

CF02

Operations of Financial Institutions

9 MAY 2000

1. Time allowed : Three (3) hours
2. Total number of questions : Five (5) questions
3. Number of questions to be answered : Four (4) questions
Part A : Compulsory questions [40 marks]
Part B : Three (3) questions [20 marks each]
4. Show details of workings, where appropriate. Silent, non-programmable calculators may be used.
5. Begin each answer to a new question on a fresh page.
6. Answer **all** questions in **English**.

PART A

COMPULSORY QUESTION

1. (a) Encik Ibrahim has imported some goods for the fasting month under a Letter of Credit issued by your bank. The goods have arrived and are now at the port. However, the documents to the goods have not arrived and Encik Ibrahim wants to take delivery of the goods so that he can start selling them before the end of the fasting month. He has inquired about obtaining a shipping guarantee to enable him to take delivery of the goods.
- (i) What is a shipping guarantee? [4]
- (ii) What are the main features of a shipping guarantee? [4]
- (b) What are the rights and duties of a customer in a banker-customer relationship? [8]
- (c) Foreign exchange rates are normally quoted in **two** ways. The USD is quoted in the market at 3.7987/97. Based on the quote, what is the
- (i) bid rate? [2]
- (ii) offer rate? [2]
- (iii) spread? [2]
- (d) Gerald, a valued customer of your bank, came to cash a cheque issued by another customer of the bank. There was not enough funds in the customer's account to honour the cheque. The cheque was returned to Gerald with the reason "Refer to drawer". Gerald demanded to know the reason for the return and whether it was because there was insufficient funds in the account.
- Can you disclose the information to Gerald? Give reasons for your answer. [8]
- (e) The Bills of Exchange Act 1949 states that "a bill is not invalid by reason only that it is ante-dated or post-dated, or that it bears date on a Sunday".
- (i) What is meant by "ante-dated" and "post-dated"? Give an example of each. [6]
- (ii) What is a "stale" cheque? [4]
- (Total:40 marks)

PART B

ANSWER THREE (3) QUESTIONS ONLY

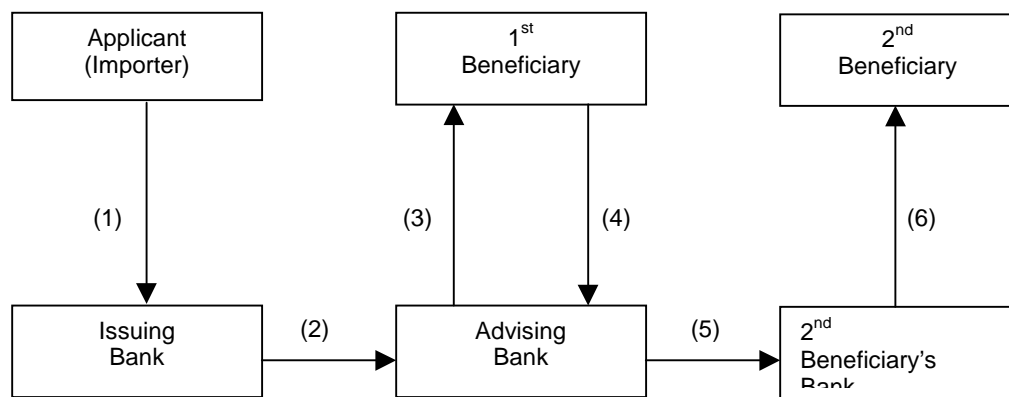
2. The Biro Maklumat Cek (BMC) was set up to monitor and curb the issuance of "bad" cheques. Explain the following, in respect of BMC's definitions and rules regarding "bad" cheques:
- (a) bad cheques [4]
- (b) twelve months roll-over time frame [4]
- (c) prohibition period [4]
- (d) probation period [4]
- (e) "global closure of accounts" concept [4]
- (Total:20 marks)

3. (a) Below are **two** diagrams which depict the flow of a transferable Letter of Credit (LC) and a back-to-back LC. Match the number on the diagrams with the steps listed in the table below. The steps listed may be repeated. As an example, number 1 has been done for you. [13]

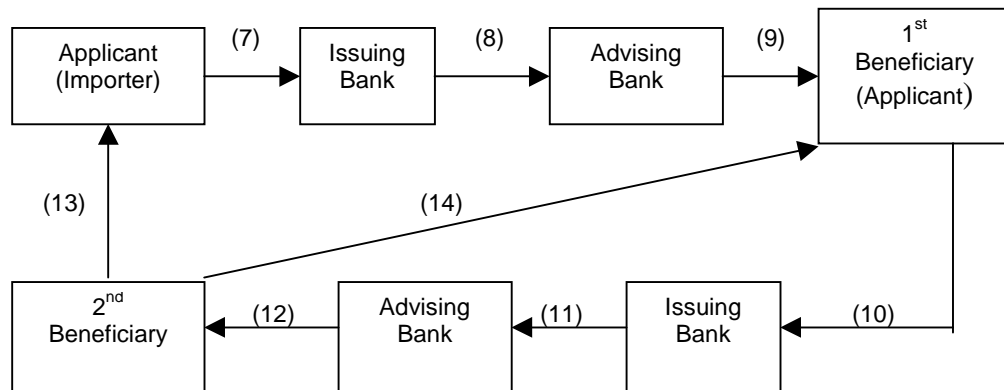
Example: (1) Applies for transferable LC

- | | |
|--|--|
| <ul style="list-style-type: none"> • Applies for transferable LC • Applies for LC • Advises 1st beneficiary • Advises 2nd beneficiary • Revised terms passed on | <ul style="list-style-type: none"> • Issues transferable LC • Issues LC • Instructs changes • Sends goods • Sends documents |
|--|--|

Transferable LC



Back-to-back LC



- (b) What is a red Clause LC? [7]
(Total:20 marks)
4. (a) In a hire-purchase agreement, what are the rights and duties of a hirer? [13½]
- (b) Natasha bought a car on hire-purchase from your company. Based on the following information, what is the monthly rental that she has to pay?

Cost of car	RM60,000
Deposit paid	RM10,000
Interest charged	5.0% per annum
Hiring period	4 years

[6½]
(Total:20 marks)

5. (a) What are the **five** basic types of International Offshore Financial Centres? [6]

(b) One of your bank customers, Multiskills Sdn Bhd has submitted its financial statements to you for your annual credit review exercise.

Based on these financial statements, calculate the following financial ratios:

- (i) Return on assets [2]
- (ii) Gross profit margin [2]
- (iii) Current ratio [2]
- (iv) Quick/acid test ratio [2]
- (v) Debt ratio [2]
- (vi) Times interest covered [2]
- (vii) Total assets turnover [2]

MULTISKILLS SDN BHD

**PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 DECEMBER 1999**

Sales	RM	RM	RM
		380,000	
Opening stock			
Purchases	100,000		
	<u>220,000</u>		
Closing stock	320,000		
	150,000	170,000	
		<u>210,000</u>	
Operating Expenses:			
Rental			
Electricity and water	24,000		
Depreciation	6,000		
Salaries	10,000		
Interest	38,000		
Miscellaneous	28,000		
	9,000	115,000	
	<u> </u>	<u> </u>	
Net profit before tax			<u><u>95,000</u></u>

MULTISKILLS SDN BHD

BALANCE SHEET AS AT 31 DECEMBER 1999

	RM
Current assets:	
Bank	22,000
Rental and utilities deposit	25,000
Stock	150,000
Debtors	170,000
	367,000
Fixed assets:	
Van	55,000
Other fixed assets	75,000
	130,000
TOTAL ASSETS	497,000
Current liabilities:	
Bank loan	60,000
Creditors	70,000
	130,000
Long-term liability:	
Bank loan	160,000
TOTAL LIABILITIES	290,000
Net assets	207,000
Represented by:	
Paid-up capital	100,000
Accumulated profit	10,000
Profit for the year	97,000
	207,000

(Total:20 marks)

- END OF QUESTION PAPER -

OUTLINE ANSWERS

PART A

Question 1

Candidates performed well in the compulsory question which covered various areas, such as rights and duties of a customer, banking secrecy and cheques. About 53% of the candidates managed to pass this question. Those who failed, made mistakes in certain areas, such as shipping guarantees and providing the rights and duties of a banker instead of a customer. Many candidates were confused between “ante-dated” and “post-dated” cheques.

1. (a) (i) A shipping guarantee is an indemnity given by the consignee to a shipping company or its agent, so that the shipping company may release the merchandise to the consignee named in the shipping guarantee without the presentation of relevant bills of lading. The indemnity is countersigned by the bank.
- (ii) The main features of a shipping guarantee are:
 - It does not specify the total liability of the bank – it does not have an amount stated in the guarantee.
 - It does not specify an expiry date.
- (b) Customers’ rights are:
 - Right to repayment
 - Right to draw chequesCustomers’ duties are:
 - To exercise reasonable care in drawing cheques
 - To disclose forgery
- (c) (i) Bid rate - 3.7987
(ii) Offer rate - 3.7997
(iii) Spread - 10 pips
- (d) No. Any information regarding the conduct of a customer’s account is confidential between the customer and his banker. Section 97 of BAFIA 1989 specifically touches on this subject of banking secrecy. The duty of secrecy is not only while the staff is in the employment of the bank but also extends to after he has left the employment of the bank.
- (e) (i) **Ante-dated** means that the cheque bears a date before the date it is issued.
For example, today is May 3, 2000. A cheque issued today but is dated February 10, 2000.

Post-dated means that the cheque bears a future date.
For example, today is May 3, 2000 but the cheque is dated June 3, 2000.
- (ii) Stale cheque is a cheque that is more than six months old. For example, today is May 3, 2000 and the cheque is dated October 10, 1999.

PART B

Question 2

The question on “bad” cheques was attempted by most candidates. Only a quarter of the candidates managed to score above 60% of the allocated marks for this question. Candidates were unable to explain these terms – “12-months roll-over time frame” and “global closure of accounts”.

2. (a) Bad cheques are cheques returned unpaid for the following reasons:
- (i) Insufficient funds
 - (ii) Effects not cleared
 - (iii) Not arranged for
 - (iv) Account closed
- (b) When there are three bad cheques incidences in an account within a twelve-month period, the account has to be closed. The twelve-month period works on a roll over basis. For example,
- | | |
|-----------------|----------------------|
| First incident | - January 3, 1999 |
| Second incident | - September 10, 1999 |
| Third incident | - December 27, 1999 |
- The third incident is within the twelve-month period from the first incident. A bad cheque offence has been committed. However, if the third incident is on January 10, 2000, it is then outside the twelve-month period from the first incident.
- (c) Once an account is blacklisted, the offender will not be allowed to open another account during the prohibition period. The prohibition period commences from the date of the third bad cheque and will end at the end of the month stated in the BMC blacklist. The prohibition periods are:
- | | |
|--------------------------------|-------------|
| First offence | - 6 months |
| Second offence | - 12 months |
| Third offence | - 12 months |
| Fourth and subsequent offences | - 24 months |
- (d) After the prohibition period, the offender is allowed to open an account but he will have to serve a probation period. If he does not commit any bad cheque offence during the probation period, he will be given a clean record. The probation periods are:
- | | |
|--------------------------------|-----------|
| First offence | - 2 years |
| Second offence | - 2 years |
| Third offence | - 3 years |
| Fourth and subsequent offences | - 3 years |
- (e) All offenders will be blacklisted and any account whose name appeared in the blacklist would be closed, even though the account may be properly conducted. All banks in Malaysia are required to close all accounts whose names appear in the blacklist. This is the concept of global closure of accounts. Global closure will affect the offender’s accounts with other banks in the following manner:
- For individual account:
- (i) All accounts in his own name will be closed.
 - (ii) Offender’s account with others will not be closed.
 - (iii) Offender will not be allowed to open an account in his own name or a joint account with others.
- For joint account:
- (i) The account of the individuals will be closed.
 - (ii) The joint accounts maintained by the same individuals will be closed.

Question 3

The question on transferable Letter of Credit (LC), back-to-back LC and red Clause LC was a straightforward question. Yet only 50% of the candidates managed to pass this question.

3. (a) (1) Applies for transferable LC (example)
(2) Issues transferable LC
(3) Advises first beneficiary
(4) Instructs changes
(5) Revised terms passed on
(6) Advises second beneficiary
(7) Applies for LC
(8) Issues LC
(9) Advises first beneficiary
(10) Applies for LC
(11) Issues LC
(12) Advises second beneficiary
(13) Sends goods
(14) Sends documents
- (b) A red Clause LC is one which has a unique clause in it. This clause authorises the advising/negotiating bank to make advances to the beneficiary before the presentation of documents. This is to enable the beneficiary to source for materials to fulfill the order. This clause is inserted at the request of the applicant to the LC.

Question 4

Only a few candidates managed to pass this question on hire purchase agreement. Although some were able to work out the calculation of the monthly instalment, almost all were unable to explain the rights and duties of the hirer.

4. (a) Rights of hirer:
- (i) At any time before the final payment is made, the hirer can request the owner to supply him with a written and signed statement showing amount paid, amount due but unpaid, amount still payable and interest overdue.
 - (ii) When a payment is made, notwithstanding any agreement to the contrary, the hirer can specify to the owner that that payment is to be appropriated to a particular agreement or to any agreement in such amounts as he desires.
 - (iii) If it is specified in the hire-purchase agreement that the removal of goods needs the consent of the owner, and the owner refuses to give such consent, the hirer can apply to the Magistrate's Court for an order approving such removal.
 - (iv) Although the title to the goods rests with the owner, the hirer can assign his "right, title, interest" under the hire-purchase agreement to a third party.
 - (v) Should the hirer die or become a bankrupt, his rights, title and interest is passed on to his personal representative /official assignee.
 - (vi) The hirer has the right to complete the purchase of the goods by giving written notice to the owner and by paying the owner the net balance due under the agreement anytime before the expiry of the notice period of the Fifth Schedule.
 - (vii) The hirer may terminate the hire-purchase agreement at any time by returning the goods to the owner during ordinary business hours at the place where the owner ordinarily carries on business or to the place specified in the agreement.

Duties of hirer:

- Duty to pay rental
- Duty to inform owner

$$\begin{aligned} \text{(b) Monthly rental} &= \frac{50,000 + (50,000 \times 5\% \times 4)}{4 \times 12} \\ &= \text{RM1,250.00} \end{aligned}$$

Question 5

The least popular questions among the candidates were on International Offshore Financial Centres (IOFC) and calculating financial ratios. The first part on IOFC was poorly attempted. However, students managed to better in the second part.

5. (a) Five basic types of International Offshore Financial Centres (IOFC)

- (i) No income tax
- (ii) No income tax on foreign source income
- (iii) Low tax
- (iv) Low tax and special privileges
- (v) Special incentives and privileges

$$\begin{aligned} \text{(b) (i) Return on assets} &= \frac{95,000}{497,000} \times 100 = 19.11\% \\ \text{(ii) Gross profits margin} &= \frac{210,000}{380,000} \times 100 = 55.26\% \\ \text{(iii) Current ratio} &= \frac{367,000}{130,000} = 2.83 \\ \text{(iv) Quick ratio} &= \frac{217,000}{130,000} = 1.67 \\ \text{(v) Debt ratio} &= \frac{290,000}{497,000} \times 100 = 58.35\% \\ \text{(vi) Times interest covered} &= \frac{123,000}{28,000} = 4.39 \\ \text{(vii) Total assets turnover} &= \frac{380,000}{497,000} = 0.76 \end{aligned}$$