CHARTERED INSTITUTE FOR SECURITIES & INVESTMENT

ICAEW

DIPLOMA IN CORPORATE FINANCE SPECIMEN PAPER

CORPORATE FINANCE TECHNIQUES & THEORY MARK SCHEME

The following information is provided solely for the guidance of candidates and should not be read as providing a model answer, or, in some instances, as the only possible response.

SECTION A

Candidates required to answer 5 questions from 7.

Each question is worth 10 marks.

Question 1

a) With some exceptions Aggressor will have to notify Target that it has reached a shareholding in its shares of 3%. Target must notify the market by forwarding the information to a Regulated Information Service provider.

1 mark for each point

b) Aggressor has a 28 day deadline to either make an offer ("Put Up") for Target, or it must state that it has no intention to make an offer ("Shut Up"). This will normally exclude Aggressor from making an offer for six months.

1 mark for each point

c) The Code prohibits any offer-related arrangement between the target and the bidder. This will prohibit deal protection measures such as inducement fees.

1 mark

However the Code provides an exemption when a hostile takeover is announced and the target seeks a "White Knight". In such circumstances the target can agree a break fee with the preferred bidder. The break fee must be no more than 1% of the value of the offer and only payable if the offer becomes or is declared wholly unconditional. *2 marks*

d) Any public statement of intentions relating to a course of action to be taken after the offer period ends must be adhered to during the time period stated. *1 mark*

In the event of no time period being stated this will be twelve months from the date that the offer becomes wholly unconditional. This twelve month period may be revised if there is a material change of circumstances. *2 marks*

Question 2

ai) This would be permitted since warrants are rights over shares yet to be issued and not rights over existing shares. *2 marks*

aii) This transaction would result in a holding of 32.5% but since it is a purchase from a single shareholder it would be permitted under rule 5 provided no firm intention to make an offer had been announced by Zeta. However the transaction would trigger a rule 9 offer. *3 marks*

b) If Zeta intends to announce an offer for Gamma and the offer is to be recommended, acquisitions, which would be prohibited by rule 5.1, are permitted as long as they are conditional upon the announcement of the offer. *3 marks*

It is by virtue of this exception to rule 5.1 that the irrevocable undertakings can be obtained. *2 marks*

Question 3

a) Gross assets = (80 + 12)/(240 + 32) = 34%; Profits = 12/36 = 33%; Consideration = 80/360 = 22%; Gross capital = (80 + 16 - 12)/(360 + 31) = 21%. This is a Class 1 transaction.

3 marks for the ratios. 1 mark for the correct classification

b) Students should summarise the requirements of a Class 1 transaction.

2 marks for requirements. 1 overall understanding

c) A reverse takeover is a transaction where any of the ratios is equal to, or more than, 100%. The Listing Authority will suspend listing of the Offeror's shares until a Class 1 circular or listing particulars, covering the Offeror and the Offeree on an enlarged basis, have been issued. *2 marks*

The reverse takeover requirements do not apply if the Offeree is a listed company.

1 mark

(Note: This is the FSA approach in April 2012 and may well change as a result of proposed changes to the Listing Rules which are due to be released later in 2012.)

Question 4

a) Candidates should conclude that in addition to the additional finance for the new project the company also needs to rearrange its current financing arrangements. *1 mark*

Consideration of the maximum borrowing of a multiple of EBITDA taking into consideration that Totalclean is a service company. *1 mark*

Discussion of debt versus equity. *2 marks*

b) Marks will be awarded for appropriate sources of finance in Totalclean's circumstances. *3 marks each for each source of finance*

Question 5

a) Answers should include a description of share buybacks and special dividends together with their advantages and disadvantages. *3 marks for each*

b) Students should mention for example: Loss of shareholder confidence; the effect on the share price; the company may become a takeover target. *1 mark overall and 1 for each point mentioned*

Question 6

a) Students should identify the transaction risk between the various currencies: UK£ and Esperanza's currency; US$ and Esperanza's currency; UK£ and US$; UK£ and A$. *2 marks*

Instruments that students might mention together with advantages and disadvantages are: forwards; money market hedges; futures; options. *1 mark for each; 2 for advantages and disadvantages, max 5*

b) Students might mention: cheaper borrowing; long term forward contract. *2 marks*

Mention of a possible difficulty with finding a counterparty in Esperanza. *1 mark*

Question 7

a) Students might mention for example: Call options; Exercise prices; premiums; expiry dates; pricing options and warrants. *1 mark for each point, max 4*

b) Students might mention for example: Raising finance without having to issue shares and pay dividends; attaching to a debt issue; capitalising on an overvalued share price. *1 mark each, max 3*

c) The meaning *1 mark*
The significance *1 mark*
Reasonable calculations *1 mark*

SECTION B

Candidates required to answer both questions.

Each question is worth 25 marks.

Question 8

a) Students' analysis should cover: profitability; margins; asset turnover; short and long term liquidity; growth. Students should give a supported conclusion as to the financial health of Carpetright.

10 marks allocated to the analysis and 5 to the supported conclusion

b) Marks will be awarded to realistic refinancing alternatives for Carpetright. Marks will not be awarded where students do not relate their suggestions to the circumstances of the company. *5 marks for each alternative*

Question 9

a) Candidates should:

i) In their DCF valuation include: adjustments for CAPEX; working capital; depreciation: a computation of WACC: assumptions and limitations.

4 marks for adjustments
4 marks for reasonable computations and overall understanding

ii) In their multiples valuation: consideration of the comparability of the comparable companies to McBride. Justification for their choice of multiples.

4 for choice of multiple. 2 for reasonable computations

If a candidate arrives at a valuation that is clearly out of line they should comment on this.

b) Any sensible suggestions will be given marks however students must relate their answers to the current share price of McBride and their range of values.

1 mark for mention of the range
1 mark for bid premium
1 mark for sensible suggestion

c) Students should make comment on the alternatives from considering both the offeror and offeree shareholders. *4 for loan stock; 4 for shares*