Case 2: Ms. Urvashi (Reference Date: 1st April, 2016)

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:

<u>Salary Income (2016-2017)</u>		<u>Annual (Rs. lakh)</u>
Basic Salary	:	25.00
HRA	:	5.00
Other allowances and reimbursements	:	3.00
<u>Regular Outgoings:</u>		<u>Monthly (Rs.)</u>
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
<u>Outgoings towards investment and insurance:</u>		<u>(Rs.)</u>
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
<u>Assets: (Valued on 31st March, 2016)</u>		<u>(Rs. lakh)</u>
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

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[1] Diversified open-ended growth equity schemes; 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 2008

[7] Purchased on 1st March 2013 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 7.75% p.a. interest, maturing on 1st date of months from April to September 2016, all deposits created from 15th September 2015 to 20th October 2015 on weekly intervals

Liabilities: (Outstanding on 31st March, 2016) (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 pre-tax returns on various asset classes (1-3 years):

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 : 6.50% p.a.
6) Real Estate appreciation : 7.00% p.a.
7) Bank/Post Office Term Deposits (> 1 year) : 7.25% p.a.
8) Public Provident Fund/EPFO : 8.00% p.a.

Assumptions regarding economic factors:

1) Inflation : 5.00% p.a.
2) Expected return in Risk free instruments : 6.00% p.a.

Cost Inflation Index:

1981-82	100	1987-88	150	1993-94	244	1999-00	389	2005-06	497	2011-12	785
1982-83	109	1988-89	161	1994-95	259	2000-01	406	2006-07	519	2012-13	852
1983-84	116	1989-90	172	1995-96	281	2001-02	426	2007-08	551	2013-14	939
1984-85	125	1990-91	182	1996-97	305	2002-03	447	2008-09	582	2014-15	1024
1985-86	133	1991-92	199	1997-98	331	2003-04	463	2009-10	632	2015-16	1081
1986-87	140	1992-93	223	1998-99	351	2004-05	480	2010-11	711	2016-17	1125

<u>Questions:</u>

1) Urvashi asks if you can show her the actual financial plan made of another client. Under which of the following Code of Ethics you are prohibited 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) You have just defined and discussed with Urvashi the basic terms of the financial plan construction. As per Financial Planner Practice Standards, what should be your next logical step?

   [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 expertise in certain areas to elicit her goals accordingly

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. 103,653
   B. Rs. 44,228
   C. Rs. 56,353
   D. Rs. 62,057

4) Looking at Urvashi's various insurance policies and the coverage they provide, what is the most appropriate conclusion from the following?

   [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 to take personal accident cover which is required as she drives her own car.
   C. Urvashi's life cover 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 a Rs. 70 lakh house to accommodate both children and their living expenses currently estimated at annual Rs. 7 lakh till Dhruvi attains 27 years of age. The expenses involve education and higher education, hence are required inflation-adjusted at 8.5% escalation when drawn from risk free instruments. Estimate additional insurance cover to achieve thus.

[3 marks]

A. Rs. 36 lakh
B. Rs. 75 lakh
C. Rs. 180 lakh
D. Rs. 5 lakh

6) Urvashi's net contribution to family in the current year is after an estimated tax of Rs. 7.5 lakh in the current year 2015-2016 and self consumption of 25% of such post-tax income. This contribution is expected to increase at 5% p.a. in her service tenure. You estimate Urvashi's income replacement considering investment yield of 8.5% p.a. What additional life cover would be needed?

[4 marks]

A. Rs. 1.16 crore
B. Rs. 52 lakh
C. Rs. 1.90 crore
D. Rs. 1.45 crore

7) Urvashi's retirement corpus is arrived at by considering current household expenses, services availed, power, telecom and fuel at her life expectancy. The investment yield at 7% p.a. and average inflation at 5% p.a. is considered. On a conservative note, at investment yield of 6% p.a. and 5 more years of expected life, what curtailment of expenses in the first year of retirement would be needed?

[3 marks]

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

8) Urvashi's retirement corpus as envisaged needs to be accumulated by considering only the Demat account holding along with a separate asset allocation fund. She invests 70:30 in Equity:Debt for 5 years. Subsequently, the accumulated amount in asset allocation fund and further monthly investments are rebalanced 40:60 in Equity:Debt for the next 11 years. At this stage, the accumulations in equity, debt and Demat account are redeemed and transferred to a designated retirement fund yielding 6.5% p.a. which is used for drawing retirement expenses. Cumulative monthly investments maintained up to this period are doubled in the last 5 years up to retirement. What quantum of monthly investment is required?

[5 marks]

A. Rs. 29,000
B. Rs. 63,200
C. Rs. 30,500
D. Rs. 32,100

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 investing Rs. 1.05 lakh from the maturity proceeds of each of the bank fixed deposit on the respective maturity dates in an asset allocation fund. The accumulated amount from this fund is switched to Risk free instruments three years prior to the actual usage for the purpose. What return needs to be generated from the asset allocation fund to achieve the goal?

[4 marks]

A. 12.08% p.a.
B. 7.03% p.a.
C. 15.00% p.a.
D. 14.19% p.a.

11) Urvashi utilizes fund in her PPF account for creating a combined corpus to meet the professional course expenses of Dhruvi and later to meet her marriage expenses. She would invest Rs. 1.5 lakh in the beginning of every financial year, starting immediately, in the PPF account and extend the account for a term of 5 years with the same discipline of investment. A lump sum equivalent to 50% of the professional course charges then is withdrawn from the PPF account after which it is extended for one more term of 5 years without further contributions. What percentage of sum required for Dhruvi's marriage would be available on the final maturity of the account?

[5 marks]

A. 57%
B. 31%
C. 45%
D. 71%

12) In order to balance growth, volatility and taxes of cash flows, equity and debt MF schemes are managed to achieve basic and higher education expenses. Expenses for the current year will be met by redeeming suitably from equity schemes. For the expenses needed in the block period of next 3 years, necessary amount to the extent of shortfall in debt schemes today would be switched immediately in one lump sum from equity schemes. The SIP in equity and debt schemes would continue for 8 years and 6 years respectively. Consider expenses required to be withdrawn in the beginning of the year. You find the shortfall in equity schemes to achieve Suryansh's higher education, in debt schemes to meet Dhruvi's remaining basic education expenses, and the increment in equity SIP then to achieve Dhruvi's higher education expenses.

[5 marks]

A. Rs. 13.5 lakh shortfall in Suryansh's higher education; Rs. 3 lakh shortfall in debt schemes; Rs. 50,250 increase in equity SIP
B. Rs. 14.7 lakh shortfall in Suryansh's higher education; Excess Rs. 2.6 lakh shortfall in debt schemes; Rs. 32,000 increase in equity SIP
C. Rs. 8.2 lakh shortfall in Suryansh's higher education; Rs. 1.5 lakh shortfall in debt schemes; Rs. 25,000 increase in equity SIP
D. No shortfall in Suryansh's higher education; Rs. 1 lakh shortfall in debt schemes; Rs. 75,000 increase in equity SIP

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 marks]

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

14) On 1st April, 2016, Urvashi sold gold jewellery worth Rs. 10.12 lakh, which she had acquired for Rs. 2.90 lakh in FY 2007-08, for partially self funding of her house three years down the line. She incurred transfer expenses 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.

[3 marks]

A. Rs. 4.18 lakh, by 31st March, 2017
B. Rs. Nil, since Section 54EC does not allow for capital gains on sale of gold
C. Rs. 4.18 lakh, by 30th September 2016
D. Rs. 7.20 lakh, by 30th September, 2016

15) Calculate Urvashi's income tax liability for AY 2017-18. She contributes Rs. 1 lakh to her PPF account. Also, the Health Insurance premium is eligible for deduction under the Income Tax Act 1961. In addition to this, she also contributes Rs. 80,000 towards NPS. Her employer contributes 12% of salary towards NPS. She earns interest of Rs. 8,986 on her savings bank account and Rs. 28,960 on the fixed deposits during FY 2016-17.

[5 marks]

A. Rs. 7,41,790
B. Rs. 7,49,600
C. Rs. 7,56,430
D. Rs. 7,46,510