

Practice Exam Questions



Series 6

Investment Company and Variable
Contracts Products Representative



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Total Question: 375 QAs

Question No: 1

Which signifies the maximum amount of equity shares a public company can issue?

- A. Issued shares
- B. Total Preferred stock
- C. Authorized shares
- D. Total Common stock

Answer: C

Explanation: Authorized shares. The maximum number of shares a corporation may issue, authorized shares is first set in a corporation's Articles of Incorporation. They may be changed only by shareholder vote. Authorized shares govern the distribution of Common stock. Issued shares are Common shares that are actually held collectively by the shareholders, either through purchase directly from the company or on the open market, or through the company's issuance of shares as compensation to insiders. The number of issued shares will be an amount up to the number of authorized shares.

Question No: 2

What is the record date of a dividend?

- A. The date on which the Board of Directors decides to pay a dividend
- B. The date by which a shareholder must own the stock in order to receive the dividend
- C. The date the dividend will be paid
- D. A date set by FINRA or NYSE

Answer: B

Explanation: The date by which an investor must own the stock in order to receive the dividend. On the declaration date, the board declares the dividend and explains who will receive it. Investors are entitled to a dividend if they own the stock on or before a certain date, known as the record date.

The board also selects a date upon which the dividend payment will be made, called the payable date. The ex-date (or ex-dividend date) is set by FIN RA/NYSE. If a stock is purchased on or after the ex-date, an investor is not entitled to a dividend because he will not become the owner "of record" of the share until after the record date.

Question No: 3

How does the Securities Exchange Act of 1934 affect the rights of shareholders?

- A. It requires public companies to report financial information to both the SEC and the general public
- B. It sets penalties for companies that do not meet certain financial expectations
- C. It requires companies to register any offer or sale of securities
- D. It regulates the securities exchanges

Answer: A

Explanation: It requires public companies to report financial information to both the SEC and to the general public. The Securities Exchange Act of 1934 requires publicly owned companies to report financial information to the SEC and the general public. Companies must file quarterly (10-Q) and annual reports (10-K) to the SEC, and make these reports available to shareholders and the public.

Shareholders also have the right to examine meeting minutes, lists of shareholders and any other company

record. The Securities Act of 1933 regulates the offer and sale of securities. It also requires that these securities be registered.

Question No: 4

Which type of Preferred stock can be exchanged for Common by decision of the owner?

- A. Callable Preferred
- B. Participating Preferred
- C. Adjustable Preferred
- D. Convertible Preferred

Answer: D

Explanation: Convertible Preferred. Convertible Preferred stock can be exchanged for Common stock. One share of Convertible Preferred is generally worth multiple shares of Common stock and the exchange rate is expressed using a ratio. Callable Preferred stock can be repurchased by the issuing corporation at a set date and at a set price. Participating Preferred shares can earn a dividend higher than the rate listed on the stock certificate at the approval of the board of directors.

Adjustable Preferred does not have a fixed rate of return; the rate of return changes with an independent economic indicator such as the T-bill rate.

Question No: 5

What is the "cooling-off period" for a public offering of securities?

- A. A period of 20 days in which the preliminary prospectus is prepared and reviewed by the SEC
- B. A period of 30 days in which the preliminary prospectus is prepared and reviewed by the SEC
- C. A period of 30 days after filing the preliminary prospectus with the SEC during which no securities may be sold
- D. A period of 20 days after filing the preliminary prospectus with the SEC during which no securities may be sold

Answer: D

Explanation: A period of 20 days after filing the preliminary prospectus with the SEC during which no securities may be sold. The underwriters of an initial public offering (IPO), which may be broker dealers or investment bankers, complete the paperwork for companies that will be going through the IPO process. They fill out registration statements (or SIs), generate interest for the stock and circulate shares through the primary market. The issuing company and its underwriters go through a mandatory cooling off period after filing the preliminary prospectus with the SEC. This lasts a minimum of 20 days, during which the company cannot sell shares or promote its intended offering within the investment community. It can, however, distribute the preliminary prospectus, commonly called a red herring, to potential investors, with follow-up at the conclusion of the cooling-off period.

Question No: 6

In which market are the initial offerings of securities sold?

- A. Secondary market
- B. Over the Counter market
- C. Primary market
- D. Auction market

Answer: C

Explanation: Primary market IPO stock is sold into the primary market, which is also called the "new issue market." Any trading of the security subsequent to the IPO is done in the secondary market, when an investor sells shares through a brokerage and via a stock exchange to another investor.

Exchanges such as the New York Stock Exchange (NYSE) and American Stock Exchange (now called NYSE Amex Equities) are actual, physical locations where stocks are bid, bought and sold by traders. The Over the Counter (OTC) and NASDAQ markets are not physical places but electronic systems over which trades are conducted. In the US, most regional exchanges such as the Pacific, Boston and Philadelphia are still in operation but have been acquired by either the NYSE or NASDAQ. The exchange market is also referred to as the auction market.

Question No: 7

How do rising interest rates affect the price of a bond?

- A. There is no change in the price of the bond
- B. The price of the bond decreases
- C. The price of the bond increases
- D. The bond will offer a higher interest rate

Answer: B

Explanation: The price of the bond decreases. An existing bond's worth is determined by fluctuations in interest rates: If rates increase, corporations issue new bonds paying a higher nominal yield. If rates decrease, corporations issue new bonds paying a lower nominal yield. Since bonds do not trade at par (face value) in the secondary market, a bond that may have originally sold for \$1,500 will not likely sell for \$1,500 in the secondary market if interest rates rise. If an existing bond pays 10% and interest rates increase, a corporation will issue new bonds at a higher rate, making the older 10% bonds less attractive investments because investors can purchase new bonds that pay the higher rate. A holder of an existing 10% bond wishing to sell will have to discount the value below par to make it attractive to a potential buyer.

Question No: 8

In a bond investment, which of the following pays periodic interest payments but also repays the principal in one lump sum?

- A. Serial maturity
- B. Balloon Maturity
- C. Variable maturity
- D. Term maturity

Answer: D

Explanation: Term maturity. Bonds are debt securities, or loans, and can be repaid in one of three ways: term maturity, serial maturity or balloon maturity. Term maturity denotes that periodic interest payments are made, with the principal paid in one lump sum on a specific date. A serial maturity bond, often issued by governments as part of a set of bonds, matures at periodic intervals, with both the principal and interest covered. A balloon maturity is a structure that pays off the principal at the end of the loan term, with the final payment substantially larger than the previous payments.

Variable maturity describes a particular strategy of buying and selling bonds rather than the structure of an individual bond.

Question No: 9

What is the dollar value of one bond point?

- A. \$1
- B. \$10
- C. \$100
- D. None of the above

Answer: B

Explanation: \$10. Bond prices are quoted using bond points, with each point equaling \$10. A quote of "85" or "107" would indicate that those bonds are selling at \$850 and \$1,070, respectively. Simply multiply the point value by 10. Fractional points are also used when quoting bond prices and are expressed as a fraction of 10, therefore $1/2$ equals \$5 and $1/4$ equals \$2.50. A bond trading at $105 \frac{1}{8}$ would have a dollar value of \$1,051.25 ($105 = \$1,050 + 1/8 = \1.25).

Question No: 10

Which of the following corporations would be regulated under the Trust Indenture Act of 1939?

- A. A corporation that issues \$5,000,000 in bonds with a maturity period of ten years
- B. A corporation that issues \$1,000,000 in bonds with a maturity period of one year
- C. A corporation filing for bankruptcy that issues \$5,000,000 in bonds with a maturity period of one year
- D. A corporation that issues \$1,000,000 in bonds with a maturity period of ten years

Answer: A

Explanation: A corporation that issues \$5,000,000 in bonds with a maturity period of ten years. The Trust Indenture Act of 1939 regulates corporations that issue \$5,000,000 or more in bonds, among other provisions. (However, corporations reorganizing under Chapter 11 bankruptcy are exempt so long as their bond maturity date is at most one year after their reorganization plan's effective start.)

These corporations must sign a contract, also known as an indenture, with a trustee who protects the interest of bondholders. In the event of a default on this bond, the indenture trustee can compel the issuer to sell assets through a bankruptcy court and transfer the proceeds to the bondholders as recovery. In some cases, issuers may decide to designate specific assets as collateral against defaulting payments. The titles to those items are then pledged to the trustee, who will begin selling them if the issuer's payments fall behind.

Question No: 11

What type of government security has a maturity period of between two and 10 years?

- A. T-notes
- B. T-bills
- C. T-bonds
- D. Treasury receipts

Answer: A

Explanation: T-notes. T-notes, short for Treasury Notes, have maturities as short as two years and as long as 10 years, with other maturities of three, five and seven years. T-bonds, or Treasury Bonds, are issued with maturities of between 10 and 30 years, with 30 being the most common. Quotes for both securities are quoted in $1/32$ s. T-bills, or Treasury Bills, are government securities that repay only the face amount with terms from 4, 13, 26 or 52 weeks. There is no coupon rate and no interest installments associated with T-bills. When investors purchase T-bills, they are seeking the largest discount possible off the face amount. Treasury receipts, which are similar to treasury strips, are purchased at a discount and paid at face value upon maturity. There is no interest payment, but because the par value is increased every year, the investor receives more than he

paid.

Question No: 12

What factor determines if a municipal bond will be taxed at the local level?

- A. The bondholder's residence and location where bond was issued
- B. The bondholder's residence only
- C. The amount of interest received by the bondholder
- D. The amount of time the bondholder owned the bond

Answer: A

Explanation: The bondholder's residence and location where bond was issued. Two factors determine whether the interest generated by a municipal bond will be taxed at the local level; where the bondholder lives and where the municipal bond was issued. If an investor holds a municipal bond issued by the state of Texas and the bondholder resides in Texas, the state government isn't likely to tax the bond. However, if the bondholder resides in Oklahoma, the state government of Oklahoma could levy a tax. The same principle applies to city issued municipal bonds. If an investor holds a municipal bond issued by the city of Austin, Texas and the bondholder lives in Austin, the bond isn't likely to be taxed by the city. But, if the bondholder moves to Dallas, a tax becomes likely.

Question No: 13

What type of risk refers to an issuer unable to make interest payments on its bond?

- A. Power/constant dollar risk
- B. Junk bond risk
- C. Default/credit risk
- D. Interest rate risk

Answer: C

Explanation: Default/credit risk. Default/credit risk occurs when an issuer is unable to make interest payments on its bonds. Interest rate risk occurs when interest rates rise above an existing bond's fixed coupon rate, thus decreasing a bond's value to investors in the secondary market. Investors may turn to adjustable securities instead. Power/ constant dollar risk is the risk of inflation and poses a threat to fixed-rate securities, such as bonds. As inflation increases, the purchasing power of a fixed coupon rate decreases.

Question No: 14

Which issuer's security is backed by the full faith and credit of the US Government?

- A. FNMA
- B. Freddie Mac
- C. GNMA
- D. None of the above

Answer: C

Explanation: GNMA. GNMA, or Ginnie Mae, is the Government National Mortgage Association, and its mortgage-backed securities, issued as pass-through certificates, are supported by the full faith and credit of the US government. The Federal National Mortgage Association, FNMA or Fannie Mae, also issues pass-through certificate securities, but as a publicly traded company, does not offer the same guarantee on its securities as GNMA. The Federal Home Loan Mortgage Corporation or Freddie Mac, also issues mortgage-backed securities in the form of pass-through certificates, and is likewise a public company, thereby offering

no guarantee on its securities.

Question No: 15

What is the name of the rate banks charge other banks for a loan?

- A. Discount rate
- B. Broker call loan rate
- C. Federal funds rate
- D. Prime rate

Answer: C

Explanation: Federal Funds Rate. The Federal Funds Rate is the interest rate banks charge each other when they borrow money. The transaction is actually an overnight transfer of funds from the lending institution's available balance held at the Federal Reserve. The Discount Rate refers to the interest rate banks pay to borrow short-term funds from the Federal Reserve Bank. A Broker call loan rate is the short-term interest rate banks charge to broker -dealers who borrow money, usually for use with margin accounts. The Prime Rate is the interest rate at which a bank's best customers can borrow funds, and is usually the base rate from which banks and other lenders determine what to charge for mortgages and small business loans.

Question No: 16

Which is not considered a security?

- A. Certificates of interest
- B. Certificates of interest or participation in profit
- C. Certificates of deposit
- D. Fractional undivided interests in mineral rights

Answer: C

Explanation: Certificates of Deposit. Under The Securities Act of 1933, a corporation wishing to sell securities to the general public must register the offering with the SEC. Securities are defined as the following types of paper: stocks; bonds; notes; certificates of interest, ownership or participation in profit; sharing agreements; investment contracts; transferable shares; fractional undivided interests in oil, gas or mineral rights; certificates of deposit for a security; temporary or interim certificates of interest or participation in profit, including receipts, warrants, rights, and guarantees; and evidence of indebtedness. Ambiguous language or misleading terminology must be corrected and attempts to circumvent the Act's requirement will lead to a stop order.

Question No: 17

What type of securities may be issued under Regulation D?

- A. Limited partnerships
- B. Mutual funds
- C. Restricted securities under Rule 144
- D. Private placements

Answer: D

Explanation: Private placements. According to Regulation D, issuers can sell securities, either equity or debt, through a non-advertised or non-solicited private placement which limits the issuer to offering restricted securities to accredited or "sophisticated" investors. Most issuers under Reg D are smaller companies, many in startup and development phases, and while they're still required to provide proper paperwork and disclosure documentation, the filing requirements are far less intricate and costly than a registration of public

securities.

Question No: 18

Under which Regulation D rule can companies sell securities totaling less than one million dollars per year?

- A. Rule 504
- B. Rule 505
- C. Rule 506
- D. Rule 507

Answer: A

Explanation: Rule 504. Rules 504, 505, and 506 are all exemptions under Regulation D. Rule 504 states that if a company sells no more than \$1,000,000 (one million) in securities per year, it can sell restricted securities rather than filing a registration statement with the SEC. Rule 505 offers a similar exemption to companies selling up to \$5,000,000 (five million) in securities per year, enabling them to sell restricted securities to accredited investors and up to 35 other non-accredited or non-sophisticated investors. Rule 506 enables a company to raise an unlimited amount of capital through the sale of restricted securities to accredited investors and up to 35 other investors who must be sophisticated. The issuer must make available to non-accredited investors generally the same disclosure documents distributed to accredited investors.

Question No: 19

Which condition or event would cause the SEC to revoke a pending registration of a broker-dealer or representative?

- A. Bribing a customer to purchase a security
- B. Business misconduct by an issuer
- C. Failure to meet business objectives
- D. Non-sufficient funds in a personal banking account

Answer: A

Explanation: Bribing a customer to purchase a security. The Securities Act of 1934 empowers the SEC's authority to decide who can become registered within the securities market. Before broker-dealers and representatives can register with an investment firm, or before firms can register with an SRO (self regulatory organization), they must complete Form U-4. The SEC reviews these forms and rejects certain applicants if the applicant has been convicted of a felony in the past 10 years or a misdemeanor involving theft, deceit or embezzlement. Certain types of misdemeanors can cause a pending registration to be revoked:

- With respect to securities trading, bribery, perjury, burglary, taking a false oath, making a false report, or conspiracy to commit any of the listed offenses
- Business misconduct as a broker, dealer, investment adviser, bank, insurance company, fiduciary, transfer agent, or any agent whose role is similar to the ones listed
- Theft, larceny, robbery, extortion, counterfeiting, forgery, fraudulent concealment, misappropriation, and fraudulent conversion of securities or funds

Question No: 20

Which is exempt from registration under FINRA Rule 1032?

- A. A floor member of a national securities exchange
- B. A futures trader registered with a futures association
- C. The assistant to the General Principal

D. All of the above

Answer: D

Explanation: All of the above. FINRA requires registration for all principals and all representatives of all securities firms doing business in the United States. Principals are the people who manage a member organization's investment banking or securities business, such as partners, officers, directors and managers. Representatives are primarily the sales force, and may also have some supervisory functions. Those exempt from registration include:

1. Clerical employees
2. Those not performing work associated with a member's investment banking or securities business
3. Those only filling a member's immediate need for nominal corporate officers or capital participation
4. Those conducting business on the floor of a national securities or commodities exchange and are already registered with their respective organizations, such as securities and commodities traders

Question No: 21

According to FINRA, what is the definition of a branch office?

- A. Any place where customer orders are reviewed
- B. Any place where orders are executed
- C. Any place where investment banking or securities business is conducted
- D. Any place where private placements are structured

Answer: C

Explanation: Any place where investment banking or securities business is conducted. FINRA considers any place where a member conducts investment banking or securities business to be a branch office. The member firm can identify these locations to customers and the public in any way. Branch offices may be considered an office of supervisory jurisdiction (OS), or non-OS. An OS is defined by FINRA as any place where the following is conducted:

- Order execution/ market making
- Maintaining possession of customer funds and securities
- Reviewing/endorsing customer orders
- Supervising other branch offices
- Structuring public offerings or private placements
- Authorizing new accounts

Question No: 22

What condition must be satisfied before an employee of a FINRA member firm can accept employment or compensation from another business?

- A. The member firm must authorize the employee's employment
- B. None, an employee can work for another business without the member's knowledge
- C. The member firm must be verbally notified
- D. The member firm must be notified in writing

Answer: D

Explanation: The member firm must be notified in writing. A person cannot simultaneously work for a member firm and another organization unless the member firm receives prompt written notice.

After the member firm receives written notice, the employee can accept employment or financial compensation from another business, regardless of its nature. The exception to this rule is when a member firm

rm employee receives payments from passive investments, such as limited partnerships and direct participation plans (DPPs).

Question No: 23

What charge may result from a registered representative generating an abnormally large amount of commissions?

- A. Fraud
- B. Churning
- C. Unauthorized trading
- D. Selling away

Answer: B

Explanation: Churning. Churning describes excessive securities trading in a customer account by a broker, without regard to the customer's investment objectives, for the purpose of generating commissions for the benefit of the broker. It's a violation of SEC Rule 15c1-7. For the churning charge to be valid, the broker must have been proven to exercise investment decisions in the customer account. Fraud is the broader term that covers an intentional misleading of clients regarding their investments, primarily by misrepresenting facts or conditions, or by withholding material information. Unauthorized trading occurs when a representative executes an order on behalf of a customer without the customer's consent. The term "selling away" refers to the sale of securities by a registered representative in a private transaction without permission from the member firm.

Question No: 24

Which amendment to the Securities Exchange Act of 1934 allowed the Securities And Exchange Commission to delegate powers to self-regulatory organizations?

- A. The Uniform Practice Code
- B. The Maloney Act
- C. The code of procedure
- D. None of the above

Answer: B

Explanation: The Maloney Act. The Maloney Act was an amendment to the Securities Exchange Act of 1934 that allowed the SEC to delegate power to self-regulatory organizations (SROs). The SEC and FINRA are examples of SROs. The Uniform Practice Code ensures that procedures and regulations remain consistent, or uniform, among all member firms. Regardless of where an account is held, the customer can expect adherence to the same set of practices and policies. The code of procedure refers to the set of rules by which the FINRA investigates a breach of proper conduct.

Question No: 25

Under what type of retirement plan does an employer contribute a certain amount to an employee's retirement fund each year?

- A. Defined benefit plan
- B. Deferred compensation plan
- C. Payroll deduction plan
- D. Defined contribution plan

Answer: D

Explanation: Defined contribution plan. The 401(k) is an example of a defined contribution plan, wherein an employer contributes to an employee's retirement fund each year through matching a percentage, sometimes up to 100%, of the funds contributed by the employee. The employee has a degree of control over how his retirement funds are invested. This differs from a defined benefit plan, wherein the company controls the risk management of the retirement portfolio and contributes to an employee's retirement fund based on a formula that considers length of employment and salary, among other things. Defined benefit plans may be "qualified benefit plans" or "non-qualified benefit plans." Deferred compensation and payroll deduction plans are nonqualified retirement accounts in which the employer withholds a portion of the employee's paycheck and secures it until retirement.

Question No: 26

Which retirement plan can be used by self-employed individuals who want to exempt certain employees from coverage?

- A. Keogh plan
- B. SEP-IRA
- C. Tax sheltered annuity
- D. Roth IRA

Answer: B

Explanation: SEP-IRA. A SEP-IRA, or Simplified Employee Pension-IRA, is a non-qualified retirement account into which a business owner makes tax deductible contributions. These contributions, made at the discretion of the employer, vest immediately and the IRA holder (employee) can then direct the investment. Keogh retirement plans are used mainly by self-employed persons or unincorporated businesses. They're qualified plans with higher contribution limits than a SEP-IRA, based on a percentage of the business' pre-tax income. The contribution made to the proprietor's account must equal the contribution made to the employees' accounts.

A TSA, or a tax sheltered annuity, is a qualified retirement plan intended for nonprofit organizations. Roth IRAs are funded by after-tax contributions and can be withdrawn from beginning at age 59 1/2. The withdrawn money is not taxed if done so during retirement.

Question No: 27

On which person is the maximum contribution limit based for an Educational Savings Account (ESA)?

- A. The person that pays into the account
- B. The person controlling the account
- C. The parent
- D. The child

Answer: D

Explanation: The child. Parents can use an Educational Savings Account (ESA) to save money for their children's higher education. An ESA is funded by after -tax contributions, with the maximum contribution limit based on the number of children. The dollar amount is subject to change, per the IRS. Distributions from the account are tax-free unless plan rules have been violated. The Section 529 Plan is a common type of ESA. Under 529 plans, holders may contribute larger after -tax sums than are normally allowed and the distributions will be tax-free at the federal level. State taxes may be levied. ESAs are also called Coverdell Accounts and Education IRAs.

Question No: 28

Which section of the Securities Act of 1933 states that misrepresentations or omissions of material fact are prohibited in the issuer's written and oral communications?

- A. Section 8
- B. Section 11
- C. Section 12
- D. Section 17

Answer: C

Explanation: Section 12. Section 12 regulates the distribution of securities information and states that any misrepresentations or omissions of material fact are strictly prohibited in both the issuer's written and oral communications. Section 12 explains the civil liabilities associated with distributing a misleading prospectus and other fraudulent communications. Section 11 states that if a registration statement leaves out, or misrepresents, a material fact concerning its effective date, the issuer and underwriters may incur civil liabilities. Investors can file a suit if damages result from an omission or misrepresentation. Section 17 forbids an issuer from making misleading or false statements concerning the offer or sale of securities.

Question No: 29

Under Rule 2210, which does not fall under FINRA's regulation of online mutual fund advertising?

- A. Advertisements intended for small audiences
- B. Correspondence intended for a single customer
- C. Sales literature intended for a targeted audience
- D. Live forum communications

Answer: A

Explanation: Advertisements intended for small audiences. As technology develops and creates new mediums and opportunities for advertisement, FINRA amended Rule 2210 to include provisions for online advertising and communication. Liability is still assessed by examining the advertisement's intended audience. FINRA created four categories for the placement and regulation of electronic media:

1. Advertisements intended for large audiences
2. Correspondence intended for a single customer
3. Sales literature intended for a targeted audience
4. Live forum communications

Question No: 30

FINRA Conduct Rule 2211 exempts which type of institutional sales material and correspondence?

- A. Correspondence sent to more than 25 existing retail customers within 15 calendar days
- B. Correspondence sent to less than 25 existing retail customers within 15 calendar days
- C. Correspondence sent to less than 25 existing retail customers within 30 calendar days
- D. Correspondence sent to more than 25 existing retail customers within 30 calendar days

Answer: C

Explanation: Correspondence sent to less than 25 existing retail customers within 30 calendar days Approval from a registered principal is required for correspondence sent to more than 25 existing retail customers within 30 calendar days, and if it advertises a certain good or service, or recommends securities. Member firms create their own rules and regulations regarding the approval and registration of institutional sales materials. These rules depend on the size, structure and business activities of the firm and are documented in writing.

Not every institutionalized sales material needs approval from a registered principal prior to its use. The firm works to uphold compliance by providing training and education to people affiliated with the member firm. FINRA requires evidence that the member is following the guidelines.

Question No: 31

Which situation, according to FINRA, does not constitute a business relationship?

- A. A customer with a current security position with a member broker-dealer
- B. The firm has done business with the person in the past 18 months
- C. A person who inquired about products sold by the firm within the past three months
- D. A person who inquired about products sold by the firm within the past 18 months

Answer: D

Explanation: A person who inquired about products sold by the firm in the past 18 months A member firm and a person are deemed to have established a business relationship if:

- The person has had an account, money balance or security position with a firm in the past 18 months
- The firm has served as the broker-dealer on record for the person in the 18 months prior to the call
- The person has inquired about the goods and services provided by the firm in the three months prior to the call

FINRA Rule 2212 also regulates the telemarketing activities of member firms, stating that a telemarketer can call only between the hours of 8 AM and 9 PM. This rule does not apply when the person being solicited has a prior business relationship with the caller, or if the person is a brokerdealer or has given the firm permission.

Question No: 32

Which FINRA rule governs how customer complaints are to be handled?

- A. Rule 2211
- B. Rule 3010
- C. Rule 3110
- D. Rule 3040

Answer: C

Explanation: Rule 3110. Rule 3110, entitled "Books and Records," states that member firms must create and store records of correspondence, accounts, books and memoranda in accordance with the Securities Exchange Act of 1934. These records include customer complaints. Customer complaints are defined as a written statement expressing a grievance against persons associated with a member firm.

- Rule 2211 covers the approval of institutional sales material and correspondence.
- Rule 3010 governs the supervisory system that each member firm must have in place to ensure that representatives, principles and associates comply with FINRA rules and procedures.
- Rule 3040 prohibits any person who works for a member firm from conducting private securities transactions unless written notice is given to the firm.

Question No: 33

Which type of investor would be best equipped to invest in volatile stocks?

- A. An investor looking for investment growth without taxation
- B. An investor that wants cash flow at periodic intervals
- C. An investor with a high liquid net worth
- D. None of the above

Answer: C

Explanation: An investor with a high liquid net worth. Liquid net worth is the accumulated value of only those assets that are easily convertible into cash, such as securities and savings accounts. An investor with a high liquid net worth is better equipped to invest in volatile stocks. Investors seeking tax relief want investment growth without taxation until their securities have reached maturity. Municipal bonds, annuities and retirement accounts that produce tax-free interest payments are suited to this type of investor. Current income investors want income payments at periodic intervals, monthly, quarterly, or biannually. Debt securities, money market mutual funds or purchase pass-through certificates are among suitable investments instruments for current income investors.

Question No: 34

Which assessment is most important when determining specific stocks to recommend to a client?

- A. Time horizon
- B. The client's age
- C. The client's current income
- D. Risk tolerance

Answer: D

Explanation: Risk tolerance. Considering a client's risk tolerance is crucial to planning his investment strategy. How much risk is the investor willing to take on? Representatives must be candid about a security's potential for growth and failure, as well as the price variation it may undergo. Risk-averse or low-risk tolerant clients should keep investment in equity securities to a minimum, while highrisk clients may be more attracted to speculative stock. Many investors have a specific length of time in which they need their investments to mature or, at the very least, produce a certain income.

This is called a time horizon. Common stocks can be suitable for investors with a 20-year time horizon. Short-term investors, who expect a return within a few months, are good candidates for money market securities. Investors who need a substantial return within four or five years may be attracted to income-producing securities that also provide inflationary protection, such as government bonds. A client's age determines the type of investment. Older investors often invest in bonds to provide for income and capital preservation. Younger investors are able to absorb more risk, therefore a loss incurred by investment in equity shares can potentially be recouped due to longer time horizons.

Question No: 35

Which type of mutual fund offers shares on a continual basis, issues Common stock and invest in bonds.

- A. Closed-end mutual fund
- B. Open-end mutual fund
- C. Both closed-end and open-end mutual funds
- D. Neither closed-end nor open-end mutual funds

Answer: B

Explanation: Open-end mutual fund. Open-end mutual funds, which comprise the majority of mutual funds, have no restrictions on the number of shares they can issue, therefore the net asset value (value of a single share) remains constant and investors receive regularly scheduled distributions of additional shares of the fund's common stock. Open-end mutual funds issue Common stock and invest in a mix of securities that can include bonds. They allow for the purchase and sale of shares whenever an investor is willing. Closed-end funds behave like a company that sells stock, selling a fixed number of shares through an IPO, then trading

like a company on a stock exchange.

Question No: 36

What is the public offering price for a mutual fund with a net asset value of \$17.50 and a 10% sales charge?

- A. \$15.75
- B. \$19.44
- C. \$17.50
- D. \$19.25

Answer: B

Explanation: \$19.44. Net Asset Value, or NAV, measures the worth of each separate mutual fund share. NAV is influenced by the appreciation or depreciation of the securities within the fund's portfolio.

Determining the offering price is a two-step process:

- Subtract the sales charge percentage from 100% to find the complement. In this example, the answer is .90 (100% - 10%), expressed as a decimal.
- Divide the net asset value (\$17.50) by the complement (.90). In this example, the answer is \$17.50 divided by .90 equals \$19.44.

Question No: 37

What method can an investor use to reduce the sales charge on multiple purchases of shares of the same mutual fund?

- A. Use breakpoints
- B. Purchase a closed-end mutual fund
- C. Purchase an open-end mutual fund
- D. Sign a letter of intent

Answer: D

Explanation: Sign a letter of intent. An investor can purchase mutual fund shares in installments, and reduce overall sales charges, by signing a letter of intent. This will permit the payment of the sales charge at the breakpoint rather than adjusting the breakpoint incrementally. The investor can purchase additional shares with the savings; however, the fund will withhold those shares until the account becomes fully vested. If the investor fails to make the full contribution per the letter of intent, the mutual fund keeps the extra shares and charges the appropriate breakpoint

Question No: 38

A capital gain in a mutual fund is taxed as a short-term gain when...

- A. the investor holds the mutual fund shares for less than one year
- B. the mutual fund holds the underlying security for less than one year
- C. the investor has owned the fund shares for less than one year, and the fund holds the security for less than one year
- D. the fund holds the security for less than one year, and the investor sells his shares

Answer: B

Explanation: The mutual fund holds the underlying security for less than one year. When a mutual fund sells the securities in its portfolio at a higher price than the purchase price, a capital gain is realized.

Capital gains are distributed to investors on an annual basis and are taxed according to the length of time the securities have been held in the fund. The length of time an investor has owned the fund is irrelevant. If the