Practice Exam Questions

FINRA Investor Education FOUNDATION

Series 7

General Securities Representative

EXAMAIDES

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Total Question: 650 QAs

Question No: 1
Which of the following preferred issues is likely to fluctuate most in value?
A. cumulative preferred
B. callable preferred
C. convertible preferred
D. broker preferred
Answer: C
Explanation: convertible preferred. Because of the conversion feature, convertibles are more closely linked to the price of the common stock. In addition, since the dividend rate on convertible preferred is usually lower than other preferred issues, the convertibles are more sensitive to interest rate fluctuations.

Question No: 2
Which of the following rights does an ADR holder not have?
A. preemptive rights
B. the right to vote for your mother-in-law as a board member
C. the right to transfer ownership
D. the right to see financial statements
Answer: A
Explanation: preemptive rights. Holders of ADRs do not have preemptive rights, although they have most other rights of shareholders, including the right to vote for board members-even a mother-in-law

Question No: 3
A corporation makes a rights offering to raise $10 million of new capital by issuing one million shares of common stock. If it already has six million shares outstanding at the time of the offering. How many rights will the corporation distribute to its shareholders?
A. one million
B. six million
C. ten million
D. sixteen million
Answer: B
Explanation: six million. One right for each outstanding share is distributed.

Question No: 4
A corporation makes a rights offering to raise $10 million of new capital by issuing one million shares of common stock. If it already has six million shares outstanding at the time of the offering. What is the subscription price per share?
A. $4
B. $6
C. $7
D. $10
Answer: D

Explanation: $10. There are one million shares divided into the $10 million of new capital.

Question No: 5
A corporation makes a rights offering to raise $10 million of new capital by issuing one million shares of common stock. If it already has six million shares outstanding at the time of the offering. What subscription ratio is the corporation establishing for each new share?
A. 6 rights per share
B. 10 rights per share
C. 6 million rights per share
D. 10 million rights per share
Answer: A
Explanation: 6 rights per share. Each share receives a right and there are six million shares receiving rights to one million new shares. So six rights are required for one share.

Question No: 6
Bubba owns stock with cumulative voting rights. There are five vacancies on a board and he owns 100 shares of stock. Bubba is entitled to cast the following votes:
A. a total of 100 votes
B. a total of 100 votes per
C. a total of 500 votes
D. you are not allowed to vote
Answer: C
Explanation: 500 votes. Under cumulative voting, the number of directors is multiplied by the number of shares owned. The votes may be cast all for a single director or divided in any manner among the directors.

Question No: 7
The definition of debentures is:
A. a loan secured by real estate
B. collateralized securities
C. a worthless security
D. securities backed by the general credit of the issuers but no specific collateral
Answer: D
Explanation: securities backed by the general credit of the issuers but no specific collateral. And in the case of some issuers, that may be fairly worthless.

Question No: 8
Convertible bonds have all of the following features except:
A. an ability to protect a short position on the stock into which they are convertible
B. permissibility for use as collateral
C. a normally higher yield than non-convertible bonds of the same issuer
D. fluctuations influenced by changes in the price of the underlying common stock
Answer: C
Explanation: a normally higher yield than non-convertible bonds of the same issuer. Remember that the question says “except” for this feature. Convertible bonds normally do NOT have a higher yield than non-

convertible bonds of the same issuer. Convertibles usually have a lower yield than non-convertible sisters.

Question No: 9
Although a corporation has no earnings in a particular year, it is obligated to pay interest on all its outstanding debt except the following:
A. convertible subordinated debentures
B. collateral trust bonds
C. adjustment bonds
D. equipment trust certificates
Answer: C
Explanation: adjustment bonds. These bonds are also known as income bonds. Interest is paid only if there is income.

Question No: 10
Interest rates rise from 5.10% to 5.30%. For a prospective buyer of five $1,000 bonds, what is the increase in interest payments as a result of the rise?
A. $20
B. $100
C. $2
D. $10
Answer: D
Explanation: $10. Interest rates increased by 20 basis points. One basis point is 10 cents. So 20 basis points is $2. But…since there are five bonds, that $2 x 5 = $10.

Question No: 11
Common stocks for which of the following industries are most likely to decline in value when interest rates rise?
A. automobile manufacturers
B. airlines
C. stock brokers
D. public utility companies
Answer: D
Explanation: public utility companies. Interest rates most affect the companies with the greatest amount of debt. Public utility companies are highly leveraged. Hence, they most likely incur the largest affect of rising interest rates.

Question No: 12
Convertible preferred stock has all of the following characteristics except:
A. a lower dividend rate than non-convertible preferred
B. a dilution of earnings if converted into common stock
C. a requirement for shareholders to always accept the call price when called
D. required dividend payments to shareholders before any dividends are paid to holders of common stock
Answer: C
Explanation: a requirement for shareholders to always accept the call price when called. All of the other

statements are true “except” this one. Convertible preferred shareholders have an opportunity to convert to common stock. There is no forced call price.

Question No: 13
Bubba buys a 5% bond that matures in 15 years with a 5.10 basis. How much did he pay for the bond?
A. 5.00
B. 98.96
C. 100.00
D. 105.10
Answer: B
Explanation: 98.96. A calculator is not required for this. Even Bubba knows the bond is obviously trading at a slight discount by yielding 5.10% instead of the coupon rate of 5%. If the yield was the same as the coupon rate, the price is 100.00.

Question No: 14
Bonds are most often quoted as a percentage of:
A. face value
B. book value
C. market value
D. whatever value the broker says
Answer: A
Explanation: face value. The price is 100.00 if the yield is the same as the coupon rate. A price of less than 100.00 means the yield is higher than the coupon rate. A price of more than 100.00 means the yield is lower than the coupon rate. The prices are a percentage of 100.00. However, treasury bonds and municipal bonds are not quoted in this way.

Question No: 15
Which of the following is a right for shareholders of common stock?
A. the right to have the stock price increase
B. the right to vote about important matters of the company
C. the right to dividends
D. both B and C
Answer: B
Explanation: the right to vote about important matters of the company. Shareholders have no expectation of stock price increase or dividends. They are entitled to receive dividends only if the board of directors declares them.

Question No: 16
Who owns a corporation?
A. the owners of debentures
B. the holders of common stock
C. the holders of common stock and the holders of preferred stock
D. the government
Answer: C

Explanation: the holders of common stock and the holders of preferred stock. The holders of all classes of stock are the owners. Each stock class has separate privileges, but all represent ownership. Even if the government is an owner, it holds shares of stock.

Question No: 17
Which of the following is true of treasury stock?
A. it has voting rights
B. it is entitled to receive dividends
C. it is stock that has not been issued
D. it is stock that has been reacquired by the issuer
Answer: D
Explanation: it is stock that has been reacquired by the issuer. Treasury stock has no voting rights and is not entitled to receive dividends. The shares have been issued but are no longer outstanding in the market.

Question No: 18
Bubba decides to buy equity securities. Which of the following statements is always true about what Bubba is buying?
A. they are readily marketable
B. they have a fixed rate of return
C. they have a fixed maturity date
D. they are not secured by collateral
Answer: D
Explanation: they are not secured by collateral. Equity is ownership, which has no collateral security…or any other kind of security such as a guaranteed return, maturity, or marketability.

Question No: 19
Which of the following securities provides the longest term of option privilege?
A. puts
B. calls
C. warrants
D. rights
Answer: C
Explanation: warrants. All of the others always have fixed maturity dates. Warrants often have no finite life and, if they do, it is a very long time.

Question No: 20
A company may pay a declared dividend in which of the following ways:
A. with stock in a subsidiary company
B. with property
C. with cash
D. all of the above
Answer: D
Explanation: all of the above. Dividends can be paid in all of these ways. They can also be paid with treasury stock or authorized but unissued stock.

Question No: 21
Bubba owns a subordinated debenture in a company that is liquidating. When will he get paid?
A. after the company pays its outstanding bills, but before paying bank loans
B. after the bills are paid and the bank is paid, but before the preferred shareholders
C. before the holders of secured debt
D. after the shareholders of preferred stock
Answer: B
Explanation: after the bills are paid and the bank is paid, but before the preferred shareholders. As a creditor, Bubba is paid before any of the shareholders. But his position is subordinated to other creditors, like the bank and accounts payable.

Question No: 22
When a corporation dissolves, who gets paid first?
A. bank lenders
B. senior bond holders
C. the tax collector
D. the lawyer
Answer: C
Explanation: the tax collector. Taxes always have preference over any other creditors.

Question No: 23
Bubba wants to buy a $4 convertible preferred with that has a $50 par value and is exchangeable for common stock at $47.50. If the preferred stock is trading at 52, what does Bubba calculate as the common stock price in order to be at parity with the preferred?
A. 47.50
B. 52.00
C. a little less than 49.38
D. a little more than 54.50
Answer: C
Explanation: a little less than 49.38. Bubba needs a calculator to divide the par value of the preferred stock by the price of the common stock. He then divides the result into the price at which the preferred stock is trading.50 divided by 47.50 = 1.05352 divided by 1.053 = 49.38

Question No: 24
Which of the following is an analyst most likely to classify as a defensive issue?
A. the securities of a company that airplanes to the military
B. a stock of a large company
C. the common stock of a utility company
D. a corporate bond
Answer: C
Explanation: the common stock of a utility company. The term “defensive issue” refers to a security that is least susceptible to swings in the business cycle.

Question No: 25
Which securities do not receive dividends?
A. ADRs
B. warrants
C. common stock
D. preferred stock
Answer: B
Explanation: warrants. All of the other choices receive dividends if they are declared. But only warrants are a specific security that never pays dividends.

Question No: 26
Bubba buys a bond issued at par with a 5% coupon that is convertible into common stock at $40. What conversion ratio does Bubba determine?
A. 40
B. 30
C. 25
D. 15
Answer: C
Explanation: 25. The conversion ratio is how many shares of common stock Bubba obtains by converting. Divide the bond price - $1,000 for a single bond - by the $40 conversion price.

Question No: 27
Bubba buys a bond issued at par with a 5% coupon that is convertible into common stock at $40. The bond increases in value by 20 points. What is the conversion parity of the stock?
A. $25
B. $40
C. $48
D. $50
Answer: C
Explanation: $48. A 20-point increase results in a bond value of $1,200. Divide that by the conversion ratio of 25 shares to arrive at $48.

Question No: 28
The most common type of bond issued by a well-established company is:
A. a debenture
B. a senior secured note
C. a convertible
D. an open-end mortgage
Answer: A
Explanation: a debenture. Because of the company's well-established financial condition, it issues a debenture that has no specific collateral and is only backed by the creditworthiness of the issuer.

Question No: 29
A corporate bond is quoted as having a net change in value of plus one point. By how much did the bond

price increase?
A. $1,000
B. $100
C. $10
D. $1
Answer: C
Explanation: $10. A point is 1% and bonds are priced in $1,000 increments. Multiplying $1,000 by 1% equals $10.

Question No: 30
A basis point is:
A. 0.10%
B. 0.01%
C. 1.00%
D. 0.001%
Answer: B
Explanation: 0.01%. A basis point is one-hundredth of a point. Since a point is 1%, a basis point is 0.01%. A bond price change of one basis point is ten cents ($1,000 x 0.01%).

Question No: 31
Bubba buys a $4 convertible preferred with a $50 par value that is exchangeable for common stock at 47.50. If the preferred stock is trading at 52 and the common stock at 51, Bubba determines that the preferred stock is:
A. overpriced and will quickly decline
B. selling at a 4% premium over conversion value
C. underpriced and should rise quickly
D. going to be called when the common stock price is $52
Answer: C
Explanation: underpriced and should rise quickly. The parity price for the common stock is about $49.38 - determined as:50 / 47.50 = 1.053 52 / 1.053 = 49.38 Since the common stock is trading at 51, the preferred is underpriced.

Question No: 32
A case of leverage is:
A. selling common stock short and buying warrants for the equivalent number of shares followed by subscribing to the shares and covering the short
B. borrowing at 6% and investing the funds at 10%
C. buying stock on the NYSE and later selling it the same day on the CBOE
D. redeeming a convertible bond before maturity
Answer: B
Explanation: borrowing at 6% and investing the funds at 10%. Leverage is all about using money obtained at a lower cost than what can be earned deploying the funds elsewhere. It is unrelated to arbitrage.

Question No: 33

Bubba holds 200 shares of common stock in a utility company and receives rights to subscribe to an additional 100 shares at $20. The utility company is raising $40 million of new capital. How many rights does Bubba receive?
A. 20
B. 50
C. 100
D. 200
Answer: D
Explanation: 200. In an issue of rights, there is always one right per share. Bubba owns 200 shares and thus receives the same number of rights.

Question No: 34
Bubba holds 200 shares of common stock in a utility company and receives rights to subscribe to an additional 100 shares at $20. The utility company is raising $40 million of new capital. How many shares of common stock for the utility company were outstanding prior to the rights offering?
A. 2,000,000
B. 4,000,000
C. 1,000,000
D. 40,000,000
Answer: B
Explanation: 4,000,000. Bubba owns 200 shares and receives rights for 100 more. The basis for the rights offering is therefore one new share for each two shares outstanding. The utility company is raising $40 million by selling shares at $20. Therefore, the company is selling 2,000,000 new shares. Since the ratio of existing shares to new shares is 2 to 1, there must be 4,000,000 presently outstanding shares.

Question No: 35
Bubba owns a perpetual warrant to buy one share of Internet Corporation common stock at $30. Internet Corporation stock is trading at 41.50 and is ex-dividend today at $0.75. What is the market value of Bubba's warrant?
A. 5.75
B. 5.62
C. 5.38
D. cannot be determined from this information
Answer: D
Explanation: cannot be determined. Bubba can put away the calculator. The warrant is "perpetual" so the value is not determinable from today's price of the common stock.

Question No: 36
The preferred stock of Greatest Technology Corporation has a $100 par and is convertible into four shares of common stock. The preferred is trading at 104.50. The preferred is callable at 101. If the common stock price is presently 27.89, which of the following actions would be a successful arbitrage:
A. purchase 400 shares of common stock and sell 100 shares of preferred stock as "short exempt" (that is, the sale is exempt from the uptick rule)
B. purchase the preferred stock and sell an appropriate amount of the common stock "short exempt"

C. purchase both the common and the preferred stocks as a hedge against further market risk
D. purchase the preferred stock and let it be called, which is inevitable at these market prices
Answer: B
Explanation: purchase the preferred stock and sell an appropriate amount of the common stock "short exempt". Arbitrage is the nearly simultaneous purchase and sale of equal securities in different markets for a profit. Selling four shares of common stock for every one share of preferred stock purchased provides a profit. The transactions involve the same number of common shares because the preferred is convertible to common at a four to one ratio.

Question No: 37
Commercial paper is typically issued with a maturity date not exceeding:
A. 90 days
B. 6 months
C. 270 days
D. 1 year
Answer: C
Explanation: 270 days. A characteristic of commercial paper is relatively short duration, normally not exceeding 270 days.

Question No: 38
The minimum denomination for a US treasury bond is:
A. $100
B. $1,000
C. $10,000
D. $100,000
Answer: B
Explanation: $1,000. This is the minimum denomination. Normally, US treasury bonds are in much larger denominations.

Question No: 39
Which of the following has the least active secondary market:
A. treasury bills
B. banker's acceptances
C. certificates of deposit
D. commercial paper
Answer: D
Explanation: commercial paper. The sizes of secondary markets for these securities are listed in order with treasuries first, then banker's acceptances, followed by certificates of deposit. There is only a very small secondary market for commercial paper.

Question No: 40
Which of the following is not classified as a money market instrument?
A. banker's acceptances
B. commercial paper

C. American Depository Receipts
D. treasury bills
Answer: C
Explanation: American Depository Receipts. American Depository Receipts are used to facilitate transfer of ownership in foreign securities. They are not money market instruments.

Question No: 41
Which of the following is not a characteristic of treasury bills?
A. they are quoted on yield-to-maturity percentages
B. their payments are exempt from state income tax
C. the bid price is higher than the offer price
D. they mature one to three years from the date of issuance
Answer: D
Explanation: they mature one to three years from the date of issuance. Remember the question asks what is "not" a characteristic of treasury bills. The other choices are aspects of treasury bills, which most commonly have maturities of 90 days but never longer than one year.

Question No: 42
Which of the following price quotes is representative of a treasury bill?
A. 98.9 - 100
B. 96 - 96½
C. 5.78 - 5.73
D. 5.55 - 5.75
Answer: C
Explanation: 5.78 - 5.73. Prices for treasury bills are quoted as percentage yields. A quotation in yield means the first price in the spread - the bid price - should be higher than the offer price. A higher yield means a lower price.

Question No: 43
Bubba want to buy a CMO. In general, how often should he expect to receive interest payments?
A. every week
B. every month
C. every year
D. at maturity
Answer: B
Explanation: every month. Collateralized Mortgage Obligations generally pay interest each month. However, some CMOs pay interest quarterly or semiannually.

Question No: 44
A CMO is issued that has three tranches. One has an average life of 2 years. A second has an average life of 10 years. The third has an average life of 30 years. Initially, interest payments are distributed in this order:
A. first to the holders of the 2-year tranche
B. first to the holders of the 10-year tranche
C. first to the holders of the 30-year tranche

D. equally to all CMO holders of any tranche
Answer: D
Explanation: equally to all CMO holders of any tranche. All bondholders share equally in the interest payments. Only principal payments are directed to the owners in each tranche in sequential order.

Question No: 45
Which of the following have a stated interest rate on the face of the certificates?
A. treasury bills
B. treasury notes
C. treasury bonds
D. both B and C
Answer: D
Explanation: both B and C. Treasury notes and treasury bonds have stated interest rates. Treasury bills are always sold at a discount to the face amount payable at maturity.

Question No: 46
Bubba buys a US treasury bond. The interest he earns is:
A. subject to federal and state income tax
B. exempt from federal and state income tax
C. subject to state income tax but exempt from federal income tax
D. subject to federal income tax but exempt from state income tax
Answer: D
Explanation: subject to federal income tax but exempt from state income tax. The interest on US government securities is taxed by the US government but not by state governments. The opposite is true of bonds issued by a state, which are exempt from federal tax but subject to state taxes-except for taxes of the state that issues them.

Question No: 47
Which of the following does not issue debt securities that trade in the open market?
A. Fannie Mae
B. Freddie Mac
C. Federal Reserve Banks
D. Federal Land Banks
Answer: C
Explanation: Federal Reserve Banks. Debt securities are not issued by Federal Reserve Banks. All of the other entities do issue debt securities.

Question No: 48
When depositors withdraw money from savings institutions to invest in US treasury securities, this is called:
A. the multiplier effect
B. disintermediation
C. reverse repo
D. open market operations
Answer: B

Explanation: disintermediation. An easier word would be preferable, but that’s the correct term.

Question No: 49
Smart Company, Inc., has cash it intends to use in six months for purchase of equipment. The most prudent investment during the six-month period is:
A. common stock
B. preferred stock
C. treasury bills
D. treasury bonds
Answer: C
Explanation: treasury bills. The most prudent investment provides the cash in the six-month short-term period. Common and preferred stock are subject to significant price uncertainty. US treasury issues provide the most safety of principal. Treasury bonds have longer maturities than the six-month terms available for treasury bills.

Question No: 50
Which of the following is identified as a funded debt instrument?
A. US treasury bond
B. Series EE savings bond
C. corporate bond
D. Fannie Mae bond
Answer: C
Explanation: corporate bond. All of the other securities are issues backed by the US government, which are not considered funded debt.

Question No: 51
A typical money market instrument carries which of the following?
A. serial bond maturity date
B. long-term maturity date
C. medium-term maturity date
D. short-term maturity date
Answer: D
Explanation: short-term maturity. A money market maintains liquidity and is defined as having maturity of less than one year.

Question No: 52
An offering price of 102 plus accrued interest applies to which of the following securities?
A. treasury bills
B. certificates of deposit
C. commercial paper
D. banker’s acceptances
Answer: B
Explanation: certificates of deposit. CDs trade with “accrued interest” as part of the price.

Question No: 53

Bubba Corporation owes income tax. Which of the following may be tendered at par value for payment of the tax?
A. term bond
B. tax anticipation bill
C. special tax bond
D. pre-issue bond
Answer: B
Explanation: tax anticipation bill. These are specifically designated securities that may be used at face value for payment of corporate taxes.

Question No: 54
An advertisement for a CMO security by a member of FINRA should disclose which of the following?
A. the exact yield investor will earn
B. the yield based upon the prevailing discount rate
C. that the stated yield is an estimate that may vary passed upon prepayments and market factors
D. that the yield may be greater than the stated percentage but never less
Answer: C
Explanation: that the stated yield is an estimate that may vary passed upon prepayments and market factors. The only guarantee is that nothing is guaranteed, especially the yield.

Question No: 55
Which of the following statements incorrectly describes US securities markets?
A. a capital market comprised of long-term debt and equity issues
B. a money market comprised of short-term debt and equity issues
C. a municipal market comprised of tax-exempt issues of state and local governments
D. a government and agency market comprised of both short-term and long-term debt issues
Answer: B
Explanation: a money market comprised of short-term debt and equity issues. This is the statement that is “incorrect”. Equity issues are not traded in the money market, which consists only of high-quality short-term debt securities.

Question No: 56
What rate of return takes into consideration appreciation or depreciation in market value relating to the par value of a debt security?
A. current yield
B. yield to maturity
C. nominal yield
D. basis yield
Answer: B
Explanation: yield to maturity. The premium or discount in the security price relative to par value is considered when computing the yield to maturity.

Question No: 57
Which of the following is not an attribute of US treasury bills?