CA FINAL N'19

SUBJECT- FINANCIAL SERVICES N CAPITAL MARKETS

Test Code – FNJ 7295

(Date :)

(Marks - 100)

The Question paper comprises three case study questions.

The candidates are required to answer any two case study questions out of three.

CASE STUDY - 1

P Limited on 19th January 2018 intimated to consider at Board Meeting a proposal of Buy Back Offer. As approved at its Board Meeting on 24th January, 2018 it made a Cash Offer for Buy-back of 2,50,000 (Two Lac Fifty Thousand) fully paid-up Equity Shares of the Company of face value Rs. 10/- (Rupees Ten Only) each ("Equity Share(s)") from all the fully paid-up Equity Shareholders / beneficial owners of the Equity Shares of the Company as on the record date i.e. Friday, 23rd March, 2018, on a proportionate basis, through the Tender Offer Route using stock exchange mechanism, at a price as per the audited standalone financial statements of the Company for the nine months period ended 31st December, 2017.

As required under the Buy-back Regulations, Equity Shares to be bought back are divided into two categories: (i) Reserved Category for Small Shareholders; and (ii) General Category for all other shareholders.

The members of the Company approved the Buy-back Offer by way of a special resolution through the postal ballot, the results of which was declared on Monday, 12th March, 2018. Further, the members of the Company have authorized the Board, inter alia, to finalize the final terms of buy-back offer, fix Record Date, determine entitlement ratio and such other matters as may be necessary in connection with the buy-back of Equity Shares with a power to delegate all or any of these powers to any committee of the Board or to any other director(s) or executive(s) or officer(s) of the Company.

The Buy-back shall be undertaken on a proportionate basis from the Eligible Shareholders as on the Record Date through the Tender Offer route prescribed under Regulation 4(1)(a) of the Buy-back Regulations. Additionally, the Buy-back shall be, subject to applicable laws, facilitated by tendering of Equity Shares by such Eligible Shareholders and settlement of the same, through the Stock Exchange Mechanism.

As on the date of Public Announcement i.e. 13th March, 2018 the Promoters and Members of Promoter Group of the Company were holding 42,76,958 Equity Shares of the Company of the existing paid up equity share capital of the Company which is as follows:

Sr. No.	Category/ Name of Shareholder	No. of Equity Shares Held
1	CRA	1,54,518
2	CRA HUF*	32,846
3	UCA	53,994
4	N Private Limited	21,29,220

5	A Limited	12,21,230
6	S Limited	4,74,738
7	MCA	78,546
8	PCA	59,198
9	SCA	53,998
10	Ujwal Vidyalaya	10,894
11	Arogya Society	6,730
12	Vidhrati Trust	246
13	Ladu Family Trust	400
14	Virasat Family Trust	400
Total		**42,76,958**

* Held by CRA in capacity of Karta.

Salient ***financial parameters*** of the audited standalone financial statements for the nine months period ended 31st December 2017 are as under:

Parameters	Pre Buy-back
Net Worth (Rs. in Lac)	36,814.44
Return on Net Worth (%)	14.87%
Earnings Per Share (EPS) (in Rs.)	85.38
Book Value per share (in Rs.)	573.94
Price / Earnings (PE) Multiple	20.52

BRIEF INFORMATION ABOUT THE COMPANY

1. Corporate and Business:

The Company was incorporated on 6th May, 1972 in the name and style of “D Limited” under the Companies Act, 1956 as a public limited company. The Company changed its name to P Limited pursuant to and as part of the scheme of amalgamation of erstwhile P Lim ited with the Company approved by Hon’ble High Court of Gujarat vide its order dated 7th July, 2005 and obtained fresh certificate of incorporation dated 19th September, 2005. The registered office of the Company is situated at M G Road, Panjim – 403001, Goa, India.

The Company is engaged in the business of manufacturing and trading of phosgene and non- phosgene based specialty chemicals and intermediates. These chemicals are used in diverse fields such as agrochemicals, pharmaceuticals, dyes, etc. The Company’s manufacturing facility is located at Kundaim Industrial Estate in the State of Goa, India.

2. Stock Market Data and Information:

2.1 The Equity Shares of the Company are listed on BSE.

2.2 The high, low, average market prices and total volume of Equity Shares traded in the last three Financial years (April to March) and the monthly high, low, average market prices and total volume of Equity Shares traded for the six completed calendar months preceding the date of publication of Public Announcement and the corresponding volumes on BSE are as follows:

Period	High Price (Rs.)	Low Price (Rs.)	Average Price (Rs.)	Total Volume Traded in the period (No. of shares)
PRECEDING 3 FINANCIAL YEARS				
FY 2016-17	1,569.5	1,010	1,226.04	5,24,090
FY 2015-16	2,300	714	1,524.28	9,17,486
FY 2014-15	1,020	250	527.86	14,81,362
PRECEDING 6 MONTHS				
February-18	3,100	2,544.1	2,855.58	72,036
January-18	3,084	2,384	2,609.42	92,692
December-17	2,588	2,010	2,211.6	71,224
November-17	2,136	1,520	1,828.32	2,15,618
October-17	1,553.2	1,303	1,391.94	1,08,666
September-17	1,576	1,322.2	1,442.64	57,134

2.3 The closing market price of the Equity Shares on BSE as on Friday, 19th January, 2018, was Rs. 2,640.40.

2.4 The closing price on BSE on 23rd March 2018 was Rs. 2,740.60.

2.5 The Volume Weighted Average Price of the Equity Shares on Friday, 5th January, 2018 was Rs. 2,514.05.

2.6 The Volume Weighted Average Price of the Equity Shares on Wednesday, 19th October, 2017 was Rs. 1,899.50.

3. Financial Growth:

As per audited standalone financial statements for the financial years ended 31st March, 2017, 2016 and 2015, the Company recorded total income of Rs. 30,967.12 Lac, Rs. 32,241.52 Lac and Rs. 28,666.28 Lac respectively and profit after tax of Rs. 4,376.92 Lac, Rs. 4,967.24 Lac and Rs. 5,197.72 Lac respectively. Further, as per audited standalone financial statements for the nine months period ended 31st December, 2017; the Company recorded total income of Rs. 27,923.48

Lac and profit after tax of Rs. 5,476.04 Lac.

4. Financial Information about the Company

The salient financial information of the Company as extracted from the latest audited standalone financial statements for the nine months period ended 31st December, 2017 and audited standalone financial statements for the preceding three financial years ended 31st March, 2017, 31st March, 2016 and 31st March, 2015 are as under:

(Rs. in Lac)

Particulars	Nine months period ended	Year ended		
	31st December, 2017	31st March, 2017	31st March, 2016	31st March, 2015
Total Income	27,923.48	30,967.12	32,241.52	28,666.28
Total Expenses (Excluding Finance Costs and Depreciation)	19,334.84	24,011.48	24,452.72	20,601.32
Finance Cost	20.80	23.64	24.12	15.64
Depreciation	1,008.04	1,284.96	1,120.80	854.44
Profit / (Loss) before tax	7,559.80	5,647.04	6,643.88	7,194.88
Provision for tax (including Deferred Tax)	2,083.76	1,270.12	1,676.60	1,997.16
Profit / (Loss) after tax	5,476.04	4,376.92	4,967.28	5,197.72
Other Comprehensive Income	(10.56)	(429.96)	-	-
Total Comprehensive Income	5,465.48	3,946.96	-	-
Equity Share Capital	1,282.84	1,282.84	1,282.84	1,282.84
Reserves & Surplus*	35,531.60	30,528.20	26,179.08	21,675.04
Net worth*	36,814.44	31,811.04	27,461.92	22,957.88
Total debt (excluding working capital loans)	-	-	-	-

PROCESS AND METHODOLOGY FOR THE BUY-BACK

5. Fractional Entitlements

If the Buy-back Entitlement under the Buy-back, after applying the above mentioned ratios to the Equity Shares held on Record Date, is not a round number (i.e. not in the multiple of 1 Equity Share), then the fractional entitlement shall be ignored for computation of Buy-back Entitlement to tender Equity Shares in the Buy-back for both categories of Eligible Shareholders.

On account of ignoring the fractional entitlement, those Small Shareholders who hold 11 or less Equity Shares as on Record Date will be dispatched a Tender Form with zero entitlement. Such Small Shareholders are entitled to tender Additional Equity Shares as part of the Buy-back and will be given preference in the acceptance of one Equity Share, if such Small Shareholders have tendered for Additional Equity Shares.

5.1 Adjustment of fractional results for Small Shareholders

(a) For any Small Shareholder, if the number of Additional Equity Shares to be accepted, calculated on a proportionate basis is not in the multiple of 1 (one) and the fractional Acceptance is greater than or equal to 0.50, then the fraction would be rounded off to the next higher integer.

(b) For any Small Shareholder, if the number of Additional Equity Shares to be accepted, calculated on a proportionate basis is not in the multiple of 1 (one) and the fractional Acceptance is less than 0.50, then the fraction shall be ignored.

5.2 Adjustment of fractional results for other Eligible Shareholders

(a) For any Eligible Shareholder, if the number of Additional Equity Shares to be accepted, calculated on a proportionate basis is not in the multiple of 1 (one) and the fractional Acceptance is greater than or equal to 0.50, then the fraction would be rounded off to the next higher integer.

(b) For any Eligible Shareholder, if the number of Additional Equity Shares to be accepted, calculated on a proportionate basis is not in the multiple of 1 (one) and the fractional Acceptance is less than 0.50, then the fraction shall be ignored.

6. Basis of Acceptance of Equity Shares validly tendered

Subject to the provisions contained in this Letter of Offer, the Company will accept the Equity Shares tendered in the Buy-back by the Small Shareholders in the Reserved Category in the following order of priority:

(i) Acceptance of 100% Equity Shares from Shareholders, who have validly tendered their Equity Shares to the extent of their Buy-back Entitlement or the number of Equity Shares tendered by them, whichever is less.

(ii) In case there are any Equity Shares left to be bought back in any Category, the Additional Equity Shares tendered by the Small Shareholders over and above their Buy-back Entitlement, shall be accepted in proportion of the Additional Equity Shares tendered by them and the Acceptances shall be made in accordance with the Buy-back Regulations, i.e. valid acceptances per Small Shareholder shall be equal to the Additional Equity Shares validly tendered by the Small Shareholder divided by the total Additional Equity Shares validly tendered and multiplied by the total pending number of Equity Shares to be accepted in the same Category.

Adjustment for fractional results in case of proportionate Acceptance, as described in paragraph above.

7. Basis of Acceptance of Equity Shares validly tendered

Last date of receipt of completed Tender Forms and other specified documents including physical share certificates by the Registrar to Buy-back is 16th May 2018 and last date of completion of Buy

Back process including dispatch of share certificate(s) by Registrar to Buy-back / return of unaccepted demat shares by Stock Exchange to Shareholder Broker is 23rd May 2018.

In light of above information, answer the following:

1.1 Please fill up the Schedule of activities in following format:

S. No.	Activity	Date
1.	Date of the Board meeting held to approve the proposal for Buy-back of Equity Shares	
2.	Date of declaration of the result of the postal ballot through which the Shareholders approval for the Buy-back was sought	
3.	Last date upto which publication of Public Announcement for the Buy- back is allowed	
4.	Last date of extinguishment of Equity Shares Certificates bought back	

Note: Please don't reproduce the above table just mention the dates against each Serial No. **(2 Marks)**

1.2 Determine the Buy-back price (rounded-off to 100) and Buy Back size if Board decides the following criteria:

(i) A premium of 78.96% over the Volume Weighted Average Price of the Equity Shares on BSE for 3 months preceding the date of intimation to consider the proposal of the Buy-back Offer in the board meeting;

(ii) A premium of 35.24% over the Volume Weighted Average Price of the Equity Shares on BSE for 2 weeks preceding the date of intimation to consider the proposal of the Buy-back Offer in the board meeting; and

(iii) A premium of 28.77% over the closing market price of the Equity Shares on BSE as on the date of intimation to consider the proposal of Buy-back Offer in the Board Meeting.

(iv) 5.92 times of the book value per Equity Share of the Company.

(2 Marks)

1.3 To meet the Escrow Account requirement the Board has decided to transfer lien on Units of ITU Mutual Fund (owned by the Company) in favour of Merchant Banker before or on opening of Offer of Buy-back. The Merchant Banker will keep a margin of 10.76%. Company is holding Units of ITU Direct Plan – Growth Unit the details of which are given below.

Based on the following information, determine the NAV of a regular income scheme on per unit basis. Also calculate the No. of Units to be pledged:

Particulars	Rs. Crores
Listed shares at Cost (ex-dividend)	40
Cash in hand	2.46
Bonds and debentures at cost	8.60
Of these, bonds not listed and quoted	2
Other fixed interest securities at cost	9.00
Dividend accrued	1.60
Amount payable on shares	12.64
Expenditure accrued	1.50
Number of units (Rs. 10 face value)	40 lacs
Current realizable value of fixed income securities of face value of Rs. 100	106.50
The listed shares were purchased when Index was	2,000.00
Present index is	3,881.30
Value of listed bonds and debentures at NAV date	16

There has been a diminution of 20% in unlisted bonds and debentures. Other fixed interest securities are at cost. **(8 + 2 = 10 Marks)**

1.1 Determine the number of shares required to be eligible for Small Shareholder category (rounded off to lower whole number). **(2 Marks)**

1.2 Determine the minimum number of shares required to be reserved for Buyback from Small Shareholders category. Further also suggest the ratio (upto 5 decimal points) of the Buy Back for the Equity Shares held by eligible Shareholders for both categories i.e. Small and other than Small.

(3 Marks)

1.3 What measures Company can take to ensure that the same shareholders with multiple Demat accounts/ folio do not receive a higher entitlement under the Reserved category. **(2 Marks)**

1.4 Can the Company issue any further Equity Shares till the closure of the Buy-back Offer. **(1 Mark)**

1.5 Promoters of the company have expressed their intention to tender up their holdings in the Buy- back offer. Can they do so? **(1 Mark)**

1.6 Assuming that response to Buy-back is 100% (full acceptance) from other Eligible category shareholders in proportion to their respective entitlement fill up the blank figures in the following table.

Parameters	Pre Buyback	Post Buyback
Net Worth (Rs. Lac)	36,814.44	
Return on Net Worth (%)	14.87	
EPS (Rs.)	85.38	
Book Value Per Share (Rs.)		
PE Multiple	20.52*	

* Based on Price of Rs. 1,752 per Equity Share.

(3 Marks)

1.7 Assuming except Ladu Family Trust and Virasat Family Trust all other promoters and others have choosen 100% and some holders also applied in excess of their entitlement to participate in Buy- back Offer, fill up the following Capital Structure and Shareholding pattern:

Category of Shareholder	**Pre Buy-back**		**Post Buy-back**	
	Number of Shares	**% to existing Equity Share capital**	**Number of Shares**	**% to post Buy-back Equity Share capital**
Promoters and Members of Promoter Group	42,76,958	66.68		
Foreign Investors (including Non- Resident Indians, FIIs and Foreign Mutual Funds)	21,354	0.33		
Financial Institutions / Banks & Mutual Funds promoted by Banks / Institutions	1,81,262	2.83		
Others (Public, Public Bodies Corporate, etc.)	19,34,654 *	30.16		
Total	64,14,228	100.00		

* Of this holding there are 16,496 shareholders holding shares not more than 72 shares with aggregate shareholding of 4,41,820 shares. **(2 Marks)**

1.4 The following data pertains to some companies which carried out Buy Back of Shares during last year.

Companies	Buyback Price	Current Price
SC Ltd.	Rs. 1,956	Rs. 76
IRE Ltd.	Rs. 480	Rs. 138
BE Ltd.	Rs. 366	Rs. 160
UL Ltd	Rs. 860	Rs. 394
LEHB Ltd.	Rs. 172	Rs. 118

Briefly express your opinion whether the Buyback is useful for investors or not.

(2 Marks)

Choose the correct answers to the following questions:

(2 Marks x 10 = 20 Marks)

1.5 A company may buy-back its shares from

(a) The existing shareholders on a proportionate basis through the tender offer

(b) The open market

(c) Odd-lot holders

(d) Any one of the above

1.6 No offer of buy-back for____or more of the paid up capital and free reserves of the company shall be made from the open market.

(a) Fifteen per cent

(b) Twenty per cent

(c) Ten per cent

(d) None of the above

1.7 The company shall by way of security for performance of its obligations under the SEBI Regulations for buyback, offer deposit in an escrow account which consists of –

(a) cash deposited with any bank

(b) bank guarantee in favour of the merchant banker

(c) deposit of acceptable shares only with appropriate margin, with the merchant banker

(d) all of the above

1.8 The company shall immediately after the date of closure of the buyback offer open a____with a banker to an issue.

(a) Savings Account

(b) Special Account

(c) Escrow Account

(d) Current Account

1.9 The company shall extinguish and physically destroy the security certificates so bought back in the presence of ……….

(a) Merchant Banker

(b) Registrar to issue

(c) Merchant Banker and the Statutory Auditor

(d) Registrar to issue or the Merchant Banker and the Statutory Auditor

1.10 The offer for buy back shall open to the security holders for a period …………

(a) not less than seven days and not exceeding fourteen days

(b) of fifteen days

(c) of thirty days

(d) Not less than fifteen days and not exceeding thirty days

1.11 An issue shall be opened after at least …….. working days from the date of registering the red herring prospectus with the Registrar of Companies.

(a) seven

(b) three

(c) four

(d) five

1.12 The requirement of giving security deposit before the opening of the subscription list shall be exempt if

(a) the equity shares of the issuer have been listed on any recognized stock exchange having nationwide trading terminals for a period of at least five years immediately preceding the reference date

(b) the average market capitalization of public shareholding of the issuer is at least one thousand crore rupees in case of public issue and two hundred and fifty crore rupees in case of rights issue

(c) the issuer has redressed at least ninety per cent of the complaints received from the investors till the end of the quarter immediately preceding the month of the reference date

(d) none of the above

1.13 The listed entity shall use the electronic mode of payment facility approved by the Reserve Bank of India for the payment of …….

(a) dividends

(b) interest

(c) redemption or repayment amounts

(d) all of the above

1.14 The listed entity shall file with the recognized stock exchange(s) on a quarterly basis, within …….. from the end of each quarter, a statement giving the number of investor complaints pending at the beginning of the quarter, those received during the quarter, disposed of during the quarter and those remaining unresolved at the end of the quarter.

(a) seven days

(b) fifteen days

(c) twenty one days

(d) thirty days

CASE STUDY - 2

PART-I

Reachout Ltd. is a company incorporated in India which is in the business of human health care products, testing labs, medical equipment manufacture and hospitals. It is looking at its expansion plan in India for achieving strategic growth. The following entities have been identified after intensive market survey and the top management of Reachout Ltd. has certain queries relating to the laws applicable to different forms of investments and has appointed you as its advisor.

Entities:

(1) Recover easy Ltd. is a publicly held insurance company with two subsidiaries-Recover health Ltd. which offers health insurance products and Recover motor Ltd. which offers vehicle insurance products.

(2) Minimedicals Ltd., is an unlisted company with just 22 members which is successful in making medical kits for self-testing to detect common ailments of diabetes, blood pressure and cardiac malfunction. These kits are being used in India and the cardiac kit is a new product which is expected to have a huge market even outside India. The share capital is Rs. 5 crores, with reserves of 3 crores and Minimedicals Ltd. has not borrowed funds in the past and has managed to be profitable for the past five years out of the seven years of its existence. Profits have been steadily increasing.

(3) Testearly Co. is a partnership entity which has two main divisions: the Test Centre Division, which has branches at all strategic locations and a Mobile Testing Division which has ambulances and collects samples/readings of patients in their residences and then provides test results. Testearly Co. operates only in the metros of India.

(4) There is a group of four engineers who are designing algorithms for mobile applications and television interface. They have already been successful in another breakthrough software application and are now ready for a strategic project for Reachout Ltd. Reachout Ltd. wants these engineers to develop an application interface that will trigger a warning on the mobile of registered and connected users, at their option, on the adverse medical parameters found through Testearly Co. and Minimedical equipments to the immediate relatives or caretakers of potential patients. This will help even remotely located relatives to take care of the patients and provide help immediately.

The strategic plan of Reachout Ltd. is to have a sizeable market share of the Indian healthcare sector. Apart from metros, it intends to set up franchise units at smart cities and then take their services to villages and other rural areas. When the cardiac kit achieves considerable volume, there will be a mobile mini hospital which will rush to patients identified with cardiac parameters requiring immediate attention.

Some more detailed information is presented below:

(i) The shares of Reach out Ltd. are listed on the BSE and NSE.

(ii) The shares of Recover easy Ltd. are traded on the BSE and NSE and command an average market price of Rs. 450 per share of face value Rs. 10 per share.

Recover easy holds 60% shares in Recover health Ltd. which has a share capital of Rs. 8 crores. Reach out Ltd. wants to have 15% interest in Recover health Ltd. and is not looking at the motor insurance business. Recover health has 20 shareholder members with Recover easy Ltd. owning 60% and the balance by nineteen other individual shareholders.

Recoverhealth has been in business for the past two years and has done well. Recovermotor Ltd. has been in business as such for the past ten years.

(iii) Minimedicals Ltd. has no intention of quitting its business. However, the current set up does not permit largescale fund raising and therefore, the founder members are trying to identify an investor who will scale up the operations while retaining the founder members with importance. Reachout Ltd. is interested in joining hands with Minimedicals Ltd. While Reachout Ltd., is willing to fund 25% of the requirements for operations by itself, it requires that these shares are listed on the stock exchange. The proposed funds to be raised by equity capital is Rs. 100 crores.

(iv) Regarding Testearly, Reachout Ltd. is not interested in partnership firm as an entity. However, it would like to take the team of Testearly and make it Testearly Ltd., a Public Limited company. The first phase of expansion would be to go in for an equity capital of Rs. 10 crores.

(v) Reachout Ltd. views the application interface to be developed by the engineers as a strategic success point and hence wants to invest in the software development to kickstart and maintain its Testearly Ltd.'s business.

(vi) The medium term plan of Reachout Ltd. is to nourish the insurance business and to further the mobile mini hospitals to be set up in two years' time. Its long term plan is to be a successful, profi table, integrated service provider in health care as a major player.

In the context of the above information, answer the following questions:

3.1 In order to expand its business in accordance with the long term plan of Reachout Ltd., Recoverhealth is planning a public issue. Reachout Ltd. is willing to act as promoter to the issue. Assume that only equity shares are being considered and at present, Reachout Ltd. has no holding in Recoverhealth. State the relevant regulation number, and explain the provisions applicable under the appropriate regulation relating to the merchant banker, deposit with SEBI, prospectus, mode of public offer, role of Reachout Ltd. and its minimum investment, assuming that Rs.150 crores is proposed to be raised in the new issue. Assume no party is debarred. **(10 Marks)**

3.2 Explain the steps involved and the regulations applicable in formulating a plan for the alliance and growth of Minimedicals Ltd. into a listed company. Can Minimedicals Ltd. go ahead without offering the shares to public? The companies - Minimedicals and Reachout Ltd. prefer not to offer to the public, but they want it to be listed on the stock exchange. Is their requirement possible? What are the limitations and how do you overcome them? State and explain the regulation applicable and the steps involved in the process of working out a suitable plan.

(12 Marks)

3.3 What will be the ideal mode of achieving the immediate alliance between Reachout Ltd. and Testearly Co.? **(4 Marks)**

3.4 What may be the appropriate strategies by which Reachout Ltd. could invest in the application interface to be designed by the engineers? **(4 Marks)**

PART - II

Choose the correct answer from the following. Each question carries two marks.

3.5 The following is not an intermediary of a capital market:

(2 x 10 = 20)

(a) Merchant Banker

(b) Investment Banker

(c) Register to an issue

(d) Promoter

3.6 The following is not true in the context of trade in a stock market:

(a) The prices are rising in the market and there are many persons who want to buy securities rather than sell, the market is termed bullish.

(b) The prices are rising in the market and there are more persons wishing to sell the securities than those wanting to buy, the market is termed bullish.

(c) The prices are falling and there are more number of sellers than buyers, then the market is bullish.

(d) The prices are falling and there are more number of buyers than sellers, then the market is bullish.

3.7 Refunding is the following:

(a) When the bond issuer does not have money to give back on redemption, it issues new bonds and uses the proceeds for redemption of old bonds.

(b) When the book built issue of share capital is oversubscribed, the application money is given back to the applicants who have not been allotted shares.

(c) When a debt instrument matures, the principal is paid back along with the last interest.

(d) The amount given back to a holder of convertible security on conversion of the convertible debt into equity.

3.8 In the case of a bond transaction, the market convention of trade is the following: (For example if the face value of the bond is Rs. 100, the current price is 105, the interest due is 3, a transaction relating to 100000 bonds will be termed the following:

(a) 103 lac bond transaction

(b) 105 lac bond transaction

(c) 108 lac bond transaction

(d) 100 lac bond transaction

3.9 For the above details relating to a single bond, the following is true:

(a) Rs. 103 is the clean price

(b) Rs. 105 is the clean price

(c) Rs. 105 is the dirty price

(d) Rs. 103 is the dirty price

3.10 A listed company is in the process of a rights issue of two shares for every five held. The equity shares are being actively traded in the stock exchanges. This rights issue is said to be in the

(a) Primary market

(b) Secondary market

(c) Neither (a) nor (b)

(d) Both (a) and (b)

3.11 Default risk is not the following:

(a) Credit risk

(b) Risk of a borrower not paying back the principal due on time.

(c) Risk of a borrower not paying back the interest due, but who has paid back the principal falling due on time.

(d) Risk of fall in the value of collateral security

3.12 The yield to maturity of a bond is

(a) Less than the coupon rate if the redemption value is more than the purchase price

(b) More than the coupon rate if the redemption value is more than the purchase price.

(c) Equal to the coupon rate, whatever be the redemption value

(d) Independent of coupon rate and depends on the difference between the purchase price and the redemption value.

3.13 The following is true in the context of trade in the stock market.

(a) If the price of a share is higher in one stock exchange than another, a speculator can buy the stock at a lower price and sell the same stock at the higher price and have an assured gain.

(b) The price will be the same in all the stock exchanges.

(c) The buy and sell as in (a) above is possible only to the extent of the stock he already holds in both the exchanges.

(d) One has access only to end of day prices and by the time he takes action the next day, the prices will not hold.

3.14 The following is true in the case of an initial public offer:

(a) The company can resort to over allotment of shares to investors participating in the issue and have the merchant banker to buy them back from the open market after listing.

(b) The promoters to the issue must have brought at least one week before the issue date, the minimum amount to be held by promoters to be held until allotment in an escrow account.

(c) The issue price or the price band must be known at least one week before the issue.

(d) If SEBI does not approve an IPO within ten days of application, it is deemed to have approved the offer and the regulations apply accordingly.

CASE STUDY – 3

HRS Ltd. is an asset financing company with a proven track record and has been in the business of mainly providing finance to purchase trucks, tractors, farm equipment and commercial vehicles. In the past, it was financing used and new vehicles, but over the recent years, it prefers to concentrate on new vehicles only. Trucks form the major part of the financing business. There is a lot of competition in this field, but due to the increasing norms on pollution control and the decrease in the value of second hand vehicles, the company wants to strategically confine itself only to new vehicles in the coming years. HRS Limited mainly uses debt finance for its operations. The debt-equity ratio is in the range of 5:1 on an average. This is in line with the industry.

The company feels that in addition to truck financing, it can expand its business to finance smaller vehicles such as passenger cars and tempo travellers. The current expansion plan is described in the succeeding paragraphs:

There has been a recent entrant in the country wide market by a mobile application provider who has not only ushered in a revolution in the way cars are being hired by common man, but also in the manner of documentation of bookings, charges, cancellations and in the ownership of vehicles for such hire. This operator has also lured many entrepreneurs to successfully earn money either as drivers or as owners of self-driven cars and be engaged by users of the mobile app. This app has found immense success in the car segment and is also being considered for trucks for transport as well as connections from goods trains to factories so that companies can track the distribution of material and finished goods on an optimal cost.

While discussing with this app provider, HRS Ltd. has discovered a huge potential to finance vehicles to be demanded by virtue of the app users who may be new entrepreneurs, small transport companies, etc. Since the individual entrepreneurs may turn out to be risky and counterproductive for HRS for repossession in the event of failure to repay, the app provider, who has a wide data base and the recovery mechanism for fares realized, has agreed to be the co-borrower for the vehicles. Under such an arrangement, the vehicles financed will be hypothecated to HRS by the entrepreneur who is the principal borrower, fully guaranteed by the app provider. The app provider will also ensure that the used vehicle is also be handed over to another entrepreneur attached to him. Thus, only the repossessed vehicles will form the used vehicle financing segment. Agreements are proposed to be drafted with conditions for repossession within one month of default and redeployment of such vehicles for earning money, by continuing to be hired. GPS system to be installed in the trucks will provide information to the delivery destination and the origin of loading so that better inventory management and production processes are ensured. Thus the whole new business is expected to have a huge success story, going by the success rate in the passenger car booking segment.

In case the app provider or the app itself fails due to technical faults or user-unfriendly situation or in the event of fierce competition that this app provider may face, the large number of vehicles financed would have to be managed by another app provider or alternatives set up in-house. These could take some time.

In the near future, HRS Ltd. would like to cater to vehicle financing as in the earlier line of business, but mainly to the customers targeted through the app provider, who would be entrepreneurs in the categories of first time vehicle owners, repeat vehicle owners, small transport operators, etc. Thus, HRS is not deviating essentially from its vehicle financing activity.

HRS Ltd. has also accepted deposits from the public in the past through its country wide branches.

The financial information relating to HRS Ltd. is given in Tables 1 and 2. HRS Ltd. was promoted by HS Holdings Ltd. which has subscribed to 63% of the equity capital of HRS Ltd. There have been no negative pointers under any law on the company or its directors or management.

The company is professionally managed and has had qualified persons of repute heading the respective operations and the middle lever managers are also carefully chosen to be able to manage the country wide operations and to take decisions quickly and efficiently. The managers who have retired have done so only due to age reasons and there have been no adverse publicity in any media about any internal mismanagement or controversy.

The company proposes to issue Rs. 500 crores worth debentures comprising 50,00,000 debentures of Rs. 1,000 each face value, for a period of five years, the full value being payable on application. Most of this issue is to be used for redeeming an earlier issue which is due to mature during the next twelve months.

The company intends to patronize active trading and hence prefers to have tradability of even one debenture. There will be no option for the company to redeem earlier than the committed period nor does it allow the holder to claim redemption earlier than stipulated. Land and buildings worth Rs. 950 crores are the intended security for this offer. The debentures are proposed to be issued and redeemed at par. The rate of interest is fixed at 9.5% p.a. throughout the tenor and interest will be paid on the 30th day of June and December every year.

The company has fulfilled all the conditions under the various regulations and plans for the issue to open on 15th January, 2019 and remain open for only the minimum period required under law.

Choose the correct answers to the following questions: (**2 Marks x 10 = 20 Marks)**

(1.1) This company is:

(A) required to disclose the debt service coverage ratio to SEBI every half year.

(B) required to disclose the debt service coverage ratio to SEBI every quarter.

(C) not required to disclose to SEBI the debt service coverage ratio except at the time of issuing the prospectus.

(D) not required to disclose to SEBI at any time any debt service coverage ratio.

(1.2) The following is true:

(A) The debenture trust deed must be signed with the debenture trustee and submitted
to SEBI before every issue of debentures.

(B) The debenture trust deed can be signed with the debenture trustee after the issue of debentures.

(C) The debenture trust deed has to be signed only for and before the first issue of debentures. For subsequent different debenture issues the deed need not be signed if the trustee is unchanged.

(D) The debenture trust deed has to be signed with the debenture trustee and can be submitted to SEBI after the issue of debentures. There need not be submissions for every tranche.

(1.3) In case this company does not pay the debenture interest or the redemption amount on time, then

(A) The debenture trustee pays it on behalf of the company to the debenture holders and later recovers it from the company.

(B) The debenture trustee does not pay the holders any amount, but the debenture holders have recourse against the company by way of liquidating the assets based on which the debentures are secured.

(C) SEBI will wait for two months to lapse and suspend the trading of the debentures and enforce payment of interest.

(D) It can issue fresh debentures and use the proceeds for paying up the principal and interest overdue.

(1.4) If the redemption of debentures is drawing near and the company wants to use the funds it has set aside for redemption for some other purpose,

(A) It can, before the redemption becomes due, arrange for a fresh issue of debentures of any category and use the proceeds of issue to fund the redemption.

(B) Only the shortfall between the redemption amount and the funds set aside can be raised by a fresh issue of debentures before the due date of redemption.

(C) Only the same type of debentures can be issued afresh for funding the redemption.

(D) It cannot use the fresh issue proceeds to fund the redemption of debentures.

For the purpose of paying interest for the first half year, the date from which the interest i s to be reckoned is:

(A) from the date of allotment

(B) from the date of application

(C) from the date of deemed allotment

(D) from the record date.

(1.6) A company

(A) can list its debentures only if it has listed its equity shares in the exchange.

(B) can list its debentures even without listing its equity shares.

(C) has to list its debentures if it has listed its equity shares.

(D) is itself a listed entity and hence all its securities are tradeable on the exchange.

(1.7) Some debenture-holders of this company have not updated their addresses and their bank account numbers. Hence the interest payments sent to their bank accounts have been returned unpaid. There has not been any response to intimations from the company.

Redemption is due next year. Then, for this year, the company

(A) can use this amount for other purposes such as redemption of other debentures or to provide for the redemption to these debenture-holders themselves.

(B) can write back this amount from interest expenses.

(C) cannot use this amount for any other purpose, but retain it in unpaid interest account until redemption is due.

(D) cannot use it for any other purpose but transfer it to Investor Protection Fund, treating the amount as unclaimed interest.

(1.8) The company had an earlier issue of debentures of Rs. 500 crores which is due for redemption in eleven months from now. Those debentures were secured by fixed assets consisting of land and building then worth Rs. 750 crores. The value of the land and building has now risen substantially to Rs. 950 crores and the company therefore proposes to secure these debentures also with the same assets. The current issue size is Rs. 500 crores.

(A) The same assets cannot be used for securing another issue of debentures unless the earlier issue has been redeemed in full.

(B) The cost of the underlying assets is what has to be considered for security. Hence once offered as security, it cannot be taken again as security.

(C) The company has to provide for the coverage of the shortfall in the security of Rs. 50 crores before it can issue.

(D) The company can go ahead and use the same assets for coverage of the next issue also.

The following is true of the debenture issue given in the case study:

(A) The promoters of the company should subscribe to at least 20 per cent of the face value of the debentures viz. Rs. 100 crores worth debentures and to have a lock in period of 3 years.

(B) The promoters should subscribe to the market value of the debentures to the extent of 20 per cent of the issue value and then retain it for at least 3 years.

(C) The promoters should not subscribe to the debenture issue at all.

(D) The promoters are not required to subscribe any value, but they may do so to the extent they wish to invest or for underwriting purpose and they have no lock in period, their subscription not being compulsory.

(1.10)The company had NSE as the designated stock exchange in the earlier issue of the Rs. 500 crore debentures due for redemption in eleven months from now. BSE listing was also done. Then, the following is true:

(A) NSE has to be the designated stock exchange for this issue also. BSE listing has to be done as earlier.

(B) There can be listing on any other exchange also, but NSE has to be the designated exchange.

(C) Any recognized stock exchange can be designated for this issue. Further listing of this issue in any other exchange is optional.

(D) NSE has to be the designated exchange. Listing on BSE or other stock exchange can be optional.

(1.11) You are an analyst at a credit rating agency and are part of the team involved in the rating process of the company. Prepare a report to your director indicating:

(a) assessment of risks;

(b) rating that you would consider appropriate along with a short note on CAMEL criteria considered. **(5 marks each)**

(1.12) Assuming that you are the company's senior official liaising with the investment banker to get the prospectus successfully through, how would you present the draft prospectus to SEBI for approval in accordance with the regulations prevailing as on date?

(You are required to present only the following portions of the prospectus in your answer):

(a) Introduction of the issue (the portion in capital letters forming the first paragraph relating to the issue)

(b) Credit Rating, assuming independent of your answer to (1.1) that a good rating has been given by CRISIL and India Research and Ratings

(c) Minimum Subscription

(d) General Risks

(e) Issue Details

(f) Listing

(g) Objects of the Issue and Interim use of the funds

(h) Debt Equity Ratio (pre and post issue)

(i) Regulatory authorities for the Company. **(15 marks)**

(1.13) Write a short note on the potential benefits on the proposed new unit of business.

(5 marks)

Table ·1

	Statement of Profit and Loss		**(Figs. in Rs. lacs)**				
	Particulars		**For the year ended March 31,**				
			2018	**2017**	**2016**	**2015**	**2014**
A	Revenue						
(i)	Revenue from Operations		122000	108000	102800	86300	78800
(ii)	Other Income		750	20	30	70	80
	Total Revenue		**122750**	**108020**	**102830**	**86370**	**78880**
B	Expenses						
(i)	Finance Costs		53700	51800	50500	43800	39000
(ii)	Depreciation and amortisation		360	330	360	400	290
(iii)	Provision and Write offs		31200	24400	21000	12900	11400
(iv)	Employee Costs		7150	5500	5800	4300	4000
(v)	Other Expenses		7000	6500	7200	6530	5410
	Total Expenses		**99410**	**88530**	**84860**	**67930**	**60100**
C	Profits before tax (A - B)		23340	19490	17970	18440	18780
D	Tax Expense after adjustment for deferred tax		800	6600	6000	6050	5600
E	Profit after tax from continuing operations (C - D)		22540	12890	11970	12390	13180
F	No. of o/s shares (lakhs)	327					
G	EPS -Basic		68.93	39.42	36.61	37.89	40.31
H	EPS - Diluted		68.93	39.42	36.61	37.89	40.31
	Nominal Value of equity share (Rs./share)		10	10	10	10	10

Table-2

State of Assets and Liabilities		(Figures Rs. Lacs)				
Particulars		For the year ended March 31,				
	Liabilities	2018	2017	2016	2015	2014
A	Shareholders' Funds					
	Share Capital	3270	3270	3270	3270	3270
	Reserves and Surplus	120610	110000	99300	90000	80500
	Total Shareholders' Funds	**123880**	**113270**	**102570**	**93270**	**83770**
B	Non-Current Liabilities					
	Long Term Borrowings	400000	335000	300000	290000	220000
	Other Long Term Liabilities	16000	14000	12000	11000	9000
	Long Term Provisions	55000	38000	25000	16000	12500
	Total non-current liabilities	**471000**	**387000**	**337000**	**317000**	**241500**
C	Current Liabilities					
	Short term borrowings	75000	50000	33000	26000	29000
	Total Outstanding dues of creditors other than micro enterprises	2200	1340	1180	750	850
	Other Current Liabilities	200000	180000	195000	120000	115000
	Short term provisions	4000	3900	5000	4100	2900
	Total Current Liabilities	**281200**	**235240**	**234180**	**150850**	**147750**
D	**Total Equity and Liabilities (A+B+C)**	**876080**	**735510**	**673750**	**561120**	**473020**
	Assets					
E	Fixed assets					
	Property, Plant and Equipment	1100	8200	9900	9850	9890
	Intangible Assets	20	18	14	12	16
	Non-Current investments	15000	14500	12500	11500	7000
	Deferred Tax Assets (Net)	4300	3600	3000	2500	2400
	Long Term Loans and Advances	580000	475000	440000	350000	275000

	Total Non-Current Assets	**600420**	**501318**	**465414**	**373862**	**294306**
F	Current Assets					
	Current Investments	105	520	1040	22130	20350
	Cash and Bank Balances	36500	44400	23600	47500	70800
	Short term loans and advances	238430	188687	183186	117003	86764
	Other Current Assets	625	585	510	625	800
	Total current Assets	**275660**	**234192**	**208336**	**187258**	**178714**
	Total Assets (E+F)	**876080**	**735510**	**673550**	**561120**	**473020**