referred to as the mortgagee
    - The borrower sometimes referred to as the mortgagor

Capital Repayment Mortgage

- Also called Capital & Interest mortgage or a repayment mortgage.

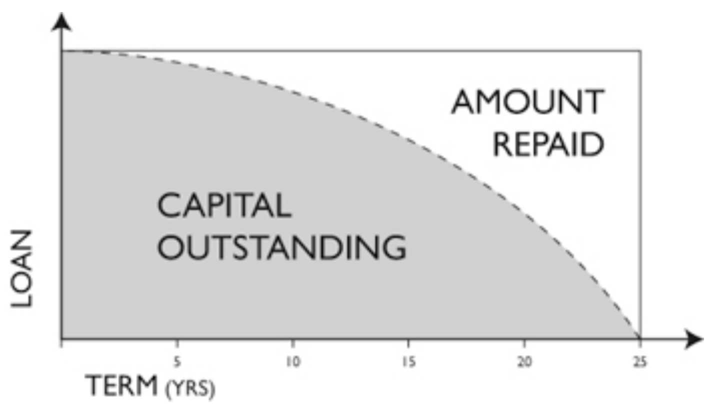
- Each monthly payment involves an element of interest and an element of capital.

- Therefore, it is a reducing loan with the balance outstanding decreasing all the time.

- In the early years, by far the biggest element of the payment is interest with this imbalance being reversed over time.

- So the capital decreases slowly at first but towards the end of the term the decrease is much quicker.

- If all the monthly payments are made the loan will be repaid in full at the end of the term.

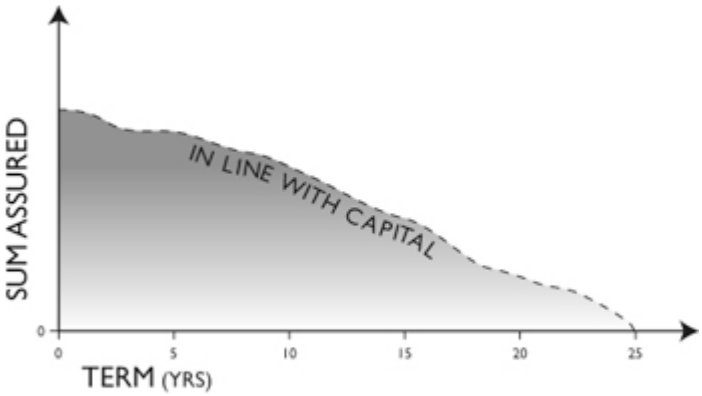


Advantages

- Easy to understand
- Easy to borrow more as the loan is reducing while the house value is probably rising
- Good method if you have a low risk profile
- Quite flexible in that the term can be extended if the borrower suffers hardship

Disadvantages

- This method does not automatically include life insurance which must be taken separately – usually decreasing term assurance.
- No chance of a surplus at the end of the term



Interest Only Mortgages with a Repayment Vehicle

- The borrower pays only the interest due each month, no capital is repaid at all during the term.
- The repayment of the capital is achieved at the end of the term through a capital repayment vehicle such as an endowment (see later).
- This method not very popular these days due to poor performance particularly by endowment policies.

Advantages

- For endowment options only life insurance is included in the plan
- Some products such as ISAs, Personal Pensions have tax advantages
- There is the possibility of a surplus at the end of the term.

Disadvantages

- With most of these there is no guarantee that the mortgage debt will be cleared at the end of the term – dependent on stock market performance
- Not a good method for the risk averse

- The loan amount does not reduce during the term

- In the past people may have taken out a **Pure Interest Only** mortgage without a capital repayment vehicle. Many lenders may not now allow borrowers to take out this sort of mortgage on a normal residential mortgage.

- Under the rules that have come into force under the Mortgage Market Review(MMR) an interest only mortgage can now only be taken if the lender is satisfied that there is a 'credible' repayment strategy and the lender must contact the borrower at least once during the term to check that the strategy remains in place.

Endowments

Endowment Policies – A quick guide

- An endowment policy is in essence a 'savings plan' that you make regular monthly payments into each month in addition to your monthly payments on an interest only mortgage.

- The idea is that by the end of the mortgage term, this 'savings plan' will be at the very least equal to the mortgage balance – **on maturity** e.g. when the policy ends

- In addition, all endowments have built in life insurance so that if the policy holder dies during the term, the full mortgage balance will be paid off – **death benefit.**

Non Profit Endowment Policies

- This policy guarantees to pay the sum assured on the earlier of:

    - Death during the term of the policy
    - On maturity

- No risks with these as you know the exact amount it will pay out.

- The policy holder does not share in any of the profits that the life company gets so for that reason these are rare today.

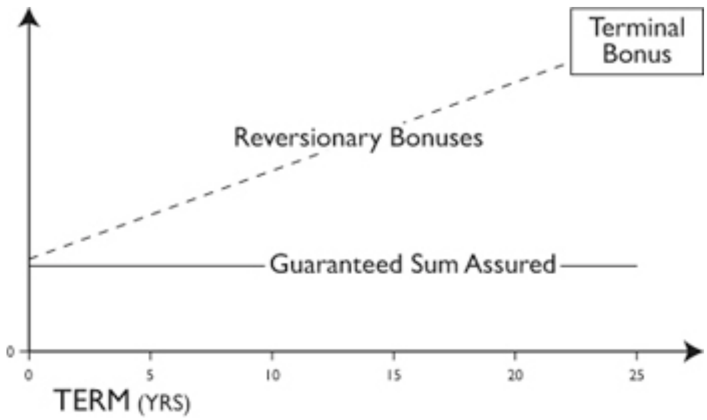
Full with Profits Endowment Policies

- This policy guarantees to pay off the mortgage debt on the earlier of:

  - Death during the term of the policy
  - On maturity as long as the sum assured is equal to the mortgage

- No risks with these but because they are guaranteeing so much they are extremely expensive.

- Also get the chance to receive bonuses which may give a surplus



Low Cost with Profits Endowment Policies

- Designed to be a cheaper alternative to the Full Endowment
- This option does not guarantee to pay off the mortgage in full on maturity
- The main features of the Low Cost Endowment (LCE) are:

  - The policy starts with a guaranteed sum assured of around half of the mortgage balance
  - It is hoped that through the addition of bonuses, by the end of the term the fund will be large enough to fully clear the mortgage
  - As the fund is in theory always growing the amount needed to clear the mortgage on death is reducing, so in effect the life policy works on a decreasing term basis.

Bonuses

There are two types of bonus that can be added.

Reversionary (Annual)

- Not guaranteed to get these but once added it can't be taken away
- Added to the plan annually if given

Terminal

- Not guaranteed to be given this bonus either
- Paid on death or maturity
- On a low cost endowment the granting and size of the terminal bonus will determine whether there will be enough to pay off the mortgage

Unit Linked Endowment Policies

- Different to all the With Profits plans – no basic sum assured

- Carry a greater risk but also a greater reward – chance of a surplus

- Premiums are used to purchase units on the stock market

- Some units are cancelled each month to pay for life cover which is built in as are all endowments – guaranteed death benefit

- No guarantee of what the fund will be on maturity as it will depend on how all these units will have performed on the stock market

- The units have two prices:

    - Offer Price – you buy the units at the offer price
    - Bid Price – you sell the units back to the Fund Manager at the bid price

- **Charges**

    - the difference between the bid and the offer price – bid/offer spread
    - policy fee charge – a fixed monthly deduction
    - annual charge – around 0.5-1.5% of the fund value

- Most providers offer periodic reviews to see if the plan is on target usually after 10, 15, 20 years and then every year thereafter.

Flexibility

- Unit linked plans have a flexible maturity date so the policyholder can repay the mortgage early if he chooses or extend the term if necessary

- Very important note – all With Profits plans have a fixed maturity date which cannot be reduced or extended.

Unitised With Profits Endowments

- A combination of the with profits and unit linked
- For those who like the guarantees provided by the with profits with the guaranteed sum assured but who like the high reward element of the unit linked and the ability to purchase units on the stock market
- Are entitled to bonuses as with all with profits plans and if given they are used to purchase more units
- Unitised with profits plans have a minimum guaranteed sum assured (GSA)

Endowment Performance

- Low Cost endowment performance has been very poor in recent years due mainly to low interest rates and poor stock market performance.

- Endowment providers were ordered by the regulator to review all endowments that are being used for mortgage repayment.

- One other feature of endowments is that they can be legally assigned (transferred) to someone else who will then receive the benefits on death or maturity. Some lenders insisted on the endowment being assigned to them if the endowment was being used as a repayment vehicle for an interest only mortgage.

Pension Mortgage

- A PPP or a stakeholder pension(SHP) can be arranged for anyone under the age of 75 including children

- Since April 2006 the maximum annual contribution is the higher of

    - Up to 100% of their UK earnings
      OR
    - £3,600

- Whether the individual has retired or not benefits can be taken at any time after age 55.

- Up to 25% of the fund can be taken as tax free cash. The 25% tax free cash would normally be used to repay the mortgage if possible.

- Since April 2015, you can now choose to take the remainder of the pension fund as a lump sum although this would be taxed at the individual's marginal rate of income tax. This new rule may well have made a pension plan a more viable repayment vehicle for an interest only mortgage.

- Contributions are paid net of basic rate tax, so an actual contribution of £100 into your pension fund would cost you £80. Higher rate taxpayers would be able to reclaim a further 20% so for them it would only cost them £60.

- There is however an overall maximum annual allowance for tax relief purposes which is currently £40,000 and a lifetime allowance for the size of any pension fund which is reduced to £1,055,000.

- Another advantage that a pension plan has over any endowment is that it will grow quicker as the fund itself isn't being taxed every year.

- One disadvantage for the lender is that the pension cannot be assigned to them unlike an endowment. The lender cannot therefore become entitled to the proceeds from the pension and there is no life cover automatically built into the pension fund so level term assurance may be necessary.

Individual Savings Account Mortgage (ISA)

- It is possible to use an ISA account as a repayment vehicle for a mortgage.

- Payments into the ISA can be regular or by lump sum but they cannot exceed the current limits considered earlier. Please note that he raising of the ISA allowance per person to £20,000 and the introduction of the Lifetime ISA, ISAs have become a more viable option than previously.

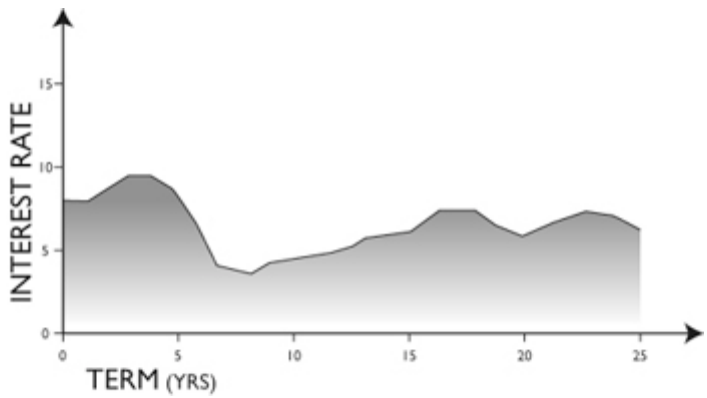
- The main benefits are that the fund is extremely tax efficient and if the growth exceeds expectations, then it is possible to repay the mortgage early.

- The main disadvantages are that there are no guarantees of repaying your mortgage and that there is no built in life cover so level term assurance should be arranged.

Mortgage Products

Standard Variable Rate (SVR)

- This is the rate of interest set by each individual lender as their standard product
- It will vary from lender to lender – some will be lower than others
- It is a variable rate of interest so that when rates go up the SVR will tend to go up and vice versa according to the wishes of the lender



Discounted Rate

- This is a discount off the SVR for a specific period – e.g. 1% off SVR for 2 years

- It is still a variable rate so if interest rates rise or fall, the rate that the borrower will pay will change but it will always be a saving on the SVR for that period

- May be an arrangement fee to pay

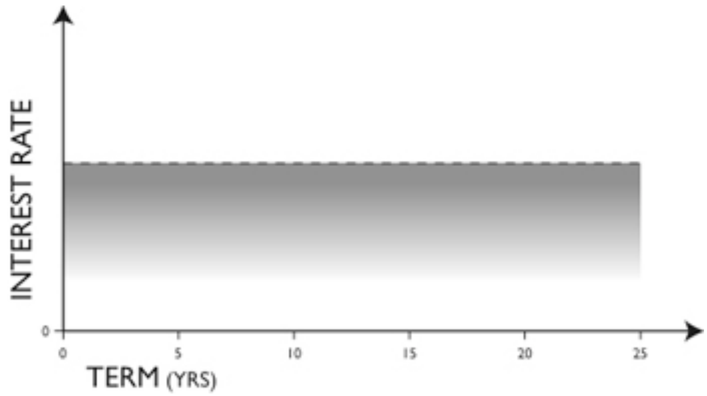
- Early redemption penalties are likely to apply during the discounted period

- Lenders may attach other products to the offer such as buildings insurance

- After the discounted rate ends the rate will revert to SVR which will always be an increase in rate

Fixed Rate

- Does 'what it says on the tin' – rate is fixed for a period of time
- If interest rates rise or fall, your rate will always stay the same for that period
- An arrangement fee sometimes called a booking or reservation fee is usually payable
- After the fixed rate the rate will revert to the SVR which may be higher or lower
- Early repayment charges are usually payable during the fixed rate



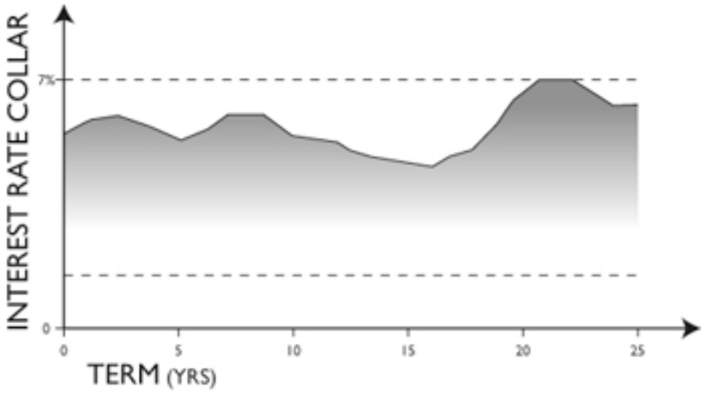
Base Rate Tracker

- The interest rate is variable and it varies in line with the Bank of England Base Rate who announce any changes in interest rates monthly – BoEBR
- A common example would be BoEBR + 0.50%. So the rate paid would be the current BoEBR plus 0.50% for the period stated
- Whenever the BoEBR goes up or down, your rate would change accordingly, so you are not subject to the whim of the lender.

Capped Rate & Collared Rate

- For the period stated a ceiling is set above which the interest rate cannot go above
- A good idea for people who believe that interest rates are likely to rise in the short term
- You can still take advantage of falls in interest rates but you are protected against rises in interest rates above a certain level

- Some lenders whilst agreeing to a capped rate also insist on a collared rate which is a rate set which the actual rate charged cannot go lower than.



Product Incentives

These could be available on any mortgage and include

- Free valuation
- Free legal fees
- No arrangement fees
- No early repayment charges
- Cash Back – the higher the LTV the lower the cashback. Note that when the mortgage is redeemed early the cashback may be required to be paid back. This is known as 'clawback'.
- Portability – moving the product to a new property

Mortgage Schemes

Flexible Mortgages

Can almost be anything it wants to be but the following are common:

- Overpayments, underpayments & payment holidays
- Additional borrowing facilities up to an agreed limit e.g. 80% LTV
- Interest calculated on a daily basis.

Current Account Mortgage

- This is a variation of the flexible mortgage which enables the borrower to carry out all of his personal and financial transactions within the one account
- The account is able to receive salary credits and pay direct debits to the lender.

- The combination of salary credits and daily interest considerably reduces the amount of interest payable and the term of the mortgage.

Offset Mortgage

- This requires the borrower to have a savings account with the lender and enables the interest payable on the savings account to be offset against the mortgage interest charged.

- If a borrower has an offset interest only mortgage for £100,000 and has £25,000 in a savings account, he can opt to waive the interest on the savings account enabling interest to be charged on a net loan of £75,000.

- This calculation is repeated on a daily basis.

The Low Start Mortgage

- These repayment mortgage schemes assist in keeping costs low during the early years of the mortgage, often by deferring the repayment of any capital during a specified initial period.

- Borrowers must be made aware that at the end of the initial period, no capital has been repaid.

- Borrowers must also be made aware that payments will increase beyond the initial period, as no capital has been repaid.

- If you had a 25 year repayment mortgage with a 3 year deferred capital period, in effect you pay interest only for the first 3 years and then it becomes a capital repayment mortgage for the remaining 22 years.

- May be appropriate for those currently on low earnings, but with realistic expectations of higher earnings by the end of the initial period, for example, a soon to be qualified professional.

Deferred Interest Mortgage

- During the early years, some of the interest is capitalised (added to the loan balance) rather than being paid by the borrower

- This can be unattractive to both lender and borrower where the borrowing requirement is of a high LTV, for example, 90% since the lender's security will be gradually erased as will the borrower's equity. The result is an increased danger of negative equity.

- Attractive to those who need a high LTV (low deposit) but want to keep repayments low during the early years.

- Again, this may be appropriate for those currently on low earnings, but with realistic expectations of higher earnings by the end of the initial period, for example, a soon to be qualified professional.

CAT Standard Mortgages

This is a government backed initiative to show that the mortgage meets certain criteria.

<u>Charges</u>

- Must be daily interest

- No separate charge for a higher lending charge

- All other fees disclosed as up-front cash

- Intermediaries cannot charge fees

- Arrangement fees

    - No arrangement fee for a variable rate mortgage
    - Maximum arrangement fee of £150 for a fixed or capped rate

- Interest rate cannot be more than 2% more than the BoEBR on a variable rate mortgage

- Maximum redemption charges apply to fixed or capped rate mortgages

- No early redemption charges on a variable rate.

<u>Access & Terms</u>

- No compulsory products

- Lender's normal lending criteria must apply

- All advertising and paperwork must be clear and in plain language

- Customer chooses the monthly repayment date

Lifetime Mortgages (formerly known as Home Income Plans)

- Allows a person usually retired and over a certain age who own their home outright to mortgage their property

- No repayments are made to the lender during the lifetime of the borrower

- The interest is 'rolled up' and added to the capital which is repaid after the death of the borrower when the property is sold

- The lender will place a limit on the LTV – 25% to 55%. The younger the person applying the lower the LTV. This is because a person who takes it out at 60 will accrue more unpaid interest than an 80 year old as they are likely to live longer.

- Due to the vulnerable nature of the people that this is aimed at, the main lenders in this area have formed the **Equity Release Council** who have agreed that:

    - any applicant be encouraged to seek independent legal advice
    - any negative equity situation be funded by the lender
    - the borrowers will be entitled to stay in the home for the rest of their lives e.g. until the death of the second party on a joint mortgage
    - the plan must be portable although part of the loan may have to be repaid if the next property is insufficient security.

Home Reversion Schemes

- The owner sells part or all of the equity to a lender in return for a lump sum

- The lender will normally ask for a discount on the value of the property. If a homeowner was looking to sell 100% of the property to a provider and the property was worth £200,000, the planholder would receive less than £200,000 for selling that 100% equity stake.

- No mortgage is created here and therefore no interest is charged

- The lender will take life expectancy into consideration before deciding how much of a lump sum to award for what proportion of equity.

- The provider will have to wait until the death or second death before they can recover their capital when the property is sold.

Most of these schemes are covered by the same Code of Practice which offers individuals the same safeguards as for lifetime mortgages.

Shared Ownership Mortgage

- This combines rental with owner occupation to help those on low incomes to become owner-occupiers.
- Involves borrowers, the lender and the local authority or housing association
- A borrower will buy a share, 25% for example in a property and pay rent on the remaining 75%
- The borrower also has the chance to buy further shares in the property from the housing association until the whole property is owned – 'stair-casing'
- When the property is sold the equity is split according to the proportion of ownership that each party holds.

Mortgage Related Property Insurance

- The property needs to be insured with a policy that is acceptable to the lender
- Have its interest as mortgagee noted on the policy
- Secure a right over the proceeds of any claim to remedy the problem

Second Mortgages/Secured Loans

- Borrower uses the property again as security for a loan to a new lender
- Would have to be sufficient equity in the property to make the lender comfortable
- The first lender retains the mortgage deeds
- If the property is sold the first lender has the first claim to the proceeds, passing any surplus onto the second lender
- As there is therefore a higher risk of the second lender not recovering their loan higher rates of interest are charged on second and subsequent mortgages.

Regulation of Second Mortgages/Charges

- As of March 2016 under the Mortgage Credit Directive, these second charges are now regulated under the Mortgage Conduct of Business rules (MCOB) as most other mortgages are.
- Prior to this change, they were regulated under the Consumer Credit Act.
- This change will apply to second mortgages taken out both before and after March 2016.

Bridging Finance

- Arises when a new property is bought before the current property has sold.
- It is short term lending that is repaid when the original property is sold.
- There are two main types of bridging:

    - Open bridging - buying a new property before you have found a buyer for the current property. This is considered to be much higher risk

- Closed bridging - Buying a property with a firm buyer in place for the current property.

Unsecured/Personal Loans

- Generally for shorter terms up to 7 years
- Interest rate is fixed and remains unchanged throughout the term

Overdrafts

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- Interest rate charged for overdrafts will depend on whether the overdraft is authorised or unauthorised.

Credit Cards

- Agreed credit limit with a minimum monthly payment
- No interest is charged if the full balance is repaid within a specified period
- Credit card companies charge retailers a fee for offering this payment method to the public

Charge Cards

- This time the outstanding balance needs to be paid in full at the end of the month.

Debit Cards

- Chip and Pin services. Present your debit card as payment for goods.

Commercial Loans

- This is a loan where the purpose of the loan has some commercial activity e.g. for a business, shop, office, factory, often taken out by a company.

UNIT 1 - TOPIC 13 – SECURED & UNSECURED LENDING			
Question	**Answer**	**Mark**	**Comments / Notes**
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Total		
Result %		**Result % = (Total / 28) x 100**
NOW TRANSFER YOUR RESULT TO PERFORMANCE TRACKER 1		

Unit 1 – Topic 13 Test

1 Peter takes a loan from a building society to buy a new house. He is the:

A mortgagor
B mortgagee
C assignee
D vendor

2 Which of the following is one way in which a repayment mortgage differs fundamentally from a full endowment mortgage?

A The higher the interest rate, the higher the monthly repayment to the lender
B Separate life cover is required
C The loan will be fully repaid at the end of the term
D Interest is payable on the outstanding loan

3 Which one of the following statements, about repayment mortgages, is TRUE?

A The older the borrower, the higher the monthly repayment.
B The shorter the term, the higher the total amount of interest paid.
C The higher the interest rate, the higher the monthly repayment.
D The longer the term, the higher the monthly repayment.

4 Which one of the following is a feature of a repayment mortgage?

A Repayments will be fixed throughout the term of the mortgage
B The capital and interest payment proportions change over the term of the mortgage
C The capital balance does not reduce over the term of the mortgage
D The borrower will have to take out an investment policy to cover the shortfall at the end of the mortgage

5 If Kim and Chris opt for a repayment mortgage, the most suitable way to ensure that the loan will be repaid if one of them dies is by:

A making contributions to a critical illness policy
B taking out joint life decreasing-term assurance
C investing in an endowment assurance
D contributing to a permanent health insurance policy

6 What happens to the capital outstanding during the duration of an interest only mortgage?

A It reduces by an even amount each year
B Most capital is repaid towards the beginning of the term
C Most capital is repaid towards the end of the term
D It remains the same

7 What is the main advantage of using a pension plan to support an interest only mortgage?

A They often run over a longer term
B They are assigned to the lender
C They guarantee to repay the loan
D They benefit from favourable tax concessions

8 With a pension mortgage, the loan is repaid using the:

A open market option
B tax-free cash
C market value adjustment
D protected rights fund

9 Nick and Lynne are keen to take advantage of a better deal and remortgage with a new lender. However, their existing lender has informed them that if they move, they will have to pay an additional six months' interest. The most likely reason for this is that:

A they have a variable rate mortgage
B they have arrears on their mortgage account
C they have a fixed rate mortgage
D their lender is reclaiming the valuation fee outlay

10 Which one of the following types of mortgage provides a genuine reduction in the normal variable rates of interest?

A Low start mortgage
B Low cost mortgage
C Deferred interest mortgage
D Discounted mortgage

11 What is the main advantage of a 'capped' interest rate option when taking out a mortgage?

A If interest rates go up the mortgage interest rate will be limited to a pre-set ceiling
B Interest rates are linked to the Bank of England s base rate
C The amount payable is fixed for the duration of the capped rate
D There is a genuine discount off the normal variable mortgage interest rate

12 Which one of the following statements regarding a cap and collar mortgage is CORRECT?

A They normally appeal to clients who believe rates are more likely to rise than fall
B They are specifically aimed at clients with low loan to value ratios
C They can only be used in conjunction with endowments
D They are particularly appropriate when interest rates are falling

13 Which one of the following is NOT an advantage of a flexible mortgage?

A The ability to borrow further money for lump sum expenditure
B Over payments are allowed so enabling early repayments
C Unlimited further advances
D The ability to have repayment holidays when clients' budget is tight

14 Which of the following is true in relation to re-mortgages and second mortgages?

A A second mortgage is an additional loan from a new lender
B A re-mortgage is an additional loan from a new lender
C A re-mortgage is a way for a lender to charge a higher interest rate
D A second mortgage increases the loan from the same lender

15 What type of mortgage scheme would help someone on low income to become an owner occupier?

A Buy to Let
B Shared ownership
C Full endowment
D Home reversion

16 Dick and Margaret have had their mortgage for two years and are concerned that interest rates have fallen but their monthly payment to the lender has stayed the same. Which type of mortgage do they have?

A A base rate tracker
B A fixed rate
C A discount rate
D A capped rate

17 An advantage of a variable rate mortgage is that:

A arrangement fees may be added to the loan.
B first time buyers are able to budget accurately in the early years.
C borrowers are able to benefit from reductions in interest rates.
D repayments to the lender are lower than any other product.

18 For which one of the following borrowers might a fixed rate mortgage be most suitable?

A Bob who is convinced interest rates will fall sharply in the short term
B Neil who believes interest rates will rise significantly in the near future
C Rachel who feels that interest rates will stay the same for the next few years
D Tony who feels that lenders should never charge arrangement fees

19 Clive, at age 27, started a stakeholder pension plan, which he intended to use to repay the capital under his interest only mortgage. His stated occupation is office manager. After how many years minimum, will he be able to access his pension?

A 20 years
B 23 years
C 25 years
D 28 years

20 Which is true of the capital repayments on a repayment mortgage?

A It reduces by an even amount each year
B Most capital is repaid towards the beginning of the term
C Most capital is repaid towards the end of the term
D It remains the same

21 **Which one of the following types of endowment will normally guarantee that the original mortgage loan will be repaid in full at the end of the term?**

A Qualifying unit-linked
B Low start unit-linked
C Non-profit
D Low cost

22 **On a with-profits policy, a reversionary bonus is:**

A one that reverts to a minimum level in the event of a claim.
B declared each year and, once declared and attached to the policy, it is guaranteed payable as long as premiums are maintained.
C an irregular payment determined by the type of policy and the number of lives assured.
D a payment made on maturity at the discretion of the assurance company.

23 **Which one of the following statements in respect of a unit-linked endowment policy is correct?**

A A pre-determined guaranteed benefit is payable on maturity of the policy.
B The guaranteed sum assured only is paid on death of the policyholder before the maturity date.
C The appropriate level of life cover is funded by encashing units on a monthly basis.
D The value of the policy at any time is the number of units held multiplied by the offer price.

24 **Compared to a full endowment, a traditional low cost endowment has a:**

A lower premium for a given death benefit but less guarantees on maturity
B lower death benefit for a given premium but more savings
C higher premium for a given guaranteed maturity value
D higher premium for a given sum assured but more chance of bonuses

25 **If a low-cost endowment is used as a mortgage repayment vehicle, the mortgage is GUARANTEED to be repaid:**

A providing interest rates do not exceed 12%.
B on death or maturity as long as premiums are paid.
C as long as the policy is held for 25 years.
D on death only.

26 Which one of the following describes an advantage which a unit-linked policy has over a with profit policy, for mortgage repayment purposes?

A A guaranteed minimum maturity value
B Tax relief on the premiums
C The chance of a surplus at the end of the term
D The possibility of repaying the loan early

27 Why have endowment policies become less popular as a capital repayment vehicle for mortgages?

A Because of poor performance
B Because of 'front end loading'
C Because of the lack of flexibility
D Because of the lack of premium waiver benefit

28 How does a unit linked endowment plan running alongside an interest only mortgage work in practice?

A The client pays interest and capital to the lender and the policy covers the outstanding loan in the event of death
B The client pays interest only to the lender and the policy aims to repay the capital at the end of the term or on earlier death
C The client makes interest and partial capital repayments to the lender and the policy clears any capital debt on death or maturity
D The client makes no payment to the lender and the policy pays off the accrued interest and outstanding capital on death or maturity

Unit 1- Topic 14

Understanding and satisfying customer needs

Financial Life Cycle

It is fair to say that while all clients are different, typically, at different stages of our lives, different financial issues will be relevant for us.

Youngsters

- Attracted by small savings schemes (NS&I) often opened by parents or grandparents

Teenagers and Students

- Little surplus income at this stage – borrow to fund college/university

Post Education/Young Adults

- Saving towards a deposit for a house so short term easy access savings vehicles the most common

Young Families

- Major borrowing is now likely to have taken place with a mortgage
- One partner may have had to stop work to raise children
- Protection of the income of the main breadwinner is crucial
- Should begin to think about pension provision

Established Families

- Money perhaps less tight with a return to two incomes
- Might trade up to a larger property, maybe a bigger mortgage
- May have greater creditworthiness enabling more expensive household goods
- Could receive legacies from deceased parents/grandparents

Mature Households

- Often the period of highest earning and outgoings may decrease if children leave the family home
- Pension provision now becomes a major priority.

Retirement

- As retirement approaches people looking to convert income into lump sums for retirement
- In retirement, people tend to take a more cautious approach to the money that they've saved.
- IHT mitigation could now also be a priority
- Continued good health and long term care could also be an important issue.

Saving Patterns

- Generally speaking there is a well-established pattern in the way people build up and hold their assets.
- It always tends to start with the need for liquidity and safety e.g. being able to get your hands on savings to cover an unwelcome event such as an emergency fund.
- Once that has been established and maintained, there is often a gradual move away towards accepting greater risk.

Gathering Information – The Fact Find

- The Financial Services & Markets Act 2000 (FSMA) requires that advisers must 'know their customer' and the adviser must be able to identify a client's needs.

- The adviser should ensure that a questionnaire or fact find is completed which will highlight the client's:

  - Current and future needs
  - Ability to meet these needs
  - Attitude to their importance

- The fact find will uncover the following:

- Personal details (hard facts)

- Financial details (hard facts)
  - Occupation
  - Income & expenditure
  - Assets

    - Liabilities

- Objectives (soft facts – subjective)

    - Hopes and aspirations
    - Goals in the future
    - Views on alternatives
    - Whether they are willing to take action

The adviser should always give priority to a hard fact over a soft fact.

Note

Once the fact find has been completed, it is also important for the adviser to recommend further meetings at regular intervals to see if circumstances have changed and their willingness to review objectives to discuss new opportunities.

The adviser can best help those clients who are prepared to follow this approach.

Attitude to Risk

- It is essential to ascertain a client's attitude to risk before recommending a solution.
- The adviser always needs to explain the risks involved with a product and ensuring that the client understands and accepts the risks involved and to examine the client's capacity to absorb 'loss'.

Client Preferences

- Whilst the adviser should acknowledge a client's preferences, if those preferences are based around an incorrect assumption about a product, the adviser has a duty of care to correct that misunderstanding.

Identifying and Agreeing Needs and Objectives

- If there are a number of ways that a client can be helped it is best to agree with the client an order of priority.

    - It is generally accepted that the first priority should be to ensure that there is adequate protection in the event of death.
    - Secondly, is there adequate protection in the event of illness.
    - Thirdly, retirement planning would be the next priority.
    - Fourthly, savings and investment planning
    - Lastly, the need to investigate tax savings.

- Please note that the FCA also expects advisers to pay attention to customers who may be termed 'vulnerable' and have policies in place to deal with this.

Recommending Solutions

The adviser needs to be aware of the following issues when recommending solutions:

- State benefits
- Affordability
- Taxation
- Risk
- Is timescale an issue
- Current arrangements
- Looking for income or capital (or both)

Implementing Solutions

- Presenting recommendations

    - Explain how each recommendation matches their needs
    - Explain the benefits the client will get from this product
    - Explain risks or limitations
    - Provide a summary for why that product has been recommended such as a features and benefits analysis – what specific benefits these features provide

- Handle Objections

- Obtain a commitment to buy

    - Application form completion is the responsibility of the client but the adviser can complete it with the client's permission
    - The client must be made aware of the effects of non-disclosure of material information
    - Adviser must formally ask the client to read and check before signing

- Documentation

    - Adviser must provide a business card at the start of the meeting
    - Duty to explain any cancellation notice or period e.g. the client's right to withdraw from the contract within a certain period
    - Adviser must provide a Key Features Document containing an illustration before the application form is completed

    - Adviser must retain all records for three years except for:

        - Life Policies, Pensions contracts and MiFID business - 5 years
        - FSAVCs, pension transfers & opt outs - indefinitely

- After Sales Care

    - Proactive servicing – the adviser instigates contact with the client to discuss changing circumstances and needs in order to take advantage of new opportunities e.g. following a salary review or change of job.

    - Reactive servicing – the adviser responds to a request from a client or from a product provider e.g. missed premiums

Unit 1 – Topic 15

The main financial advice areas

Budgeting

- This is crucial to all areas of financial advice and advisers when recommending a product should not put any pressure on household income.

Protection

- This is the concept of protecting a financial product against various risks such as death or illness. There are different types of protection:

Family Protection

- **Losses due to death**

    - Any loss of income usually has a huge impact on a family
    - That loss of income could make loans unaffordable
    - There could be a risk of losing the family home as a consequence
    - Missed payments that occur could jeopardise future borrowing

These problems can be prevented by ensuring either:

- Arranging an income protection policy to cover the loan

  OR

- Arranging a capital sum to be paid on death to clear the loan in full

Losses due to Illness

- Similar problems can occur if the main breadwinner suffers a serious illness which prevents them from working.

- These needs can be solved by:

  - Providing an income protection policy to replace that lost income
  - Providing an income to pay for treatment or adaptations to the house
  - Providing a lump sum (critical illness policy)

Losses due to Unemployment

- The same concerns exist here as for losses due to illness

Business Protection – (Death of a key employee)

- Could have a big impact particularly on small companies where there are one or two key personnel involved in that business
- Should those key personnel die, this could have a drastic effect on the business
- Calculating the level of cover required can be difficult. A simple method would be to multiply the key person's salary 5 or 10 times.
- The company would then take out a term assurance policy on the life of the employee for the period that the employee is expected to be a key person
- Policies are taken by the company on the life of a key person
- If the policy is taken for 5 years or less then it is classed as a business expense
- If this is the case, any proceeds would be subject to corporation tax.

With all protection policies, it may also be important for the policy holder whether it is personal or business to consider whether the potential pay out from the policy will keep pace with inflation.

Death of a Business Partner

It is important that the surviving partners of a business insure against the death of a business partner with a view to covering the claims of a deceased's partner's beneficiaries.

- **The automatic accrual method**

  - Deceased's share automatically shared among surviving partners
  - Proceeds of a life policy paid to deceased's beneficiaries
  - Normally 100% business property relief for IHT with regard to the deceased's share of the business.

- **The Buy and Sell method**

    - Deceased's executors obliged to offer to sell the deceased's share of the business to the surviving partners
    - The surviving partners have to buy
    - Life policies are taken on each of the partners for the benefit of the surviving partners.

- **The Cross Option method**

    - This time the deceased's estate has the option to sell the deceased's share to the partners within a specified time
    - Surviving partners' have the option to buy
    - As this is an option rather than an obligation, relief from IHT may be available.

The effect of inflation

- While there is inflation the buying power of a capital sum will decrease over time. £10,000 in 2030 will not be able to buy you as much as £10,000 will in 2019.

- The adviser needs to be aware of this and consider products that grow in real terms – i.e. at a rate greater than inflation.

- Equity or shares based investments have proved to be effective in achieving this.

- The real rate of return is the interest rate minus the rate of inflation.

Retirement Planning

- One of the government's most pressing problems concerns most people's inability to adequately provide for their retirement.

- The Basic State Pension is unlikely to be adequate for most people.

- Stakeholder Pension Plans were designed to encourage people to make pension provision as they were designed to be easy to understand with a maximum charge of 1.5% of the fund for the first 10 years and 1% thereafter.

- This imposed maximum 1.5% charge has made stakeholder plans unattractive for the quality pension fund manager as he can make more on other pension schemes. This has resulted in poor take-up rates on stakeholder plans.

Estate Planning

- Remember that beyond the allowed threshold IHT is payable on the deceased's estate at 40%.

- It is possible to reduce this liability by making use of exemptions and making Potentially Exempt Transfers (PETs).

- Other possibilities include:

    - Married couples and civil partners can now use both their nil rate bands with the percentage of unused nil rate band on the first death being carried forward to be used on the second death.

    - The Residence Nil Rate Band is also available to help spouses and civil partners with regard to IHT mitigation as considered earlier.

    - Another method is to place assets in trust, since trust property does not become part of the deceased's estate – known as 'ring fencing.'

    - If you give property away while continuing to live in it, this is covered by the 'gift with reservation of benefit' rule with the asset being treated as never having been given away at all.

    - In the past many people avoided this problem by placing their property in trust. The tax authorities have closed this loophole by means of Schedule 15 of the Finance Act 2004 which introduced new rules for the taxation of 'pre owned assets' such as properties. The tax charge is based on a realistic annual rental for the property that they occupy. If the rental amount is less than £5,000 no tax charge is levied.

    - The importance of making a valid will is also a vital element.

    - Life Assurance Policies can also be used to cover an IHT liability. Usually this is done on a joint life, second death basis – last survivor policy. On the first death the spouse exemption applies and on the second death, as the policy is written in trust, it will pass direct to the beneficiaries.

Tax Planning

- It is always vital to consider the tax implications of any product recommendation.

UNIT 1 – TOPICS 14 & 15 – UNDERSTANDING CUSTOMERS & ADVICE AREAS			
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Unit 1 – Topics 14 & 15 Test

1 Which of the following ought to be a priority consideration when assessing the needs of retired couples?

A Pensions planning
B Protection advice
C Inheritance Tax planning
D Mortgage advice

2 A client wants to invest actively into equities with a view to capital growth. Which one of the following is going to be least important to him?

A Regular fixed income
B Favourable tax treatment
C Fund managers with a good track record
D Low dealing costs when buying/selling

3 The concept of 'know your client' means:

A Understanding a client's current position in terms of assets and liabilities
B Getting your client to identify all his existing life and pension policies
C Gaining a detailed knowledge of a client's personal and financial circumstances
D Establishing a client's current financial position in terms of income and expenditure

4 When gathering 'fact find' information about your client's financial plans and objectives, which of the following is a fundamental consideration that should always be taken into account?

A Levels of indebtedness
B Attitude to risk
C Employment details
D Mortgage arrangements

5 A client is a self-employed building contractor and is considering a personal pension plan. Which one of the following is likely to be most important to him?

A The ability to find out the value of the pension fund
B The ability to transfer in monies from other schemes
C The ability to increase or decrease contributions at his convenience
D An explicit set of policy charges with no hidden extras

6 Which one of the following would be important to a customer when considering their protection needs?

A An interest rate that suits their budgeting requirements
B Money payable under the policy to keep pace with inflation
C To be able to access money immediately
D To be able to track the record of fund managers

7 If a client does not agree with your priority of needs based on the information you have obtained from your fact find on him, what should you do?

A Tell the customer that they are wrong and, as such, you cannot advise them further.
B Advise of the risks that could arise from the absence of the products to match those needs.
C Insist that your recommendations are right and only provide them with the products to fill those needs.
D Choose to say nothing as this may upset the customer.

8 When presenting your recommendations to a client you need to ensure that your client understands the features and benefits of the products. How can you check the client has understood?

A By watching their body language
B By noting the number of questions they ask
C By asking them questions
D By ensuring they sign all the relevant forms

9 If an adviser has filled out an application form on behalf of a client the adviser should recommend that the client:

A reads over the form and confirm that the adviser may sign it.
B signs the declaration after the adviser has read out the answers on the form.
C checks the form for accuracy and signs the declaration.
D signs an execution only form.

10 Which one of the following is a reactive service call?

A Calling a customer after the non-payment of premiums
B Calling a customer to discuss whether their circumstances have changed
C Visiting a customer to talk to them about a new product
D Visiting a customer following a diary note prompt

11 Of the information below, gathered in respect of Alice, which item represents a hard fact?

A Her investment portfolio performance has been below expectations
B Her savings account balance has fallen to £5000
C She intends to increase her pension plan monthly contribution to £500
D She plans to retire by the age of 60

12 Brian is reviewing a range of investment products before selecting the most appropriate solution for his client, Claire. Which factor is he LEAST likely to take into account when selecting an appropriate solution?

A The possibility of Claire getting married in the future and having children
B Claire's existing portfolio of investment products
C The fact that she has recently moved into a higher rate tax bracket
D Claire's desire to access her investments in five years to purchase a time share in Portugal

13 What is the advantage of including benefit statements when making a product presentation to a client?

A It ensures that all point of sale FCA regulatory requirements are met
B It enables the client to better understand how the product will meet his needs
C It ensures that the client understands the risks involved with the product
D It enables the adviser to focus on the sale rather than client queries

14 Wally keeps £500 under his mattress. Which one of the following represents the effect of inflation on this amount over the period of one year?

A It now purchases fewer pints of bitter
B It now purchases fewer euros
C It would have been worth £525 if it had been invested in XYZ shares
D It would have earned £15 interest in a savings account

15 Which one of the following will usually be the priority need associated with young people taking out their first mortgage during early working life?

A An emergency fund
B Medium term investments
C Income protection
D Pension planning

16 A programme of proactive servicing by the adviser is designed to ensure that the client:

A can take early advantage of new market opportunities.
B checks that records are destroyed at the earliest opportunity.
C has no need to request a further meeting.
D will have no cause to cancel during the cooling off period.

17 Which one of the following factors that you cover during a fact find will affect your ability to improve your client's situation on an ongoing basis?

A The client's attitude to risk
B The client's willingness to review objectives if personal circumstances change
C The client's current financial circumstances
D The client's job prospects

18 What is the usual financial priority of a retired individual?

A Build up a capital reserve
B Minimise capital gains tax liability
C Increase income from investments
D Maintain his / her standard of living

19 Ethel has £1000 in a basic building society account. Her son has pointed out that her savings are now failing to keep pace with inflation. This is specifically because:

A sterling is performing strongly against the dollar.
B she is now eligible to receive gross interest payments.
C her savings interest rate has recently been reduced.
D the government borrowing requirement has increased.

20 Which one of the following usually becomes the priority financial need on becoming a parent?

A Savings
B Investment
C Protection
D Pensions

21 Which ONE of the following could be described as 'proactive servicing'?

A A telephone call to a client to arrange a pre-agreed review following a salary increase
B A strongly worded letter to a client who is querying the charges on his unit trust
C A call to a client's wife who has contacted you to advise of her husband's death
D A letter to a client asking the reason for non-payment of three premiums

22 The main advantage of writing a life assurance policy in trust is to:

A create a tax exempt fund
B ensure the policy obtains qualifying status
C ring fence the proceeds outside the individual's estate
D increase personal allowances

Unit 1 – Topic 16

Key legal concepts

Personal Representatives

- These people represent deceased people in order to distribute the estate
- How it is distributed depends on whether there is a valid will

- If there is a Will they are called Executors nominated by Grant of Probate
- If there is no Will they are called Administrators nominated by Grant of Letters of Administration

- The person who makes the Will is called the Testator

- Modifications to a Will are recorded on a codicil
- You must be 18 to make a Will in English law, 16 in Scotland.

- For a Will to be valid it must be:

    - Written
    - Signed by the testator
    - 2 witnesses to the testator's signature (not beneficiaries nor spouses of beneficiaries)
    - Testator must witness the witnesses' signatures

- A Will is invalid if:

    - It is destroyed with the intent to revoke it
    - A later Will is made
    - Testator marries or remarries unless it is made in contemplation of marriage

Deed of Variation

- Sometimes it is an advantage to the beneficiaries to vary the way the estate is distributed. In effect you are 'varying' the terms of the Will.

- This can only be done for family or more commonly tax reasons.

- In order to do it all beneficiaries under the existing Will must be over 18 and all must be in agreement to the variation.

- It must be done within 2 years of death and HMRC must be informed within 6 months of the variation.

Intestacy

- A person has died intestate if there is no Will or no valid Will
- The person who deals with the estate is the Administrator who applies for Grant of Letters of Administration.
- The rules of intestacy will apply which are:

    - Spouse but no children

        - Spouse receives all of the estate absolutely.

    - Spouse and Children

        - Spouse receives the first £ 250,000 plus half of anything above £250,000.

        - The other half of the estate above £250,000 goes to the children.

        - So, if a man dies leaving a wife and children and an estate of £500,000, the wife will receive £250,000 plus £125,000 with the other £125,000 to be divided between the children

    - Children but no spouse

        - Estate shared equally among the children.

    - Neither spouse nor children

        - Estate goes to the deceased's parents or if dead to the siblings

If no blood relative can be found, then the Crown will inherit the estate.

Trustees

- A Trust is created by the person who creates the trust – the settlor.

- When the trust is created the settlor has no legal interest in the trust property, unless the settlor is also a trustee. It now belongs to the trust itself.

- The trustee is now the person who has legal responsibility for that trust according to the trust deed.

- Trustees must be of sound mind and aged 18 or over. If a trustee dies the remaining trustees can appoint a new trustee.

Trustees must:

- Act in accordance with the trust deed. If they have discretion in exercising their powers then all trustees must agree
- Act in the best interests of all beneficiaries
- Under the Trustee Act 2000 trustees also need to:
    - Obtain proper advice when reviewing investments
    - Be aware of the need for suitable and diversified assets

Companies

- Limited companies are distinct legal entities – separate from the shareholders
- Therefore, the shareholders are not liable for the debts of the company
- Each company must have a Memorandum which sets out the powers of the company and Articles of Association which sets out the powers of the directors

Partnerships

- A partnership is not a separate legal entity and therefore the partners are responsible for the liabilities of the partnership
- The Partnership Deed is a written agreement which specifies how profits and liabilities are allocated amongst the various partners.
- A Limited Liability Partnership (LLP) is one where each partner's liability is limited to the amount they have invested into the partnership. In this sense, an LLP is very similar to a company except that each partner would be taxed as though they are self-employed on an income tax basis.

Law of Contract

- Contracts are binding whether made orally or in writing
- To be valid the following must exist:
    - All parties must have capacity – 18 or over and of sound mind
    - An offer and acceptance of that offer
    - Consideration – what each party exchanges – money or promise to pay money in return for a product or service
    - Intention to create a legal relationship
    - Must be legal
    - Terms must be clear and unambiguous
    - Contract must not have been coerced through misrepresentation, duress or undue influence

- Most contracts are based on the assumption of caveat emptor which means buyer beware.

- Life assurance contracts were always in the past based on the principle of ‘utmost good faith’ which meant that all material facts relevant to the application needed to be disclosed.

- However, life assurance companies in the past used this principle to sometimes not pay out on claims due to the fact that the policy holder had not disclosed all medical information irresepctive of whether it was relevant or not.

- This concern led to the introduction of the Consumer Insurance (Disclosure and Representations) Act 2012. The law has now been clarified on this issue. The duty of utmost good faith doesn’t require customers to volunteer information but it does require them to take reasonable care in relation to answering the insurer’s questions truthfully on the application form.

- The policy holder must take reasonable care in answering questions that they don’t make a ‘misrepresentation’ to the insurer.

- Therefore, if the insurer believes that the policyholder was careless in answering those questions, they can reject the claim but they would have to refund the premiums.

- If the insurer was of the opinion that the policyholder was reckless in answering the questions, then they can reject the claim and wouldn’t have to refund any premiums.

- If one of the parties to a contract does not perform its side of the contract, that person is then in breach of contract.

- If it was to go to court damages would be sought and if proven awarded to indemnify the claimant or to reinstate him for his loss – this will include legal expenses.

Law of Agency

- An agent is a person who acts on behalf of another person. The person he is acting for is known as the principal.

- The fundamental rule is that agents can enter into contracts on behalf of the principal and in law the actions of the agent are considered to be those of the principal.

- An agent should only act in accordance with the power and authority that they have been given. This is called actual authority.

- If the agent has exceeded their authority and this could be proved then the principal would not be held liable for the actions of the agent, and the agent could be sued for breach of contract.

- However, it may be the case that the agent is claiming that they acted within their 'apparent authority'. This occurs when the principal has done or said something which a reasonable person would conclude represented a further granting of authority. The court would have to decide or rule on this.

- If the agent has acted outside his authority and it can be proven then the agent could be held liable for his actions by a third party.

- Where the agent has exceeded his authority but the principal is happy with the outcome then this is called 'ratification'.

Ownership of Property

There are 2 types of property:

- Realty – land and everything attached to land
- Personalty – any property which is not land

Jointly owned Property

Joint Tenants

- Each joint owner owns 100% of the property – there is no division in percentage terms between them. Where one of them dies, the property passes to the surviving joint owner automatically.
- This is irrespective of any provisions made in a Will.

Tenants in Common

- This time each tenant in common owns a specific share of the property which may or may not be 50/50.
- On death the deceased's person's share is passed via their estate e.g. Will or intestacy.

Power of Attorney

- These are people who act on behalf of others. The donor grants the authority, the donee is given the authority.

- A person who is a minor or of unsound mind cannot create a power of attorney.

- A standard power of attorney will expire if a person becomes of unsound mind.

- A person of sound mind can appoint a Lasting Power of Attorney which only comes into force when a person becomes of unsound mind.

- If a person of unsound mind does not have a valid lasting power of attorney in place, no decisions can be made regarding their affairs until an application can be made to the Court of Protection to appoint a deputy. This process can take some time and can be expensive.

- Prior to October 2007, lasting powers of attorney were referred to as enduring powers of attorney. Existing enduring powers of attorney will remain in force, but all new arrangements must be lasting powers of attorney.

- Lasting powers of attorney can also cover personal and health matters whereas an enduring power of attorney can only cover financial and property issues.

- Lasting powers of attorney must be registered with the Public Guardianship Office, now referred to as the Office of the Public Guardian.

- Lasting Powers of Attorney can only be revoked by the Court of Protection

Insolvency and Bankruptcy

- Insolvency occurs when the value of a person's liabilities is greater than their assets and they are unable to meet their financial obligations.

- Bankruptcy occurs when an insolvent person is subject to a bankruptcy order by the court.

- An individual can petition for their own bankruptcy or a creditor can petition for it if they are owed £ 5000 or more.

- Enterprise Act 2002 reduced the period of bankruptcy from 3 years to 1 year. In Scotland, it used to be 3 years too but is now also 1 year.

- During that period the person is known as an undischarged bankrupt and cannot borrow more than nominal amounts of money and they may struggle to open a current account but may be able to open a basic bank account.

- Once declared bankrupt that person is assigned to the 'trustee in bankruptcy' whose duty is to recoup as much as possible for the creditors. Certain assets such as clothing, certain household items and work related items cannot be taken.

- Following discharge a person is referred to as a discharged bankrupt and must always disclose the existence of the bankruptcy in any credit or mortgage application.

- An individual voluntary arrangement (IVA) is an alternative to bankruptcy. The debtor will arrange with the creditors to re-schedule debts over an agreed period often 5 years.

- An IVA can only be achieved if creditors holding 75% of the aggregate debt are in agreement.

- An individual with an IVA will find it difficult to obtain credit while the IVA is in force and is likely to be impaired even after the end of the arrangement.
- For a company in financial difficulties with money owed to creditors, they can take out a Company Voluntary Arrangement which operates in a similar way.

UNIT 1 TOPIC 16 - LEGAL CONCEPTS			
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Unit 1 - Topic 16 Test

1 What is the benefit of a 'deed of variation' to a beneficiary under a will?

A That tax advantages can be obtained
B That a person can reject a gift given to them
C It is way of avoiding intestacy
D It is a way of meeting the deceased's wishes

2 When a single person dies intestate without any children, with an estate of £150,000, which one of the following would apply?

A The estate is shared equally between any brothers and sisters
B The estate is shared equally between the parents and grandparents
C The estate is shared equally between the parents
D Everything goes to the Crown

3 If a man dies intestate leaving a widow and children and an estate valued at £500,000, what is the MAXIMUM cash sum the widow will receive from the deceased's estate?

A £250,000
B £125,000
C £100,000
D £375,000

4 If a person dies intestate, what document will the deceased's legal representatives require in order to deal with the estate?

A Grant of probate
B Grant of Letters of administration
C Codicil
D Deed of variation

5 If there is a valid will, the insurer will determine the identity of the personal representatives by:

A obtaining a copy of a grant of letters of administration.
B obtaining a copy of a grant of probate.
C requesting clarification of the laws of succession.
D requesting a signed declaration from the solicitor.

6 **Your customer, Mr Smith, wants to know the best way of ensuring that his 16 year-old son, Tom, has a legal interest in the new house he has just bought. What would be the best way of doing this?**

A By creating an equitable interest
B Tom already has a legal interest
C By creating a trust
D By granting Tom a lease

7 **Martin has set up a trust fund for the benefit of his three grandchildren and has appointed two trustees with discretion to exercise their powers. In these circumstances:**

A Martin is known as a testator and the grandchildren as beneficiaries.
B the Trustee Act 2000 requires the grandchildren to obtain advice when reviewing investments.
C the trustees have no legal interest in the trust property.
D both trustees must agree before exercising their discretionary powers.

8 **Where a person with an invalid will dies, the insurer will determine the identity of the personal representatives by:**

A obtaining a copy of the grant of letters of administration
B obtaining a copy of the grant of probate
C requesting a certified copy of the will
D requesting a signed declaration from the solicitor

9 **Under the Consumer Insurance Disclosure Act 2012, the basis of 'utmost good faith' is that:**

A the proposer must answer honestly and truthfully all questions on the application form.
B the insurer is legally obliged to manage the client's money in an ethically and legally sound manner.
C all life assurance contracts are based on anticipated financial loss.
D companies base their underwriting on the information provided, rather than prejudice.

10 **When acting as the agent of a principal, it is a fundamental rule that:**

A a principal must ratify the acts of his agent.
B a principal must act within their apparent authority.
C a principal is always responsible for the acts of the agent.
D an agent can conclude contracts on behalf of the principal.

11 Walter and Winnie own their house on a joint tenant's basis. If Walter dies:

A his share of the property will pass automatically to Winnie.
B Winnie will need to purchase Walter's share of the property.
C his share will pass to whoever is nominated in his will.
D Winnie will own 50% of the property but retain an interest in the other 50%.

12 The difference between a lasting power of attorney and an ordinary power of attorney is that:

A a lasting power of attorney can be revoked at any time by the donor, whereas an ordinary power of attorney can only be revoked by the Court of Protection.
B an ordinary power of attorney becomes invalid if the donor becomes mentally incapable, whereas a lasting power of attorney remains effective.
C a lasting power of attorney can be agreed on a verbal basis between donor and donee but ordinary power of attorney must be registered at the Public Trust Office.
D an ordinary power of attorney remains valid if the donor becomes mentally incapable whereas a lasting power of attorney becomes invalid.

13 Tom was declared bankrupt in June 2018. For how long will his bankruptcy order remain in place?

A Until June 2022
B Until June 2024
C Until June 2019
D Until June 2020

14 Despite his recent marriage to Katrina, John's existing will has remained in force. Why is this?

A The will was written with the wedding in mind
B The will was witnessed by Katrina and her father
C John has no children or other dependents
D John's estate is valued at £199,000

15 Under the rules of intestacy, which one of the following ranks the highest should a divorced person die intestate?

A Brother and sister
B Ex-wife
C Father
D Son and Daughter

16 Which one of the following has the capacity to enter into a legal contract?

A A person under the age of eighteen years
B A limited company
C An unauthorised insurance company
D Someone who was purchasing guns for terrorist activities.

17 Peter, Paul and Pamela own a house on a 'tenants in common' basis, each having a 1/3 share. In the event of Paul's death:

A Peter and Pamela will automatically increase their share to 50%.
B his estate is obliged to sell his share to Peter and Pamela.
C the beneficiary of Paul's share will be determined by his will or the laws of intestacy.
D Peter and Pamela are obliged to purchase Paul's share from his estate.

18 What role does the Court of Protection play with lasting powers of attorney?

A Lasting powers of attorney can only be revoked with the consent of the Court of Protection.
B Lasting powers of attorney must be registered with the Court of Protection.
C Any action taken by attorneys must be agreed by the Court of Protection.
D The Court of Protection retains a list of all those qualified to act as attorneys.

19 What requirement rests on a discharged bankrupt when applying for a mortgage?

A As he is now discharged, there is no requirement
B To disclose the previous bankruptcy to the lender
C To disclose the previous bankruptcy to a credit reference agency
D To ensure the lender conducts a thorough credit search

20 When an individual dies intestate, leaving a spouse, children and an estate valued at £110,000, which one of the following applies?

A The estate is divided equally between the surviving spouse and children
B The entire estate passes to the spouse
C The surviving spouse inherits a life interest only in the deceased's entire estate
D The first £50,000 passes to the surviving spouse absolutely, along with a life interest in half the remaining estate

21 Any loss made by a partnership is usually:

A allocated amongst the partners in the same ratio as profits are shared.
B written off.
C held to be offset against future profits.
D held to reduce any potential tax liability.

22 Which ONE of the following items of property would be referred to as personalty?

A A collection of vintage wines
B A detached house
C A paddock used for grazing horses
D A Victorian factory building

23 One of the financial restrictions placed on undischarged bankrupts is that:

A they are only able to borrow nominal amounts of money
B they are unable to buy goods except for their own consumption
C they are unable to contribute to protection policies
D they are only able to work on an employed basis

UNIT TWO

UK FINANCIAL REGULATION

Topic 17

The Financial Conduct Authority's Aims and Activities

Introduction

- One of the primary objectives of the government is to balance the need for protection of the consumer with the need for businesses to make a profit.

- These two objectives are among the principles on which the European Union (EU) are based.

The Financial Services and Markets Act 2000

- There was a Financial Services Act 1986 where there was an attempt for the industry to self-regulate itself. This was not wholly successful.

- There were a number of reasons for the establishment of the Financial Services Authority (FSA) but the main problem was that the existing regulatory structure was too fragmented and there was need to have one single regulator which covered the whole industry.

- In June 1998 regulation of the banking sector, including products from banks, building societies and National Savings & Investments, and the Bank of England were transferred to the newly created single regulator, the FSA.

- In December 2001, The Financial Services & Markets Act 2000, transferred regulation of virtually the whole industry to the FSA.

- On 31 October 2004 the regulation of mortgages was transferred from the voluntary Mortgage Code Compliance Board (MCCB) to the FSA.

- In January 2005 the regulation of general insurance was transferred to the FSA.

How did regulation change after the financial crisis?

- The financial crisis of 2007-09 was essentially caused by a failure of prudential regulation. A number of firms were found to have inadequate management systems and financial safeguards.

- This led to concerns about the effectiveness of the existing regulatory system and its ability to prevent and then deal with a similar situation in the future.

- In the years following the financial crisis, there have been a number of issues related to the conduct of firms including the mis-selling of payment protection insurance, the LIBOR rate fixing scandal and the sale of interest rate products to corporates.

- These concerns led to the implementation of the Financial Services Act 2012.

Regulatory Reform – The Financial Services Act 2012

- A new body called the Prudential Regulatory Authority (PRA) operating within the Bank of England now has responsibility for the prudential supervision of the banks, building societies, insurance companies and other significant financial institutions**.** This means looking into their financial wellbeing, safety and soundness.

- A new Financial Policy Committee will also look at the economy in general and try to identify risks that may threaten the economy.

- The consumer protection role that the FSA used to perform has been transferred to another body called the Financial Conduct Authority (FCA) which has responsibility for the conduct and behaviour of all financial firms.

- So, some firms will be authorised and regulated by the FCA, whereas more ‘significant’ firms will be authorised and regulated by both the FCA and PRA.

Statutory Objectives, Role & Activities

- The role of the FCA and PRA is to oversee the regulation of the financial services industry. Their powers come from Parliament under the Banking Act 1987, the Financial Services and Markets Act 2000 and the Financial Services Act 2012.

- The FCA is a ‘quasi-government department and as the independent regulator of financial services, it has to report to the Treasury and to Parliament.

- The PRA and the FCA are jointly responsible for the Financial Services and Compensation Scheme and the FCA is responsible for the Financial Ombudsman Service and Money Advice Service.

- The FCA's single strategic objective is to ensure the financial markets work well so customers get a fair deal.

- The FCA has **three operational objectives**:

    - Protect consumers

    - Enhance the integrity of UK financial system

    - Help maintain and promote effective competition.

- With regard to competition the following will apply:

    - There are no undue barriers to entry to enable new providers to enter the market
    - Consumers are able to drive competition by being able to easily switch providers
    - No single firm is able to dominate the market.

- The Competition & Markets Authority also has powers in this area making it a concurrent or joint regulator with the FCA in this area.

- The FCA also provides a Handbook which gives guidance on the rules and regulations for authorised firms and individuals.

- The rules in the Handbook are binding obligations. Guidance explains the rules but does not have to be followed.

The Handbook (divided into five sections):

- High Level Standards (authorisation rules)

    - Threshold conditions – requirements for firms to be authorised

    - Statements of Principle for approved persons and the Fit & Proper Test for approved persons

    - The principles for business.

    - Senior Management Arrangements – what procedures are in place to ensure control of the business?

    - Training and competence

- Prudential Standards

    - This deals with the financial soundness of solely FCA regulated firms.

- Business Standards (rules on conducting business)

    - Conduct of Business Sourcebooks (COBS) such as MCOB for mortgages, ICOB for insurance and BCOB for banking. These relate to the rules in relation to the marketing and sale of products in these specific areas.

    - Market Conduct Sourcebook – rules concerning investment markets including insider dealing.

- Regulatory Processes

- Redress/Specialist Sourcebook

    - Redress – investor complaints and compensation
    - Specialist Sourcebook – supervision arrangements for credit unions, professional firms such as solicitors and accountants.

Principles for Firms & Approved Persons

- The FCA has a set of 11 Principle of Business with which firms must comply:

1. **Integrity** – a firm must conduct its business with integrity.

2. **Skill, care and diligence** – conduct its business with skill, care and diligence

3. **Management & control of the business** – organise and control its affairs responsibly and effectively with adequate risk management systems.

4. **Financial prudence** – a firm must maintain adequate financial resources.

5. **Market conduct** – a firm must observe proper standards of market conduct.

6. **Customers' interests** – firm must pay regard to its customers and treat them fairly.

7. **Customer communication** – a firm must communicate with its customers in a way that is clear, fair and not misleading.

8. **Conflicts of interest** – a firm must manage any conflicts of interest.

9. **Customers' relationship of trust** – a firm must take reasonable care to ensure the suitability of its advice.

10. **Clients' assets** – a firm must arrange adequate protection for its clients' assets

11. **Regulator relations** – a firm must deal with the regulator in open and co-operative way and to disclose anything which the FCA/PRA would reasonably expect.

Treating Customers Fairly

- One of the potential drawbacks of having a strict regulatory system was that it became apparent that firms and individuals could 'hide behind' the rules, using loopholes or technicalities to their advantage.

- The former regulator (FSA) quickly became aware of this and so launched its principles based initiative **Treating Customers Fairly (TCF)**. Its aim is to develop a more ethical frame of mind leading to more ethical behaviour.

- Responsibility for ensuring that TCF is introduced and built consistently into the firm lies with the senior management of the firm.

- Firms are expected to be clear about the services they offer and the true cost to the consumer. Firms need to consider how customers are able to compare their products against others in the market place to ensure a fair comparison can be made.

In summary, TCF is designed to deliver six improved outcomes for retail financial consumers.

- Consumers will be confident that the firm is committed to fair treatment of the consumer.

- Products are designed to meet the needs of customer groups

- Consumers are provided with clear information at all stages

- Any advice given is suitable for that client's circumstances

- Products perform as customers have been led to expect

- There are no unreasonable barriers to switching product or provider or making a complaint.

From 2009 onwards firms must be able to demonstrate that they are consistently treating their customers fairly and delivering the six consumer outcomes.

Prevention of Crime

The FCA is committed to reducing financial crime which includes:

- Market abuse

    - Insider dealing – taking advantage of information not yet known to the public, usually people who have access to restricted or confidential information.

- Market manipulation – where a person gives false or misleading information with the intention of influencing the share price.

- Money laundering (see Topic 23)

UNIT 2 TOPIC 17 – FCA Aims & Activities			
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Unit 2 – Topic 17 Test

1 **The Financial Conduct Authority's single strategic objective is to:**

A govern organisations that manage investments on behalf of other people.
B ensure that relevant markets work well so that customers get a fair deal.
C regulate the marketing and sale of all life assurance products.
D oversee the administration of all types of investment business.

2 **Individuals who are allowed to carry out certain functions in relation to a firm's regulated activities are often referred to as:**

A authorised persons
B approved persons
C appointed persons
D appropriate persons

3 **The second key Principle of Business as defined by the regulator is that firms must act with skill, care and:**

A control
B integrity
C diligence
D honesty

4 **'A situation where individuals use information about a company that is not generally available to deal for their own financial advantage' is a definition of:**

A insider dealing
B best execution
C market manipulation
D money laundering

5 **When did mortgages become regulated?**

A October 2004
B January 2005
C April 2006
D June 1998

6 **Which of the following is NOT one of the FCA's operational objectives?**

A Reducing the scope for financial crime
B Protecting and enhancing the integrity of the UK financial system
C Protecting competition in the interests of consumers
D Securing an appropriate degree of protection for consumers

7 Which one of the following is NOT one of the Financial Conduct Authority's Principles for Business with which a firm must comply?

A Conduct its business with integrity
B Communicate with customers in a clear manner
C Observe proper standards of market conduct
D Maintain an independent compliance function

8 Knowingly giving out false information to influence the price of shares for personal gain is known as:

A money laundering
B market manipulation
C best execution
D insider dealing

9 In seeking to promote competition, the FCA uses its power to ensure all of the following except which of the following:

A customers are engaged to drive competition
B there are no undue barriers preventing new providers from entering the market
C offering 'light touch' regulation for providers that show a strong record in product innovation
D preventing any single firm from dominating the market

10 What was the main driver for the Financial Services and Markets Act 2000?

A Increasingly high levels of fraud
B The lack of compliance within the banking industry
C Lack of consumer confidence in existing provisions
D The need for integrated legislation and regulation

11 One of the operational objectives of the Financial Conduct Authority is to:

A oversee the activities of financial organisations such as clearing houses, the London Stock Exchange and Lloyd's.
B provide appropriate customer protection.
C regulate mortgage lending and enforce the Mortgage Code.
D maintain market confidence and recommend suitable investments.

12 Who has prudential responsibility for deposit takers and insurers?

A Financial Policy Committee
B Financial Conduct Authority
C Financial Services Authority
D Prudential Regulatory Authority

13 There are three main areas of financial crime that the FCA seeks to control. Which one of the following is the exception?

A Mis-selling investments
B Money laundering
C Fraud and dishonesty
D Criminal market conduct

14 The FCA has powers under the Competition Act 1998 and the Enterprise Act 2002, meaning in respect of competition, it is a concurrent regulator with the:

A Competition Commission
B Office of Fair Trading
C PRA
D Competition and Markets Authority

15 Which one of the following contained within the FCA Handbook is binding on authorised firms?

A Rules
B Guidelines
C Standards
D Procedures

16 In which sourcebook does the FCA Handbook cover investor complaints and compensation?

A Interim Prudential
B Market Conduct
C Specialist
D Redress

17 In which sourcebook does the FCA Handbook cover standards for stockbrokers and financial market traders?

A Interim Prudential
B Market Conduct
C Specialist
D Redress

18 Which one of the following BEST describes the reason why the Financial Services and Markets Act 2000 was introduced?

A The existing regulatory structure was too fragmented
B It was necessary to make the Treasury the main authorising body
C The existing regulatory structure was too bureaucratic
D It was necessary to make the Home Office the main authorising body

19 Which one of the following is NOT covered by the Financial Conduct Authority's Principles for Business?

A A firm's relations with its regulators
B The protection of customers' assets
C Guidelines on financial promotions
D Maintenance of adequate financial resources

20 In relation to how a firm deals with its regulator, which one of the following is NOT defined within the Principles of Business? A firm must:

A deal with its regulators in an open way
B disclose appropriate data to its regulator
C deal with its regulators in a co-operative way
D disclose data on a regular basis to its regulator

21 Which of the following is NOT one of the Financial Conduct Authority's Principles of Business with which a firm must comply?

A Be open and honest with the market in all respects
B Communicate with clients in a clear manner
C Conduct business with integrity
D Observe proper standards of market conduct

22 The FCA considers that responsibility for the fair treatment of consumers lies with which of the following?

A A firm's advisers
B A firm's senior management
C All employees
D Operational managers

Unit 2 – Topic 18

Regulating firms and individuals

FCA Regulation of Firms and Individuals

- All financial services firms need to be authorised by the FCA if it carries out regulated activities with regard to regulated investments.

- These activities/investments are all the investments or activities studied in Unit 1 such as deposits, insurance, collective investments, gilts, shares, pensions, mortgages etc.

- Once authorisation is granted, these are sometimes referred to as 'permissions' with which the firm is allowed to deal in that area, often referred to as Part IV Permission.

Approved Person's Regime

- The Approved Person Regime (APER) still applies for many smaller firms but for larger firms, this has been replaced by the Senior Managers' Regime (see below).

- The central point regarding the Approved Persons Regime is that individuals who are looking to work in certain functions, referred to as **controlled functions,** had to gain approval from the FCA to perform that role and once approved, that person is registered with the FCA.

- To be approved, a 'fit and proper' test was necessary and this was also applied on an ongoing basis and there was also a code of practice that had to be adhered to.

The Senior Managers' and Certification Regime (SMCR) Framework

There are 3 tiers under SMCR:

- **Core –** firms in this tier will have to follow the basic requirements outlined in the rest of this section**.**
- **Enhanced –** firms representing the greatest risk to consumers will have additional requirements to fulfil
- **Limited –** these will be exempt from some requirements.

The core element will apply to the majority of firms and will consist of three key elements:

- The Senior Mangers Regime
- Certification Regime
- Code of Conduct

The Senior Managers Regime

- In addition to regulating the activities of firms, the FCA also regulates the appointment and activities of individuals within the firm. These rules are within the High Level Standards mentioned earlier.

- Two issues that had to be addressed after financial crisis of 2007 were firstly criticism of the approved person regime that exists and secondly, difficulties in identifying who was responsible if anyone for a business's failings.

- In response, the FCA and PRA introduced a new Senior Manager's and Certification Regime from March 2016. This establishes accountability for senior managers in relevant firms who are now personally accountable.

- This has now replaced the Approved Person Regime (APER) for most firms but smaller firms will still be operating under APER until 2019.

- The FCA and PRA personally vet those who are applying for a senior management role and firms must take action to ensure the ongoing fitness and propriety of their senior managers.

- Each firm must maintain a 'responsibilities map' which outlines the way responsibilities are allocated. This helps the regulators to identify which person is responsible.

- There is a duty for senior managers to take 'reasonable steps' to prevent regulatory breaches in their area of responsibility.

- One of the problems experienced by regulators in recent years has been their inability to take enforcement action against the senior management of the firm.

- These rules give the FCA/PRA the power to prosecute a senior manager for 'reckless misconduct' that has caused the institution to fail and the maximum punishment is a prison sentence of 7 years and/or an unlimited fine.

- The FCA/PRA define a number of senior management functions which fall under these rules; the most significant are:

    - Chief Executive
    - Chair
    - Executive Director
    - Partner
    - Compliance oversight function
    - Money laundering reporting function

A more comprehensive list applies to enhanced firms and a condensed one for limited scope firms.

The Certification Regime

- The regulators also recognise that there could be actions by individuals below senior management level that could still cause significant harm to a business and its customers.

- Individuals in 'significant harm' roles are subject to a Certification Regime: they are not required to secure direct approval from the FCA/PRA but the firm effectively certifies that they are fit and proper to carry out the role. This must also be re-assessed on an annual basis.

- Roles covered under the certification regime are likely to include:

    - Individuals in customer facing roles who need to be qualified such as mortgage advisers/investment advisers
    - Anyone who supervises or manages a certified person
    - Material risk takers
    - Proprietary traders
    - Significant management functions
    - Roles involved in algorithmic trading

- A designated senior manager must be responsible for each firm's certification regime.

The Code of Conduct

There is a code of conduct about standards of behaviour for those employed in firms covered by the Senior Managers Regime, other than support staff:

- You must act with integrity
- You must act with skill, care and diligence
- You must be open and co-operative with the regulators
- You must pay due regard to customers and treat them fairly.
- You must observe proper standards of market conduct.

For senior managers, there are specific conduct rules that they must follow:

- **SM1** - You must take reasonable steps to ensure that the business that you are responsible for is controlled effectively.
- **SM2** - You must take reasonable steps to ensure that the business that you are responsible for complies with the regulatory system.

- **SM3** - You must take reasonable steps to ensure that if any roles are delegated, they are delegated to an appropriate person and that you oversee the discharge of the delegated activity.
- **SM4** - You must disclose any information to the PRA/FCA that they would reasonably expect notice of.

Firms must make individuals aware of these rules and provide appropriate training and take action if staff fall below the required rules.

The FCA also requires firms to report to them if they take disciplinary action against a member of staff as a result of breaching the conduct rules including:

- The FCA requires firms to report to the FCA within 7 days if they take disciplinary action against a senior manager for breach of the conduct rules. For all other staff, an annual report is sufficient.

Implementation of the Senior Managers and Certification Regimes

- For banks, building societies and credit unions these rules came into force in March 2016. The regime will be extended to 'FCA only' regulated firms from 9 December 2019.

The Fit & Proper Test

There is a criteria to determine whether a person is 'fit and proper' to be approved to undertake a senior management function or a controlled function or subject to the Certification Regime.

This relates to:

- Honesty and integrity judged by:
    - Criminal record
    - Disciplinary proceedings
    - Any previous record with regard to FCA rules
    - Complaints record
    - Insolvency record
    - Dismissal from a position of trust

- Competence and capability in meeting FCA's training and competence requirements

- Financial soundness based on current financial position, any previous bankruptcies and credit rating.

- As part of the test, references from current and former employers over the last 6 years must be provided including any disciplinary action taken against the individual also covering the last 6 years

Responsibilities, Systems & Controls for Senior Managers

- Senior managers have to take responsibility for a firm's compliance and this will involve:
    - A clear chain of responsibility
        - Senior managers will be held responsible for the firm's activities. In large firms, this can be delegated but there needs to records and controls in place regarding this
    - Systems & Controls
        - Firms must have appropriate systems and controls and these must be documented and regularly reviewed. These will include:
            - Chains of responsibility – delegation & reporting
            - Compliance
            - Assessment & risk reporting
            - Management information reporting
            - Competence and honesty of staff
            - Controlling business risks strategy (recovery from fire or computer failure)
            - Readily accessible records (secure backup systems)
            - Independent audit of the systems and controls must be made

The FCA approach to supervision

- The FCA seeks to ensure that firms are complying with regulatory requirements through a programme of supervision based on 10 principles.
    - Ensuring fair outcomes for consumers
    - Being forward looking – identifying potential risks before they impact
    - Being focused on the big issues
    - Taking a judgment based approach
    - Ensuring firms act according to the spirit of the law
    - Examining business models
    - An emphasis on individual accountability
    - Being robust when things go wrong
    - Communicating openly with the industry
    - Having a joined up approach – consistent messages

- The starting point in relation to how they will supervise a firm is assessing which of the supervision categories a firm falls into:

Fixed Portfolio

- Banking and insurance groups with a very large number of retail customers. They are subject to the highest level of supervision, are supervised using continuous assessment and there will be a named FCA/PRA supervisor.

Flexible Portfolio

- Firms with smaller numbers of retail customers, smaller firms and almost all intermediaries. Their business model is analysed and the first contact point would be the FCA customer contact centre.

- These tend to be lower risk firms that are supervised by a mixture of targeted supervisory work and programmes of education and communication.

The FCA's supervision model is based on 3 pillars:

- Proactive firm or group supervision – assessing whether the firm are committed to the interests of the consumer.

- Event driven reactive supervision – dealing faster with problems that have emerged.

- Issues and products – each sector of the market is examined to analyse current events and to identify potential problems

Training & Competence

The FCA has set out rules and guidance for all firms to ensure competence of all individuals employed in a controlled function

There are three categories of employees with detailed competency and training rules:

- Financial advisers and those dealing in or managing investments

- Supervisors of those advisers

- Supervisors who oversee certain 'back office' functions such as supervisors of underwriting or claims staff in a life insurance firm

Other approved persons are not subject to these rules unless they are involved in the sales process.

Training

- Firms must determine each employee's training needs and arrange training. The success of the training in meeting its objectives must be evaluated.

Assessing Initial Competence

- Investment advisers must not be allowed to begin advising until the employer is satisfied that they:

    - the knowledge and skills to operate under supervision **AND**
    - they have passed the relevant modules of an appropriate examination e.g. DiPFA 1

- Individuals must work under supervision until they:

    - Have passed ALL modules of an appropriate exam AND
    - Demonstrated an ability to work competently with minimum supervision

- If an employee carries out a regulated activity, the employee must attain any appropriate qualification within 30 months of starting that role.

- There are different examination standards for advisers in different roles. For mortgage advisers, CeMAP is the standard qualification.

Maintaining Competence

- A firm must also have arrangements to ensure staff maintain competence. This is known as Continuing Professional Development (CPD)

- A review must take place on a regular basis to assess this competence.

- For retail investment advisers, a minimum of 35 hours per annum is required in any 12 month period, of which 21 hours must be 'structured CPD.

- Structured CPD could include seminars, lectures, conferences, workshops, eLearning activities of 30 mins or more.

- Unstructured CPD could be independent research, reading industry publications, coaching sessions.

Record Keeping

- Employers must retain records showing how an employee's continuing competence is being assessed.

- These training records must be kept for a certain period after an employee has left the firm or ceased a particular role. The periods are:

    - 3 years for non MiFID business
    - 5 years for MiFID business (higher risk investment business)
    - indefinitely for pension transfer staff

- Since January 2013, advisers have been required to obtain a 'Statement of Professional Standing' (SPS) each year from an FCA accredited body. In order to receive this, an adviser must meet professional standards, and adhere to a code of ethics and confirm that they hold a required qualification.

Discipline and Enforcement

- Where the FCA suspects that the rules have been broken they can undertake an investigation.

- The person appointed to lead the investigation has the power to demand that questions are answered, information and documentation are provided.

- Firms should also have 'whistle blowing' procedures in place to enable employees to report serious inappropriate circumstances or behaviour within the firm. Any employees who do report misbehaviour have a right to protection under the **Public Interest Disclosure Act 1998**.

Enforcement Powers

If a firm fails to comply the FCA has range of disciplinary powers including:

- Varying the firm's permissions – removal of a specific permission e.g. mortgages

- Withdrawal of approval/authorisation – an approved person being struck off.

- Seek an injunction – FCA freezes the assets of the firm

- Seek restitution – FCA applies for a court order to have proceeds forfeited to them

- Seek redress – this time the court order forces the gains to be returned to clients.

- The FCA also has the power to make disclosures about a firm, announcing that it has begun disciplinary action against a firm although they must consult the firm before making the announcement.

- Enhanced supervision – intense supervision where there are serious governance failings.

- Disciplinary action – more minor issues can be dealt with a private warning, statement of misconduct or financial penalty.

- Before taking action against a dual regulated firm, the FCA will consult with the PRA. They could then decide to pursue a joint investigation or for one of them to act alone.

UNIT 2 TOPIC 18 – Regulating Firms & Individuals			
Question	**Answer**	**Mark**	**Comments / Notes**
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Unit 2 – Topic 18 Test

1 The FCA rules insist that an organisation's systems and controls are clearly documented. Which ONE of the following is also an FCA rule with regard to systems and controls?

A They must be regularly reviewed
B They must be notified to customers
C They must be agreed by the FCA before implementation
D They must meet an agreed industry standard

2 Which statement BEST describes the relationship between the 'fit and proper' test and the Senior Managers and Certification Regime?

A A 'fit and proper' test is recommended by the FCA for anyone applying for a senior management role.
B A satisfactory 'fit and proper' test is necessary before an individual can be accepted for a senior management role.
C The 'fit and proper' test is mainly designed to establish the creditworthiness of an approved person
D The 'fit and proper' test relates solely to previous business activity in a controlled function

3 If the FCA discovers a contravention of its rules, one of the steps it may take is to vary a firm's permissions. This means that:

A the firm may have one of its regulated activities removed
B the firm will be required to sell assets to provide restitution
C the firm will need to seek authorisation from a different regulator
D the firm will be required to submit each sale to the FSA for approval

4 Which one of the following areas is NOT included in the 'fit and proper' test required by the FCA?

A Criminal record
B Complaints received
C Disqualification as a director
D Previous levels of earning

5 **In the FCA Handbook there is a section on rules relating to arrangements, systems and controls within authorised firms. These rules:**

A detail the actual size, staffing structure and form which all firms' control systems must take.
B identify and categorise all the types of risks which firms are required to manage.
C require directors and senior managers to take responsibility for the effective management of their firms.
D state that all responsibilities relating to a firm's control systems must only be delegated to the firm's compliance officer.

6 **What is the FCA's most severe disciplinary power?**

A Financial penalties
B Withdrawal of authorisation
C Public censure
D Private warning

7 **Which one of the following job applicants is LEAST likely to meet the FCA 'fit and proper' requirements?**

A Gill, who has recently been made redundant from a firm of independent financial advisers
B Veronica, who has missed her last two mortgage payments following a divorce
C Josie, whose father's house was repossessed three years ago
D Irene, who currently has an authorised overdraft limit of £2000

8 **The FCA Training and Competence Sourcebook is PARTICULARLY prescriptive in relation to three groups of employees who are subject to detailed training and competence rules. These three groups include:**

A the company accountants, financial advisers and supervisors of certain 'back office' functions.
B supervisors of certain 'back office' functions, clerical claims staff and supervisors of advisers.
C financial advisers, supervisors of those advisers and supervisors of certain 'back office' functions.
D supervisors of advisers, supervisors of certain 'back office' functions and clerical staff.

9 **Training and competence records for an individual working for a non MIFID firm must be retained for a specified period after they have left the firm. This period is:**

A three years
B five years
C seven years
D ten years

10 **Peter has almost completed his induction training with Haddon Bank, prior to taking up a position of trainee financial adviser. The FCA require that the training he receives is:**

A documented and retained for 12 months
B evaluated to check its success
C at least 50 hours per annum
D carried out only by approved persons

11 **Simon has undergone his initial financial adviser training with Brington Bank, but has not yet passed an appropriate examination. Under what circumstances might he be allowed to advise customers about regulated products, if at all?**

A He may do so provided investments are below an agreed level
B Under no circumstances can he offer advice to customers
C He may do so provided he acts under appropriate supervision
D If all advice is double-checked by a representative of the FCA

12 **Which of the following statements is FALSE in relation to Training and Competence regulation?**

A Firms must monitor continuing competence
B Records of assessment criteria must be kept
C All approved persons are subject to the detailed rules
D Those subject to the rules may need to pass a detailed examination

13 **Which one of the following areas is NOT specifically covered by the 'Training and Competence' requirements?**

A Practical Assessment
B Initial training
C Business production levels
D Ongoing supervision of 'competent' advisors

14 Tom has been successful in his training as an authorised adviser. What happens next?

A His continued competence will be monitored
B He will have to complete 15 hours continuing professional development per annum
C He will be required to take further examinations
D His line-manager will draw up a development plan

15 Which of the following group of company employees would NOT be subject to detailed rules of training and competence under the FCA's Conduct of Business rules?

A Directors
B Back office supervisors
C Investment advisers
D Sellers of stakeholder pensions

16 Before an employee carries out duties that fall under the FCA's regulatory responsibility he should:

A have successfully completed his probation period.
B have completed the required number of hours' continuing professional development.
C assessed as competent to undertake the role without supervision.
D be assessed on technical knowledge and its application.

17 Those individuals categorised by the FCA/PRA as performing a 'significant harm' function must be approved by:

A both the FCA and PRA
B either the FCA or PRA
C their employing firm under the certification regime
D their employing firm under the senior managers' regime

18 Individuals performing which of the following roles will be individually vetted and approved by the FCA/PRA?

A Those performing an ancillary role
B Those performing senior management functions
C Those in significant harm functions
D Those in significant harm and senior management functions

19 The FCA categorises roles into various functions; into which type of function would the Money Laundering Reporting function be categorised?

A Customer function
B Governing function
C Risk function
D Senior management function

20 Which of the following bank employees would not normally require individual FCA/PRA approval?

A A financial adviser
B Director of regulated sales
C Chair Person
D Money laundering reporting officer

21 The FCA's supervisory model would see a fixed portfolio firm as being one that:

A does not have a named supervisor at the FCA
B is a small firm and has a small market presence
C is subject to the highest level of supervisory attention
D is supervised through targeted supervisory work and programmes of communication and education.

Unit 2 – Topic 19

Prudential supervision

The rules and regulations in relation to prudential regulation concentrates on the risk systems that need to be in place to minimise the risk for a customer of their money being put at risk due to financial failure of the firm.

The Global Context for International Prudential Regulation

- The Basel Committee on Banking Supervision is the primary global standard for the global prudential regulation of banks.
- The Basel Accord was agreed set out the minimum capital requirement for banks, this has been extended by Basel II and Basel III is also to be phased in over a number of years.

Capital Adequacy Regulations

- Regulations about capital adequacy broadly state that institutions must have sufficient capital to make it unlikely that any deposits will be at risk.

- In this respect, capital means the bank's own capital base not funds deposited by customers. In other words, any losses made by the bank should be borne by the shareholders and not the investors.

- Minimum capital adequacy is set to prevent depositors from losing their deposits.

- Minimum capital adequacy is specified in terms of an absolute amount of capital that a business must hold, a solvency ratio, as it's known.

- The solvency ratio details required capital as a proportion of the bank's assets with allowances made for the risk level of these assets.

- In respect of regulatory capital, under Basel III banks are required to reach a minimum solvency ratio of 7% by 2019 taking account of the risk of the asset.

- Banks holding UK government gilts have a risk weighting of zero as these are very safe whereas unsecured loans would have a risk weighting of 100%.

- In summary therefore, the higher the risk element of the asset that the bank holds, the higher the level of capital that the bank is required to hold.

- There are additional capital requirements for banks deemed to be 'too big to fail'.

- The Financial Stability Board, an international organisation issued a minimum Total Loss Absorbing Capacity(TLAC) standard for 30 banks identified as globally systemically important banks (G-Sibs) that Basel has identified as being too big to fail.

- The TLAC requirements aim to bolster these G-Sibs capital and solvency ratios. From 1 January 2019, the minimum TLAC for G-Sibs will need to be at least 16% rising to 18% from January 2022.

Liquidity – Liquidity Risk

- This issue has been at the heart of the credit crunch and concerns the measure of a bank's ability to acquire funds immediately to meet cash demands.

- The Northern Rock crisis illustrated this problem. Their business model was based on the continuing availability of being able to borrow on the interbank market to fund their lending. When this dried up, the bank's liquidity disappeared.

- When this information became public knowledge, it led to a large number of depositors choosing to withdraw their savings referred to as a 'run on the bank' They didn't have access to these amounts as most of their deposits are lent to customers who wish to borrow.

- Therefore, it is viewed that banks should try and avoid having a high concentration of liabilities around the same time which could drain their resources and that they should be looking to match receipts from assets against liabilities as much as possible.

- Banks and other deposit takers are required to have risk management systems in place to monitor this on an ongoing place and to carry out stress testing simulations to see how they would cope with specific and global scenarios.

Operational Risk

- Operational risk is the risk of loss caused by failed internal processes, or failed systems in place to prevent issues such as staff fraud, computer failure or even natural disasters.

- Capital requirements for operational risk now have to be in place and firms are required to cover this by multiplying the institutions average gross income over the last 3 years by 0.15.

FCA/PRA Prudential Standards

- The FCA and PRA Handbook has a section on prudential standards and requirements for firms with different subsections.

- GENPRU is the general prudential sourcebook which applies for banks, building societies and insurers.

- More specific prudential sourcebooks apply for banking (BIPRU), investment firms (IFPRU), insurance (INSPRU) and mortgages (MIPRU).

IFPRU

The Capital Requirements Directive sets out minimum capital requirements that are within IFPRU, which sets out the minimum amount of capital that an investment firm must hold which are;

IFPRU 50K Firm

- a firm that does not deal on its own account or underwrite issues of financial instruments and does not hold client money is required to hold capital of at least €50,000.

IFPRU 125K Firm

- a firm that does not deal on its own account or underwrite issues of financial instruments and is authorised to hold client money is required to hold capital of at least €125,000.

IFPRU 730K Firm

- Any firm that does deal on its own account and can underwrite issues of financial instruments and therefore does not fall under the 50K or 125K category must be a 730K firm and is required to hold capital of at least €730,000.

Unit 2 – Topic 20

Conduct of business requirements (part one)

This section looks at some of the rules in relation to the advice and sales process.

Types of Customer

Under the regulations customers are defined within three categories:

- Eligible Counterparty
  - This is someone or an organisation with a high degree of financial knowledge such as the government, banks, building societies, other financial firms and individuals who work in a controlled function. It is usually where the counterparty requires a limited service with no advice being given.
  - As such, they are given the lowest level of customer protection.

- Professional Client
  - A customer who has some knowledge or experience of financial services. The main difference here from an eligible counterparty is that advice is being given.
  - When dealing with professional clients, advisers can assume that the client has an adequate level of knowledge and an ability to accept certain risks.

- Retail Client
  - Someone with very little knowledge of financial services
  - Most customers fall into this category, 'person in the street'
  - These people require the highest level of customer protection

Different Categories of Investment Adviser

Investment advisers are grouped into one of two categories:

- **Independent advisers** where recommendations in relation to a 'retail investment' product are made which are unrestricted and unbiased based on a comprehensive and fair analysis of the market

- **Restricted adviser** – simply someone who does not meet the requirement to be able to call themselves independent - restrictions may be in terms of the number of product providers or the range of individual products.

- It is still possible for an independent adviser to use a panel as long as the panel is sufficiently broad and diverse, the client is not materially disadvantaged and the client must have the ability to go 'off panel'.

- If the firm uses a 'specialist' adviser who just deals in one area e.g. IHT advice. Then if the firm are to call themselves independent, the specialist adviser must also meet the independent rules.

- From January 2018, as part of MiFID II the FCA has clarified its rules on independent advice to confirm that a firm can call itself independent even if it only offers advice on a certain area eg pensions. To do this, the firm would have to offer advice on all pension product types and the range would have to be 'sufficiently broad and diverse'.

- Therefore, in summary as of 2018, to justify being 'independent' there will no longer be a requirement to advise on all retail products, an independent adviser may choose to just focus on a particular area eg investments or pensions.

- Retail investment products covers:

    - Life policies
    - Personal and stakeholder pensions
    - Other packaged investments such as investment trusts, unit trusts, OEICs
    - Structured capital at risk products

These rules don't apply to mortgages which will be considered later.

Execution Only

- This is where the customer directs the advisor to arrange the transaction for a specific product from a specific provider.

- For these types of transaction, the adviser does not have a duty to fully explain the risks involved. The customer is acting on his own responsibility.

- The Financial Ombudsman Service (FOS) has indicated that it expects firms to be able to provide 'clear and credible' evidence that a transaction was conducted on an execution only basis. Therefore, advisers must also obtain the client's signature to confirm that the transaction is execution only.

- A different situation arises where an adviser provides advice to the client but the client wishes to go against the advice – 'insistent customers'. In this situation, the adviser should also require the customer to sign to confirm that they are acting against the advice given.

- MiFID has introduced an 'appropriateness test' for these types of sales whereby the firm has to ask the consumer for more information to help them to decide whether the consumer has the necessary knowledge and experience to understand the risks involved in the transaction. This applies mainly to more complex products.

Advertising and Financial Promotions Rules

These cover invitations or inducements to enter into investment activity and include advertisements in all media forms and telephone calls.

- There is a distinction made between **'real time'** promotions – personal visits, telephone conversations and '**non real time'** – letter, newspaper, TV, website.

- The overall principle is that non real time promotions to retail and professional clients (see later)

    - Must be clear, fair and not misleading. With regard to retail clients specifically, they must be accurate, be understandable by an average member of the group it's aimed at and not disguise important terms or warnings.

    - Direct offer advertisements must contain the name of the regulator, the FCA.

    - Be accurate including not only emphasising potential benefits but also an indication of any risks.

    - Information about past performance must not be the most important part of a promotion and be based on an appropriate period of not less than 5 years or the period the product has been available if shorter, but not less than one year. *Past performance is not necessarily a guide to future performance"*

    - Comparisons with other products must be meaningful and be presented in a fair and balanced way. There are also requirements for firms covered by MiFID to detail the source of information and the assumptions made in the comparison.

- The rules applying to unsolicited real time promotions are:

    - Unsolicited approaches or cold calling is allowed for packaged products such as life assurance policies and unit trusts but not permitted for the sale of mortgages or higher risk investments

    - Unsolicited calls may not be made between 21.00 and 9.00 and all day Sunday. The caller must always check to confirm that the recipient is happy to continue with the call.

Advertising Standards

- The Advertising Standards Authority (ASA) is an, independent, body that administers the British Code of Advertising and Sales Promotion.

- The ASA covers virtually all advertisements such as:

    - Press and magazines
    - Posters and hoardings
    - Direct mail leaflets
    - Cinema commercials, videos, CD ROMs and the internet
    - Competitions and prize draws
    - Television and radio

- The code requires that all advertisements should be legal, decent, honest and truthful.

- Advertisers are permitted to express opinions provided that it is made clear that it is an opinion and not a statement of fact. Anything that goes beyond opinion must be able to be objectively proven.

- The ASA can take action against advertisers if they feel that there has been a breach of the code.

Adviser Charges

- From 1 January 2013, under RDR, financial advisers advising on investment business are no longer able to receive commission and the service is now fee based.

- Commission is still allowed in relation to the sale of insurances such as term assurance, critical illness, income protection etc.

- The charging structure must be clear, fair and not misleading, based on the service provided and must be disclosed to the client at the outset. This will need to include the amount due, the frequency and the implications of cancellation before the charges are paid.

Sales Process for Investment Business

1. Information about the firm, services and charges

- Before any business is discussed, the adviser must disclose to the client certain information about themselves and the services they provide.

- This may be referred to as the **services and costs disclosure document** (SCDD) or **initial disclosure document** (IDD**).** However, firms can develop their own disclosure documentation. It will typically include:

  - The name and address details of the firm
  - How communications will be made to the client
  - Full name of the regulator and the authorisation status of the firm
  - Whether the advice is independent or restricted
  - Details of complaints procedure
  - Details of payment for the services provided

Client Agreement – designated investment business

- Designated investment business is dealing in investment assets directly for a client as opposed to selling packaged investments such as unit trusts, OEICs or investment trusts.

- If a firm is advising on **designated investments**, then the firm must enter into a written basic agreement called a **Client Agreement** setting out the rights and obligations of the firm and client.

- The types of products involved here are likely to include equities, options, futures.

- The client agreement is also likely to include the terms upon which the adviser is able to operate in respect of the client's investment including investment range and limits.

2. The Fact Find - Suitable advice rules

- Advisers must not give investment advice until they have discovered the client's personal and financial circumstances. This is sometimes referred to as the fact find. There is no prescribed format for this so firms can draft their own. It will generally include:

  - Personal information
  - Employment details
  - Assets – property, savings and investments
  - Liabilities – mortgage, loans, credit cards

- Expenditure – household expenses, travel expenses, socialising
- Attitudes & objectives – attitude to risk and tolerance of risk

- Fact find information must be retained as follows:

  - Pension transfers, opt outs & FSAVCs – indefinitely
  - Life policies, pension contracts & MiFID (stocks & shares) – 5 years
  - Other products – 3 years

- Retaining the fact find information for certain periods of time helps the firm to deal with complaints and provides an audit trail as required under the Conduct of Business Sourcebook.

3. Product Disclosure

Those advising and selling 'packaged 'products such as life policies and pensions must provide details of the key features of the product before the sale is concluded. This is sometimes referred to as a **Key Features Document**. This will include:

- The important elements of the product
- Risk factors
- Arrangements for handling complaints
- Compensation available from the Financial Services Compensation Scheme
- The right to cancel
- Information on charges

Key Information Document (KID)

- From January 2018, a Key Information Document (KID) must be provided if the customer is buying a 'packaged retail and insurance based investment product (PRIIP)

- These are products which essentially are subject to risk from market fluctuations.

- This means that from 2018, the following products will be required to be issued with a KID prior to the application:

  - Derivatives
  - Unit Trusts, OEICs, investment trusts
  - Insurance based investments eg unit linked & with profit endowments
  - Structured products and deposits

- Pension products, shares, gilts and general and pure protection policies will not need to be issued with a Key Information Document,

- The KID must be no longer than 3 sides of A4 and the language must be plain, concise and easy to understand.

4 Suitability Letter or Report

- This letter explains to the client the reasons for the recommendation

- The report should also identify any possible disadvantages of the transaction for the client such as any lock in period and needs to be in plain English.

- These letters are required for products such as:

    - Life policies
    - Pensions including pension transfers and opt outs
    - Unit trusts, OEICs and investment trusts based on savings schemes

- There is no FCA requirement for the issuing of suitability letters for mortgages although they will usually be provided.

- For life policies and investment advice, the suitability report should be provided before the contract is concluded.

- For pensions business, it should be done no later than 14 days after the contract is concluded.

- For any other case, the report should be provided as soon as possible after the transaction has been executed.

Cooling Off and Cancellation

- This concerns the customer's right to change his mind and withdraw from a sale within a specified period, either 14 or 30 days and the notice runs from the date the contract begins or the date on which they receive the contractual terms if later.

- For life and pensions and pure protection policies like critical illness the period is 30 days.

- For investments, deposits and other insurance contracts like general insurance, the period is 14 days.

- If this occurs the customer will receive a full refund unless the product is a lump sum investment where the value of that investment has fallen AND this point is explained to the client in the contract.

- In this case the customer will receive the investment's reduced value.

- At the time the product is purchased, the adviser must explain whether the client is liable to pay any outstanding adviser charges if they do cancel. It is also important that the firm can evidence that a cancellation notice is issued, otherwise the customer can cancel at any time and will not be liable for any loss.

UNIT 2 TOPICs 19&20 – Prudential Regulation & Conduct of Business Part 1			
Question	**Answer**	**Mark**	**Comments / Notes**
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Unit 2 – Topics 19 & 20 Test

1 **Justin, a financial adviser, hopes to extend his client bank by making unsolicited telephone calls to a list of people he has taken from the telephone directory. As he is aware of the FCA rules, he will only be making contact:**

A between 9am and 8pm Monday to Friday
B between 9am and 9pm Monday to Saturday
C between 9am and 9pm Monday to Friday
D between 9am and 8pm Monday to Saturday

2 **Which of the following criteria is NOT one that must be satisfied by an advertisement in order to comply with the FCA's guidelines on advertising?**

A The advert must be authorised by the FCA
B It must be tailored to the likely sophistication of the reader
C It must be clear, fair and not misleading
D It must make reference to any potential risks involved

3 **What is the minimum period for which customer records, in respect of pension transfer and opt out contracts must be kept?**

A Three years
B Six years
C Ten years
D Indefinitely

4 **A key function of a client agreement is to set out:**

A the individual contracts that the adviser is licensed to sell.
B the areas from where a potential client can obtain advice.
C the rights and obligations of the firm and client and to disclose charges.
D the Financial Services and Markets Act.

5 **A restricted adviser is one who:**

A can only make recommendations based on the products of a single provider
B has not passed all the exams to enable them to give independent advice
C can only give basic advice on stakeholder products
D does not meet the requirements to be independent

6 Under the 'know your customer' requirements, advisers should:

A assume that a private individual fully understands the risks involved
B explain the potential product risks to an execution only client
C provide the highest level of advice and duty of care to clients categorised as retail customers
D offer exactly the same duty of care and advice to all customers

7 When an adviser transacts designated investment business for a client, the basis or amount of the charges would normally be disclosed in which document?

A The client agreement
B The key features document
C The statutory cancellation notice
D The suitability letter

8 Which compliance health warning MUST appear on all advertising material containing details of past investment performance? Past performance:

A is only a general guide to the future
B of five years or more is a reasonable guide to the future
C is not necessarily a guide to future performance
D is not necessarily better than future performance

9 From 2018, a Key Information Document (KID) will be required for all these products except:

A personal pension plan
B a unit trust
C an OEIC
D a unit linked endowment

10 If a client intends to purchase an investment product from an adviser on an execution only basis, then:

A no charges will be payable
B this is only possible with high net worth clients
C no recommendation will be required
D this is only possible with professional clients

11 In terms of knowing your customer, what is an eligible counterparty?

A Where a firm acts on behalf of a private customer
B A private customer
C Where a customer is in a controlled function in financial services
D A corporate customer

12 To meet the FCA definition of independent advice, recommendations must be based on:

A a complete analysis of the relevant market.
B a comprehensive and inclusive analysis of the relevant market.
C a thorough and fair analysis of the whole market.
D a comprehensive and fair analysis of the relevant market.

13 What is the latest date, if any, that the suitability letter can be sent to a customer who is considering investing in a personal pension plan?

A Before the contract is concluded
B Five days after the final interview
C Five days after the end of the cooling-off period
D No later than 14 days after the contract is concluded

14 When carrying out a sale on an 'execution-only' basis, the responsibility for the transaction rests with the:

A adviser
B regulator
C product provider
D customer

15 Henry invested £1,000 in a unit linked lump sum product and cancelled seven days later and received back £950. What did this reduction most likely represent?

A Handling charge
B Adviser's fee
C Cancellation charge
D Reduction in market value

16 Fact Find information for firms covered by MiFID must be kept for how long?

A Indefinitely
B Five years
C Three years
D Ten years

17 A professional customer is best described as:

A a regulated collective investment scheme.
B a firm dealing on behalf of a private customer with some knowledge of the industry.
C an inexperienced private investor.
D a firm or institution dealing on its own account.

18 What does an execution only transaction require an adviser to do?

A To provide advice that will inform the customer's choice
B To make a range of recommendations for the customer.
C To ensure that the client signs to confirm it is an execution only transaction
D To effect the transaction on behalf of a market counterparty

19 For which of these customers is a specific client agreement least likely to be given to a client?

A John and Jenny who are looking for a repayment mortgage
B Bob who is looking to invest in equities
C Paula who is considering the derivatives market
D Simon who is interested in the futures market

20 Which of the following will not be included in an initial disclosure document?

A Product recommendations
B Complaints procedure
C Name of the regulator
D Services offered

21 The 'cooling-off' period usually starts from the date:

A the application form was signed
B the policy document was issued
C the contract begins
D the acceptance terms were issued

22 How long should most customer records be kept in relation to pension contracts?

A 3 years
B 5 years
C 10 years
D Indefinitely

23 A £12,000 unit linked single premium investment bond is cancelled by a customer within the cooling-off period. However, during this period, the stock market fell sharply. Consequently, so did the value of the bond. What is the customer likely to receive?

A £12,000 less a market adjustment, if specified in the contract
B £12,000 less a market adjustment, whether or not specified in the contract
C 95% of the surrender value of the investment bond
D The paid up value of the investment bond

24 An adviser must issue a key features document or key information document prior to a sale being concluded, for all of the following products except:

A life assurance
B stakeholder pensions
C unit trusts
D gilt edged securities

25 Haddon Bank are about to begin an advertising campaign to promote fresh interest in their UK Equity Fund, which was launched ten years ago. Since they intend to show recent performance of the fund, what is the MINIMUM period over which performance figures must be shown?

A 10 years
B 7 years
C 5 years
D 1 year

26 Mortgage Advice Ltd has found that their primary method of obtaining new business is NOT permitted under Financial Conduct Authority regulation. This means that they must have been using which of the following methods?

A Cold calling
B TV advertising
C Mortgage introducers
D Radio advertising

27 In order to satisfy the Capital Requirements Directive, certain investment firms must have minimum capital of at least €125,000. Under what circumstances are these firms allowed to reduce this to €50,000?

A If they only buy and sell assets to fulfil customer orders
B If they buy and sell assets with the intention of selling them to their customers
C If they do not handle client money
D If their solvency ratio exceeds 4%

28 Which of the following risks would be defined as that arising from the way that a business is run and managed?

A Capital adequacy risk
B Internal risk
C Liquidity risk
D Operational risk

29 A bank's capital as a proportion of its risk weighted assets is referred to as the:

A capital adequacy margin
B liquidity ratio
C prudential standard
D solvency ratio

30 Liquidity is a measure of:

A the excess of a business's assets over its liabilities
B an insurance company's potential exposure to claims
C the ease and speed with which a business's assets can be converted into cash
D the level of savings in notice accounts

Unit 2 – Topic 21

Conduct of business requirements (part two)

- The rules in relation to the advising and selling of mortgages are contained in the Mortgage Conduct of Business (MCOB) sourcebook which dates back to October 2004.
- In terms of training and competence requirements, every adviser must hold a relevant mortgage qualification such as CeMAP.

Regulation of Mortgage Advice

- In order for MCOB to be applicable to the mortgage
  - Property must be in the European Economic Area
  - The borrower must be an individual(s) or a trustee
  - First mortgage or second or subsequent charges now also regulated due to the Mortgage Credit Directive (MCD) as of March 2016.
  - Borrower or immediate family occupying at least 40% of the property as their residence
- Therefore, home improvement loans, debt consolidation loans and equity lease schemes such as lifetime mortgages and home reversion schemes are all regulated under MCOB.
- Buy to let mortgages and most commercial mortgages are generally therefore not regulated by MCOB due to the 40% rule above.
- If the borrower is a company or a limited liability partnership, the mortgage also will not be regulated by MCOB.
- However, the Mortgage Credit Directive, from March 2016, also allows for certain buy to lets to be also regulated which are referred to as a 'consumer buy to let'. A consumer buy to let is when an accidental landlord is created e.g. inherited a property, or moving from your property into a partners, or need to relocate for a job.
- There is no cooling off period with mortgage contracts once the mortgage deed has been completed, although there is a 7 day reflection period following any mortgage offer.
- Mortgage advisers are outside the scope of MiFID and the Mortgage Conduct of Business rules (MCOB) applies to FCA regulated mortgages.

The key areas of MCOB that we need to be aware of are:

MCOB 3 – Financial Promotions

- A copy of the promotion must be kept for a minimum of one year after it was last used – "Your home may be re-possessed if you do not keep up repayments on your mortgage"
- Non real time promotions must include contact details of the firm and they must be clear, fair and not misleading.

MCOB 4 – Advising and selling rules

- **Initial Disclosure** must be provided at the start showing if the adviser is a whole of market or multi tied or a tied adviser. Whole of market doesn't necessarily mean every lender.

- Records must be kept for at least 3 years.

- Any mortgage recommended must be suitable and special requirements apply if the mortgage is being used to consolidate debt.

- The customer must be provided with:

    - Name and contact details
    - Whose mortgages are being offered
    - Details of any fees payable
    - The firm's FCA registration details
    - How to complain
    - Details of rights under Financial Services Compensation Scheme

MCOB 5 – Pre application disclosure

- **An illustration** giving all the key facts about the mortgage and this must be given before the application is made. It will include:

    - The interest rate and the annual percentage rate of charge (APRC)
    - The amount of the monthly payment
    - The amount by which the monthly payment would increase for each 1% rise in interest rates.

- The illustration must be provided in a European Standardised Information Sheet (ESIS) which is in a prescribed format.

- The adviser must be able to justify that the advice and recommendation that they give is suitable within the 'suitable advice' rules. If there is no suitable product, no recommendation should be given.

MCOB 6 – disclosure at the mortgage offer stage

- Details of the mortgage, how long the offer is valid for and that there is no right of withdrawal after the mortgage has completed and include a tariff of charges.

- The offer is binding on the lender but can be made conditional on confirmation of certain details which could allow the lender to withdraw the offer.

- The borrower must be granted a 7 day reflection period to consider whether to accept the offer or not.

MCOB 7 – Disclosure at the start of the contract

- Before the first payment is made on the mortgage, the lender must confirm the details of the first payment and subsequent payments.
- For interest only mortgages, the responsibility is on the borrower to ensure that there is a repayment vehicle in place.
- For interest only mortgages, the lender must contact the borrower at least once during the term to check that a credible repayment vehicle is still in place.

MCOB 8 & 9 – Equity Release Schemes

- There are special rules apply to the area of equity release – lifetime mortgages and home reversion plans and anyone giving advice in this area would need to hold a specialist qualification in this area.

MCOB 10 – Annual Percentage Rate and Annual Percentage Rate of Charge

MCOB 11 – Responsible lending

- Lenders must put in place a written responsible lending policy.

MCOB 12 - Charges

- Excessive charges are not permitted – early repayment charges must be a reasonable approximation of the costs incurred by the lender

MCOB 13 – Arrears

- Borrowers in arrears must be treated fairly and customers in arrears must be given within 15 working days of the lender becoming aware of the arrears, the following:

- The Money Advice Service information sheet
- The missed payments and total arrears figure
- The outstanding debt and any further charges

Income and Expenditure

- The new affordability rules mean that the lenders will have to obtain reliable evidence that the mortgage is affordable and that the income is correct – self certification is no longer permitted.

- The rules insist that the evidence must come from a source that is independent of the borrower – pay slips, bank statements would be sufficient.
- Where the firm is aware of any future changes to income and expenditure, it should also take that into account in the affordability assessment.

- If the term of the mortgage extends beyond the retirement age, the firm should look to assess income that the borrower would have in retirement.

- **Affordability must be based on the applicant's free disposable income, in other words, the amount left each month after normal expenses.**

- Normal expenditure includes:

    - Committed expenditure e.g. credit agreements, other contractual commitments
    - Basic essential expenditure – basic living needs of the household plus utilities, council tax, insurances
    - Other basic quality of life expenditure such as childcare, clothing, basic recreation

Providing mortgage advice

- The MCOB rules state that only two levels of service can be provided by the mortgage adviser which are:

    - An advised sale
    - Execution only

- Firms have a responsibility to deal appropriately with vulnerable customers. With regard to mortgages, the FCA regards the following as being vulnerable and therefore these customers must be given advice. Should they subsequently reject the advice, they can proceed on an execution only basis.

    - Those buying a property under the 'right to buy'
    - Those entering into a 'sale and rent back' scheme
    - Equity release applicants

- The FCA requires that these customers must in the first instance receive advice. Should they reject the advice, they can then choose to proceed on an execution only basis.

Insurance Conduct of Business (ICOB)

These rules relate to advising and selling in the areas of general insurance, protection, critical illness, income protection etc.

- This area has been regulated since January 2005.

- This was prompted by the need to implement an EU Directive aimed at opening and standardising the market for insurance intermediaries throughout the EU.

- The training and competence rules are exactly the same as previously described.

- Individuals and firms have to authorised or approved through the same processes that apply to other financial services sectors.

Rules applicable to intermediaries who sell, administer or advise on general insurance are contained in a new rulebook known as the Insurance Conduct of Business (ICOB) Sourcebook.

Cancellation

- The cancellation rights are offered by the product provider but the intermediary needs to be aware of them.

- For general insurance contracts the cancellation period is 14 days. The right to cancel does not apply to certain travel policies of less than one month.

- For pure protection policies (e.g. Critical Illness) the period is 30 days.

- If a customer cancels the insurance company must return any money paid to it within 30 days of cancellation.

Banking Conduct of Business Rules (BCOB)

- This sourcebook details the rules in relation to firm accepting deposits from UK banking customers in the UK e.g. savings and current accounts.

Payment Services Regulations

- These rules cover businesses referred to as payment institutions who are authorised to process payments by card, credit transfer or direct debit.
- These institutions must be authorised or registered by the regulator.

The Standards of Lending Practice

Lending such as unsecured loans, overdrafts and credit cards are not covered by BCOB or MCOB. The Standards of Lending Practice sets out a number of customer service principles covering:

- Financial promotions
- Product sale
- Account management
- Money management
- Financial difficulty
- Customer vulnerability

Compliance is monitored by the Lending Standards Board

Basic Advice & Stakeholder Products

To try and encourage the public to participate in the financial services market the government created a suite of products branded as **Stakeholder** products.

The recommendation therefore was to develop a range of low cost, low risk, simple products that would appeal to the financially unsophisticated.

- The maximum permitted annual charge for investment products was set at 1.5% for the first 10 years and 1% thereafter. For stakeholder pensions arranged prior to April 2005, charges are capped at 1% throughout.

Basic Advice

A more simplified or basic advice sales model applies to these stakeholder products. The rules for these are included in the Conduct of Business Sourcebook.

- The adviser must explain the nature of stakeholder products and must make it clear that only basic advice will be given. A 'basic advice' initial disclosure document must be provided.

- The sales process will involve short scripted questions in plain language

- There are reasonable grounds for believing that the stakeholder product is suitable for the client.

- The client understands the basis upon which the advice has been provided.

- A record must be kept of the fact that the firm has chosen to give basic advice on the stakeholder products and this must be kept for 5 years

- The basic advice process could be appropriate for consumers who have their priority needs met (i.e. they do not need to reduce debt, or have some disposable income or capital to invest or have a specific investment need.

Robo Advice

- Robo-advisers are a class of financial adviser that provide digital financial advice with minimal human intervention based on mathematical rules or algorithms.

- This is designed to be a low cost alternative to face to face advice.

- There are FCA guidelines which make it clear that 'robo advice' has to be suitable for customers' risk tolerance and investment objectives.

Unit 2 – Topic 22

Consumer credit

Consumer credit includes personal loans, hire purchase, credit cards and store cards. It has only been regulated by the FCA since 2014, but there have been legal rules in relation to this area since 1974.

Consumer Credit Regulation

- The main legislation governing consumer credit in the UK is the Consumer Credit Acts of 1974 and 2006.

- Until April 2014 responsibility for the enforcement and regulations of the Consumer Credit Acts was with the Office of Fair Trading (OFT).

- Since April 2014, this is now the role of the FCA.

Consumer Credit Act 1974

- The Acts affected most lending including personal loans, HP agreements and credit card agreement.

- **Regulated mortgages are exempt from the Consumer Credit Act as they are covered by MCOB as are further advances from the original lender regardless of the purpose.**

- The 1974 Act only regulates credit agreements not exceeding £25,000.

Other elements of the Act are:

- Suppliers of loans and credit must be licensed.
- Clients must receive a copy of the agreement for their records.
- Prospective borrowers have a cooling off period when they can withdraw. This applies to all CCA loans except loans that are signed on the lenders' premises.
- Advertisements cannot be misleading.
- Credit reference agencies must disclose all information held about individuals on request.
- An Annual Percentage Rate (APR) must be shown for all regulated loans. This will usually be higher than the flat rate as it includes the other charges included in setting up the loan e.g. arrangement fees, legal fees etc.
- Since, the Mortgage Credit Directive was implemented in 2016, a new APR called Annual Percentage Rate of Charge (APRC) was created. This applies to

1st and 2nd charge mortgages. APR applies to personal loans, credit cards, HP etc.

Consumer Credit Act 2006

This updated the 1974 Act and the key changes are:

- The definition of individuals or consumers was widened to include sole traders and partnerships of three or fewer partners.
- The scope of the Financial Ombudsman Service (FOS) was expanded to cover credit agreements.
- Courts were granted the power to vary credit agreements if they were deemed to be unfair.
- The upper limit of £25,000 was removed completely.

The Consumer Credit Directive

The EU from 2011 has also introduced rules that are applicable to consumer credit. The main features are:

- The term 'representative APR' must be included in any advertisement for credit. Representative means at least 51% of successful applicants.
- Creditworthiness must be assessed by a lender.
- Pre contract information must be provided in good time before the borrower enters into an agreement and the information must be clear.
- The borrower has the right to withdraw from a credit agreement within a period of 14 days from the conclusion of the agreement.
- Any interest rate changes must be notified in writing.
- The borrower can terminate any open ended credit agreement by giving one months' notice. If the creditor is terminating, the notice period is 2 months.

FCA Consumer Credit Regulation

- The FCA took over this area of regulation from the Office of Fair Trading from April 2014.
- Consumer Credit firms must be authorised by the FCA and the Consumer Credit sourcebook (CONC) is applicable.

UNIT 2 TOPICs 21 & 22 –Conduct of Business Part 2			
Question	**Answer**	**Mark**	**Comments / Notes**
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Unit 2 – Topics 21 & 22 Test

1 The suggested range of stakeholder-type products have a proposed level of charges limited to what MAXIMUM percentage for the first ten years?

A 1%
B 1.5%
C 2%
D 2.5%

2 James, who is taking out a mortgage that falls within FCA regulation, has just received his customer specific illustration. This means that he is at what stage of the mortgage application process?

A He has received the mortgage offer
B He has signed and returned the mortgage offer
C He has not yet completed the mortgage application form
D He has completed on the house purchase

3 If a customer decides that they want to cancel their general insurance contract within the cooling off period, they must do so within:

A 14 days
B 7 days
C 28 days
D 30 days

4 If a customer cancels their general insurance contract within the cooling off period, the insurance company must return any sums to it, within how many days?

A 14 days
B 30 days
C 7 days
D 28 days

5 Chiara, a mortgage adviser, is assessing the suitability of a mortgage for her client. She will take into account all of the following except:

A whether a mortgage is suitable for her client in the first place.
B selecting the most appropriate property type for her client.
C what type of mortgage product is suitable for the client.
D selecting the best mortgage and provider to suit her client's needs.

6 All of the following are arranging mortgages after October 2004. Which mortgage is NOT regulated by the Financial Conduct Authority?

A Tony and Anne, who are joint borrowers
B Malcolm and Paul, who are creating the mortgage in their capacity as trustees
C John, who is a sole borrower
D 'Paste It' plc, which is a public limited company

7 Philip, a mortgage adviser, has to satisfy additional training and competence requirements under Financial Conduct Authority regulation because he offers advice on:

A further advances
B buy-to-let mortgages
C second charges
D lifetime mortgages

8 Which of the following statements is NOT true regarding the mortgage offer document?

A It must contain details of the mortgage payments
B It must state how long the offer is valid for and how the customer can withdraw from the contract once the mortgage has completed
C It must be accompanied by an up to date tariff of charges
D It must contain details of any fees associated with the mortgage.

9 Mortgage Brokers Ltd have just offered advice, post-October 2004, to a residential mortgage client and have NOT yet issued a suitability letter. This is permitted because:

A suitability letters need to be issued for commercial mortgages only.
B there is no Financial Conduct Authority requirement for the issuing of mortgage suitability letters.
C suitability letters need only be issued on buy-to-let mortgages.
D it is only necessary for a mortgage suitability letter to be issued after completion of the mortgage.

10 Which of the following will not be included in an initial disclosure document?

A Product recommendations
B Complaints procedure
C Name of the regulator
D Services offered

11 **When MUST the Initial Disclosure Document be provided by a mortgage adviser?**

A At the start of the first meeting with a prospective client
B As soon as regulated business is transacted
C Within 14 days of the first meeting
D As soon as the client requests it

12 **Gary has found that the mortgage he is arranging post-October 2004, and which is secured by a first charge is NOT regulated by the Financial Conduct Authority. This is because**:

A he is using the mortgage to buy a property to as a commercial venture to let out to tenants.
B the mortgage will be partly used to repay credit card debts.
C he is using the mortgage to build an extension on his existing residential property.
D the mortgage will be used to repay a more expensive mortgage on existing main residence.

13 **The creation of stakeholder products outlined what KEY proposal for the industry?**

A The development of simple, low cost risk-controlled products that would appeal to the less financially sophisticated.
B Tighter regulation of Occupational Pension Schemes.
C The introduction of polarisation for financial advisers
D Higher limits on the permitted Free Asset Ratio for Financial Services Companies

14 **Where MCOB rules apply to a residential mortgage, what minimum percentage of property must be occupied as a residence by the borrower?**

A 100%
B 60%
C 40%
D 10%

15 **Mortgage Advice Ltd has found that their primary method of obtaining new business is NOT permitted under Financial Conduct Authority regulation. This means that they must have been using which of the following methods?**

A Cold calling
B TV advertising
C Mortgage introducers
D Radio advertising

16 **In respect of mortgage advice, which of the following pieces of information is NOT required as part of the initial disclosures under MCOB 4?**

A Fees associated with the service
B Arrears arrangements
C Complaints and compensation details
D The providers of mortgages under discussion

17 **Pauline is offering mortgage advice to a client. Who is ultimately responsible for assuring that the mortgage is affordable?**

A Adviser
B Adviser's compliance department
C Client
D The lender

18 **Which of the following types of mortgage became regulated by the FCA under MCOB for the first time from March 2016?**

A Buy to let mortgages for consumers
B Equity release
C Home improvement loans
D Lifetime mortgages

19 **A firm intends to make a series of cold calls to promote certain mortgage contracts. What rule applies?**

A A transcript of the call must be passed to the customer
B Cold calls are not permitted
C Extended cooling off periods will apply
D Only existing clients can be approached

20 **Which of the following is exempt from the provisions of the Consumer Credit Acts of 1974 and 2006?**

A A credit card with a limit of £5,000
B A further advance for £20,000 for home improvements with the existing lender
C An authorised overdraft for £18,000
D An unsecured loan for £10,000

21 The maximum size of loan, if any, regulated by the Consumer Credit Act is:

A £15,000
B £20,000
C £25,000
D unlimited

22 Ben, an adviser, is required under FCA rules to provide a key facts illustration (KFI) detailing the APRC to his client. This confirms that the client has expressed an interest in:

A collective investment business
B mortgage business
C offshore business
D protection business

23 Jason is in the process of applying for a mortgage and he has just received a tariff of charges from the lender. What is the latest point in the process that he has reached?

A Issue of the initial disclosure documentation
B Pre application disclosure
C Offer stage
D Legal completion

24 Which of the following must be included on all quotations for loans regulated under the Consumer Credit Act?

A The annual percentage rate
B The Bank of England base rate
C The lender's registered office address
D The purpose of the loan

25 Jeremy and Sandra have an interest only mortgage and have received written advice to check the performance of their repayment vehicle. Under MCOB rules, this is most likely to have been issued by:

A the FCA
B the investment product provider
C their financial adviser
D their mortgage lender

Unit 2 – Topic 23

Anti Money laundering

Money Laundering

- Money laundering is the process of filtering the proceeds of crime through different accounts or financial products in order to conceal its true origins. For example, using cash to buy a financial product and then selling that product in order to receive a legitimate authorised cheque.

- The key legislation is the Proceeds of Crime Act 2002, the Terrorism Act 2000 and EU's Money Laundering Directives.

- Under EU rules, the definition of property includes all assets of every kind including legal documents

- Under EU rules, criminal activity is any criminal activity specified in the Vienna Convention or by a member state of the EU.

- Under the EU Money Laundering Directives, money laundering within the EU will be treated under EU rules regardless of whether the original crime took place outside the EU.

- The Fourth EU Money Laundering Directive became law in June 2017 across the EU. This includes the following key points:

    - Each state must maintain a central register of the owners of legal organisations who own or control at least 25% of the organisation.
    - Strengthening of co-operation between states
    - Inclusion of tax crimes within EU legislation

- Under the Money Laundering Regulations 2017, a new criminal offence was created. If an individual was found guilty of recklessly making a statement in the context of money laundering that is false or misleading, they face a fine and/or a maximum 2 year jail sentence.

- There is also an organisation called the **Financial Action Task Force** whose aim is to lead the fight against money laundering internationally by identifying trends in money laundering, setting standards and evaluating whether countries have met these standards. They are not a law enforcement organisation.

- The remit of the Financial Action Task Force was expanded to include terrorist financing. They also maintain a list of 'non co-operative' countries which it considers do not have adequate anti money laundering rules.

Money Laundering Offences

Under the Proceeds of Crime Act, there are three main offences that apply when people are dealing with the proceeds of crime.

- Concealing criminal property

- Arranging relating to criminal property

- Acquiring or using criminal property

This has serious implications for the financial services industry as persons working in the industry must ensure they do not become involved either deliberately or by being manipulated.

The rules require that all authorised firms must:

- Establish procedures to prevent money laundering
- Educate staff about money laundering
- Obtain satisfactory evidence of identity for transactions exceeding €15,000
- Report suspicious circumstances to avoid the possibility of being accused later of 'arranging' or 'acquiring'
- Do not alert those suspected
- Appoint a Money Laundering Reporting Officer which is a controlled function and must be a person of appropriate seniority.
- Give regular training to staff including warnings about the consequences to themselves and the firm if they fail to follow the rules
- To ensure that the procedures are up to date through monitoring reports on money laundering matters
- Request a report from the Money Laundering Reporting Officer each year and provides details on any incidents reported by staff.
- Take action to strengthen procedures and controls and to remedy any deficiencies highlighted in the report.

Other Offences – Failure to Disclose

All suspicions must be reported to the authorities. Whenever money laundering is suspected or identified a report needs to be made.

Other Offences – Tipping Off

- It is a criminal offence to disclose to a person suspected of money laundering that they are being investigated or are about to be.

- The FCA will take into account the Joint Money Laundering Steering Group's guidance notes on the steps that firms should take in verifying the identity of customers and confirming the source of deposit funds.

- They will also take into account the Financial Action Task Force's publications which will highlight any known developments in money laundering.

Customer Due Diligence – Client Identification

- A key area is determining the identity of a customer and this is required:

    - When opening a new account, investment or policy
    - When the value of an 'occasional transaction' exceeds €15,000. For a business, this figure is reduced to €10,000
    - For life assurance, where the annual premiums exceed €1,000 or €2,500 for single premium policies.
    - Where a change of circumstances of an existing customer requires new evidence to be obtained.
    - **In every case regardless of the amounts, where there is suspicion or doubts about the proof of identity previously obtained.**

- Where a client is introduced to a firm by an intermediary, it is allowed to accept that intermediary's written assurance that sufficient evidence of identity has been obtained.

- Acceptable forms of identity include current passport, driving licence with photo, entry on electoral roll, national ID card or recent utility or council tax bill. The Association of Independent Financial Advisers have a standard document that can used to evidence that identity has been confirmed.

- Where people cannot produce this evidence, the FCA has guidance to ensure that these people are not excluded from financial services. In this instance, a letter from a person such as a Church Minister, a solicitor or doctor would be good enough.

Money Laundering – Record Keeping Requirements

Records must be kept and this will include:

- Evidence of ID retained for at least 5 years after the relationship has ended.

Credit Reference Agencies

- Anti money laundering checks are often carried out by credit reference agencies on behalf of financial institutions. This will not affect an individual's ability to obtain credit.

Money Laundering – Reporting

- Each firm must have a Money Laundering Reporting Officer (MLRO). Staff must report to the MLRO if they know or suspect that a client is involved in money laundering.

- The MLRO will then decide whether to report to the National Crime Agency.

- At least annually the MLRO must report to the firm and this report will assess the firm's compliance and provide updates on any incidents submitted during that year.

Money Laundering – Enforcement

- Anyone convicted of concealing, arranging or acquiring could be sentenced up to a maximum of 14 years in prison or an unlimited fine or both.

- Anyone convicted of failing to disclose or tipping off could be imprisoned for up to a maximum of 5 years or an unlimited fine or both.

- The FCA can also discipline firms and individuals for breaches of the rules on money laundering. It also has the power to prosecute anyone who breaks the EU Money Laundering Directives.

- A partner or a director who fails to comply with money laundering regulations can be fined, receive up to 2 years in prison or both.

- The **National Crime Agency** has responsibility to reduce the impact of serious organised crime on people and for enforcing and pursuing the proceeds of crime.

- The National Crime Agency through its **Economic Crime Command** is responsible for tackling money laundering and also covers fraud, bribery and counterfeiting of currency.

The Bribery Act 2010

- This legislation created an offence of offering, promising or giving 'financial advantage' to another intended to bring about improper performance by that person.

- The offence applies to bribery of employees or officials in any business or other body. This relates to activities in the UK or abroad.

- It is also a criminal offence for the employee/official to agree, request or accept 'financial advantage'.

- The maximum penalty in the UK for an individual convicted of a bribery offence is an unlimited fine and imprisonment for up to 10 years.

UNIT 2 TOPICs 23 – Money Laundering			
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Unit 2 – Topic 23 Test

1 Which one of following is true in respect of a firm's responsibilities under the money laundering regulations? A firm must:

A report suspicious circumstances
B maintain client confidentiality at all times
C appoint its Money Laundering Reporting Officer at director or partner level
D deny access to appropriate services to anybody unable to provide detailed evidence of identity

2 Employees should receive regular training about money laundering so that:

A they are aware of the consequences to themselves if they fail to comply.
B they can complete the Money Laundering Report.
C they can assess their firm's compliance with the sourcebook.
D they can caution as appropriate any suspect individuals.

3 In relation to money laundering, how is 'property' defined under the European Directive 1991?

A Physical assets with a freehold title deed only
B Assets held in cash within the European Union only
C Physical assets with a leasehold title deed only
D Assets of every kind including legal papers giving title to such assets

4 In order to be required to report a transaction to the Money Laundering Reporting Officer, a member of staff first needs to:

A be certain that the person is involved in money laundering
B advise the person that they may be investigated
C review the circumstances of the case with other experienced staff members
D have reasonable grounds for believing that a person is involved in money laundering

5 Why might money laundering regulations create 'financial exclusion'?

A Because not everyone can provide the necessary identification
B Because certain non-residents cannot be offered banking facilities
C Because financial organisations are wary of opening bank accounts with cash deposits
D Because customers want to know why they have been declined a financial product

6 What is the MAIN reason why an authorised firm's senior management must requisition an annual report from its Money Laundering Reporting Officer?

A So that they can be compliant with the Proceeds of Crime Act
B In order to monitor activities and increase deficiencies
C So that they can be compliant with the Financial Services Act
D In order to review activities and strengthen controls

7 If a staff member of a financial services organisation were to be accused of 'arranging' under the Proceeds of Crime Act 2002, it could mean that they had:

A knowingly become involved in the process of converting criminal property.
B personally owned the proceeds of criminal activity.
C unwittingly failed to report a potentially suspicious transaction.
D personally used the proceeds of criminal activity.

8 Insurance Life plc has set up an ISA for a new client. Why was it NOT necessary for the company to obtain evidence of identity for money laundering purposes?

A The client was introduced by an intermediary who obtained the necessary evidence
B Investments into ISAs are exempt from money laundering identification requirements
C The client is only temporarily resident in the UK.
D Investment amounts of less than £10,000 are exempt from money laundering identification requirements

9 Staff training on money laundering must cover all of the following requirements EXCEPT how to:

A liaise with the National Crime Agency.
B identify potentially suspicious transactions.
C evidence client identity.
D report suspicious transactions.

10 An authorised firm's senior management must ensure that their organisation is protected from use by money launderers by doing all of the following EXCEPT:

A appointing a Money Laundering Reporting Officer.
B providing regular training for staff.
C alerting those under suspicion of money laundering.
D reporting suspicious transactions.

11 Mandy, a financial adviser, has completed a report form and submitted it to her company's Money Laundering Reporting Officer. Under what circumstances would she take this action?

A Only when she believes a colleague may be supporting money laundering
B Only when she knows, for sure, that a client is involved in money laundering activity
C When the value of the transaction exceeds €15,000
D When she knows or suspects that a client is involved in money laundering activity

12 Paul was prosecuted under the Proceeds of Crime Act 2002 and received the maximum sentence of five years and a fine. This means that he must have been convicted of which money laundering offence?

A Concealing
B Tipping off
C Arranging
D Acquiring

Unit 2 – Topic 24

Other regulations affecting the advice process

Data Protection

- Interacting with a financial institution involves the customer providing personal information about themselves. If this information is not handled appropriately and securely, there is a risk of the customer becoming a victim of identity theft.

- Until May 2018, the primary legislation dealing with this area was the Data Protection Directive 1995 and the Data Protection Act 1998.

- As of May 2018, due to the increase in online and social media activity, the **General Data Protection Regulation (GDPR)** comes into force.

- Data in this context includes data held in computerised systems and data held in manual filing systems.

- The rules on data protection aim to give individuals control over the use of any personal data held about them by organisations.

Definitions

- **Data subject** – individual whose data is processed

- **Personal data** – information relating to a living individual

- **Sensitive personal data** – such data can only be processed with consent and this includes:

    - Racial origin
    - Religious beliefs
    - Political persuasion
    - Sexual orientation
    - Health
    - Criminal proceedings – not civil – CCJs not classed as sensitive
    - Biometric and genetic data

- **Data controller** – the legal 'person' who determines the purposes for which data is processed, normally the company or business that controls the data.

- **Processing** – covers obtaining the data, recording it, organisation or alteration of that data, disclosure of it or erasure of the data.

- **Data processor** – this is the individual who works for the company or business

Data Protection Principles

There are six data protection principles:

- Data must be processed fairly and lawfully.

- Data must be obtained only for a specified purpose.

- Data must be adequate but not excessive and must be relevant.

- Data must be accurate and kept up to date.

- Data must not be kept for longer than necessary although FCA regulations could affect this.

- Processed in a manner that ensures appropriate security of the personal data and is secure from accidental or deliberate misuse, damage or destruction.

- There will also no longer be a right to charge a fee for a data subject access request except where the request is clearly excessive.

An organisation must also have a lawful basis for processing data such as:

  - Consent from the client
  - Processing is necessary for a legal contract
  - Legal obligation
  - Public interest
  - Other legitimate interests

Data Subject Rights

- To correct inaccurate personal data
- Have personal data erased in certain situations
- Object to personal data
- Move personal data from one provider to another
- To make a subject access request and to receive this within one month

In order to demonstrate compliance with GDPR, an organisation must:

- Establish a governance structure with roles and responsibilities
- Keep a detailed record of all data processing operations
- Document policies and procedures
- Carry out data protection impact assessments.

- Processing of personal data by businesses established in more than one EU country will be monitored by one data processing authority which will be in the country where its main offices are registered.

GDPR Enforcement

- The Information Commissioner oversees the application of the rules. The Commissioner can take several courses of action if the rules are broken. Firms also need to report significant data breaches to the Information Commissioner.
    - An information notice – this is less serious and it requires the data controller to specify what steps the company will take to comply with the Act.
    - Issue undertakings committing an organisation to a course of action
    - Conduct assessments or audits to check organisations are complying.
    - Issue monetary penalty notices as a result of a serious breach.
    - Prosecute those who commit criminal offences under the Act
    - Serve assessment notices to conduct compulsory audits
    - An enforcement notice or 'stop now' notice – requires the organisation to either take some action or refrain from certain activities.

- It is a criminal offence to:
    - Fail to make a proper notification to the Information Commissioner. This is the process of registering and confirming that personal data is being held and also specifying the purpose for which that data is being held.
    - For a data controller to fail to comply with an enforcement or information notice.
    - Process data without authorisation from the Commissioner.

- The maximum penalty for these offences is a fine of the higher of €20M or 4% of an organisation's worldwide turnover.

Rules Regarding Occupational Pension Schemes

The Pensions Act 2004

- These were introduced as a response to the concern regarding the security of occupational pensions in the UK. Consumer confidence had been seriously dented by the Maxwell affair. Two important aspects to this Act were:

    - Establishment of a Pension Protection Fund

    - Transfer of responsibility from the Occupational Pensions Regulatory Authority (OPRA) to the newly created Pensions Regulator

- The Pensions Regulator was created to have overall responsibility for the regulation of occupational pensions.

- Its mission is to improve confidence in work based pensions by protecting the benefits of scheme members, promote good administration and reduce the risk of claims being made to the Pension Protection Fund.

- The Pensions Regulator aims to identify and prevent potential problems by identifying and assessing the risk. E.g. inadequate funding, poor record keeping etc.

- The Pensions Regulator will consider the combined effect of the **likelihood** of the event occurring and the **impact** of the event on the scheme.

- The Regulator has a range of powers that enable it to protect members' benefits:

Investigating Schemes

- All schemes must make regular returns to the regulator. The Regulator must also be informed as to any important changes by the schemes trustees.
- The regulator demands to be informed quickly if the scheme cannot meet its funding requirement.

Putting Things Right

- Requiring specific action to be taken to improve matters within a certain time.
- Recovering unpaid contributions from an employer who does not pay them to the scheme by the 19th day of the month following the month when they were deducted from the member's salary.
- Disqualifying trustees who are not considered fit and proper persons
- Imposing fines or even prosecuting certain offences.

Acting against avoidance

- Preventing employers from deliberately avoiding their pensions obligations by issuing contribution notices or financial support directions if appropriate.

The Pension Protection Fund

- The Pensions Act 2004 established the Pension Protection Fund to protect members of private sector defined benefit pension schemes in the event that the firm becomes insolvent with insufficient funds to maintain full benefits for members of the scheme.

- The Pension Protection Fund provides different levels of compensation should the above occur, but there are limited situations where this could be 100% of what the member would have been entitled to had the scheme remained solvent.

EU Directives

- These are issued by the European Union and they are binding upon each member state to which they are addressed but the methods used to achieve them are up to the member state.

- The central issues regarding EU law has always been the right to allow the free movement of people within EU states but also to allow the free movement of business and conducting business within the EU and this is what these EU directives here are aimed at.

Investment Services Directive

- Broadened the markets for investment firms to do business freely across the EU without any separate authorisation being required. This has since been replaced by MiFID.

Markets in Financial Instruments Directive (MiFID)

- If the investment firm is authorised in its home state it does not need any further authorisation to operate in other EU states.

- This directive applies to firms involved in the following areas:

    - Stocks and shares
    - Collective investments
    - Futures and options
    - Currency speculation
    - Underwriting the issue of any of the above

EU Directives & Life Assurance

- The **Second Life Directive** laid down rules relating to the freedom for life assurance companies to provide services across the EU.

- If the policy is created on the applicant's own initiative the regulations that apply are those of the state in which that company is established e.g. Aviva.

- Applicants who create a policy with an insurer established in a different state are required to sign a declaration acknowledging that the rules of the other state apply.

- **The Third Life Directive** states among other things that:

    - Policyholders will have between 14 and 30 days cooling off period from the date they were informed of the contract's creation.

    - Policyholders must also be offered clear and accurate information about the key features of the product (Key features document).

Insurance Intermediaries

- A directive was introduced to ensure that insurance intermediaries could operate throughout the EU**.**

- Insurance intermediaries must hold professional indemnity insurance to cover at least €1,300,380 per case and €1,924,560 in total per annum.

- There is also a requirement to maintain a financial capacity equal to 4% of premiums subject to an overall minimum of €15,000.

Oversight Groups

It is important that all aspects of the institution are kept under review to ensure that the investments of both shareholders and the customer are being handled safely and that the laws and regulations are being observed. Examples include:

External Auditors

- External auditors are primarily concerned with the published financial statements and accounts and they are primarily qualified chartered or certified accountants.

- They are independent of the institution whose accounts are being published. They must conform to the professional standards of the Auditing Practices Board and the Accounting Standards Committee.

- External auditors may also be members of professional bodies, such as the Institute of Chartered Accountants in England and Wales (ICAEW) or the Association of Chartered Certified Accountants. Both of these bodies publish ethical codes that their members are expected to adhere to.

Internal auditors

- have the task to review how an organisation is managing its risks. The role of internal auditors is to identify problems and recommend solutions to the senior management who have overall responsibility.

Trustees

- A trustee is a person (or in some cases an organisation) whose responsibility is to ensure that any property held in trust is dealt with in accordance with the trust deed for the benefit of the trust's beneficiaries.

Compliance Officers

- Firms that are authorised by the Financial Conduct Authority (FCA) or the Prudential Regulation Authority (PRA) should appoint a compliance officer to have oversight of the firm's compliance function, in other words to ensure compliance with all relevant legislation and regulations.

UNIT 2 TOPIC 24 – Other Regulations & Complaints			
Question	**Answer**	**Mark**	**Comments / Notes**
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Unit 2 – Topic 24 - Test

1 **Under the General Data Protection Regulations, the definition of 'sensitive personal data' includes all of the following areas EXCEPT:**

A proceedings in civil courts
B religious beliefs
C political persuasion
D mental health

2 **Fred has requested a copy of his personal data held by his bank. The General Data Protection Regulations requires that:**

A the bank limits any administrative charge to a maximum of £25
B he first confirms his identity by providing a copy of his birth certificate or passport
C any corrections must be completed within 14 days
D the bank is unable to charge Fred for his subject access request

3 **In relation to the General Data Protection Regulations, which one of the following is INCORRECT?**

A It requires anyone holding data on individuals to be registered.
B It gives individuals the right of access to data relating to them.
C It applies only to records held on computer.
D It requires anyone holding data to have a data protection policy.

4 **If a company fails to comply with an enforcement notice under GDPR, what is the MAXIMUM fine that can be imposed?**

A Higher of €20M or 4% of worldwide turnover
B £20M
C 4% of turnover
D Lower of £20M or 4% of turnover

5 **One of the Pension Regulators powers is to be able to investigate schemes in order to identify and monitor risks. All schemes must carry out the following actions except:**

A make regular returns to the Pensions Regulator
B provide details to the regulator of every transfer out of the scheme
C give notification of any changes to important information
D inform the regulator quickly if it discovered that it cannot meet its funding requirements

6 When Henry received his payslip on 21st June 2018, his normal occupational pension scheme contribution of £250 had been deducted by his employer. What is the latest date that his employer should pass this contribution to the scheme's trustees, if the Pension Regulator's guidelines are to be followed?

A	22nd June 2018	B	19th July 2018
C	30th June 2018	D	21st July 2018

7 As an expert in EU law, Kentons Intermediaries are seeking your advice about conducting business in other EU countries. In particular, they are seeking information on the subject of client money and professional indemnity insurance. You can advise them that they will need:

A financial capacity of at least 5% of premiums received per annum to meet client money requirements and a minimum level of €lm per case professional indemnity insurance.

B professional indemnity cover of at least €1m total per annum and a minimum financial capacity of €10 000 to meet client money requirements.

C financial capacity of at least 4% of premiums received per annum to meet client money requirements and a minimum level of €2m total professional indemnity insurance.

D professional indemnity cover of at least €1,300,380 per case and a minimum financial capacity of €15000 to meet client money requirements.

Unit 2 – Topic 25

Consumer rights, complaints and compensation

Consumer Rights

Within the UK individuals have certain key rights irrespective of whether they are financial services customers or not.

Consumers have the right to buy products and services with confidence and have rights when things go wrong, in particular this refers to :

- Consumers receiving clear and honest information before they buy
- Consumers to get what they paid for
- Be supplied with goods that are fit for purpose and services performed with reasonable care and skill
- Have faults corrected free of charge or get a refund/replacement

The Consumer Rights Act 2015

- This is new legislation which gives customers enhanced rights in relation to things going wrong with goods and services.

- The Act covers:

    - What to do when goods are faulty
    - What should happen if digital content is faulty
    - What should happen if goods and services don't match up with what was agreed
    - Unfair terms in contracts

- An aim of the Consumer Rights Act when there is a disagreement between a business and a consumer is to reduce the number of disputes ending in court action. Alternative Dispute Resolution is open to all businesses to help resolve a dispute between a consumer and a business.

- The legislation also deals with unfair terms in consumer contracts which has therefore replaced the Unfair Terms in Consumer Contracts rules.

- These regulations apply to all contracts between consumers and a seller of goods or services, where the consumer has no power to change the terms of the contract.

- This means that if you have a contract with a business the contract must be fair, transparent and adhere to the principle of good faith.

- Any unfair term will not be binding on the consumer unless they choose to be bound by it. Where an element of the contract is deemed to be unfair, the rest of the contract can continue to take effect.

- Contracts with disproportionately high charges or contracts which allowed the business to change the price after the contract has started could be deemed to be unfair.

- With regard to transparency, the terms of the contract must be clear, easily understood language and if there is any doubt as to the meaning, the interpretation most favourable to the customer will be adopted.

How are customers protected within the financial services sector ?

As was discussed in Topic 17, one of the FCA's operational objectives is to protect consumers. A step towards achieving this is to make it easier for customers to know how to complain if they feel they have been badly treated by the industry.

There are various bodies that can directly or indirectly assist in this area

- The role of government departments such as The Treasury, HMRC, DWP, National Crime Agency, Claims Management Regulator.

- The role of guidance services such as Citizens Advice, Which and the Single Financial Guidance Body.

- The Single Financial Guidance Body is an organisation formed from three existing providers of government advice – The Money Advice Service, The Pensions Advisory Service and Pension Wise.

The FCA Complaints Procedure

- The key requirements are that firms must:

    - Have appropriate and effective complaints handling procedures

    - Make customers aware of these procedures through client agreement and/or initial disclosure documentation

    - Aim to resolve complaints within 8 weeks or inform the complainant that they can take the complaint to the Financial Ombudsman Service (FOS)

    - Inform complainants of their right to go to the FOS if not satisfied

    - Report to the FCA on a 6 monthly basis on their handling of hard complaints.

- Complaints may be received orally or in writing and should be acknowledged promptly in writing.

- Complaints resolved by the close of business by the third working day following the receipt of the complaint are subject to different rules and a final response letter is not needed, but there does need still to be a 'summary resolution communication' with the client.

- Complaints covered by the FCA include:

    - all private individuals
    - small businesses with turnover below £6.5 million and fewer than 50 employees or an annual balance sheet below £5 million.
    - charities with annual income less than £6.5 million.
    - trustees with assets less than £5 million

Dealing with Complaints

- All complaints must be dealt with by a person of sufficient competence who is not directly involved. There also needs to be an individual in a governing function in the firm to oversee this area.

- The firm must resolve the complaint within 8 weeks and this final response must be by letter. If a final response letter cannot be given within the 8 weeks, the client must be told that they can refer the matter to the Financial Ombudsman Service if they wish.

- Since January 2018, if there has been a complaint to a payment services provider, they must provide a full response within 15 days but can be extended to 35 days in exceptional circumstances.

- The firm's final response must be by letter and it must inform the complainant that they have the right to go the Financial Ombudsman Service. This must be done within 6 months of the date of this letter.

- Records of complaints must be maintained for at least three years from when they were received. If the complaint relates to a collective portfolio management services the minimum period is 5 years. Where the complaint relates to MiFID business, there is no minimum retention period.

The Financial Ombudsman Service (FOS)

- Since December 2001 the FOS has taken over from a number of different financial services ombudsman schemes.

- The FOS has not taken over the responsibilities of the Pensions Ombudsman who deals with complaints about occupational pension schemes.

- The FOS is:

    - Free of charge to customers

    - Funded by firms authorised by the FCA via a general levy. The firms have to pay an additional case fee for any case that goes to the FOS from the 26th case onwards per year.

    - Membership is compulsory for authorised firms

    - FOS only becomes involved when the firm's internal complaints procedure has been exhausted.

- Complainants must:

    - Complain to the firm first
    - Complain to the FOS once the internal procedures have ended
    - Complaints must be made within 6 years of the event or within 3 years of the time when the complainant should have become aware that there was cause for complaint

- The FOS can make awards of up to £350,000 plus interest and costs for complaints relating to events on or after 1 April 2019. For complaints relating to events before 1 April 2019 the maximum award is £160,000.

- Awards by the FOS are binding on authorised firms but not on individuals who could take the matter to court.

- The punishments awarded are not intended to punish the firm but to indemnify the customer for any loss or inconvenience or distress caused.

Pensions Ombudsman

- This was created by the Social Security Act 1990 to deal with certain complaints relating to the running or administration of personal and occupational pension schemes and complaints about the Pension Protection Fund.

- The Pensions Ombudsman can decide about complaints in relation to **the running of pension** schemes **but not the sale and marketing of pensions**, so these issues would still stay with the FOS. Nor would they become involved in disputes with regard to state pensions.

- Complaints should first be referred to the managers or trustees of the pension scheme. If this does not result in agreement they should be referred to The Pensions Advisory Service (TPAS) who try to resolve the matter through mediation.

- TPAS decisions are not legally binding so if they cannot resolve the matter, it will be referred to the Pensions Ombudsman.

- Complaints will relate to cases of maladministration (poor administration).

- Disputes will relate to disagreements concerning facts or laws.

- Complaints must be made in writing within 3 years of the event being complained about. Any time spent trying to resolve this is excluded from the time period.

- The Pension Ombudsman's decision is binding on **all** parties and can be enforced by the courts.

The Financial Services Compensation Scheme

There are compensation arrangements where an authorised firm based in the UK has become insolvent. It doesn't apply to firms based outside the UK or on the Isle of Man or Channel Islands. The PRA and FCA are jointly responsible for this area.

Insolvency of an insurance company (e.g. Aviva)

- For all long term insurances and certain general insurances, compensation is 100% of the value of the policy with no upper limit. These are policies that pay out on death or disability.
- Annuities which provide income also receive 100% protection
- Also 100 % for compulsory insurances such as employer's liability and motor insurance.
- For other types of insurance the compensation limit is 90% of the claim

If an insurance broker is unable to pay claims because they have become insolvent

- 90% of the loss with no upper limit

Insolvency of a firm carrying out investment business or mortgages or debt management

This could arise when an investment firm or mortgage business is unable to pay any claims against the firm due to insolvency then:

- 100% of the first £85,000 of the loss

Insolvency of a bank or building society- loss of deposited funds

- 100% of the first £85,000 or £170,000 in a joint account.
- Can be extended to 100% of the first £1M if you can show that the savings amount had been temporarily boosted by a life event such as sale of a house, inheritance, divorce settlement, pension, redundancy, criminal injury compensation.

Claims against the FSCS cannot be made for other losses such as poor advice or poor investment performance.

UNIT 2 TOPIC 25 – Other Regulations & Complaints			
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Unit 2 – Topic 25 Test

1 **Jason has just made a complaint alleging that his personal pension plan was mis-sold to him. He has complained to the pension company initially and has received a final response letter. Who should he now take this complaint to?**

A The Prudential Regulatory Authority
B The Pensions Ombudsman
C The Pensions Advisory Service
D The Financial Ombudsman Service

2 **The Financial Ombudsman Service deals with unresolved complaints in respect of:**

A general insurance brokers
B Bank of England Base Rate
C administration of occupational pension scheme complaints
D LIBOR

3 **The Financial Services Compensation Scheme will pay out compensation to customers who have:**

A been mis-sold a mortgage endowment policy
B lost money through the insolvency of an authorised firm
C been mis-sold a personal pension plan
D lost money through the mis-management of an investment fund

4 **What is the effect of the final response letter for a customer who is in the process of making a complaint about a financial services product they have bought?**

A They will now have to take legal action to obtain redress
B They can now take the complaint to the Financial Ombudsman Service
C The Financial Ombudsman Service has found their complaint frivolous
D The customer will have to pay to progress the complaint further

5 **On the insolvency of an authorised investment firm, the MAXIMUM that could be paid out to an individual investor from the Financial Services Compensation Scheme would be:**

A 100% of the first £50,000
B 100% of the first £20,000 plus 90% of the next £50,000
C 100% of the first £20,000 plus 90% of the next £30,000
D 100% of the first £85,000

6 Regulations established under the Financial Conduct Authority require firms to make a commitment to try to resolve complaints within:

A 3 working days
B 1 month
C 8 weeks
D 3 months

7 Which one of the following is FALSE regarding complaints referred to an Ombudsman?

A The company involved should investigate the complaint before the Ombudsman
B The company will often take the matter to court following the Ombudsman's ruling.
C The Ombudsman's decision is binding on the company
D The Ombudsman can give awards of up to £350,000 plus interest and costs for complaints relating to events after 1 April 2019

8 Ruth lost £90,000 when a UK investment firm became insolvent. What is the MAXIMUM amount that the Financial Services Compensation Scheme will pay her in compensation?

A £42,000
B £85,000
C £54,000
D £60,000

9 The Pensions Ombudsman may deal with unresolved complaints in respect of:

A personal pension schemes
B state pensions
C the administration of occupational pension schemes
D Stakeholder pension schemes

10 Which one of the following is NOT true in relation to the rules relating to the Financial Ombudsman Service?

A The maximum pay out under the FOS for events before April 2019 is £160,000.
B Records of complaints have to be kept for at least three years
C All complaints must be investigated where possible by someone of sufficient competence who is not directly involved.
D Authorised firms have to pay a case fee of £500 for every complaint that goes to the FOS

11 Jane opens a deposit account with the Moorland Building Society and deposits £10,000. She is worried about the money if the building society goes out of business. If this were to happen, how much would she receive from the Financial Services Compensation Scheme?

A £8,400
B £9,000
C £10,000
D £8,000

12 Which of the following statements best describes the situation applying where a contract is found to contain a term that is deemed to be unfair?

A As long as it is practical, the rest of the contract can continue
B The business can choose to bind the consumer to the contract
C The contract will continue as specified
D The whole contact will be invalid

13 David's car insurer has gone out of business and he has lost £2,000 on his compulsory third party policy. How much compensation if any may he be entitled to receive from the FSCS?

A none
B £1,000
C £1,800
D £2,000

14 Which one of the following is NOT one of the areas covered by the rules on unfairness as detailed in the Consumer Rights Act 2015?

A The contract should be made in good faith
B The contract should be transparent
C The terms should be fair
D There must be insurable interest

15 Which of the following claims would be covered by the Financial Services Compensation Scheme?

A Damian, who is talking to his motor insurer about an accident with an uninsured driver
B David who has claimed against his high street bank for the advice he received about PPI cover
C Mike whose complaint about investment advice was upheld but not honoured due to the default of his adviser
D Paul who is claiming in relation to his offshore investment with a bank in the Isle of Man

16 John held deposits with Bank A and Bank B and they were both declared insolvent on 1 May 2018. The FSCS paid a higher amount of compensation for his holdings with Bank A because:

A Bank B had recently made the annual interest payment on John's account

B John and his wife held £150,000 in a joint account in Bank A and £70,000 in his sole name in Bank B

C John had £70,000 in a joint account with his brother with Bank A and £70,000 in his sole name in Bank B

D John had £100,000 saved with Bank A and £90,000 with Bank B

CeMAP 1 - UNIT 1 – MOCK PAPER 1			
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Unit 1 Mock 1: Introduction to the Financial Services Environment

1 Who is responsible for the control of interest rates in the UK economy?

A The Bank of England
B The Treasury
C The Chancellor of the Exchequer
D The British Bankers Association

2 Which index does the government use to assess the inflation rate?

A Retail prices index
B Consumer prices index
C Construction and building prices index
D FTSE 100 index

3 Which of the following describes a function of the Bank of England?

A Depositing money with the International Monetary Fund
B Managing new issues of gilt edged securities
C Acting as banker to the government
D Regulating foreign investments

4 Which of the following factors distinguishes building societies from banks?

A They are mutual institutions owned by their members
B They are owned by their shareholders
C They cannot make regulated loans
D They can only lend for mortgage purposes

5 Under what circumstances if any can a nation state opt out of a regulation laid down by the European Council and Council of Ministers?

A None
B Only if specific dispensation has been granted
C Only if an alternative approach has been agreed
D Only if the member has joined within the previous three years

6 On which one of the following is the payment of capital gains tax most likely to arise?

A The payment of £30,000 in respect of redundancy
B The sale of an antique grandfather clock for £6,000
C The sale of a holiday home for £147,500
D The encashment of an equities ISA

7 **Damien has gifted some authorised unit trusts to his brother, on which a capital gain of £8,000 has been made. At what rate will he be required to pay capital gains tax?**

A 0%
B 10%
C 20%
D 40%

8 **Which of the following would not normally be assessable for income tax?**

A Interest on savings on a standard savings account
B Casual gambling proceeds
C Dividends from shares
D Income from gilt edged securities

9 **Which one of the following is NOT a way of establishing domicile?**

A By deed poll
B By residency
C By birth
D By choice

10 **On which one of the following would a child be subject to income tax?**

A A settlement from his parents
B An educational grant
C All earned income
D Any earned income that exceeds his personal allowance

11 **What is the threshold above which income tax is payable on redundancy payments?**

A £20,000
B £29,900
C £30,000
D £35,000

12 **Diane has been told that she must pay a certain class of National Insurance on a twice yearly basis. This confirms that she is:**

A earning more than the upper earnings limit
B on maternity leave
C self employed
D temporarily working abroad

13 **The rate of inheritance tax on a chargeable lifetime transfer when it is made is:**

A 18%
B 20%
C 22%
D 40%

14 Capital gains tax is best described as a tax:

A levied on the estate of an individual on his death.
B payable on proceeds received on the disposal of any asset.
C levied on the recipient of a gift if the donor dies within 7 years of giving it.
D payable on the gain arising from the disposal of a chargeable asset.

15 Bill sold some investments in March 2016 on which he made a taxable capital gain. When would this tax have become due for payment?

A September 2016
B January 2017
C April 2017
D January 2008

16 Gilts with 66 years to run before their redemption date are known as:

A undated
B short-dated
C medium-dated
D long-dated

17 Fiona, a higher rate taxpayer has an ordinary building society savings account. What is the MAXIMUM amount of annual interest she can receive before she is liable for income tax?

A £1,000
B Nil
C £5,000
D £500

18 Over the longer term, what risk is normally associated with deposit-based investments?

A The value of capital will fluctuate and may fall below the original investment
B There is no guarantee that the original capital will be returned at maturity
C The real value of capital may be eroded due to the effects of inflation
D There is the potential for suffering large capital losses

19 In May 2017, Alison, 45, wants an investment vehicle to save towards a deposit for her first house. She wants to invest £30,000 immediately, followed by £220 per month over the following year. Which one of the following is the MOST suitable product for her objectives?

A Investment trust
B Unit Trust
C ISA
D High interest building society account

20 Index-linked gilts are gilts where the interest payments:

A and the capital value move in line with the FTSE index.
B move in line with the Retail Price Index and the capital value remains level.
C move in line with the FTSE index and the capital value remains level.
D and the capital value move in line with the Retail Price Index.

21 Yvonne is a non-taxpayer and holds a building society deposit account. Her interest will be paid:

A net of 20% tax
B net of l0% tax
C gross
D net of 20% tax, which she can reclaim through her tax returns

22 National Savings Premium Bonds are MORE advantageous for:

A higher rate and non-taxpayers than for basic rate taxpayers
B non-taxpayers than for higher rate and basic rate taxpayers
C basic rate taxpayers than for higher rate and non-taxpayers
D higher rate and basic rate taxpayers than for non-taxpayers

23 Terry has the coupon on his Gilts paid gross. As a higher rate taxpayer he will pay:

A 20% income tax on income received
B 40% income tax on income received
C Capital gains tax at maturity
D Marginal rate income tax at encashment

24 Alec Enterprises intends to raise additional finance by issuing more shares. They are therefore obliged to:

A make a rights issue
B delay dividend payments
C guarantee no existing shareholder will be adversely affected
D make at least 25% more shares available

25 What effect does the anticipation or actual increase in interest rates have on the price and income from gilt-edged securities?

A Gilt prices rise and the income yields fall
B Gilt prices fall and the income yields rise
C Gilt prices and the coupons rise
D It depends on the coupon and redemption date of the gilt

26 Under a unit trust, what does the cancellation price represent?

A The minimum price at which investors may cash in their units
B The maximum price at which a full encashment of units may be made
C The price applicable to investors who cancel their investment during the cooling off period
D The price at which the manager will buy back units if underlying assets do not have to be traded

27 An investment trust:

A is another name for a unit trust.
B is a public limited company.
C is subject to capital gains tax.
D pays out gross income to investors.

28 Bill wants an investment where he does not have to pay capital gains tax. He is interested in unit trusts, investment trusts and open-ended investment companies. Which one of these would achieve his investing aims?

A A unit trust
B An investment trust
C An OEIC
D None of these investments would be suitable

29 When used to repay a mortgage for a client with a low - medium risk profile, which type of endowment policy is MOST likely to produce a surplus on the maturity date?

A Low-start
B Non-profit
C Full With-profit
D Unit-linked

30 The amount of 'deferred' interest under a deferred interest mortgage is:

A added to the loan outstanding.
B repaid in full at the end of the deferred period.
C written off by the lender provided the mortgage runs full term.
D collected by means of repayments calculated at a rate higher than the market rate after the deferred period.

31 William and Kate have a standard variable rate mortgage which is due to be repaid by an equity based ISA. Which factor would most immediately adversely affect their monthly budgeting?

A A fall in the FTSE
B A fall in interest rates
C A rise in the FTSE
D A rise in interest rates

32 Irrespective of the type of endowment policy he chooses, Jack has been correctly advised that his policy will:

A guarantee to repay the mortgage on death or at maturity.
B guarantee to repay the mortgage on death before the maturity date.
C ensure a lump sum at maturity in excess of the value of the mortgage.
D require additional life cover if interest rates increase over time.

33 Which one of the following is the MOST appropriate type of life policy to support an ISA mortgage?

A Decreasing term assurance
B Level term assurance
C Endowment assurance
D Whole of life assurance

34 Accident, sickness and unemployment policies provide benefits on which one of the following bases?

A Regular income payable for an unlimited period
B Regular income payable for a deferred maximum period
C Lump sum payable after a short deferred period
D Lump sum payable at the end of the term

35 Which is the INCORRECT statement regarding free standing additional voluntary contributions plans (FSAVCs)?

A FSAVCs can be used to supplement the income from an occupational pension scheme
B Employers must contribute to an employee's FSAVC plan
C FSAVCs are initiated by the employee
D FSAVCs provide an income in retirement

36 Mike is retiring from his company after 25 years. He is planning to take a cash lump sum of £30,000 and £15,000 per annum from his personal pension plan. What will the tax liability be on these benefits?

A The lump sum will be tax free but he will pay income tax on the annual pension
B He will pay capital gains tax on the lump sum above the annual allowance
C He will not have a tax liability on either of the pension benefits
D The regular pension will be tax free but Mike will pay basic rate income tax on the lump sum

37 Which one of the following statements in respect of Income Support is correct?

A Eligibility is based on the level of National Insurance Contributions made
B Claimants must be aged 18 or over
C It is not a payment to the claimant but a way of reducing taxable income
D It is means tested on both income and savings

38 Which basis would be MOST suitable for a husband and wife seeking to use whole-of-life assurance to cover a likely inheritance tax liability?

A Single life on the life of the youngest
B Single life on the life of the oldest
C Joint life payable on the first death
D Joint life payable on the second death

39 Which one of the following types of life policy is TYPICALLY used in connection with key person assurance?

A Personal pension term assurance
B Term assurance
C Endowment assurance
D Whole of life assurance

40 Which of these is the LEAST tax efficient method of providing 'partnership protection' in meeting the needs of the partners' families and the partnership itself?

A Cross option method
B Buy and Sell method
C Automatic accrual method
D With profit endowment

41 Which one of the following factors that you cover during a fact find will affect your ability to improve your client's situation on an ongoing basis?

A The client's attitude to taxation on savings interest
B The client's willingness to review objectives if personal circumstances change
C The client's current financial circumstances
D The client's job prospects

42 What is the danger for clients with a young family, where mortgage protection is the only life insurance they currently have in place?

A They run the risk of having their house repossessed should they die
B They are not making best use of their tax allowances and benefits
C The dependents would be unprotected should anything happen to either client
D The dependents would be provided for in the event of a fatal accident

43 When giving advice on a particular financial services product, what will the customer probably be most interested in about the product itself?

A Whether it is regulated
B What other customers have said about it
C How many of the products have been sold recently
D The benefits it can give them

44 In order to process a death claim for a life policy not written under trust but where there is a valid will, an insurer will need to see the:

A deed of variation
B grant of probate
C letters of administration
D deed of execution

45 Who is considered to be the legal owner of a life policy placed under trust?

A Trustees B Beneficiary C Settlor D Executor

46 Which one of the following would NOT be a benefit of writing a will?

A It can help to reduce any capital gains tax liability
B It can shorten the time taken to deal with the deceased's estate
C It can make adequate financial provision for dependents
D It ensures that the estate is distributed exactly as intended

47 When an individual dies intestate, leaving a spouse, children and an estate valued at £310,000, which one of the following applies?

A The estate is divided equally between the surviving spouse and children
B The entire estate passes to the spouse absolutely
C The surviving spouse inherits a life interest only in the deceased's entire estate
D The first £250,000 passes to the surviving spouse absolutely, along with a further £30,000 with the other £30,000 passing to the children equally.

48 Under the Consumer Insurance Disclosure Act 2012 the principle of 'Utmost good faith' is BEST described as the obligation to truthfully disclose:

A only those facts which are requested on the application form
B any deterioration in health after the plan has started
C the reasons why the proposed level of life cover is required
D any adverse credit history which may affect affordability of the policy

49 Steve has recently died having made a valid will. How can a potential beneficiary of the will determine the identity of Steve's personal representatives?

A obtaining a copy of the grant of letters of administration
B obtaining a copy of the grant of probate
C requesting a copy of the certified will
D requesting a signed declaration from the solicitor

50 Martin has set up a trust fund for the benefit of his three grandchildren and has appointed two trustees with discretion to exercise their powers. In these circumstances, which of the following is correct?

A both trustees must agree before exercising their discretionary powers
B Martin is known as the testator of the trust and the grandchildren as beneficiaries
C The Trustee Act 2000 requires the grandchildren to obtain advice when reviewing investments
D the trustees have no legal interest in the trust property

CeMAP 1 - UNIT 1 – MOCK PAPER 2			
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Unit 1 - Mock 2

1 **The European Union has issued a new directive. This means that a member state:**

A can choose whether or not to implement the directive.
B has the choice of how to meet the directive's objectives.
C must implement the directive in its precise original wording.
D is only required to implement the directive in its entirety if it is directed to them.

2 **Which of the following is always a mutual organisation?**

A bank
B friendly society
C insurance company
D stock broker

3 **The reason that the Bank of England transferred responsibility for the management of new issues of gilts to the Debt Management Office was to:**

A give control to the Treasury.
B limit the power of the Monetary Policy Committee.
C avoid conflicts of interest.
D minimise the administrative costs.

4 **Financial intermediaries can provide maturity transformation because they**:

A aggregate many small deposits from a large number of clients.
B offer a wide range of deposit accounts to a wide range of depositors.
C provide services to clients from many different geographical locations.
D reduce the risk of default or fraud by lending to a wide variety of borrowers.

5 **Who is allowed to use expenses to reduce income tax liability**?

A Employees, partners and sole traders
B Employees only
C Sole traders only
D Sole traders and partners only

6 **Sarah has been advised that during the current tax year, 30% tax relief is available to her via self assessment. This confirms that she:**

A was born before 6th April 1935
B has an occupational pension plan
C has overpaid tax in earlier years
D has invested in a venture capital trust

7 **Emma bought some shares in July that cost her £3,500. How much stamp duty reserve tax did she have to pay?**

A £35.00
B £105.00
C £140.00
D £17.50

8 **What is the phrase used to describe allowable business expenses for self-employed people to set against income tax? The expenses must be incurred:**

A 'exclusively and necessarily' for the business.
B 'wholly and necessarily' for the business.
C 'wholly and exclusively' for the business.
D 'wholly, exclusively and necessarily' for the business.

9 **In terms of individuals domiciled in the UK, which one of the following is true in relation to IHT?**

A The tax applies to all their property, whichever country it is held in
B The tax applies only to property held in the UK
C Transfers between spouses are exempt even if one of them is not UK domiciled
D UK charities have to pay tax on gifts from UK domiciled persons

10 **Rebecca, a basic rate taxpayer, received a share dividend cheque for £1,400 in May 2018. Assuming that no further dividends are received, how much further tax will she have to pay?**

A Nothing
B £24.00
C £26.66
D £54.00

11 **Which one of the following disposals in might be liable for capital gains tax?**

A Mr Griffiths' gilt-edged securities sold for a profit of £120,000
B Mr Ellis' oil painting sold for £19,800
C Mr Collins' family home sold for a profit of £1,650,000
D A BMW car imported by a dealer and sold at a profit of £9,000

12 **What rate of withholding tax applies to non UK residents earned income?**

A 22%
B 40%
C 20%
D 18%

13 **Mark recently sold some shares and made a taxable gain of £5,000. If his taxable income for this tax year is £20,000 how much capital gains tax will he be required to pay?**

A £1,000
B £2,500
C £1,500
D £500

14 **Which class or classes of national insurance contributions do self-employed people pay?**

A Class 1
B Class 4
C Class 2
D Class 2 and Class 4

15 **Gilts with 10 years to run before their redemption date are known as:**

A undated
B short-dated
C medium-dated
D long-dated

16 **If a company was to distribute 20% of its profits in dividends, what would its dividend cover be?**

A 50
B 10
C 20
D 5

17 **Grace receives income from her National Savings Income Bond. She receives the income:**

A gross but it may be liable to income tax if the amount exceeds the savings allowance amount.
B gross with no potential liability to income tax.
C net of basic rate tax with a potential further liability for higher rate tax payers.
D net of basic rate tax but with no further liability to tax.

18 **What is the MINIMUM age at which William can access the equities element of an ISA?**

A 16
B 18
C 21
D Any age

19 **Mary is retired and wishes to invest in a tax-free savings product. Which one of the following would satisfy this wish?**

A Gilt-edged security
B NS&I Income Bonds
C Premium Bonds
D A unit trust

20 **What does it mean when a gilt stock is quoted as 'ex-div'?**

A Dividends will have been paid out within the last 5 weeks
B The price of the stock is frozen until after the next dividend payment
C The seller will receive the next interest payment
D The purchaser will receive the next interest payment

21 **The risk of investment fluctuations can be reduced through which feature of the investment process?**

A Clustering
B Dynamisation
C Diversification
D Gearing

22 **What is the maximum amount that can be invested into Premium Bonds:**

A	£ 40,000	B	£ 50,000
C	£ 15,240	D	£ 25,000

23 **Terry has the coupon on his Gilts paid gross. As a basic rate taxpayer he will pay:**

A 20% income tax on interest received
B 40% income tax on interest received
C capital gains tax at maturity
D marginal rate income tax at encashment

24 **Which one of the following statements about Child Benefit is correct?**

A It can continue up to and including age 19 if the child is in full time education
B It is only available until children are 16 years old
C Payments for each child are the same
D Payments are dependent on the parents having made sufficient NIC contributions

25 **Steve, aged 47, joined his present occupational pension scheme in 1993 and now earns £120,000 per annum. Which of the following is currently unavailable to him?**

A	SERPS	B	Personal Pension
C	AVC	D	FSAVC

26 **Which one of the following features existing under some personal pension plans is NOT permitted under a stakeholder pension?**

A	Unitised with profits fund	B	Tax free cash
C	Exit charges	D	Contracting out

27 **How would the payments from a Critical Illness Cover policy be BEST described?**

A	Lump sum	B	An annuity
C	Lifelong	D	Replacement income

28 **Which one of the following CANNOT be a trustee of a unit trust scheme?**

A	A clearing bank	B	A life company
C	The fund manager	D	A firm of accountants

29 How are shares in an open-ended investment company priced?

A There is a bid and offer price based on the underlying value of the shares
B The shares are based on an historic valuation
C There is one price based on the value of the assets divided by the number of shares
D There is a cancellation price at which all shares are traded

30 Under the terms of a split capital investment trust, what minimum percentage of the income generated by the portfolio is allocated to the income shares?

A 45%
B 100%
C 80%
D 90%

31 What are the tax benefits of a group personal accident and sickness scheme arranged by an employer?

A The employees may claim tax relief against the premiums
B The employer may offset premiums against corporation tax
C The employer's National Insurance Contributions are reduced
D The premiums will not be classed as a taxable benefit in kind for the employee

32 Which one of the following is true of a second mortgage?

A It must not be greater than the first mortgage
B It must be less than £25,000
C It will usually be with a different lender
D It will be split between the existing lender and the new one

33 The interest rate on a base rate tracker mortgage is usually:

A fixed within a range above and below the base rate.
B higher than the base rate.
C lower than the base rate.
D matched to the base rate subject to annual reviews.

34 Under a home income scheme or lifetime mortgage, how is the outstanding loan normally repaid?

A By income from a purchased life annuity
B From the proceeds of the sale of the house after the borrower's death
C By the borrower's relatives after his death
D From the proceeds of a whole-of-life policy

35 **In which one of the following ways does a unit-linked endowment differ from a traditional with profits endowment?**

A There is no guaranteed sum assured at maturity
B A higher capital gains tax liability applies.
C Joint life plans are not available
D A death benefit applies throughout the term

36 **Clive at age 27 started a stakeholder pension plan for the minimum term, which he intended to use to repay the capital under his interest only mortgage. His stated occupation is office manager. The minimum term of the mortgage will be:**

A 20 years
B 23 years
C 25 years
D 28 years

37 **What is the main attraction of a capped interest rate option when taking out a mortgage?**

A If interest rates go up, the mortgage interest rate will be limited to a preset ceiling
B Interest rates are linked to the Bank of England base rate
C The amount payable is fixed for the duration of the capped rate
D There is a genuine discount off the normal variable mortgage interest rate

38 **What is the advantage of including benefit statements when making a product presentation to a client?**

A It enables the adviser to focus on the sale rather than client queries
B It enables the client to better understand how this product will meet his needs
C It ensures that all point of sale FSA regulatory requirements are met
D It ensures that the client understands the cancellation rights offered by the product

39 **Which of the following financial needs usually becomes the priority on becoming a parent?**

A Investment
B Protection
C Pensions
D Savings

40 **Of the information gathered below, in respect of Alice, which item represents a hard fact?**

A Her investment portfolio performance has been below expectations
B Her savings account balance has fallen to £5,000
C She plans to retire by the age of 60
D She wishes to be financially secure when she retires

41 **Brian is reviewing a range of investment products before selecting the most appropriate solution for his client, Claire. Which factor is the LEAST likely to take into account when selecting an appropriate solution?**

A The possibility of Claire getting married in the future and having children
B Claire's existing portfolio of investment products
C The fact that she has recently moved into a higher rate tax bracket
D Claire's desire to access her investments in five years to purchase a time share in Portugal

42 **For an investment to grow in real terms, it must increase in value:**

A after allowing dealing costs
B at a rate greater than inflation
C at regular intervals
D in line with national average earnings

43 **Which one of the following is true in relation to the manager of an investment trust?**

A He cannot borrow funds
B He can issue more units or repurchase units according to demand
C He can borrow to improve income and capital growth
D He can cancel units if the fund value falls sharply

44 **Any loss made by a partnership is usually:**

A deducted from future dividends
B the responsibility of the partners
C the responsibility of the shareholders
D written off

45 **Stewart wants to start a whole-of-life assurance, which will also provide critical illness cover. Which specific type of plan should he choose?**

A Flexible
B With-profit
C Unit-linked
D Universal

46 **When acting as the agent of a principal, it is a fundamental rule that**:

A a principal is always responsible for the acts of the agent
B a principal must ratify the acts of the agent
C an agent can conclude contracts on behalf of the principal
D an agent is always responsible for the acts of the principal

47 Walter and Winnie own their house on a joint tenant's basis. If Walter dies:

A his share of the property will pass automatically to Winnie
B Winnie will need to purchase Walter's share of the property
C his share will pass to whoever is nominated in his will
D Winnie will own 50% of the property but retain an interest in the other 50%.

48 The difference between a lasting power of attorney and an ordinary power of attorney is that:

A a lasting power of attorney can be revoked at any time by the donor, whereas an ordinary power of attorney can only be revoked by the Court of Protection
B an ordinary power of attorney becomes invalid if the donor becomes mentally incapable, whereas a lasting power of attorney remains effective.
C a lasting power of attorney can be agreed on a verbal basis between donor and donee but ordinary power of attorney must be registered at the Public Trust Office
D an ordinary power of attorney remains valid if the donor becomes mentally incapable whereas a lasting power of attorney becomes invalid.

49 Tom was declared bankrupt in June 2015. For how long will his bankruptcy order remain in place?

A Until June 2019
B Until June 2018
C Until June 2016
D Until June 2017

50 When land is owned by two or more parties, what is the term where each party owns a defined share of that land?

A Joint tenancy
B Joint ownership
C Joint and several
D tenancy in common

CeMAP 1 - UNIT 1 – MOCK PAPER 3			
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Unit 1 - Mock 3

1 **Which one of the following social security benefits is NOT tax-free?**

A Maternity allowance
B Statutory Maternity Pay
C Attendance allowance
D Carer's allowance

2 **In relation to income tax, which one of the following is not classed as a taxable benefit in kind?**

A A loan of £8000 at 3% below market rates
B Contributions to an approved pension scheme
C Employer sponsored private medical insurance
D Luncheon vouchers worth £1.50 per day

3 **Jeremy has capital losses that exceed gains made in the current tax year. What option, if any, does he have in relation to the residual losses?**

A Carry them back to last year
B None
C Claim a capital gains tax rebate
D Carry them forward to future years

4 **Doris and Fred are entitled to receive the married couple's income tax allowance. Why is this?**

A Both also qualify for state disability benefits
B Fred is a starting rate taxpayer and Doris pays no tax
C Their joint savings are below the £3000 threshold
D Doris was born in 1936 and Fred 2 years earlier

5 **Bernard received a share dividend cheque for £4,500 in May 2019. If he was a higher rate taxpayer, how much extra tax must he pay?**

A £79.20
B £812.50
C £ 2,437.50
D £0

6 **May recently sold some shares and made a taxable gain of £13,200. If her taxable income for this tax year is £15,000, how much capital gains tax will she be required to pay?**

A £ 1,320
B £2,500
C £1,500
D £1,860

7 **What is the stamp duty reserve tax due on a purchase of bearer instruments with a market value of £100,000?**

A £1000 B £2000
C £500 D £1500

8 **Two newly appointed trustees have been advised that their CGT allowance will be 100% of the standard allowance rather than 50% because:**

A none of the 2007/08 allowance was used.
B the trust assets are based overseas.
C they act as trustees for a mentally disabled person.
D the trust fully comprises business assets.

9 **A qualifying life policy is maturing and the owner has been advised that capital gains tax will apply to the proceeds. This confirms that:**

A the policy was based offshore.
B over 50% of the invested funds were held overseas.
C the policy was written under trust.
D ownership had changed hands.

10 **In terms of individuals domiciled in the UK, which one of the following is true in relation to IHT?**

A The tax applies potentially to all their assets in whichever country it is held
B The tax applies only to property held in the UK
C Transfers between husband and wife are exempt even if one of them is not UK domiciled
D UK charities have to pay tax on gifts from UK domiciled persons

11 **In calculating a firm's liability to value added tax (VAT), taxable turnover is defined as the:**

A amount liable to VAT when output tax has been deducted from input tax.
B total value of all taxable supplies made in the UK in the course of business.
C amount liable to VAT when input tax has been deducted from output tax.
D total value of standard rated and exempt supplies made in the UK in the course of business.

12 **On which one of the following savings products is interest paid gross but is potentially subject to income tax?**

A Individual Savings Account
B Premium Bonds
C ISA
D Income Bonds

13 Which of the following statements is correct in respect of a unit trust?

A Any gain made on the sale of units by an investor may be liable to capital gains tax
B The fund manager can borrow in order to take advantage of investment opportunities
C An investor who requires mainly capital growth should purchase distribution units
D The price at which an investor purchases units in the fund is referred to as the bid price

14 Which organisation is responsible for the financial stability of banks and building societies?

A The Prudential Regulatory Authority
B Office of Fair Trading
C The Financial Conduct Authority
D The Stock Exchange

15 Jane, a higher rate taxpayer, has a fixed interest unit trust. If she receives gross income from this investment of £2,000 in this tax year, how much income tax, taking into account her personal savings allowance, will she be liable for assuming she has no other investments?

A £650
B £200
C £450
D £600

16 Which of the following statements in respect of the eligibility rules for ISAs is correct?

A Any type of ISA can be opened by an individual on behalf of another
B The minimum age required to open an ISA is 18
C The minimum age to access the equities element of an ISA is 18
D An ISA can be opened in joint names

17 Which one of the following does the Government issue?

A Redeemable ordinary shares
B Gilt-edged securities
C Permanent interest-bearing shares
D Investment bonds

18 A right to buy shares at a specified price by a specified date is a:

A forward contract
B warrant
C put option
D future contract

19 Over the longer term what risk is normally associated with deposit-based investments?

A The value of capital will fluctuate and may fall below the original investment
B There is no guarantee that the original capital will be returned at maturity
C The real value of capital may be eroded due to the effects of inflation
D There is the potential for suffering large capital losses

20 What is generally believed to be the relationship between investment risk and investment return?

A The higher the risk, the lower the potential reward
B The lower the risk, the lower the guaranteed return
C The higher the risk, the higher the potential reward
D The lower the risk, the more volatile the potential return

21 Greg decided to invest in cumulative preference shares as he wanted to ensure:

A guaranteed security
B conversion to ordinary shares
C capital growth
D some certainty regarding future dividend payment

22 William is a higher rate taxpayer but his wife, Mary, has NO income at all. William has £60,000 in a high interest bank account. Which one of the following approaches would NOT reduce their overall tax bill?

A Move some of the money into Mary's name to make use of her personal allowances
B Move some of the money into ISAs (up to the maximum annual limits)
C Invest some of the money into Gilts in William's name
D Invest some of the money into National Savings Premium Bonds in William's name

23 Which one of the following statements is TRUE with regard to direct share investments?

A Both dividends and gains are liable to income tax
B Dividends are potentially subject to income tax and gains are potentially subject to capital gains tax
C Income tax is charged at the investor's highest rate and capital gains tax is charged at a fixed rate of 40%
D Income tax is charged at a fixed rate of 20% and capital gains tax is charged at the investor's highest rate

24 Which of the following statements concerning preference shares is false?

A convertible shares are most commonly a type of preference share
B they are part of the share capital of the company
C they normally rank before ordinary shareholders for dividends
D a fixed level of annual dividend income will always be received by a shareholder

25 Nancy and Ron are married and want to set up a life assurance policy that will pay their potential inheritance tax liability. Which type of policy would be the most suitable?

A Joint life first death
B Joint life second death
C Low cost endowment
D Unit linked

26 Which one of the following statements in respect of a unit linked endowment policy is correct?

A A pre-determined guaranteed benefit is payable on maturity of the policy
B The guaranteed death benefit only is paid on the death of the policyholder before the maturity date
C The appropriate level of life cover is funded by encashing units on a monthly basis
D The value of the policy at any time is the number of units held multiplied by the offer price

27 Which of the following is one way in which a repayment mortgage differs fundamentally from a personal pension mortgage?

A Life cover is not automatically built in
B The higher the interest rate, the higher the monthly payment to the lender
C Provided monthly repayments are made on time, the loan is guaranteed to be repaid in full at the end of the term
D The interest charged is usually lower

28 Which type of mortgage scheme would help someone on low income to become an owner-occupier?

A Shared ownership
B Full endowment
C Buy to let
D Home reversion

29 At what rate is tax relief initially applied to contributions made to a personal pension plan?

A Basic Rate only regardless of their income
B Starting, basic or higher rate, depending on the contributor's marginal rate of tax
C Either basic rate or higher rate, depending on the contributor's highest rate of tax
D Starting rate only, regardless of the contributor's marginal rate of tax

30 Which one of the following in relation to stakeholder pensions is correct?

A Charges must not exceed 2% of the fund's value
B There must not be any entry or exit charges
C The minimum contribution is set at £50
D The maximum gross contribution is £2,808 per annum

31 **If Kim and Chris opt for a joint repayment mortgage, the most suitable way to ensure that the loan will be repaid if one of them dies is by:**

A contributing to a permanent health policy
B investing in an endowment assurance
C making contributions to a critical illness policy
D taking out joint life decreasing term assurance

32 **Which type(s) of policy if any are used by governments to achieve their long term economic objectives?**

A Fiscal only
B Monetary only
C Monetary and fiscal
D Neither monetary nor fiscal

33 **What is gross domestic product? A measure of the value of:**

A demand within a country over a specified period
B goods and services within a country over a specified period of time
C money supply within a country over a specified period of time
D national average earnings within a country over a specified period of time

34 **How can a bank involved in wholesale banking raise money quickly in order to finance business activities?**

A By a further issue of shares
B By borrowing from the Bank of England
C From the interbank market
D By issuing gilts

35 **The regulatory framework for the financial services industry in the UK is a five tier process. Which one of the following bodies has taken over the activities in the third tier?**

A The Financial Ombudsman Service
B The Building Societies Commission.
C The Financial Conduct Authority
D The Banking Code

36 **Julian wishes to make sure that he can meet all his essential outgoings if he is unable to work due to medium or long-term illness. Which of the following insurance products would be most suitable?**

A Accident and sickness
B Income Protection
C Critical illness
D Private medical

37 Which of the following statements in respect of term assurance is correct?

A A decreasing term assurance policy will pay benefits only if the insured dies within the policy term.
B A convertible term assurance policy can be converted to an endowment or whole-of-life assurance only within two years of the date of the original policy.
C The benefits payable on the maturity of term assurance policies are always free of income tax.
D If a convertible term assurance is converted to an endowment assurance, the maturity date of the new policy must be no more than five years beyond that of the original policy.

38 Michael keeps £20,000 cash in his home. After 5 years it will always be able to purchase less:

A euros
B in local shops
C than if it had been invested in shares
D units in a unit trust

39 Which of the following does not need to be included when recommending a product to a client?

A Irrelevant details which fall outside the interests of the client
B The benefits that the client will enjoy
C The client needs that the product will address
D The risks inherent to the product

40 A relationship built between a financial adviser and a customer should be built upon mutual:

A interest
B needs
C profit
D trust

41 Which one of the following would normally be regarded as the priority financial need for an individual who has surplus cash for the first time?

A A unit trust
B An emergency fund
C An equity individual savings account
D A pension plan

42 Which ONE of the following could be described as 'proactive servicing'?

A A telephone call to a client to arrange a pre-agreed review following a salary increase
B A strongly worded letter to a client who is querying the charges on his unit trust
C A call to a client's wife who has contacted you to advise of her husband's death
D A letter to a client asking the reason for non-payment of three premiums

43 The main advantage of writing a life assurance policy in trust is to:

A create a tax exempt fund
B ensure the policy obtains qualifying status
C ring fence the proceeds outside the individual's estate
D increase personal allowances

44 What requirement rests on a discharged bankrupt when applying for a mortgage?

A As he is now discharged, there is no requirement
B To disclose the previous bankruptcy to the lender
C To disclose the information only if it occurred in the last 12 months
D To ensure the lender conducts a thorough credit search

45 When an individual dies intestate, leaving a spouse, children and an estate valued at £110,000, which one of the following applies?

A The estate is divided equally between the surviving spouse and children
B The entire estate passes to the spouse
C The surviving spouse inherits a life interest only in the deceased's entire estate
D The first £50,000 passes to the surviving spouse absolutely, along with a life interest in half the remaining estate

46 Which of these methods is NOT a recognised way of providing 'partnership protection?

A Cross option method
B Automatic accrual method
C Buy and sell method
D Back to back plan

47 Which ONE of the following items of property would be referred to as personalty?

A A collection of vintage wines
B A detached house
C A paddock used for grazing horses
D A Victorian factory building

48 Which one of the following is a definition of an attorney?

A A person who delegates authority to another to act on their behalf
B A person who does not himself have the authority to enter into a contract
C A person who moves abroad but wishes to retain a decision maker in the UK
D A person who is given the authority to act on behalf of another person

49 One of the financial restrictions placed on undischarged bankrupts is that:

A they are only able to borrow nominal amounts of money
B they are unable to buy goods except for their own consumption
C they are unable to contribute to protection policies
D they are only able to work on an employed basis

50 Despite his recent marriage to Katrina, John's existing will has remained in force. Why is this?

A The will was written with the wedding in mind
B The will was witnessed by Katrina and her father
C John has no children or other dependents
D John's estate is valued at £199,000

CeMAP 1 - UNIT 2 – MOCK PAPER 1			
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Unit 2 - Mock 1

1 **The FCA Handbook consists mainly of ‘rules’ and ‘guidance’. Members must:**

A take the ‘rules’ as advice
B be bound by the rules and take the ‘guidance’ as advice
C take the ‘rules’ and ‘guidance’ as advice
D be bound by both the ‘rules and ‘guidance’

2 **Which one of the following is NOT one of the main areas in which the Financial Conduct Authority intends to reduce financial crime?**

A Money laundering
B Share-price reductions
C Insider dealing
D Electronic fraud

3 **In terms of ‘knowing your customer’, what is an eligible counterparty?**

A Where a firm acts on behalf of a private customer
B A private customer
C Where a customer is in the financial services business in a controlled function
D A corporate customer

4 **Which of the following bank employees would not normally require direct FCA approval?**

A A branch cashier
B Money Laundering Reporting Officer
C Compliance Oversight
D Head of internal auditing

5 **Sam has been encouraged to take ‘basic advice’ as she is not financially astute. However, a friend has suggested that she receives full advice because:**

A a more detailed needs assessment would take place
B risk would then be considered
C she has no financial dependents
D she has recently started a new mortgage

6 **In relation to how a firm deals with its regulator, which one of the following is NOT defined within the Principles of Business? A firm must:**

A deal with its regulators in an open way
B disclose appropriate data to its regulator
C deal with its regulators in a co-operative way
D disclose data on a regular basis to its regulator

7 **When MUST the initial disclosure document be provided by a mortgage adviser?**

A At the start of the first meeting with a prospective client
B As soon as regulated business is transacted
C Within 14 days of the first meeting
D As soon as the client requests it

8 **Which document is sent to a client advising them of their right to change their mind?**

A Acceptance letter
B Surrender Notice
C Terms of Business Letter
D Cancellation Notice

9 **Which type of FCA regulation is Treating Customers Fairly (TCF) an example of?**

A High level
B Redress sourcebook
C Principles based
D Regulatory processes

10 **The performance of the FCA in regulating the industry is judged against:**

A a need to ensure 100% protection
B a steady measurable reduction in financial wrongdoing
C a number of 'operational objectives'
D an annually benchmarked achievement of all its statutory objectives

11 **Which one of the following areas is NOT specifically covered by the 'Training and Competence' requirements?**

A Practical Assessment
B Initial training
C Business production levels
D Ongoing supervision of 'competent' advisors

12 **What is the latest date, if any, that the suitability letter can be sent to a customer looking to take out a life assurance policy?**

A Five days after the initial interview
B Five days after the final interview
C Five days after the end of the cooling-off period
D Before the start of the contract.

13 Which one of the following is an example of a type of real time financial promotion?

A A telephone conversation
B A radio appearance
C An email
D A website

14 Which one of the following accurately relates to the advice that MUST be given by independent intermediaries?

A The cheapest product from the host employer
B The cheapest product from any provider
C A suitable product from an appropriate provider
D A suitable product from the host employer

15 Which of the following is not covered by the FCA's Principles for Business?

A A firm's relations with its regulator
B Guidelines on financial promotions
C Maintenance of adequate financial resources
D Protection of customers' assets

16 When setting up a policy to provide legal expenses cover, the adviser is operating to rules issued by the:

A Office of Fair Trading
B Financial Conduct Authority
C General Insurance Standards Council
D ABI

17 Which one of the following is FALSE of complaints referred to an Ombudsman?

A The company involved should investigate the complaint before the Ombudsman
B The company will often take the matter to court following the Ombudsman's ruling
C The Ombudsman's decision is binding on the company
D The Ombudsman may give awards of up to £160,000 plus costs

18 Paul was prosecuted under the Proceeds of Crime Act 2002 and received the maximum sentence of fourteen years and a fine. Which of the following is the most unlikely of him being guilty of?

A Concealing
B Tipping off
C Arranging
D Acquiring

19 The Financial Conduct Authority has a range of enforcement powers. Which of these is not a commonly recognised enforcement power?

A Injunctions
B Restitution
C Withdrawal of approval
D Imprisonment

20 **For how many years after an employee has left a firm, must training and competence records for a pensions transfer specialist be kept?**

A	3 years	B	4 years	C	Indefinitely	D	6 years

21 **During 2019, an individual sustained a loss of £105,000 following the insolvency of an authorised investment firm. What is his MAXIMUM claim under the Financial Services Compensation Scheme?**

A	£40,000	B	£39,000
C	£48,000	D	£85,000

22 **Which one of the following facts MUST be included on all regulated quotations as a result of the Consumer Credit Acts 1974 and 2006?**

A The annual percentage rate
B The lender's registered office
C The purpose of the loan
D The Bank of England base rate

23 **To which of the following will the provisions of MiFID always apply?**

A A firm that underwrites the issue of any of the specified instruments
B A firm that provides life assurance advice
C A firm that provides mortgage advice
D A firm that provides general insurance advice

24 **Since April 2014, consumer credit regulation has now been taken over by which of these regulatory bodies?**

A Competition and Markets Authority
B The FCA
C The Bank of England
D Office of Fair Trading

25 **The Pensions Regulator was empowered by the:**

A	FS&M Act 2000	B	Pensions Act 2004
C	FS Act 1986	D	The Financial Services Authority

26 **Maintaining competition in the UK financial system is an operational objective of the:**

A Financial Ombudsman Service
B Financial Conduct Authority
C Mortgage Code Compliance Board
D The Bank of England

27 **Which of the following figures is used to calculate the amount of capital that firms have to set aside to cover the possibility of business failure due to operational risk?**

A 0.1 B 0.25 C 0.20 D 0.15

28 **Jenny has just joined an investment firm and has been assessed as competent by her new employer. Her new employer will also be required to:**

A insist that new exams are taken
B check that competence is maintained
C no further action is needed by the company
D she will need to do 10 hours a year CPD

29 **A number of particular advantages were identified in the Stakeholder suite of products. Which of the following was not specifically identified?**

A Easier access for customers
B Larger average investments
C Reduced costs
D Reduced risk

30 **Under the rules relating to approved persons, in which function would the Money Laundering Reporting Officer be categorised?**

A Senior Management function
B Customer function
C Governing function
D Required function

31 **Which compliance health warning must appear on all advertising material containing details of past investment performance? Past performance:**

A is not necessarily better than future performance
B is only a general guide to the future
C of 5 years or more is a reasonable guide
D is not necessarily a guide to future performance

32 **Which one of the following is NOT an operational objective of The Financial Conduct Authority?**

A Protecting competition for consumers
B Controlling interest rates
C Securing protection for consumers
D Enhancing and protecting the integrity of the industry

33 **Treating Customers Fairly (TCF) is designed to produce improved service outcomes for:**

A advisers
B ombudsmen
C consumers
D providers

34 **How does the use of specialists within a firm impact on their status as independent advisers?**

A Within a firm, a specialist may claim to offer independent advice provided that he or she can meet the independence rule in every personal recommendation that he or she provides.
B A firm providing independent advice should have a specialist in every area or no specialists at all.
C A specialist in one advice area can only advise on other advice areas on a restricted basis.
D If an individual decides to specialise in one area they can no longer call themselves independent.

35 **The FCA require certain rules to be adhered to in relation to financial promotions. Which statement is specifically true in relation to these rules?**

A A record must be retained by the compliance department until the next FCA inspection.
B A record of the promotions must be supplied to the FCA archive along with proof of the factual claims made.
C The records must be maintained in a secure location for a minimum period of at least 12 months since the last date of the promotion.
D For retail customers, the financial promotion must be clear, fair and not misleading.

36 **Under the rules for investment advisers, advisers must disclose that they are either:**

A whole of market or tied.
B independent or restricted.
C independent or tied.
D whole or market or independent.

37 **In relation to 'suitable advice', which one of the following is a minimum requirement of a restricted adviser?**

A Recommending the best product in the market place
B Recommending the product closest to the client's needs
C Ensuring that no other product in the market provides a better fit
D Ensuring that the product recommended fits the client's needs

38 A mortgage adviser must disclose within the initial disclosure document, which of the following?

A Mortgage products from the whole of the market
B The authorisation status of the firm and adviser
C Details of the important elements of the mortgage
D Any commission that they are receiving from the lender

39 When is it necessary to give a customer a client agreement?

A If the transaction results from an off-the-page advertisement
B When the customer has been given a business card
C If the transaction is likely to involve designated investments
D If the transaction involves any investment advice

40 According to the Conduct of Business rules laid down by the Financial Conduct Authority, it is necessary to keep adequate records of all dealings with customers. Which one of the following is NOT a reason for this requirement?

A To assist in responding to customer complaints
B To provide evidence of compliance procedures
C To constitute an audit trail for inspections
D To verify commission income

41 Which of the following may be an eligible counterparty?

A A firm acting on behalf of a retail client
B Another authorised firm
C A small business
D A private individual

42 What is the effect of the final response letter for a customer who is in the process of making a complaint about a financial services product he has bought?

A They will now have to take legal action to obtain redress
B The can now take the complaint to the Financial Ombudsman Service
C The Financial Ombudsman Service has found their complaint frivolous
D The customer will have to pay to progress the complaint further

43 Giles has advised Malcolm regarding setting up his free standing AVC plan. For how long minimum must Giles keep Malcolm's factfind details?

A 3 months B indefinitely C 3 years D 10 years

44 The Pensions Ombudsman handles complaints about:

A the state pension scheme
B the mis-selling of pension schemes
C the administration of occupational pension schemes
D the Occupational Pensions Board

45 Which one of the following is exempt from the Consumer Credit Acts?

A A credit card account with a limit of £5,000
B An unsecured personal loan of £10,000
C A further advance of £15,000 for house repairs
D A loan of £20,000 for car purchase

46 The Financial Services Compensation Scheme will pay out compensation to customers who have:

A been mis-sold a mortgage endowment policy
B lost money through the insolvency of an authorised firm
C been mis-sold a personal pension plan
D lost money through the mismanagement of an investment fund

47 When carrying out an 'execution-only' sale, responsibility for the transaction rests with the:

A adviser B regulator C product provider D customer

48 Joe runs his own multi tied adviser firm and wishes to create his own fact find form. Under what circumstances is this permitted?

A Joe is free to prepare his own document
B It is not permitted
C Joe must seek approval from his main product providers
D Joe must seek FSA approval of the text

49 Which source book provides details of complaints procedures and external dispute resolution?

A Specialist B Business Standards C Market Conduct D Redress

50 A client has an unresolved complaint about the endowment policy linked to his mortgage. He should take his complaint to the:

A Investment Ombudsman
B Insurance Ombudsman
C PIA Ombudsman Service
D Financial Ombudsman Service

CeMAP 1 - UNIT 2 – MOCK PAPER 2			
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Unit 2 - Mock 2

1 **The Financial Action Task Force (FATF) specifically transfers law enforcement activities to:**

A money laundering officials
B The Financial Conduct Authority
C The Crown Prosecution Service
D The National Crime Agency

2 **For at least how long MUST customer records concerning stakeholder pension scheme members be retained by a life office?**

A 3 years B 5 years C 10 years D Indefinitely

3 **A customer ended his relationship with a lender 2 years and 6 months ago. For a minimum of how many more months should the evidence of identification be retained by the lender?**

A 6 months
B 30 months
C 18 months
D 42 months

4 **Jeremy and Sandra have an interest only mortgage and have received written advice to check the performance of their repayment vehicle. Under the MCOB rules, this has most likely to have been issued by:**

A the FCA B the lender
C the adviser D the investment product provider

5 **In terms of 'knowing your customer', what is a professional customer?**

A Where a firm acts on behalf of a private customer with some knowledge of the industry
B A private customer
C Where a customer is in the financial services business
D A corporate customer

6 **Hayley works for Complete Investments plc, where she offers investment advice for a MiFID firm. When is the earliest date that Complete Insurance is permitted to destroy factfind information?**

A After 5 years B 3 years
C must be kept indefinitely D 6 years

7 Tom is applying to be the new Chief Executive Officer in an authorised firm that is solely FCA regulated. Which of these statements is true?

A There are no formal rules in relation to this issue
B He must be individually vetted by the Bank of England
C The firm are able to declare Tom to be a fit and proper person
D He must be individually vetted by the FCA

8 Which of the following is most likely to be in evidence, for insider dealing to take place?

A Transmission of information
B A significant degree of trading
C A person being in a position of trust
D A person having access to restricted information

9 When MUST the client agreement be provided by an investment adviser?

A Before introducing the fact find
B As soon as regulated business is transacted
C Within 14 days of the first meeting
D As soon as the client requests it

10 Which document is sent to a client advising them of their right to change their mind?

A Acceptance letter
B Surrender Notice
C Terms of Business Letter
D Cancellation Notice

11 Since April 2014, who is responsible for considering any complaint brought about because of potential breaches of the rules in relation to consumer credit contracts ?

A The Bank of England
B Prudential Regulatory Authority
C Financial Conduct Authority
D Financial Services Compensation Scheme

12 Mortgage Advice Ltd have found that their primary method of obtaining new business is not permitted under FCA rules. This means that they must have been using which of the following methods?

A Mortgage Introducers
B TV advertising
C Cold calling
D Radio advertisers

13 **The purpose of the fact find is to:**

A enable the client to avoid disclosing personal information
B allow the adviser to formulate a binding agreement with the client
C give a complete picture of the client's personal and financial circumstances
D ensure that an adviser sells a product to the client

14 **What is the latest date, if any, that a mortgage suitability letter can be sent to a customer?**

A Five days after the initial interview
B Five days after the final interview
C Five days after the end of the cooling-off period
D There is no requirement for suitability letters for mortgages

15 **Which one of the following is an example of a type of real time financial promotion?**

A A personal visit B A radio appearance
C An email D A website

16 **Which one of the following accurately relates to the advice that MUST be given by independent intermediaries?**

A The cheapest product from the host employer
B The cheapest product from any provider:
C A suitable product from an appropriate provider
D A suitable product from the host employer

17 **Which one of the following is NOT a tool open to the FCA in setting and enforcing standards for organisations and individuals?**

A Discipline
B Compensation
C Injunctions and prosecutions
D Supervision and investigation of firms

18 **When setting up a buildings insurance policy, the adviser is operating to rules issued by the:**

A OFT B FCA C GISC D ABI

19 In order to satisfy the Capital Requirements Directive, an investment firm that does not deal on its own account but is allowed to hold client money, must have minimum capital of:

A	£ 125,000	B	€ 125,000
C	€ 730,000	D	£ 730,000

20 Jack has just received a final response letter from his insurance provider. What significance does it have?

A Jack will now have to take legal action to obtain redress
B Jack can now take the complaint to the Financial Ombudsman Service
C The Financial Ombudsman Service has found Jack's complaint frivolous
D Jack will have to pay to progress the complaint further

21 The Financial Conduct Authority has identified three operational objectives as part of its role as the new regulator. Which of these is not an operational objective?

A Protect Customers
B Enhance the integrity of UK financial system
C Reduce financial crime
D Maintain effective competition to benefit consumers

22 For how many years after an employee has left a firm, minimum, must training and competence records be kept?

A 3 B 4 C 5 D 6

23 During 2019, an individual sustained a loss of £38,000 following the insolvency of an authorised investment firm. What is his MAXIMUM claim under the Financial Services Compensation Scheme?

A	£33,170.00	B	£38,000.00
C	£30,000.00	D	£34,500.00

24 Which one of following is true in respect of a firm's responsibilities under the money laundering regulations? A firm must:

A report suspicious circumstances
B maintain client confidentiality at all times
C appoint its Money Laundering Reporting Officer at director or partner level
D deny access to appropriate services to anybody unable to provide detailed evidence of identity

25 **Which of the following is not a senior management function requiring FCA approval?**

A Complaints manager
B Money Laundering Reporting Officer
C Head of Compliance
D Chief Executive Officer

26 **What is the minimum period for which records in respect of pension transfers must be kept?**

A 3 years
B 6 years
C 10 years
D Indefinitely

27 **A mortgage lender has to write to a borrower who is in arrears within how many days of becoming aware of the missed payment?**

A 15 working days
B 7 working days
C 10 working days
D 21 working days

28 **Investment business is being transacted by an independent financial adviser with a client. In these circumstances who is responsible for presenting a key features document to the client?**

A Adviser
B Product provider
C The FCA
D Adviser's manager

29 **The Financial Conduct Authority exists to:**

A govern organisations that manage investments on behalf of other people
B set and monitor adherence to rules for the regulation of banking and investment business
C regulate the marketing and sale of all life assurance products
D oversee the administration of all types of investment business

30 **The FCA Handbook contains a section called the Specialist Sourcebook. Which one of the following would need to refer to this section?**

A A building society
B A firm of solicitors
C A stockbroker
D An authorised insurance seller

31 **Regulations require that advice given to a customer by a financial adviser MUST be in the best interests of the customer, based on the customer's particular circumstances. Since December 2001, this has been commonly referred to as:**

A suitable advice
B best advice
C execution only
D fit and proper advice

32 An independent financial adviser must select both a suitable product and its provider. Which one of the following matters does NOT need to be considered in selecting the provider?

A The adviser's fee
B The standard of service offered to clients
C The cost of the product
D The product's performance to date

33 A customer cancels a £120,000 unit linked single premium investment bond within the cooling-off period. However, during this period, the stock market fell sharply. Consequently, so did the value of the bond. What is the customer likely to receive?

A £120,000 less a market adjustment, if specified in the terms and conditions
B £120,000 less a market adjustment, whether or not specified in the contract
C 95% of the surrender value of the investment bond
D The paid up value of the investment bond

34 What does an 'execution only' transaction require an adviser to do?

A To provide advice that will inform the customer's choice
B To make a range of recommendations for the customer
C To carry out the instructions given by the client
D To effect the transaction on behalf of a market counterparty

35 Why might money laundering regulations create 'financial exclusion'?

A Because not everyone can provide the necessary identification
B Because certain non-residents cannot be offered banking facilities
C Because financial organisations are wary of opening bank accounts with cash deposits
D Because customers want to know why they have been declined a financial product

36 Mortgage advisers are permitted to operate in one of three categories. Which one of the following is the exception?

A Whole of market advisers
B Tied advisers
C Multi tied advisers
D Multi market advisers

37 Regulations established under the Financial Services and Markets Act 2000 require firms to make a commitment to try to resolve complaints within:

A 3 working days
B one month
C 8 weeks
D 3 months

38 **During 2019, a customer's £5,000 deposit account was lost when a bank collapsed. How much could he claim from the Financial Services Compensation Scheme?**

A £4,700.00 B £5,000.00
C £4,500.00 D £3,800.00

39 **If a customer decides that they want to cancel their general insurance contract within the cooling off period, they must do so within:**

A 7 days B 14 days
C 28 days D 30 days

40 **The frequency of compliance visits by the FCA to a firm depends on a number of factors. Which of these would least likely be taken into account?**

A The size of the firm, measured by the number of customers
B The regulator's risk assessment of the firm
C The firms risk classification as determined by the regulator
D The types of product offered

41 **In relation to the General Data Protection Regulations (GDPR), which one of the following is INCORRECT?**

A It requires anyone holding computerised data on individuals to be registered
B It gives individuals the right of access to data relating to them
C It applies only to records held on computer
D The Information Commissioner has the power to prosecute Data Controllers

42 **Pension deductions from employees must be paid to the pension scheme by which date in the month following deduction?**

A 1st B 6th C 19th D 25th

43 **Which regulator regulates the financial stability of deposit taking and related activities?**

A The Bank of England
B The Office of Fair Trading
C Prudential Regulatory Authority
D The Financial Services Authority

44 **Ivor deliberately leaked an incorrect story that his bank were sustaining significant losses due to credit problems and then made a profit through dealing. This is an example of:**

A professional malpractice
B money laundering
C insider dealing
D market manipulation

45 **Which one of the following organisations' responsibilities were taken over by the regulator with effect from 31st October 2004?**

A The Council of Mortgage Lenders
B The Insurance Directorate of the Treasury
C The Mortgage Code Compliance Board
D The Friendly Societies Commission

46 **What do financial services firms need before they can carry out regulated activities?**

A Authorisation
B Approval
C Permission
D Sanction

47 **Which one of the following is NOT covered by the Financial Conduct Authority's Principles for Business?**

A A firm's relations with its regulators
B The protection of customers' assets
C Guidelines on training
D Maintenance of adequate financial resources

48 **Which one of the following contained within the FCA Handbook is binding on authorised firms?**

A Rules
B Guidance
C Standards
D Procedures

49 **Under the 'know your customer requirements', advisers should:**

A assume that a private customer fully understands the risks involved.
B explain the reasons for the recommendation to an execution-only client.
C provide the highest level of advice and duty of care to clients categorised as retail customers.
D offer exactly the same duty of care and advice to all customers.

50 **Under the new rules, independent financial advisers:**

A can only sell products from one company
B must be licensed by the company whose products they sell
C can advise on products across the entire market
D can only refer business to tied agents

CeMAP 1 - UNIT 2 – MOCK PAPER 3			
Question	**Answer**	**Mark**	**Comments / Notes**
1			
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Unit 2 - Mock 3

1 **Under the 'know your customer' rules, why does an adviser need to establish a risk profile?**

A In order to match appropriate insurance solutions
B In order to match appropriate investment solutions
C To identify affordability
D To establish premium sustainability levels

2 **If a member of an Occupational Pension Scheme has an unresolved complaint after exhausting both the trustee and TPAS procedures, what period of time do they usually have to refer the matter to the Pensions Ombudsman?**

A Three months
B six months
C Three years
D one year

3 **Before an employee carries out duties that fall under the FCAs regulatory responsibility he should:**

A have successfully completed his probation period.
B have completed the required number of hours continuing professional development.
C be assessed as competent to undertake the role without supervision.
D be assessed on technical knowledge and its application.

4 **Employees should receive regular training about what is expected of them under money laundering rules so that they:**

A are aware of the consequences to themselves if they fail to comply.
B can complete the Money Laundering Report.
C can assess their firm's compliance with the sourcebook.
D can caution as appropriate any suspect individuals.

5 **The Shire Building Society employs Joe. He has complained about treatment he has received as a member of the society's Occupational Pension Scheme. He is dissatisfied with the response he has received from the scheme's trustees. Who should he now contact?**

A The Pensions Advisory Service
B The Pensions Ombudsman
C The Financial Services Authority
D The Financial Services Ombudsman

6 **Ben suffers a loss of £32,000 due to the insolvency of an authorised investment firm. What is the maximum amount that may be claimed from the Financial Services Compensation Scheme?**

A £28,800 B £29,000 C £32,000 D £30,000

7 **The Financial Conduct Authority insists that customer records must be kept for a specific period. For how long do customer records in relation to a mortgage contract have to be kept for?**

A 5 years
B 3 years
C 10 years
D Indefinitely

8 **Under what circumstances if any is a firm of IFAs permitted to select products from a panel of product providers?**

A Never
B For any type of product provided that it is sufficiently broad and is reviewed regularly
C for investment based products only
D provided that the same panel is used for all their customers

9 **Jack has a complaint about a motor insurance policy he has bought recently. The company has not resolved his complaint to his satisfaction. Who should he now turn to for help?**

A The ABI B General Insurance Standards Council
C Financial Ombudsman Service D The Office of Fair Trading

10 **Which regulatory body now supervises the rules and regulations in relation to consumer credit?**

A Financial Conduct Authority
B Competition and Markets Authority
C Department for Work & Pensions
D Bank of England

11 **Training and competence records for all individuals must be retained for a specified period after they have left the firm. This period is:**

A 3 years B 5 years C 7 years D 10 years

12 **The rules on operational risk require financial institutions to use a multiple of their averaged gross income. This multiple is:**

A 1.0 B 0.50 C 0.15 D 0.25

13 The supervisor ceases to be fully accountable for advice given by the adviser when the adviser:

A is qualified to CeFA 3 level
B has started seeing clients unaccompanied
C is deemed competent
D has achieved supervisory status

14 Which of the following group of company employees would NOT be subject to detailed rules of training and competence under the FCA's Conduct of Business rules?

A Directors
B Back office supervisors
C Investment managers
D Sellers of stakeholder pensions

15 The 2nd key Principle of Business as defined by the FCA is that firms must act with skill care and:

A control
B integrity
C diligence
D honesty

16 In a newspaper advert for a personal loan a financial service provider must satisfy certain rules which are set by which regulatory body?

A The Citizens Advice Bureau
B Consumer Credit Service
C The Lending Code Standards Board
D British Bankers Association

17 The FCA's supervision model is based on three pillars which are:

A ARROW visits, skilled persons reports, risk assessments
B proactive issues, reactive issues, issues and products
C firm systematic framework, event driven work, ARROW
D skilled persons reports, supervisor visits, risk assessments

18 Tina supervises trainee advisers but is not in a position of significant influence. Which principle SPECIFICALLY applies to her role?

A She must ensure that the business of her firm is organised effectively
B She must exercise diligence in managing the business
C She must observe proper standards of market conduct
D She must take steps to ensure the business complies with the regulatory system

19 Which one of the following BEST describes the reason why the Financial Services and Markets Act 2000 was introduced?

A The existing regulatory structure was too fragmented
B It was necessary to make the Treasury the main authorising body
C The existing regulatory structure was too bureaucratic
D It was necessary to make the Home Office the main authorising body

20 Supervision of which sector of financial services was taken over by the Financial Services Authority in January 2005 and now falls under FCA regulation?

A Mortgage lending
B General Insurance
C Life Assurance
D Banking

21 The Financial Conduct Authority intends to secure an appropriate level of investor protection for consumers. Selecting an 'appropriate level' would NOT depend on the different:

A experience of consumers
B levels of risk relating to different investments
C expertise of consumers
D levels of customer loyalty to investment companies

22 Which one of the following statements in relation to the Financial Conduct Authority (FCA), is CORRECT?

A The FCA is owned by the Government
B The Chancellor of the Exchequer is the chairman of the FCA
C The FCA oversees and regulates the industry on behalf of the Government
D The FCA is responsible to the Department of Trade and Industry

23 Individuals who are allowed to carry out 'controlled functions' in relation to a firm's regulated activities are known as:

A authorised persons
B approved persons
C appointed persons
D appropriate persons

24 Which one of the following FCA Sourcebooks provides the standards for the sale of mortgage products?

A Market Conduct Sourcebook
B Specialist Sourcebook
C Interim Prudential Sourcebook
D Mortgage Conduct of Business

25 In judging the FCAs performance, as part of its operational objectives, it must be seen to be:

A facilitating competition
B reducing innovation
C maintaining costs
D increasing regulation

26 Which one of the following job applicants is LEAST likely to meet the FCA 'fit and proper' requirements?

A Gail, who has recently been made redundant from a firm of IFAs
B Alison, who had a default notice issued in respect of a personal loan
C Josie, whose father's house was repossessed three years ago
D Irene, who currently has an authorised overdraft limit of £2,000

27 A firm of solicitors who sell investments on behalf of trustees and receive commission from the product provider, will be regulated by:

A themselves
B their Designated Professional Bodies
C the Treasury
D the Financial Conduct Authority

28 One function of the terms of the client agreement is to explain:

A the individual contracts that the adviser is licensed to sell
B the area from where a potential client can obtain advice
C the Financial Services & Markets Act
D how the adviser is to be remunerated.

29 Freda is reviewing a mortgage illustration before making a purchase. The illustration will have to:

A indicate how the product charges compare to other providers
B indicate the need for life cover
C disclose all the fees associated with the mortgage
D explain the impact of the charges on the mortgage rate

30 Under the new rules, what is the term for those investment advisers giving advice on the products and services of the full range of product providers?

A Appointed agents
B Company representatives
C Independent advisers
D Tied agents

31 Which one of the following documents must be given to a client before giving advice on packaged products?

A The Key Facts Document
B The Menu
C The FCA services and costs disclosure document or the firm's own disclosure documentation that they have decided to use
D The Initial Disclosure Document is the only option

32 When recommending a product to a client, the suitability of advice rules require the independent adviser to always abide by the fundamental principle of:

A observing the client's best interests
B observing that the client knows best
C offering the most cost effective product
D offering the top performing product

33 Giles has advised Malcolm regarding setting up his free standing AVC plan. Under the 'know your customer' rules, for how long minimum must he keep Malcolm's factfind details?

A Six years
B Indefinitely
C Ten years
D Three years

34 Janice has cancelled an investment plan within the cancellation period but unfortunately has received back less than she invested. Why is this?

A A withdrawal charge has been applied to her plan
B She invested a lump sum into a unit-linked plan
C A surrender charge has been applied to her plan
D She invested a regular premium into a unit-linked plan

35 Which of the following is an independent financial adviser NOT obliged to offer?

A disclosure of fees
B products from every provider
C Disclosure of status
D disclosure of the name of the regulator

36 If a client intends purchasing an investment product from an intermediary on an execution only basis, then:

A no recommendation will be required
B no commission will be payable
C know your customer rules will still apply
D best execution rules will not apply

37 Which of these mortgage advisers is required to issue an initial disclosure document on a mandatory basis?

A Whole of market adviser
B Multi tied adviser
C There is no requirement to use an initial disclosure document, it is up to the firm to decide how to implement their disclosure requirements
D Tied adviser

38 A customer who does not agree with the adviser's definition of priorities should:

A terminate the call
B re-appoint to a second meeting
C ask to see a supervisor
D propose their own priorities

39 John, a mortgage adviser, has NOT yet issued a suitability letter and the mortgage is about to complete. This is permitted because:

A suitability letters need to be issued for commercial mortgages only
B there is no FCA requirement for the issuing of mortgage suitability letters
C suitability letters need only be issued on buy-to-let mortgages
D it is only necessary for a mortgage suitability letter to be issued after completion

40 The key benefit of having a client agreement in place for an adviser is?

A All types of transaction are permitted
B The right for the customer to make a complaint is waived
C The adviser may have the ability to make decisions about investments
D The provider's duty of care is reduced

41 Paula is employed by the Fenwick Building Society. She wants to make a complaint about the treatment she has received as a member of the society's final salary pension scheme. To whom should she first refer her complaint if she is unable to gain satisfaction from the scheme's trustees?

A The FSA
B The Pensions Ombudsman
C The Pensions Regulator
D The Pensions Advisory Service

42 The sale of which product would NOT be covered by MCOB rules?

A Buy to let mortgages as a commercial enterprise
B A further advance for home improvements
C A lifetime mortgage
D A first time buyer mortgage on a first charge

43 Cold calling to a prospective customer would not be allowed for which one of the following products?

A Stakeholder pension
B An offset mortgage product
C With-profit endowment
D Term assurance

44 Which one of the following is NOT typically included in a services and costs disclosure document (SCDD) issued by an adviser?

A A statement that the firm is authorized and the name of the regulator
B Details of the qualifications held by each of the firm's advisers
C Details of whether the adviser offers independent or restricted advice
D Details of the charging structure

45 For mortgage sales, which of the following pieces of information is not required as part of the initial disclosures?

A Fees associated with the service
B Arrears arrangements
C Complaints and compensation issues
D The providers of mortgages under discussion

46 Which one of the following statements is FALSE in relation to regulatory risk assessment?

A The risk assessment will be made public
B The size of the firm will have no impact on the risk assessment
C A firm's compliance culture will impact on its assessment
D Firms with higher risk ratings will receive more frequent visits

47 What, if any, is the defined MINIMUM number of Continuing Professional Development hours required for a retail investment adviser?

A 35 B 30 C 40 D 50

48 Which one of the following is least likely to be a FCA regulated mortgage?

A Further Advance
B Home Income Plan
C Semi Commercial Loan
D A mortgage taken by a limited company

49 In the event of insolvency, what is the MAXIMUM claim normally allowable from the Financial Services Compensation Scheme for loss of deposited funds from a single bank?

A 100% of the first £85,000
B 100% of the first £24,000 + 90% of the next £24,000
C 100% of the first £48,000
D 100% of the first £50,000

50 Under what circumstances if any are a firm of IFAs permitted to select products from a panel of product providers?

A None
B for any type of product
C for investment based products only
D for risk benefit products only

ANSWERS

UNIT 1 – TOPIC 1&2

QUESTION	ANSWER		QUESTION	ANSWER
1	A		11	C
2	B		12	C
3	C		13	C
4	C		14	B
5	C		15	B
6	D		16	C
7	A		17	B
8	B			
9	A			
10	A			

UNIT 1 – TOPIC 3

QUESTION	ANSWER		QUESTION	ANSWER
1	D		16	B
2	C		17	C
3	A			
4	C			
5	C			
6	D			
7	D			
8	C			
9	B			
10	A			
11	D			
12	B			
13	A			
14	B			
15	D			

UNIT 1 – TOPIC 4

QUESTION	ANSWER		QUESTION	ANSWER
1	D		16	D
2	A		17	D
3	B		18	A
4	C		19	D
5	A		20	C
6	A		21	C
7	C		22	B
8	C		23	C
9	D		24	C
10	C		25	D
11	C			
12	A			
13	B			
14	D			
15	A			

UNIT 1 – TOPIC 5

QUESTION	ANSWER		QUESTION	ANSWER
1	B			
2	B			
3	C			
4	D			
5	B			
6	D			
7	A			
8	B			
9	C			
10	A			
11	D			
12	B			

UNIT 1 – TOPIC 6

QUESTION	ANSWER		QUESTION	ANSWER
1	A		15	D
2	B		16	B
3	A		17	B
4	D		18	D
5	B		19	B
6	B			
7	B			
8	C			
9	B			
10	D			
11	C			
12	C			
13	D			
14	B			

UNIT 1 – TOPIC 7

QUESTION	ANSWER		QUESTION	ANSWER
1	A		13	C
2	C		14	D
3	B		15	B
			16	C
4	B			
5	D			
6	C			
7	C			
8	A			
9	A			
10	C			
11	D			
12	A			

UNIT 1 – TOPIC 8

QUESTION	ANSWER		QUESTION	ANSWER
1	B		16	C
2	A		17	D
3	D		18	A
4	B		19	A
5	D		20	B
6	B		21	B
7	B		22	A
8	D		23	B
9	D		24	A
10	A			
11	C			
12	D			
13	D			
14	A			
15	B			

UNIT 1 – TOPICS 9/10

QUESTION	ANSWER		QUESTION	ANSWER
1	A			
2	D			
3	D			
4	B			
5	A			
6	D			
7	B			
8	A			
9	D			
10	D			
11	B			
12	A			

UNIT 1 – TOPIC 11 & 12

QUESTION	ANSWER		QUESTION	ANSWER
1	B		16	B
2	D		17	C
3	C		18	B
4	C			
5	A			
6	C			
7	A			
8	A			
9	C			
10	B			
11	C			
12	B			
13	C			
14	D			
15	B			

UNIT 1 – TOPIC 13

QUESTION	ANSWER		QUESTION	ANSWER
1	A		15	B
2	B		16	B
3	C		17	C
4	B		18	B
5	B		19	D
6	D		20	C
7	D		21	C
8	B		22	B
9	C		23	C
10	D		24	A
11	A		25	D
12	A		26	D
13	C		27	A
14	A		28	B

UNIT 1 – TOPICS 14 & 15

QUESTION	ANSWER		QUESTION	ANSWER
1	C		14	A
2	A		15	C
3	C		16	A
4	B		17	B
5	C		18	D
6	B		19	C
7	B		20	C
8	C		21	A
9	C		22	C
10	A			
11	B			
12	A			
13	B			

UNIT 1 – TOPIC 16

QUESTION	ANSWER		QUESTION	ANSWER
1	A		16	B
2	C		17	C
3	D		18	A
4	B		19	B
5	B		20	B
6	C		21	A
7	D		22	A
8	A		23	A
9	A			
10	D			
11	A			
12	B			
13	C			
14	A			
15	D			

UNIT 2 – TOPIC 17

QUESTION	ANSWER		QUESTION	ANSWER
1	B		15	A
2	B		16	D
3	C		17	B
4	A			
5	A		18	A
6	A		19	C
			20	D
7	D		21	A
8	B		22	B
9	C			
10	D			
11	B			
12	D			
13	A			
14	D			

UNIT 2 – TOPIC 18

QUESTION	ANSWER		QUESTION	ANSWER
1	A		15	A
2	B		16	C
3	A		17	C
4	D		18	B
5	C		19	D
6	B		20	A
7	B		21	C
8	C			
9	A			
10	B			
11	B			
12	C			
13	C			
14	A			

UNIT 2 – TOPIC 19 & 20

QUESTION	ANSWER		QUESTION	ANSWER
1	B		16	B
2	A		17	B
3	D		18	C
4	C		19	A
5	D		20	A
6	C		21	C
7	A		22	B
8	C		23	A
9	A		24	D
10	C		25	C
11	C		26	A
12	D		27	C
13	D		28	D
14	D		29	D
15	D		30	C

UNIT 2 – TOPIC 21 & 22

QUESTION	ANSWER		QUESTION	ANSWER
1	B		16	B
2	C		17	D
3	A		18	A
4	B		19	B
5	B		20	B
6	D		21	D
7	D		22	B
8	B		23	C
9	B		24	A
10	A		25	D
11	A			
12	A			
13	A			
14	C			
15	A			

UNIT 2 – TOPIC 23

QUESTION	ANSWER		QUESTION	ANSWER
1	A		7	A
2	A		8	A
3	D		9	A
4	D		10	C
5	A		11	D
6	D		12	B

UNIT 2 – TOPIC 24

QUESTION	ANSWER		QUESTION	ANSWER
1	A			
2	D			
3	C			
4	A			
5	B			
6	B			
7	D			
8				
9				
10				

UNIT 2 – TOPIC 25

QUESTION	ANSWER		QUESTION	ANSWER
1	D		9	C
2	A		10	D
3	B		11	C
4	B		12	A
5	D		13	D
6	C		14	D
7	B		15	C
8	B		16	B

Unit 1 Mock 1

1	A		26	A
2	B		27	B
3	C		28	D
4	A		29	C
5	B		30	A
6	C		31	D
7	A		32	B
8	B		33	B
9	A		34	B
10	D		35	B
11	C		36	A
12	C		37	D
13	B		38	D
14	D		39	B
15	B		40	B
16	D		41	B
17	D		42	C
18	C		43	D
19	D		44	B
20	D		45	A
21	C		46	A
22	D		47	D
23	B		48	A
24	A		49	B
25	D		50	A

Unit 1 Mock 2

1	**B**		**26**	**C**
2	**B**		**27**	**A**
3	**C**		**28**	**C**
4	**B**		**29**	**C**
5	**A**		**30**	**B**
6	**D**		**31**	**B**
7	**D**		**32**	**C**
8	**C**		**33**	**B**
9	**A**		**34**	**B**
10	**A**		**35**	**A**
11	**B**		**36**	**D**
12	**C**		**37**	**A**
13	**D**		**38**	**B**
14	**D**		**39**	**B**
15	**C**		**40**	**B**
16	**D**		**41**	**A**
17	**A**		**42**	**B**
18	**B**		**43**	**C**
19	**C**		**44**	**B**
20	**C**		**45**	**D**
21	**C**		**46**	**C**
22	**B**		**47**	**A**
23	**A**		**48**	**B**
24	**A**		**49**	**C**
25	**A**		**50**	**D**

Unit 1 Mock 3

1	B		26	C
2	B		27	C
3	D		28	A
4	D		29	A
5	B		30	B
6	A		31	D
7	D		32	C
8	C		33	B
9	D		34	C
10	A		35	C
11	B		36	B
12	D		37	A
13	A		38	B
14	A		39	A
15	D		40	D
16	C		41	B
17	B		42	A
18	B		43	C
19	C		44	B
20	C		45	B
21	D		46	D
22	C		47	A
23	B		48	D
24	D		49	A
25	B		50	A

Unit 2 Mock 1

1	**B**		**26**	**B**
2	**B**		**27**	**D**
3	**C**		**28**	**B**
4	**A**		**29**	**B**
5	**A**		**30**	**A**
6	**D**		**31**	**D**
7	**A**		**32**	**B**
8	**D**		**33**	**C**
9	**C**		**34**	**A**
10	**C**		**35**	**D**
11	**C**		**36**	**B**
12	**D**		**37**	**D**
13	**A**		**38**	**B**
14	**C**		**39**	**C**
15	**B**		**40**	**D**
16	**B**		**41**	**B**
17	**B**		**42**	**B**
18	**B**		**43**	**B**
19	**D**		**44**	**C**
20	**C**		**45**	**C**
21	**D**		**46**	**B**
22	**A**		**47**	**D**
23	**A**		**48**	**A**
24	**B**		**49**	**D**
25	**B**		**50**	**D**

Unit 2 Mock 2

1	D		26	D
2	B		27	A
3	B		28	A
4	B		29	B
5	A		30	B
6	A		31	A
7	D		32	A
8	D		33	A
9	A		34	C
10	D		35	A
11	C		36	D
12	C		37	C
13	C		38	B
14	D		39	B
15	A		40	D
16	C		41	C
17	B		42	C
18	B		43	C
19	B		44	D
20	B		45	C
21	C		46	C
22	A		47	C
23	B		48	A
24	A		49	C
25	A		50	C

Unit 2 Mock 3

1	B		26	B
2	C		27	D
3	C		28	D
4	A		29	C
5	A		30	C
6	C		31	C
7	B		32	A
8	B		33	B
9	C		34	B
10	A		35	B
11	A		36	A
12	C		37	C
13	C		38	D
14	A		39	B
15	C		40	C
16	C		41	D
17	B		42	A
18	C		43	B
19	A		44	B
20	B		45	B
21	D		46	A
22	C		47	A
23	B		48	D
24	D		49	A
25	A		50	B