Case 2: Ms. Urvashi (Reference Date: 1st April, 2014)

Ms. Urvashi, aged 34 years, is employed in a senior position in a Mumbai-based firm. She has a son Suryansh aged 14 years and a daughter Dhruvi aged 9 years. She is the sole guardian of her children pursuant to her recent divorce. She is currently residing in a rented house. Suryansh has just passed 8th standard while Dhruvi is studying in 3rd standard. She has approached you, a CFP[CM] practitioner, for preparing a Financial Plan for her family. She has plans to retire early from service at her age of 55 years. She shares the following financial information with you:

Salary Income:		Annual (Rs. lakh)
Basic Salary	:	25.00
HRA	:	5.00
Other allowances and reimbursements	:	3.00

Regular Outgoings:		Monthly (Rs.)
Basic Household Expenses	:	40,000
Services availed	:	18,000
School Fees	:	25,000
House Rent	:	35,000
Power, Telecom & Fuel	:	12,000
Car Loan EMI	:	18,275

Outgoings towards investment and insurance:		(Rs.)
Equity Mutual Fund[1]	:	25,000 (Systematic Investment Plan - SIP)
Debt Mutual Fund[2]	:	15,000 (Systematic Investment Plan - SIP)
Insurance Premium[3]	:	38,759
Health Insurance Premium[4]	:	27,631
Car Insurance Premium	:	8,637

Assets: (Valued on 31st March, 2014)		(Rs. lakh)
Equity Mutual Fund schemes	:	12.45
Debt Mutual Fund schemes	:	5.79
Equity Shares in Demat Account	:	23.92
Equity Linked Saving Scheme[5]	:	3.85
Public Provident Fund (PPF) A/c[6]	:	6.59
Gold & Diamond Jewellery	:	5.75
Car[7]	:	4.50
Bank Account (Salary)	:	3.82
Fixed Deposits[8]	:	6.00
Deposit with House Owner	:	3.00

[1] Diversified open-ended growth equity schemes, dividend payout option; started 3 years ago with initial investment of Rs. 1 lakh; monthly SIP

[2] Long-term long duration debt schemes with growth option, started 2 years ago, initial investment of Rs. 1 lakh; monthly SIP

[3] Total Cover Rs. 1.5 crore across three policies of Rs. 50 lakh each, all term plans having cover up to Urvashi's age of 50, 53 and 58 year respectively; annual premium

[4] Total cover Rs. 20 lakh on two policies, one is floater Rs. 10 lakh cover, the other in Urvashi's name; annual premium

[5] Invested Rs. 1 lakh in each of the previous three financial years in March every year

[6] Account opened on 21st December 2006

[7] Purchased on 1st March 2011 by availing a loan for Rs. 10 lakh (80% loan to value, 6-year, 9.5% p.a.)

[8] Six Fixed Deposits each of Rs. 1 lakh at 8.75% p.a. interest, maturing on 1st date of months from May to October 2014, all deposits created from 15th November 2013 to 20th December 2013 on weekly intervals

Liabilities: (Outstanding on 31st March, 2014) (Rs. lakh)

Car loan : 5.70

You, in consultation with Urvashi, have crystallized the following financial goals, for which the strategy is to be devised and presented to Urvashi:

1. Purchase a house in the next three years costing currently Rs. 1.25 crore; provide for own funds, transfer and stamp duty expenses to the extent of 30% of market value
2. Create a pool account and manage the same to plan for basic education of both children till their respective 18 years of age; current costs are Rs. 1.5 lakh p.a. till age 14 and Rs. 2 lakh p.a. thereafter till age 18, such expenses escalate at 10% p.a.
3. Create a corpus for higher education of both children at their respective age of 18 years; Rs. 25 lakh is the outlay in current terms for each child, such costs escalate at 8% p.a.
4. Create a combined corpus for the professional courses to be pursued by children with current outlay of Rs. 25 lakh each required at their respective age of 22 years, such costs escalating at 9% p.a., such corpus sustaining till the marriage of both the children tentatively at their respective age of 27 years; marriage costs at Rs. 20 lakh per marriage, escalating at 7% p.a.
5. Retirement Corpus for post-retirement income stream equivalent to 60% current expenses arrived at by omitting rent, EMI and school fees and considering provisions for gifting a lump sum Rs. 1 crore to her children when Urvashi attains 75 years of age; a further provision of donating Rs. 1 crore posthumously to a charitable trust.
6. Create a fund in 10 years for a family world tour at an estimated Rs. 10 lakh at current costs, such costs escalating at 5% p.a.

Life Parameters:

Urvashi's expected life currently estimated : 85 years

Assumptions regarding long-term pre-tax returns on various asset classes:

1) Equity & Equity MF schemes/ Index ETFs : 11.00% p.a.
2) Balanced MF schemes : 9.00% p.a.
3) Bonds/Govt. Securities/ Debt MF schemes : 7.00% p.a.
4) Liquid MF schemes : 5.50% p.a.
5) Gold & Gold ETF : 5.50% p.a.

Assumptions regarding economic factors:

1) Inflation : 5.50% p.a.
2) Expected return in Risk free instruments : 6.50% p.a.
3) Real Estate appreciation : 6.00% p.a.

Cost Inflation Index:

1981-82	100	1986-87	140	1991-92	199	1996-97	305	2001-02	426	2006-07	519	2011-12	785
1982-83	109	1987-88	150	1992-93	223	1997-98	331	2002-03	447	2007-08	551	2012-13	852
1983-84	116	1988-89	161	1993-94	244	1998-99	351	2003-04	463	2008-09	582	2013-14	939
1984-85	125	1989-90	172	1994-95	259	1999-00	389	2004-05	480	2009-10	632	2014-15	1024
1985-86	133	1990-91	182	1995-96	281	2000-01	406	2005-06	497	2010-11	711		

Questions:

1) Urvashi asks you to convince her of your skills and abilities by showing her the actual financial plan made of another client. You advise her that the _____ to be followed by a CFP professional prohibits you to reveal one client's details to others. [2 marks]

A) Code of Ethics of Professionalism
B) Code of Ethics of Fairness
C) Code of Ethics of Confidentiality
D) Code of Ethics of Integrity

2) As per the practice guidelines of FPSB India followed by you, being a CFP practitioner, what step you logically followed after defining and discussing with Urvashi the basic terms of the financial plan construction? [2 marks]

A) To inform Urvashi about the terms of the engagement
B) To collect the quantitative and qualitative information of Urvashi
C) To define the financial goal of Urvashi
D) To apprise Urvashi of your past successful strategies to help her decide the ones for her goals

3) Urvashi wishes to avail housing loan to the extent of 70% of the value of the desired house in the next 3 years. She wants to fully repay the loan by the time she intends to retire. You consider 8.5% p.a. as the average interest rate on the housing loan to be availed. She asks you by how much EMI on the loan would exceed her current monthly outgo towards house rent. [3 marks]

A) Rs. 99,802
B) Rs. 78,182
C) Rs. 53,815
D) Rs. 59,361

4) Looking at Urvashi's various insurance policies and the coverage they provide, what is your advice? [2 marks]

A) Urvashi needs to take cover against disability and critical illness as she is the only earner in the family; other risks are well covered.
B) Urvashi has covered life risk, health and property risk, but she has not taken personal accident cover which is required as she drives her own car.
C) Urvashi has sufficient life cover but it falls drastically after 53 years of age, she needs additional coverage till 60 years of her age.
D) Urvashi needs comprehensive householder policy considering that she is single parent, is employed and is with small children.

5) Urvashi wants to create a Trust that would receive a corpus, in case of any eventuality with Urvashi's life, towards annual living expenses of both children till Dhruvi attains 27 years of age and their housing needs. Urvashi considers such required expenses currently at Rs. 60,000 per month, inflation-adjusted with the corpus invested in risk free instruments. Further, the Trust would purchase a house worth Rs. 70 lakh immediately for the purpose. What additional insurance cover is required to accommodate this objective? [3 marks]

A) Rs. 92 lakh
B) Rs. 40 lakh
C) Rs. 10 lakh
D) Rs. 61 lakh

6) The anticipated increase in the net income contribution to Urvashi's family is expected to increase by 6% p.a. in her service tenure. Such contribution considers income tax payable in the current year of Rs. 7.30 lakh and Urvashi's self consumption of 35% of post-tax income. Considering investment yield of 10% p.a. you calculate the insurance cover to replace Urvashi's net income contribution to the family for the remaining years of her employment. You find there is shortfall in insurance cover of approximately_____. [4 marks]

A) Rs. 90 lakh
B) Rs. 50 lakh
C) Rs. 60 lakh
D) Rs. 1 crore

7) Urvashi's retirement corpus has been estimated by considering only living expenses, viz. basic household, services, power, telecom and fuel expenses till the currently estimated life expectancy at investment rate of 7% p.a. and an average inflation of 5% p.a. On a conservative note, you take the rate of return from investing corpus at 6% p.a. Also, provision is made for 5 more years of expected life. How much curtailment of expenses in the first year of retirement is needed? [3 marks]

A) 23% curtailment
B) 12% curtailment
C) 14% curtailment
D) 10% curtailment

8) You advise Urvashi to accumulate her envisaged retirement corpus through an asset allocation of 70:30 in Equity: Debt by starting separate monthly investments. You expect the current phase of market to yield 13% p.a. in Equity and 10% p.a. in long duration Debt for 4 immediate years. Subsequently, the returns are expected to normalize in accordance with long-term assumptions, and you advise to rebalance the accumulated amount in a revised asset allocation of 40:60 in Equity: Debt for the next 10 years. Thereafter, the amounts in equity and debt components are switched in a designated retirement fund yielding 6.5% p.a. Monthly investment is continued up to retirement, as once rebalanced and in the designated retirement fund. The same fund is used for drawing income lifelong. The quantum of monthly investment comes to _____. [5 marks]

A) Rs. 1,15,000
B) Rs. 65,000
C) Rs. 72,000
D) Rs. 70,000

9) Urvashi has recently heard about Inflation Indexed Bonds (IIB). She is not convinced about the real annual yield of just 1.5% in a recently issued IIB. You explain the features of such Bonds as _____. [2 marks]

A) The principal amount is protected on maturity, and is repaid inflation adjusted. The annual coupons would be 1.5% of such periodically adjusted principal amount in tune with inflation index.
B) The principal amount would be repaid on maturity just like other bond issues. The annual coupons would be paid at annual inflation rate plus 1.5%.
C) The inflation adjusted principal would be repaid on maturity. The annual coupons however would be 1.5% of the face value of the bond.
D) The principal amount would be repaid on maturity just like other bond issues. The annual coupons would be 1.5% above the cumulative percentage rise in inflation index measured annually.

10) For accumulating funds for the goal of world tour, you suggest utilizing maturity proceeds from the series of bank fixed deposits by investing in a balanced scheme a standard Rs. 1.05 lakh up to a period 5 years prior to the usage of the fund. The funds from balanced scheme are switched to a certain asset allocation fund and retained for 5 years until their use. What return needs to be generated from that asset allocation fund to achieve the goal? [4 marks]

A) 12.60% p.a.
B) 12.00% p.a.
C) 12.40% p.a.
D) 11.50% p.a.

11) You suggest Urvashi to build an auxiliary fund to withdraw a lump sum amount for Dhruvi's professional course and the balance on the occasion of Dhruvi's marriage. The lump sum to be withdrawn for professional course is 40% of outlay for such course then. You advise her to invest Rs. 1.5 lakh in her Public Provident Fund (PPF) account at the end of every financial year beginning from March 2015. After initial maturity, the account is extended for a term of 5 years with the same discipline of investment but in the beginning of every financial year. The account, after the lump sum is withdrawn for the professional course, is again extended for a term of 5 years without further contributions. What lump sum is likely to be available for Dhruvi's marriage and what percentage it would constitute of the funds required for marriage? Consider that the interest rate on PPF prevails at 8.7% p.a. throughout. [5 marks]

A) Rs. 38.74 lakh; 57%
B) Rs. 35.46 lakh; 52%
C) Rs. 26.90 lakh; 40%
D) Rs. 29.64 lakh; 44%

12) Urvashi asks you to formulate a tax efficient strategy to manage balances in her equity and debt MF schemes with continuing SIP and her equity shares Demat portfolio to achieve the basic and higher education expenses of Suryansh and Dhruvi. Your strategy is: Basic education expenses for this year

and the next four years are funded by redeeming equity MF units. The remaining years' basic education expenses are funded by redeeming debt MF units. SIP in equity MF schemes is considered up to a year prior to final withdrawal which is for Dhruvi's higher education. SIP in debt MF schemes is considered up to three years prior to such final withdrawal. The equity shares portfolio is redeemed to the extent of requirement of higher education goal of Suryansh, and the remaining redeemed at the time of final withdrawal. You consider all expenses required for a particular year to be withdrawn in the beginning. You analyze this strategy and report that_____. [5 marks]

A) Rs. 2 lakh shortfall expected in meeting Dhruvi's higher education, Strategy workable
B) Rs. 15 lakh shortfall expected in meeting Dhruvi's higher education, Strategy not workable
C) Rs. 10 lakh overall surplus after meeting Dhruvi's higher education
D) Rs. 10 lakh shortfall expected in meeting Dhruvi's higher education, Strategy not workable

13) Urvashi wants to know an appropriate Trust form for her if she wishes to create a Trust for the benefit of her children but if she wants to exercise full control over the Trust property and income. You advise her that the same would be_____. (2)

A) Revocable and Discretionary
B) Irrevocable and Discretionary
C) Revocable and Determinate
D) Irrevocable and Determinate

14) On 31st March, 2015, Urvashi sold gold jewellery worth Rs. 10.12 lakh, which she had acquired for Rs. 2.90 lakh in FY 2006-07, for partially self funding of her house three years down the line. She incurred transfer expenses of Rs. 1,000 on the purchase and of Rs. 2,000 on the sale. She wishes to invest the proceeds in bonds specified under Section 54EC. Calculate the amount that she can invest from the sale proceeds, and by which date. Cost inflation index: 2006-07:519 and 2014-15:1024. (3)

A) Rs. 4.38 lakh, by 29th September, 2015
B) Rs. 4.38 lakh, by 31st March, 2015
C) Rs. Nil, since Section 54EC does not allow for capital gains on sale of gold
D) Rs. 4.38 lakh, by 31st March, 2016

15) Calculate Urvashi's income tax liability for AY 2015-16. She contributes Rs. 1 lakh to her PPF account. Also, the Health Insurance premium is eligible for deduction under the Income Tax Act 1961. She earns interest of Rs. 8,986 on her savings bank account and Rs. 28,960 on the fixed deposits during FY 2014-15. (5)

A) Rs. 7,44,450
B) Rs. 7,49,600
C) Rs. 7,56,430
D) Rs. 7,46,510