

## CFP CERTIFICATION EXAMINATION (ADVANCED LEVEL PAPER 2)

### Case Study - Case Facts

#### David Jones

1. Today is 1 June 2010. Lily Fong, a financial planner of Happy Insurance Company, received a call from her current client, David Jones, to review his financial plan.
2. Below is some information about David that Lily has gathered so far:
3. Client information:

	Client	Client's Spouse
Name	David Jones	Nancy Jones
Date of birth	1 June 1958	2 March 1962
Nationality	Canadian	Canadian
Marital status	Married	Married
Occupation	Chief Financial Officer	Housewife
Employer	Tasty Foods Limited*	N/A
Work status	Full-Time	N/A
Time with present employer	Since 1 April 1999	N/A
Regular medical check-up?	Yes	Yes
Any long-term disability or health problems?	High blood pressure	No

\* Company listed on the Toronto Stock Exchange

## 4. Dependant information:

	Dependant 1	Dependant 2
Name	Sunny Jones	Sandy Jones
Relationship with client	Son	Daughter
Date of birth	15 May 2000	5 April 2002
Health	Good	Good

## 5. Annual income of the Jones family for the period from 1 April 2009 to 31 March 2010:

	Amount (in HKD unless otherwise specified)
<b>Salary income received*</b>	1,680,000
<b>Bonus income received</b>	280,000
<b>Reimbursement received from employer</b>	
Rent payment (Sai Kung flat) <sup>€</sup>	480,000
Annual airfare to Canada	50,000
<b>Other benefits received from employer</b>	
Scholarships for David's children	10,000
Tuition fees for David's children paid by employer directly to the school	216,000
<b>Income received from other sources</b>	
Interest and dividends	60,000
Rental income from Ma Wan flat <sup>#</sup>	Unknown

\* before deducting the premium for the group medical insurance policy for Nancy & David's children and the MPF contributions

€ rateable value of the property: HKD450,000

# rateable value of the property: HKD250,000

6. Annual expenses of the Jones family for the period from 1 April 2009 to 31 March 2010:

	Amount (in HKD unless otherwise specified)
<b>Expenditure on food</b>	240,000
<b>Housing expenses (for Sai Kung flat)</b>	
Rent	480,000
Utilities and others	80,000
Management fees	48,000
<b>Household expenses</b>	
Filipino domestic helper	54,000
Others (e.g. clothing, personal grooming, toiletries)	700,000
<b>Transportation expenses</b>	
Fuel, maintenance & repairs, parking, vehicle licence	80,000
Others (including taxis & public transport)	50,000
<b>Education and recreation expenses</b>	
Other school expenses	50,000
Vacation	100,000
Other recreation	100,000
<b>Medical expenses</b>	
Pharmacy/drugs	10,000
<b>Insurance</b>	
Life insurance premium for David	18,000
Life insurance premium for Nancy	15,000
Group medical insurance premium for Nancy, Sunny and Sandy	5,000
Building insurance premium (Ma Wan flat)	4,000
Household contents insurance premium (Sai Kung flat)	6,000
<b>Others</b>	
Contributions to Mandatory Provident Fund Scheme	12,000
Mortgage payment for Ma Wan flat	Unknown
Management fee for Ma Wan flat	12,000
Government rent for Ma Wan flat	4,800
Rates for Ma Wan flat	8,000
Support to George (David's nephew)	60,000
Donations to the Community Chest of Hong Kong	20,000

7. Assets and liabilities of the Jones family (as at 31 March 2010):

	Amount (in HKD unless otherwise specified)
Property in Ma Wan	3,200,000
Mortgage loan	Unknown
Motor car	400,000
Stocks	500,000
Unit trusts and bonds	300,000
Savings in HKD	500,000
Savings in CAD	CAD50,000
Mandatory Provident Fund Scheme account balance	180,000
Canadian superannuation account	CAD300,000
Cash value of life insurance policies	800,000
Hi-Fi system	200,000
Credit card balance	20,000

8. Both David Jones and his wife Nancy are great fans of Chinese culture. They considered Hong Kong the perfect place for them to stay. To this end, David applied to his employer to be relocated to the Hong Kong office of Tasty Foods Limited (Tasty) from the Toronto headquarters several years ago. Although he is employed on contract basis, David managed to negotiate a very generous expatriate package. As time goes by, the Jones will soon obtain the right of abode in Hong Kong.
9. The Jones live in a house in Sai Kung arranged by Tasty. Under the arrangement, David pays rent every month in advance and receives reimbursement from Tasty the month after. Sunny and Sandy attend an international school in Clearwater Bay. The annual tuition fee is HKD108,000 for each of them which are directly paid for by Tasty to their school as part of David's expatriate package. Tasty also pays a scholarship of HKD5,000 each per annum in respect of Sunny and Sandy under the company's standing policy for senior staff. Recently, the school they are attending announced that a debenture of HKD150,000 should be purchased for every student starting from the academic year 2010/11. The debenture is redeemable when a student leaves the school. Tasty agreed to buy and hold the debentures on David's behalf.
10. David is very fond of his 20-year-old nephew, George, and has been supporting him financially since he was born. David knows that George is grateful for his money because he has just entered university and needs the money to support his living and pay his tuition fees.
11. David is covered by a group medical policy and a group term life insurance policy offered by Tasty. The medical policy has an in-patient policy with hospital cash of a maximum coverage of HKD300,000 per annum, together with dental insurance. Tasty allows David to enroll his direct relatives for the same medical policy at cost, and David has exercised his right and enrolled Nancy and their children to the policy at an annual premium of HKD5,000 which is deducted from his salary income. The life policy covers 2 years of David's salary with a permanent total disablement rider.

12. On top of David's group term life policy, both David and Nancy have taken out other life insurance policies. The table below summarizes details of the life insurance policies of David and Nancy:

Insured	David	David	Nancy
Policy type	Whole life	Group term life	Term life
Sum insured	HKD3,000,000	2 x annual salary	HKD2,000,000
Year of Purchase	1990	--	1993
Policy provider	Happy Ins. Co.	ABC Ins. Co.	Happy Ins. Co.
Riders	<ul style="list-style-type: none"> <li>• Personal Accident</li> <li>• Double Indemnity</li> </ul>	<ul style="list-style-type: none"> <li>• Permanent total disablement</li> </ul>	<ul style="list-style-type: none"> <li>• Personal Accident</li> <li>• Double Indemnity</li> </ul>
Primary beneficiary	Nancy	Nancy	David
Contingent beneficiary	George	Sunny	Sunny
Cash values	HKD800,000	--	---

As a reward to loyal customers, Happy Insurance Company has recently offered two extra riders free-of-charge to David, who aims to maximize the long-term benefits he can get from them.

13. David is still uncomfortable with his current insurance coverage, and would like to make sure that Nancy and their children will be provided with the largest amount of income as soon as possible if he predeceases them, or if his children are suddenly orphaned. Because one of his friends has bought an annuity for this purpose and recommends it to him, David asks Lily for a proposal for a pure life annuity.
14. Other employee benefits provided by Tasty include annual return airfare to Canada, and a Canadian superannuation account into which Tasty contributes 9% of David's salary every month. The account balance can be withdrawn upon David's retirement. Though not required by law, both Tasty and David also contribute to the Mandatory Provident Fund Scheme in Hong Kong.
15. On 1 June 2004, Nancy bought a small residential flat in Ma Wan at HKD2,500,000 as part of her investment. The purchase of the flat was fully financed by a mortgage with Coco Bank for a term of 15 years at a fixed rate of 6% p.a. The first mortgage payment was made on 30 June 2004. The current market value of the flat is HKD3,200,000 and it is expected to grow at an annual rate of 4% in the future. The flat has been let out for rental income since it was bought. Nancy is responsible for the management fee, government rent and rates. After deducting these expenses, the remaining rental income is exactly enough to pay for the monthly mortgage. Nancy expects that the rental income will remain stable for the duration of the mortgage term. Nancy has taken out a building insurance policy on the flat since purchasing it. She is not sure if she should adjust the sum insured since it has been over 5 years when she bought the flat.

16. David would like to restructure his investment portfolio by including one of the following funds into it:

	Fund			
	SUN	MOON	STAR	EARTH
Average annual return during the last five years	9.5%	12%	13%	13.5%
Standard deviations of return during the last five years	6%	8%	8.5%	9.5%

- Fund SUN: An equity income mutual fund investing in Hong Kong stocks.
  - Fund MOON: A growth-oriented mutual fund investing in Hong Kong stocks.
  - Fund STAR: An international equity mutual fund.
  - Fund EARTH: Taiwan equity index exchange-traded fund.
- The short-term certificate of deposit rate in Hong Kong is 4%. The correlation coefficients of the above four funds during the last five years are:

	SUN	MOON	STAR	EARTH
SUN	1.0			
MOON	0.7	1.0		
STAR	0.5	0.4	1.0	
EARTH	0.7	0.7	0.2	1.0

17. As David is approaching his intended retirement date, which falls on his 60<sup>th</sup> birthday, the family has been thinking about returning to Canada. Sunny and Sandy will definitely go back to Canada for their university education, where they will work part-time and pay for their own tuition fees like their father did. The family has therefore made up its mind to return to Canada after David retires, by which time they will sell the flat in Ma Wan and use the proceeds to buy a house in Canada. David has been researching the prices of property in Canada, and found that a property that fits the needs of the family is selling at a price equivalent to HKD3,000,000 Hong Kong dollars today, and is expected to grow at an annual rate of 6%.
18. David and Nancy have both made wills two years ago while they were on their annual trip to Canada. Nancy has kept the only copy of her will with a relative in Toronto while David has kept his with a friend who Nancy does not know. In David's will, he has made bequests in favour of Nancy and his children only.
19. Other information:

Exchange rate: CAD1.00 = HKD7.80  
CAD stands for Canadian dollars.

**- End of Case Facts -**

**Question 52**

Which of the following are David's personal and financial goals?

- I. Ensure a stable stream of income for his family after his retirement and after his death.
  - II. Arrange for long-term health care protection for both himself and Nancy.
  - III. Provide for housing arrangements in retirement.
  - IV. Set up a fund for the university education of Sunny and Sandy.
- 
- A. I & IV only
  - B. II & III only
  - C. I, II & III only
  - D. I, II, III & IV

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Answer: C

**Question 53**

What is the amount of rental income from the Ma Wan flat for the year ended 31 March 2010?

- A. HKD253,152
- B. HKD257,460
- C. HKD277,952
- D. HKD325,460

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Answer: C



**Question 54**

Which of the following statement(s) about the Jones couple's current financial status and investment position is/are CORRECT?

- I. Based on the information provided, their solvency ratio is greater than 0.6.
  - II. The length of their pre-retirement investment horizon is of an intermediate term.
  - III. They have a high net worth hence they have a high risk tolerance level.
  - IV. They should allocate part of their savings to high leverage investments.
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- A. II only
  - B. I & II only
  - C. I, II & IV only
  - D. I, III & IV only

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Answer: B

**Question 55**

What is the appropriate advice for Nancy regarding the insurance policy she took out on her flat in Ma Wan?

- A. Nancy should adjust the sum insured with reference to the change in repair/rebuilding cost of the flat, if any.
- B. Nancy should adjust the sum insured with reference to the value of the household contents in the flat.
- C. Nancy should increase the sum insured to reflect the increase in the property price.
- D. There is no need for Nancy to review the sum insured since the premium is calculated with reference to the gross floor area of the flat.

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Answer: A

**Question 56**

Assume that relevant factors remain constant. Which of the following items should Lily Fong include in a Needs Approach analysis in order to ascertain whether David currently has adequate life insurance cover?

- I. Education fees for Sunny and Sandy.
  - II. Financial support to Nancy.
  - III. Mortgage repayments for the Ma Wan flat.
  - IV. Support to George.
  - V. Term life insurance cover of Nancy.
- 
- A. II & V only
  - B. I, II & IV only
  - C. I, III & V only
  - D. I, II, III, IV & V

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Answer: B

**Question 57**

To address David's aim, which TWO of the following riders offered free-of-charge by Happy Insurance Company should Lily advise him to choose?

- I. Critical/terminal illness benefit rider.
  - II. Disability income benefit rider.
  - III. Medical benefits rider.
  - IV. Waiver of premium rider.
- 
- A. I & III only
  - B. I & IV only
  - C. II & IV only
  - D. III & IV only

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Answer: A

**Question 58**

With respect to David's request for a proposal for an annuity, which of the following is/are AP-PROPRIATE piece(s) of advice that Lily should give him (see paragraph 13 of this case)?

- I. For the purposes of attaining David's goal, a Joint-and-Last Survivor Annuity is more suitable than his original choice.
  - II. David can achieve his aim to a certain extent by utilizing a suitable settlement method for his whole life policy.
  - III. David's original choice of an annuity will help him cope with the impact of inflation.
- A. I only
  - B. I & II only
  - C. II & III only
  - D. I, II & III

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Answer: B

**Question 59**

What is/are the advantage(s) of choosing Fund EARTH compared with the other three potential funds that David is considering?

- III. Easier to trade.
  - IV. International diversification.
  - V. Lower bid-ask spread.
- 
- A. I only
  - B. I & II only
  - C. II & III only
  - D. I, II & III

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Answer: A

**Question 60**

David would like to know the performance of the four funds according to the Sharpe's performance index. Which ONE has the WORST performance?

- A. Fund SUN.
- B. Fund MOON.
- C. Fund STAR.
- D. Fund EARTH.

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Answer: A

**Question 61**

Assume that David would like to restructure his portfolio so that half of his portfolio's value will be invested in Fund MOON, and the other half in Fund STAR. What would be the expected standard deviation for his portfolio after the proposed change?

- A. 0.5%
- B. 5.8%
- C. 6.5%
- D. 6.9%

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Answer: D



**Question 62**

Assume that David begins to withdraw from his superannuation account when he retires, and transfers the money to one of his following existing investments. Ignoring tax issues, which ONE of them is the MOST SUITABLE choice for him?

- A. Canadian dollar time deposit account which generates an annual return of 5%.
- B. Canadian stock market portfolio which generates an average annual return of 12%.
- C. Emerging markets long-term bond fund which generates an average annual return of 8%.
- D. Money market mutual fund which invests in Euro money market securities and generates an average annual return of 6%.

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Answer: A

**Question 63**

Which ONE of the following statements about David's tax position as a Canadian expatriate is CORRECT?

- A. David is liable to pay Salaries Tax in Hong Kong because he has made Hong Kong his home and ordinarily resides in Hong Kong.
- B. David is liable to pay Salaries Tax in Hong Kong because under the double tax treaty signed between China and Canada, anyone who spends more than 180 days in Hong Kong in a year is liable.
- C. David is liable to pay Salaries Tax in Hong Kong but income generated from any services rendered outside Hong Kong can be excluded.
- D. David is liable to pay Salaries Tax in Hong Kong but is entitled to claim exemption from Salaries Tax on the ground that all his salary income has been taxed in Canada.

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Answer: C

**Question 64**

In relation to the education benefits from Tasty to David as regards Sunny and Sandy, which ONE of the following is a CORRECT Hong Kong tax implication with respect to David?

- A. Debentures to be provided by Tasty will be taxable because they are deemed to be income from employment.
- B. Scholarships for Sunny and Sandy are not taxable because they are not income received by David.
- C. Tuition fees paid by Tasty are not taxable if Tasty enters into contract with the school and pays directly.
- D. Tuition fees paid by Tasty are taxable because this is a fringe benefit provided by the employer.

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Answer: D

**Question 65**

Which of the following ways can help the Jones to minimize their Property Tax payable in Hong Kong?

- I. Ask the tenant to pay the management fees directly to the property management company and reduce the monthly rent by the corresponding amount.
  - II. Ask the tenant to shoulder the rates and reduce the monthly rent by the corresponding amount.
  - III. End the existing tenancy agreement and enter into a new contract with rent payable annually in advance in lump sum.
  - IV. Have Nancy elect to be assessed under Personal Assessment.
- A. I only
  - B. I & III only
  - C. I, II & IV only
  - D. II, III & IV only

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Answer: A

**Question 66**

What is the net assessable value of the Ma Wan flat under the Hong Kong Property Tax for the year of assessment 2009/10?

- A. HKD169,952
- B. HKD215,962
- C. HKD253,152
- D. HKD269,952

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Answer: B

**Question 67**

For the purpose of calculating David's Salaries Tax for the year of assessment 2009/10, what is the amount of rental value to be considered as part of his assessable income?

- A. HKD201,000
- B. HKD223,600
- C. HKD240,000
- D. HKD480,000

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Answer: B

**Question 68**

Why is Tasty NOT obliged to enroll David to the Mandatory Provident Fund (MPF) Scheme in Hong Kong?

- A. David's employment is on contract basis, therefore he is not considered a permanent employee and is exempted.
- B. David has no right of abode in Hong Kong and is exempted as an expatriate.
- C. Tasty has enrolled David in a Canadian superannuation scheme and is exempted.
- D. Tasty is a Canadian company and is exempted as an overseas company.

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Answer: C

**Question 69**

What piece(s) of advice should Lily give David with respect to estate planning for himself and his wife?

- I. To arrange for ancillary probate of the Ma Wan flat with the probate court in Canada.
  - II. To ensure that their respective wills comply with the Wills Ordinance in order for them to be enforceable in Hong Kong.
  - III. To make copies of their respective wills so that they have copies in Hong Kong and Canada.
- A. II only
  - B. I & III only
  - C. II & III only
  - D. I, II & III

\*\*\*\*\*

Answer: C



**Question 70**

Assume that relevant factors remain constant. Which of the following actions should David take to help fulfill his wish in paragraph 13 of this case?

- I. Appointing more than one executor for his will.
  - II. Changing the contingent beneficiary in his whole life policy.
  - III. Having joint bank and investment accounts with Nancy.
  - IV. Setting up an enduring power of attorney for himself.
- 
- A. II & III only
  - B. II & IV only
  - C. I, II & III only
  - D. I, III & IV only

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Answer: A

**Question 71**

If David passes away in Hong Kong tomorrow and because no one can find his will, he is deemed to be intestate, which of the following statements about the succession of his estate are CORRECT?

- I. George is entitled to apply to the court for reasonable financial provisions from David's estate.
  - II. Nancy, Sunny and Sandy will be entitled to share David's personal chattels.
  - III. Nancy will first be entitled to a net sum of HKD500,000 from David's residuary estate with interest, as well as a half of the remainder of his residuary estate.
  - IV. Sunny and Sandy will be entitled to share the remainder of David's residuary estate, but their share will be held on statutory trusts.
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- A. I & II only
  - B. I & III only
  - C. I, III & IV only
  - D. II, III & IV only

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Answer: C

**- End of Sample CFP Certification Examination Questions (Advanced Level Paper 2) -**

**- End of Sample CFP Certification Examination Questions -**