



**SECURITIES & INVESTMENT INSTITUTE DIPLOMA
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CHIEF EXAMINER'S REPORT-
PRIVATE CLIENT INVESTMENT ADVICE AND MANAGEMENT**

INTRODUCTION

The overall standard was reasonable; although slightly below the last four sittings. There were many good scripts, and some excellent ones. At the lower end of the mark scale candidates generally failed because of an inability to correctly manipulate and interpret numerical data and to correctly structure answers.

In Section A the average mark was good, and by far the best of the three sections. For four questions many candidates achieved close to full marks: Q3 (Capital Gains Tax), Q7 (Market Abuse), Q8 (Settlement) and Q10 (Investment Terms). In contrast, Q4 (Yields), Q5 (Traded Options), Q6 (Taxation of Life Assurance Bonds) and Q9 (Money and Time-Weighted Rates of Return) were the worst answered by the majority of candidates.

In Section B Q11 (Riskiness of Ordinary Shares) was marginally the most popular question and generally competently answered. The distribution of marks was similar for the three questions.

In Section C most candidates had a reasonable understanding of the three questions to the case, and the range of investments requiring analysis. However a common failing was not answering the requirements of each specific question; often including material more relevant to one of the other two questions.

Section A

Q1 Most candidates were aware of the definition of a proxy, but were frequently confused as to their rights. The rights of shareholders in general were well understood.

- (a) (i) A proxy is a means by which a member may vote at a meeting which they cannot attend (when sending out proxy forms, companies usually suggest the names of directors of the company who will act as proxies, voting as they see fit unless otherwise instructed).
- (ii) A proxy can only vote if a poll is called. (a proxy can only speak to demand a poll).
- (b) The rights of the shareholders are specified in the Articles of Association, and may vary with the different classes of shares. In general these are:
- To receive the annual report and accounts
 - To receive notice of the AGM and other meetings of members
 - To attend, speak (if called) and vote at meetings
 - To appoint a proxy
 - To share in the profits of the business, and the residue on a winding up
 - To subscribe for new share capital (and securities with conversion rights) in proportion to existing holdings (‘pre-emptive’ rights)
 - To transfer shares freely.

Q2 The distinguishing characteristics of hedge funds were generally well understood and most candidates were able to outline many of the following:

- Can go short
- Extensively use derivatives
- High gearing
- High Charges and Performance fees
- Aim to achieve absolute rather than relative returns
- Lock-in periods - illiquid
- Lightly regulated through offshore centres
- Lack of transparency (‘black box’)
- High minimum sums.

Q3 Answers to this question were of highly variable standard. Many candidates who understood the changes in CGT, including the new matching rules, scored maximum marks. Many weak answers scored poorly, failing to determine the chargeable gain. The Examiner expected good answers to be set out on the following lines:

Purchase costs:

$$4,000 \text{ shares} \times \text{£}3.50 = \text{£}14,000$$

$$4,000 \text{ shares} \times \text{£}8.21 = \text{£}32,840$$

$$2,000 \text{ shares} \times \text{£}15.64 = \underline{\text{£}31,280}$$

$$\text{£}78,120$$

Average price per share of pool

$$= \text{£}7.812$$

$$\text{Gain per share} = \text{£}10.66 - \text{£}7.812$$

$$= \text{£}2.848$$

$$\text{Chargeable gain} = \text{£}2.848 \times 5,000$$

$$= \text{£}14,240$$

$$\text{Taxable gain} = \text{£}14,240 - \text{£}9,600$$

$$= \text{£}4,640$$

$$\text{CGT} = \text{£}4,640 \times 18\%$$

$$= \text{£}835.20$$

Q4 Some candidates had difficulty with the yield calculations. A frequent error was to gross up only the 4% coupon of the preference share, rather than the net yield. This sometimes led to erroneous explanations for the yield differences. Another common error was in causation; in implying the yields were high because the prices were low, rather than correctly prices being low because investors required high yields!

$$(a) (i) \text{ Flat yield} = \frac{6.0}{59} \% = \mathbf{10.17\%}$$

$$(ii) \text{ Grossed-up preference dividend yield} \\ = \frac{4.0}{27} \times \frac{100}{90} \% = \mathbf{16.46\%}$$

	= £48,000
Top slice	= £48,000/10 (years) = £4,800
Other taxable income	= £32,000
Taxable income + top slice	= £36,800
Taxable slice	= £36,800-£34,800 = £2,000
Income tax liability	= £2,000 x 10 x (40% - 20%) = £4,000

Q7

- (a) These terms were almost universally understood. Candidates demonstrated an awareness of other types of market abuse but outlines lacked clarity.
- (i) `Pump and dump` is the spreading of false stories, often on bulletin boards, in order to boost the share price, thus enabling the perpetrators to use the opportunity to dispose of shares at an inflated price.
- (ii) `Trash and cash` is the reverse of the above; it is deliberately spreading false bear stories in order to depress the share price, and using the opportunity to buy cheaply.

These amount to **Dissemination** – giving out information that conveys a false or misleading impression about an investment or the issue of an investment where the person doing this knows the information to be false or misleading.

- (b) Market abuse is an offence introduced in the Financial Services and Markets Act 2000. In July 2005 The FSA adopted the EU Market Abuse Directive (MAD!) and incorporated it into its Code of Market Conduct. The FSA states that six other types of behaviour can amount to market abuse:
- Insider dealing** – when an insider deals, or tries to deal, on the basis of inside information.
- Improper disclosure** – where an insider improperly discloses inside information to another person.
- Misuse of information** – behaviour based on information that is not generally available but would affect an investor's decision about the terms on which to deal (similar to insider dealing).
- Manipulating transactions** – trading, or placing orders to trade, that gives a false or misleading impression of the supply of, or demand for, one or more investments, raising the price of the investment to an abnormal or artificial level, such as buying large amounts of a share near the end of the day.
- Manipulating devices** – trading, or placing orders to trade, which employs fictitious devices or any other form of deception or contrivance.
- Distortion and misleading behaviour** – behaviour that gives a false or misleading impression of either the supply of, or demand for, an investment; or behaviour that otherwise distorts the market in an investment.

Q8 This question was exceptionally well answered, with many candidates earning maximum marks.

- (a) CAD provides confidence in the security of settlement because neither cash nor documents are released until both sides of the deal are ready to settle. This is also referred to as Delivery versus Payment (DVP).
- (b) A CMA is a record of a CREST member's running total of a day's payment obligations to or from its payment bank. CMAs are set to zero at the start of each day because at the end of each day net payments are settled between payment banks.
- (c) Each bank specifies a maximum amount that it will pay at the end of each day for each member of CREST. Each member has only one CMA, but can have several bank accounts linked to that single CMA.
- (d) Dynamic headroom is the difference during the day between a member's credit limit (cap) and its net payment obligations (It is dynamic because it expands as a result of a sold bargain settlement and decreases as a result of a bought bargain settlement).

Q9 Most candidates seemed aware of the meaning of money-weighted and time-weighted rates of return, but only a minority correctly calculated both figures. The comments on strategy and performance were reasonable but were misled by incorrect calculations.

- (a) (i) The money-weighted rate of return was
$$\frac{\pounds 7,500 - \pounds 5,000 - \pounds 5,000}{\pounds 5,000 + \frac{1}{2} \times \pounds 5,000} = \frac{(\pounds 2,500)}{\pounds 7,500} = -33\%$$
- (ii) The time-weighted rate of return of the portfolio was
$$(\pounds 10,000 / \pounds 5,000 \times \pounds 7,500 / \pounds 15,000) - 1 = 0\%$$

- (b) Emily's portfolio performance was poor, perhaps because she was a momentum investor, doubling her investment when the market doubled in the first six months.

The fund manager had done well in a falling market; maintaining the value of the fund when the market had fallen 10%. The 'alpha' of the fund was therefore +10%.

Q10

As with the other descriptive questions, this was generally well answered. The weakest answers were generally (d), where many candidates simply referred to the 'difference' in yields, without expressing which was greater. Other candidates wrongly assumed that the normal yield gap was for gilt yields to exceed equities; and therefore the reverse yield gap was the inverse. Confusingly, in reality, the reverse yield gap has not been the exception but the norm from 1959 until 2008 when rising dividend yields overtook falling gilt yields.

- (a) A naked bear is a short seller (or the writer of a call option, or seller of financial future or CFD) i.e. does not possess the underlying asset but believes the price will fall. The risk is unlimited if the price rises.
- (b) An 'inverted' yield curve is when the redemption yields of short dated gilts are higher than those of long dated gilts; the norm in the UK in recent years.
- (c) A backwardation is when a future price is below the cash price; it is a negative contango (common in commodity markets but anomalous in financial futures); It is also used to refer to the anomalous situation when the best bid price for share is temporarily above the best offer price.
- (d) The 'reverse yield gap' is the excess of the gross redemption yield of long-dated gilts minus the grossed-up dividend yield of equities (FTSE All-Share index); it has been the norm since 1959 in the UK because the growth rate expectation for equities exceeded the equity risk premium.

Section B

Q11 This question offered candidates plenty of scope because the riskiness of an ordinary share depends on a wide variety of factors. However, candidates often focussed on a narrow range, or simply listed ratios without explaining their relevance to risk. There was often an emphasis modern portfolio theory, with systematic and unsystematic risk, and the implication of beta. This was relevant, but such answers often made little mention of critical items such as cash flow and gearing.

The range of factors that could have been reviewed include:

- Sales volatility (which depends on the nature of the industry, including market dominance, e.g. utilities compared with house building)
- Degree of technological change affects demand and supply (e.g. online retailing affecting the high street)
- Degree of competition; Buffett refers to an 'economic moat'; e.g. regulatory monopoly, brand names
- The degree of operational gearing (reflected in the ratio of fixed to variable costs; gross profit margin relative to net profit margin)
- Stability of earnings and dividend growth; dividend cover

The financial structure of the company:

- The capital and income gearing ratios (ratio of debt to equity, both gross and net borrowing; interest cover measured by interest cover in the Income Statement and Cash Flow Statement; the Income and Capital Priority Percentages)
- Investment grade of debt
- Liquidity ratios (current and acid test ratios)
- The Cash Flow Statement (Operating cash flow; degree of self financing, ability to finance working capital and fixed asset investment)
- Pension obligations
- Contingent liabilities
- Composition of assets (property assets, inventories, trade debtors, cash, intangibles, including goodwill)

- Country of origin; is it UK or from overseas?
- Size of company and trading history
- Full listing, AIM, or Plus Markets
- Marketability of shares; normal market size
- Composition of shareholders-major shareholders; directors' holdings; institutional holdings (some candidates mentioned forced sales by hedge funds, or by trackers when a company was relegated from an index)
- Potential dilution; share options

- Corporate governance (composition of board; role of chief executive and chairman; non-executive directors)
- Auditors' Report

- Share price variability
- Momentum in share price ('don't catch a falling knife')
- Systematic risk, beta
- PE ratio, dividend yield, price:book ratio; the extent to which the share price is underpinned by earnings, dividends and assets. High growth shares, selling on high multiples to earnings and assets, and low dividend yields, can be highly sensitive to a slow down in growth rates.

Q12 Most candidates answering this question had a reasonable understanding of the purpose, characteristics and taxation of discretionary trusts.
Since March 22 2006, most family trusts are discretionary, unless they are 'bare'.
Relevant points that could have been discussed include:

- Discretionary trusts can be said to be 'discretionary' in two respects. First, the trustees usually have a power to select which beneficiaries payments will be made to from within the 'class' The class of beneficiary is stated, e.g grandchildren and great grandchildren. Secondly, the trustees can select the amount of trust income or capital that the beneficiary receives. No beneficiary has a right to demand income from a discretionary trust (Although most discretionary trusts have both types of discretion, it is not necessarily so. It would be perfectly permissible for a trust to have fixed number of beneficiaries and for the trustees to have a discretion as to how much each beneficiary receives)
- how often the payments are made
- what, if any, conditions to impose on the recipients.
- Maximum life 80 years

The surviving spouse or civil partner can be included as one of the beneficiaries of the trust. The trustees can be empowered to pay out income or the underlying capital to the surviving spouse or civil partner at their discretion. Thus the surviving spouse or civil partner can enjoy both the income and capital of the trust.

The settlor can guide the trustees. This is usually achieved by leaving a 'letter of wishes' with the will. Such letters are quite usual and are read alongside the will, though they are not binding on the trustees. It is quite normal for such a letter to state that the first aim for the trust is to ensure adequate provision is made for the surviving spouse or civil partner for the remainder of his or her days. The letter will usually say what is desired to happen thereafter, such as passing assets to the children.

Previously, well advised couples might have included a discretionary trust in their will to utilise the nil rate band on the first death rather than wasting it by passing assets to the surviving spouse under the spouse exemption. Although any unused nil rate band can now be transferred to the surviving spouse or civil partner, there are still circumstances where this type of planning remains beneficial.

These circumstance include:

- complex succession plans, particularly where there is a second marriage and/or step children
- to protect young or improvident beneficiaries against creditors - as the beneficiary has no claim to any specific part of the trust fund, none of the trust fund will be capable of attachment by the trustee in bankruptcy of any beneficiary
- to create flexibility to react to changes in circumstances
- in certain jurisdictions, a discretionary trust can be used to protect family assets from forming part of any divorce settlement

- estates containing assets where the value is expected to grow faster than the anticipated future increases in the nil rate band allowance
- estates containing assets eligible for business property relief or agricultural property relief.

The trustees are liable to tax on income received at the rate applicable to trusts (currently 40%), but dividends and other similar income are chargeable at the trust rate that applies to dividends (currently 32.5%).

All income paid to the beneficiaries carries a credit at the rate applicable to trusts. So, the payment is treated as if it had been made after the deduction of tax at that rate. If beneficiaries are basic or starting rate taxpayers, or non-taxpayers, they will be able to reclaim some or all of the tax paid.

The trustees may, or may not, be allowed to 'accumulate' income within the trust for as long as the law allows rather than pass it to the beneficiaries. That income becomes additional capital of the trust. If, in later years, the trustees distribute some of the accumulated income to the beneficiaries the payment is a capital distribution, and not an income distribution. Beneficiaries are not taxable on capital distributions.

Lifetime transfers into the trust are subject to CGT, but gains may be held over under gifts holdover relief.

Trustees are liable to tax at 18%, on any capital gains above £4,800.

The beneficiaries are not taxed on any trust gains and do not get credit for tax paid by the trustees.

When a discretionary trust is created during a lifetime transfers into the trust (in excess of £312,000) are subject to IHT at 20% as chargeable lifetime transfers. A discretionary trust is also subject to inheritance tax every 10 years after the creation of the trust at a rate of 6% (30% of the lifetime rate of 20%) of the market value of the trust's assets. A nil rate discretionary trust will escape tax altogether.

There is also a charge when assets cease to be held on discretionary trust, eg if assets pass out of trust to a beneficiary. In this case, the charge to inheritance tax is based on:

- the value of the property leaving the trust
- the proportion of the period of 10 years for which the assets have been held on discretionary trust since the last 10 year charge
- the rate of tax at the last 10 yearly charge.

Q13.

Most candidates attempting this question were reasonably familiar with the characteristics of ethical investment. However, the better answers recognised that the question involved two aspects that are inter-related. Is it disadvantageous to select from a restricted range of companies? To what extent does 'ethical investing' restrict the range of companies?

In modern investment theory, 'efficient' portfolios are composed of securities that offer the best risk/return trade-off from a global population.

It exploits the diversification advantages of investing in the widest range of sectors and countries, between which correlation of returns are low.

But it assumes information is freely available.

In contrast, many investing strategies ('share screening') involve choosing from shares that meet predetermined criteria

These may be accounting or investment criteria; value or growth strategies.

For example, Benjamin Graham and Warren Buffett both had clear criteria (but different) they used to filter shares.

Buffett recommends focus rather diversification.

Some candidates mentioned that many funds have a specific focus, either geography, sector, size or strategy; few have a totally unrestricted mandate. Most funds have some explicit or implicit restrictions. It is simply not feasible to analyse the total universe of investments.

The smaller the range of companies, the greater the opportunity to research them and obtain an information advantage.

Ethical criteria are mostly frequently applied to taking share stakes in companies, but can also be used for other types of corporate investment, and lending to governments.

Second, good answers recognised that the degree of restriction, and hence possible inefficiency, depends on what ethical stance should be adopted?

Should it be based on religious or other moral principles?

‘Ethical’ traditionally meant screening out companies that were involved in unacceptable activities.

If religion, there will be differences between say Christian and Muslim. Both would be against alcohol, tobacco, gaming. But Islamic criteria would be more restrictive; also opposed to insurance, banking, pork production, high gearing etc.

‘Socially Responsible’ can be used as a synonym, but is sometimes interpreted as emphasising positive as well as negative criteria.

Should criteria encompass both positive and negative criteria?

Should it apply 100%, or to only say, 90%, of a companies activities?

How will such screening be implemented?

Investors could rely on organizations such as EIRIS (Ethical Investment Research Information Service), which works in conjunction with FTSE4Good.

There are about 50 UK ethical funds, including ‘trackers’.

Ethical funds tend to have higher charges than normal tracker-funds.

Performance can be measured against dedicated indices, such as: FTSE4Good, which screens companies in each of the FTSE indices for specified positive and negative criteria.

FTSE4Good Index series selects from the FTSE All-Share Index and the FTSE All-World Developed Index (Global).

FTSE4Good covers Global and European regions and three countries, US, UK and Japan. Each, apart from Japan, also has a traded (size) index of leading shares.

They cover 23 markets and around 2,000 potential constituents.

It does not include emerging markets. Ethical considerations have prominence in the UK and USA, but much less so in many other countries, particularly emerging markets.

Around three-quarters of the FTSE 100 shares qualify for the UK FTSE4Good Index.

The main requirements are:

- Environmental sustainability
- Positive relationships with stakeholders
- Universal human rights
- Good supply chain labour standards
- Countering bribery
- Climate change

Excluded companies are specifically those involved in tobacco, armaments, uranium and the civil and military nuclear production.

The UK FTSE4Good Index has been accused of being 'ethics lite'; some filters can be passed by simply issuing suitable policy statements.

The investment implications are uncertain.

With ethical investment there is an emphasis on 'progressive' and 'growth' companies.

These are predominantly smaller companies, which are more volatile.

Yields tend to be below average; not suitable for income seekers.

Reducing the universe of shares can be seen as detrimental to risk/return.

This may be particularly the case when 'value' is predominating over 'growth', as in bear markets.

The alternative viewpoint is that the emphasis is on 'progressive' or 'enlightened' companies; companies embracing new technology.

It avoids companies where there may be claims for compensation or adverse publicity.

Not surprisingly, performance statistics depend to a large extent on the period of measurement.

Ethical funds showed poor relative performance when commodity prices were soaring because of their general avoidance of mining, oil and gas shares.

They were also generally overweight in financial and smaller companies securities, which produced adverse performance following the 'sub-prime' crisis.

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Section C

Q14.

Many candidates provided a reasonable analysis of the case study. The most common failings were including material in the wrong part of the answer, or discussing the merits of additional investments rather those identified in the case. In relation to the former, candidates frequently commented on the absence of bonds in part (a) of their answer. Much of this detail would have earned marks if it had been included in part (b). Similarly, often answers to part (c) included the merits of income drawdown, which should have been in part (a).

- (a) Some candidates recognised the ‘core-satellite’ approach. A good starting point was to provide a breakdown of the asset allocation. The largest core element (60% of the financial assets of £840,000) was in tracker funds of major indices of the UK and USA. These are largely multinational companies, providing a high overseas content, not just in the USA. They would provide a hedge against a weakening pound.
- The advantages of exchange traded funds were well understood:
- A cheap way of buying tracker funds; lower total expense ratio than unit and investment trusts
 - Free of stamp duty.
 - Continuous trading on the LSE
 - Low tracking error; iShares achieve it by fully replicating the shares in these indices - giving a very small tracking error

However, they can have counterparty risk (but cash based ETFs have zero counterparty risk, unlike ‘notes’; the funds hold underlying securities in ring-fenced separate accounts).

The satellite (12%) portfolio of ‘deep value’ shares was intended to offer excess return for the level of risk.

Benjamin Graham intended the selection criteria to ensure the shares offered a high secure return with good asset backing.

These might be shares that had been ‘oversold’; i.e. ‘bottom fishing’.

But many candidates commented that these figures were historic; earnings, dividends and asset valuations may not be maintained.

Many of them were companies with well-publicised difficulties which had suffered very large price falls.

They were not well diversified in terms of range of sectors; there was a heavy concentration in construction and property (Persimmon, Bellway, Barratt Developments, A&J Mucklow, Henry Boot, and Mountview Estates).

A common fallacy was to highlight the lack of diversification in terms of number of companies; 14 not meeting the 15-20 minimum identified by Markowitz to diversify away most of the unsystematic risk. But this ignored the majority of the diversification coming from the ETFs.

There might be reasons why David did (intimate knowledge of industry) or did not (redundancy, insider dealing) wish to invest in the housing building sector.

Most candidates commented upon the very high level of liquidity (28%).

This was feasible because up to 25 % of the value of the personal pensions (£190,000) could be taken as cash on encashment or with income drawdown; £80,000 was already held in the building society accounts.

The Deposit Protection Scheme guarantees individual bank and building society deposits 100% up to £50,000 (£100,000 for joint accounts).

A higher than normal deposit holding could be justified in terms of employment/income uncertainty, and a counterbalance to the high equity element.

The deposits could be used to supplement income in the short term as well as feed into regular savings investment trusts. The purchase of the investment trusts combines the advantages of pound cost averaging with buying at a discount. But few candidates commented that the funds with the highest discounts tend to be high risk specialist in sectors or strategies out of favour.

Many candidates overstated the income requirement from the portfolio because they ignored Moira's indexed pension. The minimum required yield was 2.4% (i.e. £20,000/£840, 000; the wife's £16,000 pension provided the balance).

This was below the grossed-up yield of the FTSE 100 index and money market rates, and on a par with the S&P 500 index.

In order to continue to manage the portfolio and obtain an income it would be necessary to utilise Income Drawdown ('unsecured pension').

It is available from the age of 50 (55 from 2010), and can be use in entirety or for only part of the personal pensions.

Any cash (up to 25%) must be taken at the outset.

The income taken could be used to match David and Sarah's requirements. The income taken in any year can range from zero to 120% of the equivalent single life annuity (GAD calculation uses the 15 year gilt yield as benchmark, reviewed every five years).

A 35% tax charge will apply to any lump sum death benefits payable under an income drawdown plan.

On the death of the member the remaining vested pension fund can be returned to the individual's beneficiaries and remain in pension drawdown, free from Inheritance Tax and the additional 35% tax charge.

Charges are higher for income drawdown than for a conventional annuity due the regular reviews.

By age 75 David must have bought an annuity, else the fund would be moved into an Alternatively Secured Pension (ASP).

In the meantime, drawdown has the advantage of flexibility, given David's uncertain employment prospects.

(b) The features of index-linked gilts and NSCs were reasonably well understood.

A high weighting to gilts might be attractive to David approaching retirement.

Redemption dates range from 2009 to 2055; and can be matched to the time horizon.

Unlike equities, index-linked gilts provide a guaranteed protection against inflation for both interest and capital repayment.

This may be attractive with 'stagflation' when corporate profits are under pressure.

For the purpose of indexation, inflation is measured by the RPI rather than the CPI ; RPI has generally been higher in recent years because it includes housing costs, but this may reverse.

The 14 index-linked gilts are divided into two categories - six with a 3 month indexation lag and eight with a 8month lag.

The indexation lag reduces the real return when inflation is rising, and increases the real return when inflation is falling; the impact is greatest with shorter dated 8 month lag stocks (e.g. 2.5% 2009).

Index-linked gilts are free of default risk but subject to market risk.

Longer dated stocks have high duration; (double that of conventional gilts, but real yields do not vary as much as conventional yields).

They were selling on low real yields; longer dated less than 1%, reflecting large price increases in recent years.

Good answers made reference to the break-even inflation rates for non-taxpayers; over 3% for medium and longer dated stocks.

Few candidates noted that the initial income yields for the shorter-dated stocks were similar to the income requirement, but longer dated ones less so.

Index-linked National Savings Certificates are free of both default and market risk They are tax-free and free of commission.

They are limited to £15,000 per person per issue for both the 18th Issue 3 years and 45th Issue 5 years. David and Moira could purchase £60,000 of these issues.

Both issues paid 1% real return on maturity, but did not meet income requirements and reduced return if encashed early.

Candidates frequently commented upon falling inflation rates, or even prices falling. Few commented on the longer term possibility of retail prices rising because of increased government expenditure world wide.

- (c) Many candidates were familiar with problems in taking an annuity. At 52 David would be very young to purchase an annuity ('secured pension') and would only receive a low rate because of a long life expectancy if in good health. If in ill health, an impaired life annuity would produce an enhanced rate.

He could take up to 25% as tax-free cash.

He should take an open market option to secure the best rate.

A joint life annuity can provide for a surviving spouse's income; typically 50% or 100% of the joint rate.

At 52, a joint level annuity produce only around 6% (this would increase to around 8% at age 70 at present rates).

But inflation at 5% means that purchasing power halves in 14 years

However, a joint life index-linked annuity at 52 would have barely matched the 2.4% required return.

Annuity rates have shown a downward trend in recent years because of falling gilt yields, increased longevity and loss of mortality profits as impaired lives receive enhanced benefits. 2008 was particularly bad for annuities because of falling asset values in funds. Ironically, because of the flight to safety, gilts were a rare asset class to increase in value. The 'double whammy' was a reduced fund and a reduced yield, resulting from lower gilt yields.

Once purchased, the capital would be lost and nothing left to be inherited. David would no longer have any need to make investment decisions for the fund. But he might be reluctant to crystallise the losses in the

commodity funds and accept annuity rates based on gilt yields at the lowest levels for 50 years.
Under the Policyholder Protection Act 1975 (amended 1997) the annuity is protected to 90%.

Importantly, as good answers noted, circumstances might change such that he might not need the immediate income, but once the annuity was taken it could not be reversed.

CONCLUSIONS & GENERAL OBSERVATIONS

1. Scripts were generally well presented, with most candidates using double-spacing, numbering, underlining, and sensible use of paragraphs, and occasional highlighting. The best scripts demonstrate a succinctness and clarity in summarizing the essentials of the answer, usually without the need of additional pages. However, there was a small minority of scripts which had appalling handwriting; at worst when it was small and cramped.
2. In Section A, candidates demonstrated a good breadth of knowledge. As usual, candidates tended to score better with the more descriptive questions.
3. Candidates demonstrated a good understanding of the material contained in tax tables and in the Gilts Daily Price List. The tax tables were necessary to answer Q3. The Gilts Daily Price List was often utilised in Q14(b).
4. Many candidates display evidence of essay plans and `mind maps` in Section B. Candidates are expected to be able to marshal information in a sophisticated manner to support or refute any particular assertion in an essay question.
5. The case study was generally reasonably well answered. A frequent failing in previous exams was writing in an unstructured manner, not attributing answers to the correct parts of the question; and giving inadequate justifications for recommendations. The former was apparent in this case. Most candidates made reasonable use of the range of information provided.

These same points are repeatedly made in the Chief Examiner's Reports and are the major reasons why candidates succeed or fail. Moreover, the indicative answers sometimes contain material relevant to future questions.