

## Question #1 of 210

Question ID: 606519

If a broker/dealer erroneously reports the purchase of 100 shares of ALF at 28.65 on a market order, and the firm later finds the actual price paid at execution was 29, what price does the customer pay for the shares?

- ☐ A) 28.65.
- ☒ B) 29.
- ☐ C) He has the option of canceling the order.
- ☐ D) 29.65, with the difference split between the firm and the customer.

### Explanation

If the actual price was 29, the customer must accept the trade at that price even though the trade was confirmed erroneously at a different price. Note that at the execution price of 29 the transaction is still within the parameters of the order instruction given which was to purchase 100 shares at the market.

**Reference:** 9.1.1.3.1 in the License Exam Manual

## Question #2 of 210

Question ID: 606585

Which of the following types of mutual funds has capital appreciation as its investment objective?

- ☐ A) Municipal bond.
- ☒ B) Specialized.
- ☐ C) Income.
- ☐ D) Balanced.

### Explanation

An objective of high-capital appreciation is most likely realized by a stock fund. A specialized fund is one that invests in stocks of one particular industry or region, and its main objective is capital or price appreciation.

**Reference:** 10.5.1.1.4 in the License Exam Manual

## Question #3 of 210

Question ID: 606601

A mutual fund that charges 12b-1 fees may use the money to cover all of the following EXCEPT:

- ☒ A) management fees.
- ☐ B) promotion costs.
- ☐ C) printing costs.
- ☐ D) sales fees.

### Explanation

12b-1 fees may not be used to pay for the portfolio manager's fees, only for sales promotions and fees, and other activities relating to the distribution of the fund's shares.

**Reference:** 10.7.4.5 in the License Exam Manual

## Question #4 of 210

Question ID: 606688

Hedge funds:

- I. are highly regulated.
- II. use investment techniques suitable for most investors.
- III. are unregulated.
- IV. use investment techniques most suitable for sophisticated investors.

- X **A)** II and III.
- ✓ **B)** III and IV.
- X **C)** I and IV.
- X **D)** I and II.

Explanation

Hedge funds are unregulated and have aggressively managed portfolio's employing investment techniques such as shorting positions, utilizing derivative products and trading on margin; all generally considered suitable for sophisticated investors.

**Reference:** 10.11 in the License Exam Manual

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**Question #5 of 210**

Question ID: 606554

SEC regulations for securities issued by investment companies prohibit which of the following?

- I. Closed-end funds from issuing preferred stock.
- II. Open-end funds from issuing preferred stock.
- III. Closed-end funds from issuing bonds.
- IV. Open-end funds from issuing bonds.

- X **A)** II and III.
- X **B)** I and III.
- ✓ **C)** II and IV.
- X **D)** I and IV.

Explanation

Closed-end funds may issue more than one class of security, including debt issues and preferred stock. Open-end funds may issue only one class of security: redeemable, voting common stock; they may not issue senior securities.

**Reference:** 10.2.1.1 in the License Exam Manual

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**Question #6 of 210**

Question ID: 606642

A purchase or redemption order for investment company shares must be executed at a price based on the:

- X **A)** net asset value last computed before the fund receives the order.
- X **B)** net asset value computed at the close of trading on the NYSE the day before the fund receives the order.
- ✓ **C)** net asset value next computed after the fund receives the order.
- X **D)** best net asset value computed the same day the fund receives the order.

Explanation

Purchase or redemption of mutual fund shares occurs at the net asset value next calculated after the fund receives the order; this is known as forward pricing.

**Reference:** 10.7.3.1 in the License Exam Manual

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**Question #7 of 210**

Question ID: 606507

An instrument that illustrates the transfer of title to any dividend, interest, or right that pertains to securities contracted for is called:

- ✓ **A)** a due bill.
- X **B)** a power of attorney.
- X **C)** a right.
- X **D)** a warrant.

Explanation

A due bill is an assignment of a forthcoming distribution from the seller to the new owner.

**Reference:** 9.1.4.1 in the License Exam Manual

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### Question #8 of 210

Question ID: 606597

If a customer submits a redemption order to her broker/dealer after the close of the New York Stock Exchange, she will receive a price based on the net asset value computed:

- ☐ A) the same day regardless of when the order is received.
- ☐ B) the previous business day.
- ☒ C) the next time the fund computes it.
- ☐ D) within the next 2 business days.

#### Explanation

Orders to redeem shares are executed at the next computed price.

**Reference:** 10.7.3.1 in the License Exam Manual

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### Question #9 of 210

Question ID: 606565

A transfer agent is responsible for all of the following EXCEPT:

- ☐ A) issuing new shares.
- ☒ B) safeguarding the physical assets of the investment company.
- ☐ C) distributing dividends and capital gains.
- ☐ D) canceling shares.

#### Explanation

The custodian, not the transfer agent, is responsible for safeguarding the physical assets of the investment company.

**Reference:** 10.3.4 in the License Exam Manual

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### Question #10 of 210

Question ID: 606654

An open-end investment company that does not distribute at *least* 90% of its net income:

- ☐ A) is unable to retain all or part of its realized capital gains.
- ☐ B) does not require a restricted type of management.
- ☐ C) continues to qualify as a registered investment company based on interpretations of the IRS.
- ☒ D) is liable for federal taxes on its net income.

#### Explanation

Investment companies that do not distribute at least 90% of their net investment income become liable for federal income taxes on all the net investment income. Shareholders would also be responsible for taxes on any distributions received. By distributing 90% of investment income, open-end companies can avoid double taxation.

**Reference:** 10.8.1.2 in the License Exam Manual

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### Question #11 of 210

Question ID: 606660

Last year, ABC Mutual Fund paid dividends of \$1.50 per share and distributed \$.80 per share in capital gains. The fund has a bid price of \$13.50 and an ask price of \$14.20. What is the fund's current yield?

- ☐ A) 0.1.
- ☒ B) 0.1056.
- ☐ C) 0.0492.
- ☐ D) 0.162.

#### Explanation

Find the current yield of mutual fund shares by dividing the annual dividend by the POP (ask price).  $\$1.50 \div \$14.20 = 10.56\%$ .

**Reference:** 10.8.1.3.1. in the License Exam Manual

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### Question #12 of 210

Question ID: 721451

Which of the following statements regarding fixed municipal unit trusts are TRUE?

- I. The trust is managed.
- II. The trust is not managed.
- III. The portfolio can be traded.
- IV. The portfolio cannot be traded.

- ☐ A) I and III.
- ☒ B) II and IV.
- ☐ C) I and IV.
- ☐ D) II and III.

#### Explanation

Fixed unit trusts are not managed; the portfolio of securities does not change. As bonds mature or are called, the proceeds are distributed pro rata to the unit holders. These units are redeemable by the issuer or its agent.

**Reference:** 10.1.1.2 in the License Exam Manual

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### Question #13 of 210

Question ID: 606543

Which of the following trade actively in the secondary market?

- I. Open-end funds.
- II. Closed-end funds.
- III. Unit investment trusts.
- IV. REITs.

- ☐ A) I and III.
- ☐ B) III and IV.
- ☐ C) I and II.
- ☒ D) II and IV.

#### Explanation

Closed-end funds and REITs trade actively in the secondary market. Open-end funds and unit investment trusts do not trade in the secondary market; instead, shares are redeemed by the issuer.

**Reference:** 10.1.1.3.1. in the License Exam Manual

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### Question #14 of 210

Question ID: 606574

Which of the following information should a registered representative obtain from a prospective client to ensure suitable investment recommendations?

- I. Professional society memberships.
- II. Languages spoken.
- III. Liquidity needs.
- IV. Number of dependents.

- ☐ A) I and III.
- ☐ B) II and IV.
- ☒ C) III and IV.
- ☐ D) I and II.

#### Explanation

Only information relevant to a prospective customer's investment needs and objectives is required to ensure suitable recommendations.

**Reference:** 10.5.1 in the License Exam Manual

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### Question #15 of 210

Question ID: 606498

One broker/dealer receives a don't know (DK) notice from another. Which of the following would be a reason for a DK to be sent?

- ☐ A) The broker/dealer who sent the DK is alerting the other broker that one of their clients has opened a new account with them.
- ☒ B) The broker/dealer who sent the DK was expecting 200 shares of ABC common stock and received 200 shares of ABC preferred shares.
- ☐ C) The broker/dealer who sent the DK wants to know if the other broker's customer wants to trade more stock at the same price.
- ☐ D) The broker/dealer who sent the DK is confirming that the trade specifications are good.

#### Explanation

DKs are sent between brokers when delivery is made that is either not expected or where the specifications of the delivery do not match what was expected.

**Reference:** 9.1.4 in the License Exam Manual

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### Question #16 of 210

Question ID: 606652

Investment clubs:

- I. can take advantage of breakpoints on mutual fund purchases.
- II. cannot take advantage of breakpoints on mutual fund purchases.
- III. are permitted to purchase new equity issues at the POP.
- IV. are not permitted to purchase new equity issues at the POP.

- ☒ A) II and III.
- ☐ B) II and IV.
- ☐ C) I and IV.
- ☐ D) I and III.

#### Explanation

Investment clubs are not considered restricted persons under the rules regarding sales of a new issue, and therefore are eligible to purchase new equity issues. Note that if a registered representative (a restricted person) were a member of an investment club, the club would be prohibited from buying a new equity issue. Investment clubs are never permitted to take advantage of breakpoints available on mutual fund purchases.

**Reference:** 10.7.5.1 in the License Exam Manual

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### Question #17 of 210

Question ID: 606632

Under the Conduct Rules, the maximum sales charge on any transaction involving an open-end investment company share is:

- ☒ A) 8.5% of the offering price.
- ☐ B) 9% of the offering price.
- ☐ C) 8.5% of the net asset value .
- ☐ D) 9% of the net asset value.

#### Explanation

Open-end investment companies (mutual funds) are limited to a maximum sales charge of 8.5% of the offering price.

**Reference:** 10.7.4 in the License Exam Manual

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### Question #18 of 210

Question ID: 606689

Which of the following statements are TRUE concerning hedge funds?

- I. They may not be suitable for discretionary accounts where account holders are not familiar with the risks associated with them.
- II. They are conservatively managed using no advanced or aggressive investment strategies without regulatory approval first.
- III. They may charge both an annual fee and a fee based on the funds' profits.
- IV. They are subject to the same rules as mutual funds.

- ✓ **A) I and III**
- X **B) II and III**
- X **C) II and IV**
- X **D) I and IV**

#### Explanation

Hedge funds utilize aggressive investment strategies and therefore might not be suitable for discretionary accounts where the customer may not be familiar or comfortable with the risks associated with the product. Because they are unregulated there are no limits to the fees they may charge.

**Reference:** 10.11 in the License Exam Manual

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### Question #19 of 210

Question ID: 606625

A mutual fund's unrealized loss last month results in which of the following?

- I. Lower NAV per share.
- II. Lower dividend payments to shareholders.
- III. Reduction in the proceeds payable to shareholders who liquidate their shares.
- IV. Higher tax liability to shareholders.

- X **A) II and III.**
- ✓ **B) I and III.**
- X **C) II and IV.**
- X **D) I and IV.**

#### Explanation

An unrealized loss is the same as a decrease in net asset value. An investor receives less at redemption than she would have received if the redemption had taken place before the asset's depreciation.

**Reference:** 10.7.3.2 in the License Exam Manual

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### Question #20 of 210

Question ID: 606570

If a mutual fund's objective is income, it would NOT hold which of the following securities in its portfolio?

- X **A) U.S. T-notes.**
- ✓ **B) Income bonds.**
- X **C) Preferred stock.**
- X **D) Corporate bonds.**

#### Explanation

A fund designed to generate current income for its shareholders would not hold an income bond, also known as an adjustment bond. Income bonds pay interest only if the issuer has enough earnings to do so. They are often issued by companies coming out of bankruptcy. As a result, these bonds tend to trade like zeroes.

**Reference:** 10.5.1.1.2 in the License Exam Manual

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### Question #21 of 210

Question ID: 606578

If a married couple with a long-term growth objective is considering a mutual fund and they are concerned about the fund's annual expenses, they should select a:

- ☐ A) preferred stock fund.
- ☐ B) common stock fund with a high portfolio turnover.
- ☒ C) common stock fund with a low portfolio turnover.
- ☐ D) long-term corporate bond fund.

Explanation

Of the choices given, common stock is the only vehicle capable of providing long-term growth. Preferred stock will provide dividends, but it will not provide much growth as it trades like a bond in line with interest rate changes. Of the two common stock funds, the one with the lower portfolio turnover will have lower annual expenses.

**Reference:** 10.5.1.1 in the License Exam Manual

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**Question #22 of 210**

Question ID: 606496

Which of the following items appears on the confirmation statement for a when-issued trade of municipal bonds?

- ☐ A) Total contract price.
- ☐ B) Settlement date.
- ☒ C) Principal or agency trade.
- ☐ D) Accrued interest.

Explanation

The capacity of the firm, principal or agent, must be disclosed on all confirms. The settlement date, accrued interest, and total price would not appear on a when-issued confirm.

**Reference:** 9.1.2.4 in the License Exam Manual

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**Question #23 of 210**

Question ID: 606561

Which of the following are functions of an investment company's custodian bank?

- I. Safekeeping of portfolio securities and cash.
- II. Providing portfolio advice regarding transactions.
- III. Maintaining asset records for the fund.
- IV. Safekeeping of customer securities.

- ☒ A) I and III.
- ☐ B) II and IV.
- ☐ C) II and III.
- ☐ D) I and IV.

Explanation

The custodian bank performs bookkeeping and clerical functions and retains the fund's cash and securities for safekeeping. The adviser offers portfolio advice and management services. The custodian provides for safekeeping of fund securities, not investors' securities.

**Reference:** 10.3.3 in the License Exam Manual

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**Question #24 of 210**

Question ID: 606581

If an investor wants to invest in the electronics industry but does not want to limit his investments to only one or two companies, which type of fund would be *most* suitable?

- ☐ A) Bond.
- ☒ B) Specialized.
- ☐ C) Hedge.
- ☐ D) Money market.

Explanation

A specialized or sector fund invests 25% or more of its assets in a particular region or industry.

**Reference:** 10.5.1.1.4 in the License Exam Manual

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### Question #25 of 210

Question ID: 606637

An investor redeems 200 shares of ABC Fund, which has no redemption fee. If the quote is \$12.05 bid \$13.01 asked, what amount will the investor receive?

- ☐ A) 2275.5.
- ☐ B) 1098.
- ☐ C) 2602.
- ☒ D) 2410.

#### Explanation

If a mutual fund has no redemption fee, the investor will receive the bid price per share (net asset value) multiplied by the number of shares being redeemed. In this case, the investor would receive \$2,410 (\$12.05 x 200 shares).

**Reference:** 10.7.6 in the License Exam Manual

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### Question #26 of 210

Question ID: 606573

If your great-grandmother is interested in safety, liquidity, and tax-free income, which of the following would you recommend?

- ☐ A) High yield income fund.
- ☐ B) Exploratory oil and gas pool.
- ☐ C) Income bonds.
- ☒ D) Insured short-term municipal bond fund.

#### Explanation

High-yield income funds usually invest in low-rated bonds; income bonds do not pay interest unless the board of directors declares a payment. An insured short-term municipal bond mutual fund is relatively safe, very liquid, and provides income free from federal tax.

**Reference:** 10.5.1.4.1 in the License Exam Manual

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### Question #27 of 210

Question ID: 606575

A retired customer was unhappy with the low yields paid by her CDs. In their first meeting, her registered representative recommended Class B shares of a long-term government bond fund, emphasized the safety of government bonds, and provided her with a prospectus. After signing a statement saying she had read and understood the prospectus, the customer invested all of her money in the fund. A year later, interest rates rose and the value of the fund declined. Having assumed the fund was government guaranteed, she was upset and became increasingly so when she learned that the deferred sales charge could cause her to lose additional money if she were to redeem her shares. Which of the following statements is TRUE?

- ☐ A) Since no one can predict interest rate moves, and the customer had read the prospectus, the bond fund was an appropriate investment.
- ☐ B) Because her money was originally in a single investment, it was suitable to move her funds into another single investment.
- ☒ C) The representative should have fully explained the features, charges, price fluctuations, and other characteristics of a bond fund before having the customer make such a substantial investment commitment.
- ☐ D) Because the fund invests in government bonds, it is government guaranteed and is therefore just as safe as a CD.

#### Explanation

This customer is used to low-risk investments. The prospectus must not only be supplied, but the risks fully explained as well.

**Reference:** 10.5.1.4 in the License Exam Manual

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### Question #28 of 210

Question ID: 606680



For a customer interested in buying an inverse exchange traded fund (ETF) tracking the performance of the Standard & Poor's 500 index, which of the following market views would make that purchase most inappropriate?

- ☐ A) Neutral
- ☐ B) Bearish
- ☐ C) Both bullish or bearish
- ☒ D) Bullish

Explanation

Inverse (reverse) ETFs are designed to deliver returns that are opposite of the benchmark index they are tracking. Therefore, buying an inverse ETF that tracks the S&P 500 index at a time when the market outlook is bullish would be most inappropriate. If the index rises with the anticipated bullish market, the fund that delivers returns that are the opposite of the index would fall in value.

**Reference:** 10.10.3 in the License Exam Manual

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**Question #29 of 210**

Question ID: 606527

If your client has a certificate registered in his own name, to be a good delivery, the certificate must be accompanied by:

- ☐ A) the promise that it has not been called for redemption.
- ☒ B) a properly-executed assignment to the brokerage firm on the reverse side of the certificate.
- ☐ C) the legal opinion, unless the client is selling municipal bonds.
- ☐ D) a buyer's option.

Explanation

If the certificate is registered in your client's name, a stock power or a properly executed assignment to the brokerage firm must appear on the reverse side of the certificate.

**Reference:** 9.2.2.1 in the License Exam Manual

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**Question #30 of 210**

Question ID: 606538

In which of the following markets would an investor expect to find closed-end investment company shares traded?

- I. A market maintained by the investment company itself.
- II. The over-the-counter market.
- III. The commodities market.
- IV. The exchanges.

- ☐ A) III and IV.
- ☐ B) I and II.
- ☒ C) II and IV.
- ☐ D) I and III.

Explanation

Closed-end company shares are like ordinary stock. Once issued, they trade on exchanges or in the over-the-counter market.

**Reference:** 10.1.1.3.1 in the License Exam Manual

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**Question #31 of 210**

Question ID: 606599

Which of the following statements *best* describes a breakpoint sale?

- ☒ A) Sale of investment company shares in dollar amounts slightly below the point at which the sales charge is reduced on quantity transactions, to make a higher commission.
- ☐ B) Sale of investment company shares in dollar amounts above the point at which the sales charge is reduced.
- ☐ C) Sale of investment company shares in anticipation of a distribution scheduled to be paid shortly.

- ☐ **D)** Compensation generated by commissions from a client who has reached another breakpoint, paid to the registered representative after he no longer works for the member.

Explanation

A breakpoint sale is a violation of the Conduct Rules. It occurs when a broker permits a client to purchase shares in an amount immediately below the amount that would qualify the client for a discounted sales charge, without informing him of the breakpoint.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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**Question #32 of 210**

Question ID: 606509

A confirmation of each customer trade must be given or sent:

- ☐ **A)** before the settlement date.
- ☐ **B)** on the trade date.
- ☒ **C)** on or before the settlement date.
- ☐ **D)** before the trade date.

Explanation

A confirmation must be sent to a customer on or before the completion of the transaction (the settlement date).

**Reference:** 9.1.1.4 in the License Exam Manual

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**Question #33 of 210**

Question ID: 606545

All of the following could be a redeemable security under the Investment Company Act of 1940 EXCEPT a(n):

- ☐ **A)** investment company security sold as a continuous initial public offering.
- ☒ **B)** security sold on an exchange at the market price buyers and sellers have established.
- ☐ **C)** security that pays out each investor's proportionate share of the company's assets.
- ☐ **D)** security issued by an open-end investment company.

Explanation

A redeemable security is purchased from and redeemed by the security's issuer. A security that can be traded on a secondary market is not redeemable. Open-end shares are redeemable securities, closed-end shares are not.

**Reference:** 10.1.1 in the License Exam Manual

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**Question #34 of 210**

Question ID: 606544

Which of the following investment company portfolios is supervised rather than managed?

- ☐ **A)** Real estate investment trust.
- ☐ **B)** Closed-end bond fund.
- ☒ **C)** Unit investment trust.
- ☐ **D)** Regulated open-end fund.

Explanation

A unit investment trust buys securities and holds them until redemption or until a specified future date. The securities in the portfolio are not traded, so no manager is needed. A REIT is not considered to be an investment company.

**Reference:** 10.1.1.2 in the License Exam Manual

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**Question #35 of 210**

Question ID: 606634

If the value of securities held in a fund's portfolio increases, and the amount of liabilities stays the same, the fund's net assets:

- ✓ **A)** increase.
- X **B)** are more liquid.
- X **C)** stay the same.
- X **D)** decrease.

Explanation

An appreciation in value of fund assets, without a corresponding increase in liabilities, leads to an increase in the fund's net asset value (total assets minus liabilities equals net assets).

**Reference:** 10.7.3 in the License Exam Manual

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### Question #36 of 210

Question ID: 606649

A breakpoint sale is defined as the sale of mutual fund shares in an amount:

- X **A)** at or above the dollar amount at which the sales charge is reduced.
- ✓ **B)** just below the dollar amount at which the sales charge is reduced.
- X **C)** required as the minimum investment in a fund as specified by the SEC.
- X **D)** just below the public offering price of the fund.

Explanation

The term "breakpoint sale" refers to the violation that occurs when a sale is made just below the point at which the investor would receive the reduced sales charge. The practice earns a higher commission for the salesperson but is not in the interest of the customer.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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### Question #37 of 210

Question ID: 786024

Regular way settlement for all of the following transactions must settle on the second business day after the trade date EXCEPT

- X **A)** for a customer selling a municipal bond through a broker/dealer
- X **B)** for a customer buying closed-end fund shares through a broker/dealer
- ✓ **C)** for a broker/dealer buying a Treasury bond for its own account
- X **D)** for a broker/dealer buying a corporate bond from another dealer

Explanation

Regular way settlement for U.S. government bonds occurs on the business day after the trade date (T + 1). Corporate bonds and closed-end funds settle regular way (T + 2). MSRB rules also require two-day settlement (T + 2) of municipal bond secondary transactions.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #38 of 210

Question ID: 606664

When calculating net investment income, an investment company includes:

- X **A)** just dividends plus interest.
- X **B)** only interest.
- ✓ **C)** dividends plus interest, minus operating expenses.
- X **D)** only dividends.

Explanation

Net investment income equals gross investment income minus operating expenses. Gross investment income is interest and dividends received from securities in the investment company's portfolio.

**Reference:** 10.8.1.1 in the License Exam Manual

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### Question #39 of 210

Question ID: 606510

A client places a sell stop order good for the day only. Under NYSE rules, you must:

- X **A)** partially write an order ticket and complete the ticket before market close.
- ✓ **B)** write an order ticket upon receipt of the order.
- X **C)** write an order ticket only if the order is executed.
- X **D)** partially write an order ticket and complete only upon execution.

#### Explanation

Order tickets must be written and time stamped upon receipt of the order.

**Reference:** 9.1 in the License Exam Manual

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### Question #40 of 210

Question ID: 606594

Which of the following is the *least* suitable mutual fund transaction?

- X **A)** Encouraging a retired 65-year-old investor to invest a small percentage of his savings in a large-cap growth fund.
- X **B)** Encouraging an investor in his early 30s to invest in an emerging markets mutual fund.
- X **C)** Encouraging an investor in a high-tax bracket with an income objective to invest in a municipal bond fund.
- ✓ **D)** Encouraging a mutual fund shareholder to switch from one fund family to another while a deferred load is in existence.

#### Explanation

Encouraging a mutual fund shareholder to switch from one fund family to another while a deferred load is in existence is not in the client's best interest, as the client might be subject to substantial additional sales charges.

**Reference:** 10.7.4.4 in the License Exam Manual

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### Question #41 of 210

Question ID: 786026

A customer buys a municipal bond regular way on Tuesday, December 23. The transaction will settle on the following

- X **A)** Monday
- ✓ **B)** Friday
- X **C)** Thursday
- X **D)** Tuesday

#### Explanation

Municipal bonds, like corporate bonds, settle 2 business days after the trade date. December 25 (Christmas) is not a business day.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #42 of 210

Question ID: 606677

Your customer is interested in a leveraged fund and makes the following statements about leveraged funds to you. All of the statements regarding leveraged funds are true EXCEPT

- X **A)** these funds sometimes use derivatives products to achieve their stated goals
- ✓ **B)** there are no unusual risks associated with these funds other than those one would incur with any index tracking fund
- X **C)** some leveraged funds are exchange-traded products
- X **D)** the funds attempt to return a multiple of the return of a benchmark index they are tracking, perhaps 2 or 3 times

#### Explanation

Because the fund objective is to achieve returns that are a multiple of the returns of the benchmark index, the result could be a multiple of any loss incurred by the benchmark index as well. In addition, because these funds utilize derivatives products to achieve their stated objectives, they may not be suitable for anyone that derivatives products are not suitable for, given the additional risks associated with those products.

**Reference:** 10.10.2 in the License Exam Manual

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### Question #43 of 210

Question ID: 606673

An investment adviser representative may describe dollar cost averaging to a customer as:

- ✓ **A)** a funding technique that will cause the average cost per share to be less than the average price per share.
- X **B)** a form of a mutual fund withdrawal plan.
- X **C)** a means of purchasing more shares when share prices are high.
- X **D)** a program for investing that will ensure profits even in a declining market.

#### Explanation

Dollar cost averaging is beneficial to the client because it achieves an average cost per share which is less than the average price per share over time. Using a fixed dollar amount each investment period it enables the investor to purchase more shares when prices are lower and fewer shares when prices are higher. While dollar cost averaging does not ensure profits in any market, nor does it ensure against losses, it is an economical and convenient method for acquiring shares.

**Reference:** 10.9.1.1.1 in the License Exam Manual

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### Question #44 of 210

Question ID: 606559

To make a public offering, a registered investment company must have a minimum net worth of:

- X **A)** \$10 million.
- ✓ **B)** 100000.
- X **C)** \$1 million.
- X **D)** \$100 million.

#### Explanation

Investment companies are not required to register an offering with the SEC unless they have a net worth of \$100,000.

**Reference:** 10.2.1 in the License Exam Manual

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### Question #45 of 210

Question ID: 606521

Regular way settlement for U.S. government bonds is:

- X **A)** two business days.
- X **B)** same day.
- X **C)** three business days.
- ✓ **D)** next business day.

#### Explanation

Regular way settlement of government bonds occurs on the next business day.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #46 of 210

Question ID: 606511

If a customer fails to return a proxy statement to a member firm by the 10th day before the annual meeting, the member may vote the shares:

- ✓ **A)** provided the matters to be voted on are of minor importance.
- X **B)** without restriction.

- X **C)** with the permission of the issuer.
- X **D)** under no circumstances.

Explanation

If a customer signs and returns a proxy statement and fails to indicate how the shares are to be voted, the member must vote the shares as recommended by management of the issuer. If, however, the customer does not return the proxy by the 10th day before the annual meeting, the member may vote the shares as it sees fit as long as the matters to be voted on are of minor importance. If the matters are of major importance (e.g., a merger or the issuance of additional shares), the member may never vote the shares.

**Reference:** 9.1.3 in the License Exam Manual

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**Question #47 of 210**

Question ID: 786021

A bona fide customer, upon request, may inspect a broker/dealer firm's

- X **A)** income statement
- X **B)** underwriting agreements
- X **C)** officers' personal holdings
- ✓ **D)** balance sheet

Explanation

The conduct rules require that a broker/dealer make available, for inspection to a customer, a copy of the firm's most recent balance sheet.

**Reference:** 9.1.1.7 in the License Exam Manual

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**Question #48 of 210**

Question ID: 606560

A FINRA member broker/dealer trading in shares of an open-end investment company may NOT buy shares of the fund:

- X **A)** at a discount from the public offering price.
- X **B)** for the firm's own investment purposes.
- X **C)** to cover existing orders.
- ✓ **D)** for the purpose of resale at a later date.

Explanation

A broker/dealer may buy shares only to fulfill existing orders or for its own investment account, not for inventory.

**Reference:** 10.3.5 in the License Exam Manual

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**Question #49 of 210**

Question ID: 606683

Your customer owns a leveraged ETF having a performance goal of 200% of the underlying Index. When purchased two weeks ago the ETF was priced at 50. If the index was up 10% the first week and down 20% the second week, what is the value of the ETF today if it performed as it was intended to?

- ✓ **A)** 36
- X **B)** 45
- X **C)** 40
- X **D)** 44

Explanation

Priced at 50 when purchased, after the first week's 10% increase in the index the 2X leveraged ETF would be up 20% ( $20\% \times 50 = 10$  point increase) to 60. After the second week's 20% decline in the index the 2X leveraged ETF would be down 40% ( $40\% \times 60 = 24$  point decrease) to 36.

**Reference:** 10.10.2 in the License Exam Manual

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**Question #50 of 210**

Question ID: 606495

If an order is executed for a customer and the registered representative (RR) later notices that he entered the wrong account number on the order ticket, what action must he take?

- ✓ **A)** Inform a principal, who will take or direct any action needed to correct the error.
- X **B)** Transfer the stock into his own account and pay for the purchase.
- X **C)** Contact that account's owner and ask if he wants to buy the stock.
- X **D)** Transfer the stock into the correct account.

Explanation

The representative should report the mistake and not take any action to remedy the mistake without the approval of a principal.

**Reference:** 9.1.1.3 in the License Exam Manual

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**Question #51 of 210**

Question ID: 606493

Which of the following interdealer trades does NOT settle in clearinghouse funds?

- X **A)** Corporate bonds.
- X **B)** GO bonds.
- ✓ **C)** U.S. government bonds.
- X **D)** OTC stocks.

Explanation

Trades in securities backed by the federal government are settled in federal funds, not clearinghouse funds.

**Reference:** 9.1.2.1 in the License Exam Manual

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**Question #52 of 210**

Question ID: 606515

Every transaction made by a registered representative for a customer's account

- X **A)** must be based on a written order from the customer.
- X **B)** is subject to cancellation by either party.
- X **C)** is subject to FINRA approval.
- ✓ **D)** must be reviewed by a principal of a FINRA member firm.

Explanation

FINRA does not approve transactions, and requiring customers to provide written instructions for each trade would be impractical. Transactions represent verbal contracts not subject to cancellation. A principal must review and approve every order either by signature or initials.

**Reference:** 9.1.1.2 in the License Exam Manual

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**Question #53 of 210**

Question ID: 606636

A father opens 4 custodial accounts for each of his children with the same mutual fund company. He invests \$15,000 in each account. The fund company has breakpoints at \$50,000, \$100,000, and \$200,000. The sales charge is:

- X **A)** based on a \$15,000 investment and is charged for each account.
- X **B)** based on the total \$60,000 investment and qualifies for the \$100,000 breakpoint.
- X **C)** ineligible for a breakpoint discount because these are custodial accounts.
- ✓ **D)** based on the total \$60,000 investment and qualifies for the \$50,000 breakpoint.

Explanation

An investment made by one person in 4 custodial accounts for his children at the same fund company would qualify for the breakpoint that is applicable to the total amount invested. In this case, \$60,000 was invested, so the applicable breakpoint is at \$50,000.

**Reference:** 10.7.5.1 in the License Exam Manual

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### Question #54 of 210

Question ID: 606614

If you invest in a front-end load mutual fund and choose automatic reinvestment, you should expect that:

- I. dividend distributions will be reinvested at net asset value.
- II. dividend distributions will be reinvested at the public offering price.
- III. capital gains distributions will be reinvested at net asset value.
- IV. capital gains distributions will be reinvested at the public offering price.

- ☐ A) I and IV.
- ☒ B) I and III.
- ☐ C) II and III.
- ☐ D) II and IV.

#### Explanation

Mutual funds that offer automatic reinvestment of dividends and gains distributions must do so at net asset value.

**Reference:** 10.7.5.3 in the License Exam Manual

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### Question #55 of 210

Question ID: 786018

Which of the following trades settle next business day?

- I. U.S. government debt
- II. U.S. government agency debt
- III. Municipal bonds
- IV. Listed options

- ☐ A) II and III
- ☐ B) I and II
- ☐ C) I and III
- ☒ D) I and IV

#### Explanation

U.S. government debt and listed options settle next day (T + 1); government agency debt and municipal bonds along with corporate securities are subject to regular way settlement of T + 2.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #56 of 210

Question ID: 606536

A customer is interested in an exchange-traded fund (ETF). With regard to the trading of ETFs, the customer should be aware that

- I. ETFs can be purchased throughout the trading day
- II. ETFs use forward pricing, the same as mutual funds do
- III. real-time quotes are available for ETFs
- IV. the NAV calculated at the end of the day, plus a sales charge, will equal the trading price

- ☒ A) I and III
- ☐ B) II and IV
- ☐ C) II and III
- ☐ D) I and IV

#### Explanation

ETFs can be traded throughout the trading day. Changing price quotes are available in real time as investors buy and sell. Although ETFs have an NAV that is calculated on the basis of the portfolio holdings, the trading price is determined by supply and demand in the open market, with customers paying commissions.

**Reference:** 10.1.1.3.4 in the License Exam Manual



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### Question #57 of 210

Question ID: 606522

In a proxy contest, a member firm holding securities in street name for clients who are beneficial owners must:

- ☐ A) vote the proxies as it wishes.
- ☐ B) send a list of the beneficial owners' names and addresses to the issuing company so that it may send proxy materials to those owners.
- ☒ C) send the proxy material to the beneficial owners at the issuing company's expense.
- ☐ D) send the proxy material to the beneficial owners at the member firm's expense.

#### Explanation

A securities firm that is a member of FINRA must forward all proxy material to the beneficial owners for all securities held in street name, and the issuers must bear the expense of shipping the proxy material.

**Reference:** 9.1.3.3 in the License Exam Manual

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### Question #58 of 210

Question ID: 606516

Which of the following must be included on a municipal securities order ticket?

- ☒ A) Indication of whether the order is solicited, unsolicited, or discretionary.
- ☐ B) Statement that the name of the contra party will be given on request.
- ☐ C) Broker/dealer firm's capacity.
- ☐ D) Statement that time of settlement will be given on request.

#### Explanation

Whether the trade is solicited, unsolicited, or discretionary on the order ticket. The other items, which may not be known yet, go on the confirmation.

**Reference:** 9.1.1.2 in the License Exam Manual

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### Question #59 of 210

Question ID: 606671

Your mutual fund has sent you a Form 1099, listing some long-term capital gains on which you must pay taxes. You are concerned that the 1099 is in error because you have owned your shares for only 4 months. Which of the following statements is TRUE?

- ☐ A) The gain need not be reported since you have not redeemed your shares, and therefore have not realized any gain.
- ☒ B) The 1099 is correct because in this case, the holding period to be considered is that of the investment company, not yours.
- ☐ C) The gain need not be reported since you have instructed the company to reinvest your dividends and capital gains, thus deferring your tax liability.
- ☐ D) The 1099 form is incorrect because you have held your shares for less than 1 year, which indicates a short-term gain.

#### Explanation

The investment company designated the gains as long term, because the company held the securities for more than a year before selling them. The holding period on your shares is relevant only if you redeem your shares for a gain.

**Reference:** 10.8.1.3 in the License Exam Manual

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### Question #60 of 210

Question ID: 606690

Your customer lists liquidity as an important investment objective. Which of the following would be least suitable to meet the liquidity requirement?

- ☒ A) Hedge funds
- ☐ B) Money market fund
- ☐ C) Preferred stock mutual fund
- ☐ D) A real estate investment trust (REIT)

#### Explanation

Of the choices listed, hedge funds would be the least liquid. Because they are unregulated they can require minimum holding periods during which time shareholders cannot make withdrawals. Mutual fund and money market fund shares can be readily redeemed and REITs are equity securities trading on exchanges and therefore considered liquid.

**Reference:** 10.11 in the License Exam Manual

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### Question #61 of 210

Question ID: 606523

You received a proxy in the mail from one of your customers. He signed it but did not specify a vote. Which of the following statements is TRUE?

- ☐ A) None of these..
- ☒ B) His proxy will be voted as recommended by management.
- ☐ C) He has transferred the power to specify a vote to your firm.
- ☐ D) He has given up the right to vote.

#### Explanation

If a customer returns a signed proxy and fails to indicate how the shares are to be voted, the member must vote the shares as recommended by management of the issuer.

**Reference:** 9.1.3.3 in the License Exam Manual

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### Question #62 of 210

Question ID: 606491

If a registered representative marked a solicited order ticket as unsolicited, this act is:

- ☐ A) a violation of FOMC regulations.
- ☐ B) permitted with the permission of a branch manager.
- ☐ C) prohibited by the markup policy.
- ☒ D) a violation of FINRA rules.

#### Explanation

It would be a violation of FINRA rules.

**Reference:** 9.1.1.2 in the License Exam Manual

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### Question #63 of 210

Question ID: 606618

A registered representative (RR) has just explained to a customer that to purchase a particular security the customer would pay the asking price plus a commission, not a sales charge. Which of the following is the RR is speaking of?

- ☒ A) Any closed-end fund
- ☐ B) All management company offerings
- ☐ C) Mutual funds
- ☐ D) All open-end funds

#### Explanation

Closed-end funds are purchased on an exchange or over the counter where buyers pay the ask price plus a commission. The RR could not be speaking of all open-end funds because mutual funds, one classification of open-end funds, are purchased at the POP, which includes a sales charge. Management company offerings include both open-end and closed-end funds.

**Reference:** 10.7.4.1 in the License Exam Manual

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### Question #64 of 210

Question ID: 606643

The maximum sales load may be charged on the purchase of shares from an open-end investment company that offers all of the following EXCEPT:

- X **A)** dividend reinvestment at NAV.
- X **B)** rights of accumulation.
- ✓ **C)** exchange privileges.
- X **D)** quantity discounts.

Explanation

Investment companies may charge the maximum sales load of 8.5% if they offer dividend reinvestment at NAV, rights of accumulation, and quantity discounts (breakpoints). If a fund offers none of these features, it cannot assess a sales charge of more than 6.25%.

**Reference:** 10.7.5 in the License Exam Manual

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**Question #65 of 210**

Question ID: 606627

Five years ago, the ABCD mutual fund bought 200,000 shares of Comet Industries at an average price of \$42.25. After a series of accounting scandals, the shares are now trading at \$6. If the fund decides to sell its shares, what will be the impact of the sale of Comet shares on the NAV of the ABCD fund?

- ✓ **A)** The NAV will not change.
- X **B)** The NAV will fall.
- X **C)** This depends on whether the fund can claim a tax loss on the sale.
- X **D)** The NAV will rise.

Explanation

Portfolio holdings in a mutual fund are marked to the market each day. Therefore, the NAV of the fund already reflects the current value of each security in its portfolio, including Comet Industries. When the fund sells the position, the value of the stock is replaced by an equivalent amount of cash, so net asset value does not change.

**Reference:** 10.7.3.2 in the License Exam Manual

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**Question #66 of 210**

Question ID: 606525

In a seller's option, securities may be delivered before the date specified if the seller

- X **A)** cannot deliver on the specified date.
- X **B)** gives notice to the buyer on the day of delivery .
- X **C)** wishes to be paid earlier.
- ✓ **D)** gives 1 day's written notice to the buyer.

Explanation

In a seller's option trade, the seller may (at his option) give the buyer written notice 1 day before making delivery.

**Reference:** 9.1.2.3 in the License Exam Manual

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**Question #67 of 210**

Question ID: 606604

All of the following describe the price of a no-load mutual fund EXCEPT:

- X **A)** NAV.
- X **B)** bid.
- ✓ **C)** POP.
- X **D)** book value.

Explanation

No-load open-end investment company shares are sold to investors and redeemed through the issuer at their book value, which is the same as their net asset value, or bid price.

**Reference:** 10.7.1.3 in the License Exam Manual

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### Question #68 of 210

Question ID: 606640

Reduced sales charges are allowed under all of the following circumstances EXCEPT:

- ☐ A) the customer signing a letter of intent.
- ☐ B) additional purchases that qualify for breakpoints under rights of accumulation.
- ☒ C) combining separate purchases made by a client and his business partner in their respective IRA accounts.
- ☐ D) a lump-sum purchase that qualifies for a breakpoint.

#### Explanation

Two unrelated adults may not combine transactions to receive a breakpoint.

**Reference:** 10.7.5 in the License Exam Manual

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### Question #69 of 210

Question ID: 606651

A broker/dealer selling open-end investment company shares will be required to return its entire selling concession if the principal underwriter has to repurchase those shares from a customer within how many business days of trade date?

- ☐ A) 30.
- ☒ B) 7.
- ☐ C) 15.
- ☐ D) 60.

#### Explanation

Any concession earned by the member selling the shares must be returned to the principal underwriter of the fund if the shares are redeemed within 7 business days of purchase.

**Reference:** 10.7.6.1 in the License Exam Manual

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### Question #70 of 210

Question ID: 606644

If a registered representative is seeking to sell shares of an investment company to a client, which of the following statements would be accurate and permissible regarding her recommendation?

- I. When the client redeems his shares, he will not immediately know their dollar value.
- II. If the client invests just before the dividend distribution, he can benefit by receiving the added value of that dividend.
- III. If the client purchases the shares of 2 or more funds in the same family of funds, he may be entitled to a reduced sales charge.
- IV. The purchase of Class B shares always provides the greatest return on investment.

- ☐ A) I and IV.
- ☐ B) II and III.
- ☐ C) II and IV.
- ☒ D) I and III.

#### Explanation

The purchase of two funds in the same family of funds may qualify an investor for combination privileges. At redemption, he will receive the next price calculated (forward pricing), which is not yet known. Class B shares, or deferred sales charge shares, may or may not provide the best return. Share class suitability can depend on the amount invested and the client's individual needs. Lastly, while the dividend is received if the fund shares are purchased before the ex-dividend date, there is no added value. The fund share price is reduced by the amount of the dividend on the ex-dividend date, just as it would be for a cash dividend paid on equity securities.

**Reference:** 10.7.5.4 in the License Exam Manual

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### Question #71 of 210

Question ID: 606583

Each of the following is a characteristic of money market funds EXCEPT:

- ☐ A) Offered without a sales load .

- X **B)** Stable NAV.
- X **C)** Portfolio of short-term debt instruments .
- ✓ **D)** High beta .

Explanation

Money market mutual funds invest in a portfolio of short-term debt instruments such as T-bills, commercial paper, and bankers acceptances. They are offered without a sales load or charge. The principal objective of the fund is to maintain a stable NAV (\$1 per share). Beta is a measure of volatility; money market funds have low betas.

**Reference:** 10.5.1.6 in the License Exam Manual

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**Question #72 of 210**

Question ID: 606537

When comparing exchange-traded funds (ETFs) to mutual funds, some features available in ETFs that are NOT found in the mutual funds would include the ability to:

- I. correlate to a specific index.
- II. sell short.
- III. be bought and sold on margin.
- IV. represent an entire portfolio, or basket of securities.

- X **A)** I and II.
- X **B)** III and IV.
- X **C)** I and IV.
- ✓ **D)** II and III.

Explanation

Unlike mutual fund shares, ETF shares can be traded on margin and sold short. They are similar in that they both represent an entire portfolio or basket of securities and both can have portfolios correlated to a specific index.

**Reference:** 10.1.1.3.4 in the License Exam Manual

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**Question #73 of 210**

Question ID: 606612

Selling mutual fund shares immediately below the dollar amount stated in the prospectus that would qualify an investor to receive a reduced sales charge is called

- X **A)** selling dividends.
- ✓ **B)** a breakpoint sale.
- X **C)** front running.
- X **D)** conditional orders.

Explanation

The term "breakpoint sale" refers to a sale made at a purchase amount just below a breakpoint (the point at which an investor would qualify for a quantity discount) for the obvious purpose of earning a higher commission.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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**Question #74 of 210**

Question ID: 606691

A customer is considering an investment in a hedge fund noting he has heard much about their high yield potential from a business acquaintance. In a discussion with him about these types of funds which of the following statements is TRUE?

- ✓ **A)** Hedge funds often use higher degrees of leverage and more sophisticated investment strategies than mutual funds.
- X **B)** Mutual funds are subject to less regulatory oversight than hedge funds.
- X **C)** Mutual funds pool investors' money and manage the entire portfolio with a single objective, whereas hedge funds manage each investor's assets separately to meet their individual investment objectives.
- X **D)** Hedge funds tend to be more suitable for many different customer profiles while mutual funds are generally more suitable for high net worth sophisticated investors only.

#### Explanation

Hedge funds utilize aggressive investment strategies not limited to selling securities short, and purchasing on margin. Often hedge funds have minimum initial investment requirements and lock-up provisions making withdrawals impossible for a period of time. These qualities of hedge funds make them less suitable for all investors and more suitable for high net worth and income (sophisticated) investors. Both mutual funds and hedge funds pool investors' money to manage a single portfolio of assets. Hedge funds are unregulated while mutual funds are regulated under the Investment Company Act of 1940.

**Reference:** 10.11 in the License Exam Manual

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### Question #75 of 210

Question ID: 606595

If two customers wish to combine their purchases of a mutual fund to take advantage of the fund's breakpoints, you should advise them that they may:

- ☐ A) not do so, because they both have accounts with the same broker/dealer.
- ☒ B) not do so, because two unrelated buyers may not receive a breakpoint.
- ☐ C) do so, provided that they have no business connection with the fund sponsor.
- ☐ D) do so, provided that they indicate the proportion that goes into each separate account.

#### Explanation

Two customers cannot combine their purchases to take advantage of a fund's breakpoints. Breakpoints are never allowed for investment clubs.

**Reference:** 10.7.5.1 in the License Exam Manual

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### Question #76 of 210

Question ID: 606611

A customer with an aggressive growth investment objective and short-term (6- to 12-month) time horizon wants to invest \$50,000 in a mutual fund. He has a substantial net worth, but none of it is invested in mutual funds. You inform him that mutual fund investments are intended to be long-term investments, but he expresses his intention to make the short-term investment anyway. If the XYZ fund family (one you have dealt with in the past) offers an aggressive growth fund that has a respectable track record, your recommendation should be to:

- ☐ A) buy the XYZ Aggressive Growth Class B shares with a declining CDSC and .75% 12b-1 fee.
- ☒ B) buy the XYZ Aggressive Growth Class C shares with a 1% CDSC expiring in 1 year and .75% 12b-1 fee.
- ☐ C) buy the XYZ Aggressive Growth Class A shares with a 4% load and .25% 12b-1 fee.
- ☐ D) decline the transaction because short-term trading of funds is not allowed.

#### Explanation

If the client insists on making this type of investment, then the Class C shares are most appropriate for this customer's objectives; the sales load would be lower than that of either Class A or Class B shares.

**Reference:** 10.7.5.5 in the License Exam Manual

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### Question #77 of 210

Question ID: 606661

Which of the following statements describe the conduit theory of taxation?

- I. A fund is not taxed on earnings it distributes provided distributions equal 90% or more of net investment income.
- II. Earnings distributed by a regulated investment company are taxed three times.
- III. Dividends and interest are passed through to the investor without the fund being taxed.
- IV. Dividends and interest accumulate tax free to the shareholder.

- ☒ A) I and III.
- ☐ B) II and IV.
- ☐ C) II and III.
- ☐ D) I and IV.

#### Explanation

Under the conduit, or pipeline, theory of taxation, a fund is liable for taxes only on the income retained, provided it distributes at least 90% of its net investment income. The investor benefits because the income is only taxed twice (at the corporate level and at the individual level), and avoids taxation at the fund level. There is no tax-free accumulation

for the shareholder.

**Reference:** 10.8.1.2 in the License Exam Manual

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### Question #78 of 210

Question ID: 606569

The primary objective of a particular mutual fund is the payment of dividends, regardless of the market's current state. Capital growth is a secondary objective. Which of the following industry groups would be appropriate for the fund's portfolio?

- ☐ A) Computer technology.
- ☒ B) Public utilities.
- ☐ C) Aerospace.
- ☐ D) Consumer appliances.

#### Explanation

Utilities are defensive industries; they tend to pay dividends consistently.

**Reference:** 10.5.1.1.2 in the License Exam Manual

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### Question #79 of 210

Question ID: 606686

A customer of a registered representative is considering a hedge fund investment and asks what the lock-up period means? The registered representative correctly explains it is

- ☐ A) the length of time that is required to have the hedge fund registered with the SEC during which time the fund may not sell any shares
- ☐ B) the minimum length of time the hedge fund portfolio manager intends to hold any single investment within the portfolio
- ☐ C) a period of time during which the fund manager will not make any changes (purchases or sales) within the hedge fund portfolio
- ☒ D) a period of time during which liquidation of fund shares is prohibited by the fund, which means that there is an element of illiquidity to be considered

#### Explanation

Hedge funds generally employ a lock-up provision to ensure that capital invested by shareholders will remain with the fund long enough to ensure the manager's ability to implement the intended fund strategy and to begin to see the results of that strategy. There is no standard lock-up period, which can differ from fund to fund, and it should always be noted that during the lock-up period, the investment is essentially rendered illiquid.

**Reference:** 10.11.1 in the License Exam Manual

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### Question #80 of 210

Question ID: 606630

All of the following events will affect the NAV per share of a mutual fund EXCEPT:

- ☐ A) The fund pays dividends to its shareholders.
- ☐ B) The fund receives cash dividends on the securities in its portfolio .
- ☒ C) Wholesale redemption of fund shares .
- ☐ D) Changes in the market value of the fund's portfolio of securities .

#### Explanation

Dividends paid and received by the fund directly affect NAV. Changes in the portfolio value affect NAV because the securities are marked to market daily. While share redemption will reduce total net asset value, the number of shares outstanding decreases in proportion, so the NAV per share stays the same.

**Reference:** 10.7.6 in the License Exam Manual

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### Question #81 of 210

Question ID: 606648

A retiree contacts an agent to discuss investing his retirement savings of approximately \$2.1 million; his investment objective is long-term growth. The representative and customer discuss the advantages and disadvantages of diversifying among 5 different mutual funds within 2 fund families, as opposed to purchasing just 1 fund. Consequently, the agent made the following purchase recommendations:

XYZ Emerging Growth Class B \$495,000  
XYZ Research Class B \$310,000  
XYZ Investors Growth Stock Class B \$495,000  
ABC Capital Enterprise Class B \$495,000  
ABC Capital Opportunity Class b \$310,000  
Total \$2,105,000

These recommendations are:

- ☐ A) unsuitable because the investments are not equal in amount.
- ☒ B) unsuitable because Class A shares in either (or both) fund family could be purchased for a sales charge breakpoint discount at or near 0%.
- ☐ C) suitable because the customer fully understands all of the ramifications and is satisfied.
- ☐ D) suitable because they achieve the diversification the customer seeks.

#### Explanation

Class A shares, in most mutual funds, provide breakpoint sales charge discounts so there is no sales charge when purchasing \$1 million worth of shares (or less in some cases). Class A shares also have lower operating expenses than Class B shares. This retired investor would be subject to back-end loads with Class B shares if the funds were needed unexpectedly within a few years.

**Reference:** 10.7.5.5 in the License Exam Manual

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## Question #82 of 210

Question ID: 606550

If an investment company invests in a fixed portfolio of municipal or corporate bonds, it is classified as a:

- ☐ A) growth fund.
- ☐ B) utilities fund.
- ☒ C) unit investment trust.
- ☐ D) closed-end company.

#### Explanation

A unit investment trust issues shares that represent units of a particular portfolio; management has no authority, or only limited authority, to change the portfolio. The portfolio is fixed, it is not traded.

**Reference:** 10.1.1.2 in the License Exam Manual

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## Question #83 of 210

Question ID: 606631

When discussing mutual funds with a customer, each of the following statements are prohibited EXCEPT:

- ☐ A) Get a few friends to join with you to form an investment club and you may qualify for a breakpoint.
- ☒ B) Buy shares of different funds in the same fund family and you may qualify for a breakpoint on the total purchase.
- ☐ C) The income yield of the fund consists of both dividends and capital gains.
- ☐ D) Buy the shares on record date in order to receive the dividend. .

#### Explanation

Most funds provide a combination privilege, allowing investors to aggregate purchases made in different funds in the same family to qualify for a breakpoint. The income yield of a mutual fund includes dividends only. A group of friends is not eligible for a breakpoint (investment clubs are not eligible). "Selling dividends" is a prohibited practice because of the immediate tax liability incurred with the dividend and share price adjustment that results after the dividend distribution.

**Reference:** 10.7.5.1 in the License Exam Manual

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### Question #84 of 210

Question ID: 606674

An investor who makes transactions once a month using dollar cost averaging would:

- ☐ A) buy the same number of shares of a stock.
- ☒ B) buy the same dollar amount of stock.
- ☐ C) put equal amounts of money in a bond and stock mutual fund.
- ☐ D) allocate assets equally among cash, stocks, and bonds.

#### Explanation

In the dollar cost averaging investment strategy, the amount of dollars invested each month remains constant. Accordingly, the investor will automatically buy more shares when the price is low to reduce the average cost per share.

**Reference:** 10.9.1.1.1 in the License Exam Manual

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### Question #85 of 210

Question ID: 786023

A customer sells \$5,000 worth of a security in a cash account and on the same day purchases \$8,000 worth of a different security in the same account. At the close of the 4th business day following these transactions, no payment has been received from the customer and no extension has been obtained. Assuming no change in market value, the firm must

- ☐ A) cancel both the purchase and the sale and freeze the account for 90 days
- ☐ B) liquidate \$5,000 of securities and freeze the account for 90 days
- ☐ C) liquidate the \$8,000 transaction and freeze the account for 90 days
- ☒ D) liquidate \$3,000 of securities and freeze the account for 90 days

#### Explanation

When an investor buys and sells different securities in the same account on the same day, the two transactions can be netted against each other to determine whether money is due to the client or the client owes money to the firm. In this question the client owes the firm \$3,000 (an \$8,000 purchase netted against a \$5,000 sale). According to Regulation T, the investor has 2 additional business days after settlement (4 days total) to pay the amount owed. Since he has failed to do so and no extension has been obtained, the unpaid-for portion of the trade, which is \$3,000, will be liquidated and, according to Regulation T, the account will be frozen for 90 days.

**Reference:** 9.1.2.5.2 in the License Exam Manual

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### Question #86 of 210

Question ID: 606589

The management fees paid by an investment company are part of:

- ☐ A) the sales load.
- ☐ B) the underwriting agreement.
- ☐ C) the custodial fees.
- ☒ D) the operating expense of the fund.

#### Explanation

The management fees paid by an investment company are part of the operating expenses of the fund. Custodial fees are also part of the operating expenses. A sales load is a selling cost contained within the underwriting agreement.

**Reference:** 10.6.2.2 in the License Exam Manual

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### Question #87 of 210

Question ID: 606505

A customer's sell-at-market order was reported as executed at 29.75. Later it was discovered that the report was an error; the trade actually was executed at 29.50. Which of the following is TRUE?

- ☐ A) The customer must receive the 29.75.
- ☐ B) The customer may choose to receive either 29.50 or 29.75.
- ☐ C) The customer may choose to cancel the order.

- ✓ **D)** The customer must accept the 29.50.

Explanation

A market order means the customer states that he is willing to accept the best price at the time of execution. A mistake made in reporting does not alter that fact.

**Reference:** 9.1.1.3.1 in the License Exam Manual

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**Question #88 of 210**

Question ID: 606592

After a mutual fund's tenth year, performance statistics must show results for each of the following periods EXCEPT:

- X **A)** 10 years.
- X **B)** 1 year.
- X **C)** 5 years.
- ✓ **D)** 3 years.

Explanation

Mutual fund performance statistics must show results for 1, 5, and 10 years, or the life of the fund, whichever is shorter.

**Reference:** 10.6.1 in the License Exam Manual

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**Question #89 of 210**

Question ID: 606549

Closed-end investment company shares may be:

- I. traded in the secondary markets, including the exchanges and OTC markets.
- II. sold in the OTC primary market only.
- III. redeemed by the closed-end investment company.
- IV. traded by institutional investors.

- X **A)** II and III.
- X **B)** I and II.
- ✓ **C)** I and IV.
- X **D)** III and IV.

Explanation

Once a closed-end investment company has distributed shares, those shares are traded in the secondary market by both individual and institutional investors.

**Reference:** 10.1.1.3.1 in the License Exam Manual

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**Question #90 of 210**

Question ID: 606653

Last year, ABC Mutual Fund paid dividends of \$1.50 per share and distributed \$.80 per share in capital gains. The fund has a bid price of \$13.50 and an asked price of \$14.20. An investor who purchased shares in this fund 9 months before the distributions receives \$100 in eligible dividend income and \$53 in capital gains. If this is the individual's only investment, he will:

- I. not be required to pay any federal taxes on the dividend income.
- II. be required to pay federal taxes at the ordinary income rate on the dividend income.
- III. be required to pay capital gains tax on \$53.
- IV. not be required to pay capital gains tax on \$53.

- X **A)** II and IV.
- ✓ **B)** II and III.
- X **C)** I and IV.
- X **D)** I and III.

Explanation

Investors are required to pay taxes on all distributions from mutual funds, whether reinvested or received in cash.

**Reference:** 10.8.1.3.4 in the License Exam Manual

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### Question #91 of 210

Question ID: 606646

A customer seeks a significant long-term investment in the Ajax fund, a growth-oriented mutual fund. To take advantage of breakpoints applicable to large investments, the customer should purchase:

- ☐ A) Class D shares.
- ☐ B) Class B shares.
- ☐ C) Class C shares.
- ☒ D) Class A shares.

#### Explanation

For initial purchases, breakpoints are only available if the customer purchases Class A shares, which are sold with a front-end load deducted from the initial investment. A substantial purchase can often reduce the sales charge to zero. Class-B and Class-C shares are sold with annual 12b-1 fees as well as a contingent deferred sales charge. Class D shares are sold with a level sales load plus a redemption fee.

**Reference:** 10.7.5.5 in the License Exam Manual

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### Question #92 of 210

Question ID: 606667

Which of the following constitutes selling dividends?

- ☐ A) Encouraging investors to postpone purchases of mutual fund shares until after the ex-date for a dividend distribution.
- ☒ B) Enticing customers to buy mutual fund shares just before the ex-dividend date.
- ☐ C) Encouraging customers to sell their mutual fund shares just before the ex-dividend date.
- ☐ D) Withdrawing dividends, rather than reinvesting them in additional shares.

#### Explanation

Selling dividends is an unethical sales practice in which a member intentionally misleads customers into believing they will receive the equivalent of a rebate on their investments because the fund will soon pay a distribution. The customers suffer out-of-pocket losses because the cash immediately coming back is dividend income subject to tax. At the same time, the NAV of the fund is reduced.

**Reference:** 10.8.1.3.3 in the License Exam Manual

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### Question #93 of 210

Question ID: 606629

All of the following are redeemable securities EXCEPT:

- ☐ A) variable annuities.
- ☒ B) REITs.
- ☐ C) unit investment trusts.
- ☐ D) mutual funds.

#### Explanation

A redeemable security has no secondary market. To sell (redeem) a redeemable security, the investor must go back to the issuer or its agent. REITs trade in the secondary markets either on exchanges or OTC.

**Reference:** 10.7.6 in the License Exam Manual

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### Question #94 of 210

Question ID: 606489

Of the following customer services, which must a broker dealer provide with no service charge?

- ☐ **A)** Safekeeping of customer's securities, exchanges, or transfer
- ☐ **B)** Collection of customer's interest or dividends
- ☒ **C)** Forwarding of proxy material to the customer
- ☐ **D)** Loans made to customers

Explanation

The Conduct Rules permit FINRA members to charge reasonable fees to their customers for a variety of services. Included in chargeable services are the collection of interest and dividends, finding a buyer for a client who wishes to sell a relatively illiquid investment, and holding customers' securities in safekeeping. Members may also charge interest on loans made to customers. However, the expenses associated with sending proxy statements to customers whose securities are being held in trust by the member cannot be charged to the customer. Instead, the member may seek (and receive) reimbursement from the issuer for these expenses, since the issuer would have incurred these expenses had the customer/shareholder been holding the securities directly.

**Reference:** 9.1.3.3 in the License Exam Manual

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**Question #95 of 210**

Question ID: 606635

An investment company share purchased at its NAV that can always be redeemed later at its then-current NAV is a:

- ☒ **A)** Class C share.
- ☐ **B)** Class A share.
- ☐ **C)** Class B share.
- ☐ **D)** Class D share.

Explanation

Class A shares are purchased at NAV plus sales charge. Class B shares pay the sales charge upon redemption. Class D shares have a level load plus a redemption fee. Class C shares have only a level load (a 12b-1 fee) which is taken from net assets during the year.

**Reference:** 10.7.5.5 in the License Exam Manual

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**Question #96 of 210**

Question ID: 606681

A customer of your broker/dealer is bullish on US equity securities across a broad spectrum of industries. He would like to participate in an anticipated upward movement of an equity stock index. Which of the following investments would you recommend as being closely related to the movement of equities in general?

- ☐ **A)** Variable rate demand obligations (VRDOs)
- ☐ **B)** Real Estate Investment Trusts (REITs)
- ☒ **C)** Standard & Poor's depository receipts (SPDRs)
- ☐ **D)** American depository receipts (ADRs)

Explanation

The spider (SPDR) is an index fund designed to replicate and track the performance of the S&P 500, a broad based equity index.

**Reference:** 10.10.1 in the License Exam Manual

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**Question #97 of 210**

Question ID: 606626

One of your clients purchased shares of the Ajax Mutual Fund several months ago. At that time, the NAV of the fund was \$17.20. Today, the NAV is \$17.56 and your client wants to know what accounts for the difference. You should advise him that the difference likely represents:

- ☐ **A)** capital losses.
- ☒ **B)** unrealized appreciation.
- ☐ **C)** realized appreciation.
- ☐ **D)** capital gains.

Explanation

The NAV of mutual funds is marked to the market daily; the increase reflects higher market prices for the securities in the fund's portfolio.

**Reference:** 10.7.3.2 in the License Exam Manual

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### Question #98 of 210

Question ID: 606615

When a customer transfers the proceeds of a sale from one fund to another within the same family of funds, what are the tax consequences?

- ☐ A) Losses are deducted at the time of the transfer, but gains are deferred until the final redemption.
- ☒ B) All gains and losses are recognized on the transfer date.
- ☐ C) No gains or losses are recognized until the final redemption.
- ☐ D) Gains are taxed at the time of the transfer, but losses are deferred until the final redemption.

#### Explanation

Although a transfer within a family of funds is generally not subject to a sales charge, the customer is liable for any taxes due. The IRS considers this transaction a sale and a purchase. Any losses or gains must be declared on that year's tax form.

**Reference:** 10.7.5.4.1 in the License Exam Manual

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### Question #99 of 210

Question ID: 606556

Which of the following may be done only with the approval of the shareholders of an investment company?

- I. A change from diversified to nondiversified status.
- II. The purchase of particular bonds on the open market.
- III. Personnel changes in the transfer agent's organization.
- IV. A change in the fund's objectives.

- ☐ A) II and III.
- ☐ B) I and III.
- ☒ C) I and IV.
- ☐ D) II and IV.

#### Explanation

Any substantive change in an investment company's form, structure, investment objective, or business operation must be approved by a majority vote of the outstanding shares. Bond purchases are left to the fund's portfolio manager, and the transfer agent is trusted with its organization's personnel changes.

**Reference:** 10.2.2.1 in the License Exam Manual

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### Question #100 of 210

Question ID: 640160

Mutual fund Class B shares assess

- ☒ A) a deferred sales load
- ☐ B) a front-end load
- ☐ C) no load
- ☐ D) a level load

#### Explanation

Class B shares carry a deferred sales load. This is sometimes referred to as a back-end load. Class A shares carry a front-end load. Class C shares charge a 12b-1 fee quarterly with a small back-end load in the first year.

**Reference:** 10.7.5.5 in the License Exam Manual

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### Question #101 of 210

Question ID: 606607

A client invests \$2,200 in an open-end investment company and signs a letter of intent for a \$10,000 breakpoint. If he deposits \$11,000 6 months later, which of the following statements is TRUE?

- ☐ A) He will receive a reduced load on \$8,800 worth of the shares.
- ☒ B) He will receive a reduced load on \$13,200 worth of the shares.
- ☐ C) He will receive a reduced load on \$10,000 worth of the shares.
- ☐ D) He will not receive any reduction in the sales load.

Explanation

An investor signing a letter of intent has 13 months to contribute funds to reach the reduced load. The sales charge in this case, then, will be based on the total investment of \$13,200. If at the end of the 13 months the investor had not invested up to the breakpoint, the fund would liquidate enough shares to pay the difference in sales load.

**Reference:** 10.7.5.1.1 in the License Exam Manual

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**Question #102 of 210**

Question ID: 721455

Wanting to be clear about an upcoming mutual fund dividend distribution, a shareholder does some research on his own. He comes away with what he thinks are all correct understandings, but one of them is not. Which is the incorrect understanding?

- ☒ A) An investor is not liable for taxes if he automatically reinvests the distributions.
- ☐ B) Dividend distributions are not guaranteed to occur annually, quarterly, or at any time.
- ☐ C) An investor can receive dividends in the form of cash or choose to reinvest them in more fund shares.
- ☐ D) The dividends are paid from the fund's net investment income.

Explanation

Mutual funds pay dividends from net investment income, and shareholders are liable for taxes on all distributions, whether reinvested or taken in cash. Dividend distributions from mutual funds like individual corporate dividend distributions are not guaranteed.

**Reference:** 10.8.1 in the License Exam Manual

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**Question #103 of 210**

Question ID: 606679

Inverse exchange-traded funds (ETFs), also known as reverse or short funds, are managed to

- ☒ A) perform contrary to a benchmark market index such as the S&P 500
- ☐ B) be profitable only when interest rates are rising
- ☐ C) outperform a benchmark market index such as the S&P 500
- ☐ D) be used only by professional traders and market makers

Explanation

Inverse funds, which are also commonly referred to as "short" funds, try to deliver returns that are the opposite of the benchmark index they are tracking. When they are exchange traded, they can be bought on margin and are priced throughout the trading day like other exchange-traded products. They are available to individual public investors and firm proprietary traders as well.

**Reference:** 10.10.3 in the License Exam Manual

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**Question #104 of 210**

Question ID: 606490

All of the following information must be on an order ticket EXCEPT:

- ☐ A) number of shares.
- ☒ B) price of a market order.
- ☐ C) stock symbol.
- ☐ D) time stamp.

Explanation

Price would not be included on a ticket for a market order, but it would be on the ticket for a limit, stop, or stop limit order.

**Reference:** 9.1.1.2 in the License Exam Manual

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### Question #105 of 210

Question ID: 606526

A municipal bond in default is in good delivery form if

- I. past-due and current coupons are attached
- II. the bond is insured
- III. subsequently due coupons are attached
- IV. the issuer files a default guarantee letter with the MSRB

- ☐ A) II and III
- ☐ B) I and IV
- ☐ C) II and IV
- ☒ D) I and III

#### Explanation

To be in good delivery form, a municipal bond must be accompanied by all unpaid coupons: past due, currently due, and subsequently due. Insurance or letters of guarantee do not constitute good delivery.

**Reference:** 9.2.1.5 in the License Exam Manual

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### Question #106 of 210

Question ID: 786028

Under the Uniform Practice Code, regular way transactions for common stock settle on the

- ☐ A) same day as the trade date
- ☒ B) 2nd business day following the trade date
- ☐ C) next business day following the trade date
- ☐ D) 4th business day following the trade date

#### Explanation

Under the Uniform Practice Code, regular way trades settle 2 business days after the trade date (T+2). Cash settlement for a trade occurs on the same day as the trade date, and Regulation T settlement is T+4.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #107 of 210

Question ID: 606609

A shareholder invested in a mutual fund and has signed a letter of intent to invest \$25,000. Her original investment was \$13,000, and her current account value is \$17,000. For her to complete the letter, she must deposit:

- ☐ A) 13000.
- ☒ B) 12000.
- ☐ C) 27000.
- ☐ D) 8000.

#### Explanation

Under a letter of intent, the full contribution is required for the letter to be completed. Appreciation is not considered.

**Reference:** 10.7.5.1.1 in the License Exam Manual

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### Question #108 of 210

Question ID: 606533

A prospectus must be delivered to customers in the sale of all of the following transactions EXCEPT

- ☐ A) new issues of registered common stock
- ☒ B) exchange traded funds (ETFs) trading in the secondary market
- ☐ C) unit investment trusts
- ☐ D) mutual funds

Explanation

Exchange traded funds trading in the secondary market, like other securities that are already trading in the secondary market, do not require the delivery of a prospectus.

**Reference:** 10.1.1.3.4 in the License Exam Manual

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**Question #109 of 210**

Question ID: 606656

Capital gains distributed by a mutual fund to shareholders are reported and taxable for the year:

- ☐ A) the shares are redeemed by the fund.
- ☐ B) paid by the fund.
- ☐ C) the shareholder chooses but not later than 2 years after all shares are redeemed.
- ☒ D) earned (accrued).

Explanation

Capital gains can be distributed to shareholders by a mutual fund no more than once per year and are reported and taxable for the year earned (accrued).

**Reference:** 10.8.1.3 in the License Exam Manual

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**Question #110 of 210**

Question ID: 606658

Your customer redeemed 200 of her 500 Kapco common shares without designating which shares were redeemed. Which of the following methods does the IRS use to determine which shares she redeemed?

- ☒ A) FIFO.
- ☐ B) Identified shares.
- ☐ C) Wash sale rules.
- ☐ D) LIFO.

Explanation

When a customer does not choose a method, the IRS uses FIFO (first in, first out). This will likely result in shares with the lowest cost basis being redeemed first, which creates a greater taxable gain.

**Reference:** 10.8.1.5.1 in the License Exam Manual

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**Question #111 of 210**

Question ID: 606546

Which of the following statements regarding a unit investment trust is NOT true?

- ☐ A) It is considered an investment company.
- ☐ B) It charges no management fee.
- ☐ C) It invests according to stated objectives.
- ☒ D) Overall responsibility for the fund rests with the board of directors.

Explanation

A unit investment trust has no board of directors; rather, it has a board of trustees. A UIT must follow a stated investment objective (as must any investment company) and does not charge a management fee because it is not a managed portfolio.

**Reference:** 10.1.1.2 in the License Exam Manual

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### Question #112 of 210

Question ID: 721453

A customer begins to explain what he understands about open-end investment companies registered as mutual funds. He makes several statements, all of which are correct EXCEPT

- ☐ A) if I want to sell my shares, the fund must redeem them no matter how many I want to sell within 7 days of my order
- ☒ B) I can purchase or sell these shares during normal trading hours at the current market value at the time my order is entered
- ☐ C) the fund can sell new shares in any amount at any time it wants to
- ☐ D) if I invest in fund shares, it gives me mutual ownership of all of the assets in the fund portfolio

#### Explanation

An open-end investment company registered as a mutual fund may sell any quantity of new shares, must redeem shares within 7 days, and provides for mutual ownership of portfolio assets by shareholders. For purchases and redemptions mutual funds use forward pricing which means that all transactions will be done at the next calculated net asset value (NAV) after an order is received.

**Reference:** 10.7.6 in the License Exam Manual

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### Question #113 of 210

Question ID: 606566

A mutual fund must, at a minimum, provide which of the following periodic reports to shareholders?

- I. Audited annual reports.
- II. Unaudited annual reports.
- III. Audited semiannual reports.
- IV. Unaudited semiannual reports.

- ☒ A) I and IV.
- ☐ B) II and III.
- ☐ C) II and IV.
- ☐ D) I and III.

#### Explanation

An investment company must send an unaudited report to shareholders at least semiannually and an audited report of its financial condition at least annually.

**Reference:** 10.4.2 in the License Exam Manual

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### Question #114 of 210

Question ID: 786027

A municipal bond transaction is labeled T+2. This means that

- ☒ A) the trade is settled regular way in 2 business days
- ☐ B) it is a dealer-to-dealer trade involving a 3% markup
- ☐ C) the bond has 3 months of accrued interest
- ☐ D) the bond was issued at a premium of 3 points over par

#### Explanation

T+2 means settlement takes place 2 business days after the trade. This is regular way settlement.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #115 of 210

Question ID: 606633

Under the Investment Company Act of 1940, redemption payments for mutual fund shares must be made within how many days?

- ☒ A) 7.
- ☐ B) 5.
- ☐ C) 10.

X **D)** 15.

Explanation

Under the Investment Company Act of 1940, if a customer tenders mutual fund shares for redemption, payment must be made within 7 calendar days, unless the NYSE is closed on other than a weekend or holiday, or the SEC grants an exception.

**Reference:** 10.7.6 in the License Exam Manual

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**Question #116 of 210**

Question ID: 721454

Certain events will affect the net asset value (NAV) per share of a mutual fund. Which of the following events will NOT affect NAV?

- X **A)** The value of the fund portfolio's securities fluctuating
- X **B)** The fund paying dividends to its shareholders
- ✓ **C)** Fund shares being redeemed by the fund upon the request of shareholders
- X **D)** The fund receiving cash dividends on the securities in its portfolio

Explanation

Dividends paid and received by the fund directly affect NAV. Changes in the portfolio value affect NAV because the securities are marked to market daily. Although share redemption will reduce total net asset value, the number of shares outstanding decreases in proportion, so the NAV per share stays the same.

**Reference:** 10.7.6.1 in the License Exam Manual

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**Question #117 of 210**

Question ID: 606514

A confirmation sent to a customer must include:

- X **A)** amount of any commission.
- X **B)** whether the member acted as agent or principal.
- X **C)** markup or markdown if the member acted as a principal in a Nasdaq security.
- ✓ **D)** all of these.

Explanation

A customer confirmation must disclose the amount of markup for a principal transaction in a Nasdaq security, whether the member acted in an agency or a principal capacity, and the amount of commission if the member acted as an agent.

**Reference:** 9.1.1.4 in the License Exam Manual

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**Question #118 of 210**

Question ID: 606639

A front-end sales load is defined as the:

- ✓ **A)** difference between the public offering price and the net asset value of a mutual fund share.
- X **B)** commissions paid on the purchase or sale of securities.
- X **C)** concessions allowed on the purchase or sale of securities.
- X **D)** fee paid to the investment adviser.

Explanation

A sales load is the difference between the public offering price and the net asset value per share of the fund.

**Reference:** 10.7.4.3 in the License Exam Manual

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**Question #119 of 210**

Question ID: 606663

If a customer transfers his holdings from one fund to another within the same family of funds, what are the tax consequences?

- X **A)** Gains are taxed and losses are deferred.
- ✓ **B)** On the transaction date, any gain or loss is recognized for tax purposes.
- X **C)** No gain or loss is recognized until redemption.
- X **D)** Losses are deducted and gains are deferred.

Explanation

An exchange is a taxable event. The cost basis of the shares in the original account must be compared to their redemption value. Any gain or loss is recognized in the year of the exchange. The exchange privilege allows the investor to avoid paying an additional sales charge. It does not allow the investor to avoid taxes.

**Reference:** 10.8.1.6.3 in the License Exam Manual

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**Question #120 of 210**

Question ID: 606645

Encouraging a customer to purchase mutual fund shares in an amount just under the next dollar volume bracket (which entitles the customer to a reduction in sales charges) or remaining silent on the matter is called:

- X **A)** interpositioning.
- X **B)** selling away.
- X **C)** front running.
- ✓ **D)** a breakpoint sale.

Explanation

In a breakpoint sale, a customer unknowingly buys investment company shares in an amount just under a dollar bracket that would qualify for reduced sales charges. As a result, the registered representative receives a somewhat higher commission but the customer pays higher sales charges, reducing the number of shares purchased and resulting in a higher cost per share.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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**Question #121 of 210**

Question ID: 606582

If ABC Fund pays regular dividends, offers a high degree of safety of principal, and appeals especially to investors seeking tax advantages, ABC is a(n):

- X **A)** money market fund.
- ✓ **B)** municipal bond fund.
- X **C)** corporate bond fund.
- X **D)** aggressive growth fund.

Explanation

Municipal bonds are considered second only to U.S. government securities in terms of safety. Also, interest received from the bonds is generally exempt from federal income tax.

**Reference:** 10.5.1.4.1 in the License Exam Manual

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**Question #122 of 210**

Question ID: 606665

According to investment company rules, open-end investment companies may NOT distribute long-term capital gains to their shareholders more frequently than:

- ✓ **A)** annually.
- X **B)** semiannually.
- X **C)** quarterly.
- X **D)** monthly.

Explanation

Under the Act of 1940, investment companies may not distribute long-term capital gains more frequently than once per year.

**Reference:** 10.8.1.3 in the License Exam Manual

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### Question #123 of 210

Question ID: 606584

A tax-exempt bond fund may invest in:

- ☐ A) corporate bonds.
- ☐ B) short-term money market instruments.
- ☐ C) common stock.
- ☒ D) municipal bonds.

#### Explanation

Bond funds will distribute taxable income or dividends unless invested in municipal bonds. Although dividend distributions from a municipal bond fund are tax exempt, capital gains distributions are fully taxable.

**Reference:** 10.5.1.4.1 in the License Exam Manual

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### Question #124 of 210

Question ID: 606672

The result of dollar cost averaging is to:

- ☐ A) take advantage of a bullish market by buying more shares in a rising market.
- ☒ B) obtain a lower average cost per share than average price per share.
- ☐ C) obtain a lower average price per share than average cost per share.
- ☐ D) take advantage of a non-fluctuating market.

#### Explanation

The result of dollar cost averaging is to obtain a lower average cost per share than the average price per share. This is accomplished by making regular investments of a fixed amount when prices are fluctuating.

**Reference:** 10.9.1.1.1 in the License Exam Manual

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### Question #125 of 210

Question ID: 606563

The principal underwriter of an open-end investment company is also known as the:

- ☒ A) sponsor.
- ☐ B) trustee.
- ☐ C) registrar.
- ☐ D) dealer.

#### Explanation

A mutual fund's underwriter is also known as the sponsor or distributor of the fund.

**Reference:** 10.3.5 in the License Exam Manual

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### Question #126 of 210

Question ID: 786022

Government agency securities settle

- ☐ A) the next business day following the trade date
- ☐ B) the seventh calendar day following the trade date
- ☐ C) in 3 business days following the trade date
- ☒ D) the second business day following the trade date

#### Explanation

Most government agencies are treated as a corporate issue. Trades of corporate securities settle regular way (in 2 business days).

### Question #127 of 210

Question ID: 606638

An investor redeems 300 shares in ACE Fund. When the investor bought the shares at \$12, the NAV was \$11.08. If the current POP is \$12.50 and the NAV is \$11.80, the investor receives:

- ☐ A) 3750.
- ☐ B) 3324.
- ☐ C) 3600.
- ☒ D) 3540.

#### Explanation

Shares are redeemed at NAV. If the investor redeems 300 shares at an NAV of \$11.80, he receives \$3,540 ( $300 \times \$11.80$ ).

Reference: 10.7.6 in the License Exam Manual

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### Question #128 of 210

Question ID: 606624

A customer wishes to redeem 1,000 shares of a mutual fund. The NAV and POP are \$10, and a redemption fee of 0.5% will be charged. How much will the customer pay in redemption fees?

- ☐ A) 9950.
- ☐ B) 500.
- ☒ C) 50.
- ☐ D) 9500.

#### Explanation

The question did not ask how much he would receive upon redemption, but how much he would pay in redemption fees. Mutual fund shares are redeemed at the NAV (bid):  $1,000 \text{ shares} \times \$10 \text{ each} = \$10,000$ .  $\$10,000 \times .005$  (.5% redemption fee) = \$50.

Reference: 10.7.6 in the License Exam Manual

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### Question #129 of 210

Question ID: 606617

A broker/dealer with a sales agreement with a mutual fund must return all concessions to the underwriter if a customer redeems his shares:

- ☐ A) under no circumstances.
- ☐ B) within 5 business days of purchase.
- ☒ C) within 7 business days of purchase.
- ☐ D) within 10 business days of purchase.

#### Explanation

If any security issued by a mutual fund is tendered for redemption within 7 business days after the date of the transaction, the broker/dealer must refund to the underwriter the full concession allowed to the broker/dealer on the original sale.

Reference: 10.7.6.1 in the License Exam Manual

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### Question #130 of 210

Question ID: 786031

The ex-date for a closed-end fund listed for trading on the NYSE is set by

- ☐ A) the SEC
- ☐ B) FINRA
- ☒ C) the board of directors of the fund

✓ **D)** the NYSE

Explanation

The ex-dates for closed-end funds (typically 1 business day before the record date) are determined by the exchanges on which they trade. The ex-date for open-end funds (typically the business day following the record date) is determined by the board of directors of the fund.

**Reference:** 10.1.1.3.1 in the License Exam Manual

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**Question #131 of 210**

Question ID: 606613

The main purpose of dividend reinvestment in a mutual fund accumulation plan is to:

- X **A)** avoid taxes.
- X **B)** protect against capital loss.
- ✓ **C)** compound the growth of a mutual fund investment.
- X **D)** avoid commissions or sales charges.

Explanation

Reinvesting dividends compounds the growth of the fund with periodic purchases of new shares. Taxes are due on dividends whether or not they are reinvested. Capital gains or losses will occur whether or not dividends are reinvested. The purchase of additional shares with reinvested dividends may increase the capital gain or loss in proportion to the dividends reinvested. Avoiding commissions or sales charges is not the main rationale for reinvesting dividends, even though sales charges are not applied to reinvested dividends.

**Reference:** 10.7.5.3 in the License Exam Manual

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**Question #132 of 210**

Question ID: 606567

In the sale of open-end investment company shares, the prospectus must be delivered:

- X **A)** within 7 days of request.
- X **B)** before the sales solicitation .
- ✓ **C)** to the client either before or during the sales solicitation.
- X **D)** at or before redemption.

Explanation

Potential mutual fund customers must receive a prospectus before or during the sales solicitation.

**Reference:** 10.4.1 in the License Exam Manual

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**Question #133 of 210**

Question ID: 786019

Regulation T requires payment from a customer in a margin account

- X **A)** before purchase
- ✓ **B)** within 4 business days
- X **C)** within 10 business days
- X **D)** within 3 business days

Explanation

The Regulation T payment date is the fourth business day from the trade date. Regular way settlement, according to FINRA rules, is 2 business days from the trade date and Regulation T allows for two additional business days after settlement date; four business days total.

**Reference:** 9.1.2.5 in the License Exam Manual

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**Question #134 of 210**

Question ID: 721449

A broker-dealer has chosen to close out a customer's position in a cash account rather than request an extension for payment. The account will now be frozen for

- X **A)** 30 days
- X **B)** 120 days
- X **C)** 20 days
- ✓ **D)** 90 days

Explanation

When a broker-dealer chooses to close out a customer's position rather than request an extension for payment, the customer's account will be frozen for 90 days.

**Reference:** 9.1.2.5.1 in the License Exam Manual

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**Question #135 of 210**

Question ID: 606568

Investment company shareholders must receive financial reports at least semiannually. All of the following are true regarding these reports EXCEPT

- X **A)** one of the semiannual reports must be audited
- ✓ **B)** the report is regulated under FINRA's rules regarding communications with the public
- X **C)** a statement of all compensation paid to the board of directors (BOD) must be included
- X **D)** a valuation of all securities in the IC portfolio as of the date of the balance sheet provided in the report must be included

Explanation

The reports are required to be supplied to IC shareholders under the Investment Company Act of 1940. They are prepared and distributed by the investment companies. Unless forwarded by broker/dealers to their customers, the semiannual reports would not be regulated under FINRA's communication with the public rules for broker/dealers.

**Reference:** 10.4.2 in the License Exam Manual

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**Question #136 of 210**

Question ID: 606586

A mutual fund invested in bonds with medium-length maturities. As the bonds matured, the fund reinvested the proceeds and purchased long-term bonds with maturities of up to 20 years. What might have happened to the fund if the reinvestment had occurred during a period when interest rates were rising?

- I. Decrease in yield.
- II. Decrease in income.
- III. Increase in yield.
- IV. Increase in income.

- X **A)** I and IV.
- ✓ **B)** III and IV.
- X **C)** I and II.
- X **D)** II and III.

Explanation

The longer a bond's maturity, the greater the risk to the investor. As a result, long-term bonds generally pay higher interest rates than medium- or short-term bonds. If a fund replaces medium-term bonds with long-term bonds, the bonds would pay higher interest rates and thus generate more income. Additionally, as interest rates increase, so do yields.

**Reference:** 10.5.1.4 in the License Exam Manual

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**Question #137 of 210**

Question ID: 606610

A customer with no other mutual fund investments wishes to invest \$47,000 in the XYZ Technology Fund. If the Class A shares are eligible for a breakpoint sales charge discount at the \$50,000 investment level, the action *least* appropriate for an agent is to:

- ✓ **A)** place the order as instructed.
- X **B)** inform the customer that he can reduce his sales charge by investing an additional \$3,000.
- X **C)** inform the customer that he can reduce his sales charge by combining purchases in other funds offered by XYZ group.
- X **D)** inform the customer that he can reduce his sales charge through a letter of intent.

#### Explanation

If a customer intends to invest an amount just below a breakpoint threshold, he should be informed of the breakpoint discount, as well as the various methods by which he can receive it.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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### Question #138 of 210

Question ID: 606529

A certificate in the name of Smith & Company may be signed:

- X **A)** Smith & Company or "Smith & Co."
- ✓ **B)** Smith & Company, "Smith & Co.," or "Smith and Company".
- X **C)** Smith & Company.
- X **D)** Smith & Company, aka SmithCo.

#### Explanation

Corporate signers are the exception to the general rule that endorsement of a certificate must match exactly the name on the front. The word "and" may be substituted with "&" and the word "company" may be abbreviated.

**Reference:** 9.2.2.3 in the License Exam Manual

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### Question #139 of 210

Question ID: 606531

All of the following are true regarding a fail to deliver EXCEPT

- X **A)** the buyer may buy in the securities owed to him and charge the seller for any loss incurred
- ✓ **B)** even though a fail to deliver has occurred and is still outstanding, FINRA mandates that the seller still be paid
- X **C)** fail to deliver occurs when the selling BD does not deliver the securities in good deliverable form
- X **D)** the BD representing the seller can also be liable for buying in the securities if the BD's customer has not made good delivery on the securities sold

#### Explanation

The seller cannot be paid as long as the fail to deliver exists. Fail to deliver occurs when the selling BD does not deliver the securities in good deliverable form. The buyer or the selling BD can buy in the securities to complete the transaction, and any loss incurred to do so will become the responsibility of the seller who failed to deliver.

**Reference:** 9.2.5 in the License Exam Manual

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### Question #140 of 210

Question ID: 606494

A customer receives a call from his registered representative (RR) telling him that he purchased 200 shares of RCA at 34.50 for the market order he had entered earlier that day. Later that day, his broker tells him that the report he received was in error, and the shares were bought for 34.75. The customer:

- X **A)** may require that his broker pay the difference.
- ✓ **B)** must pay 34.75 per share.
- X **C)** must pay 34.50 per share.
- X **D)** may cancel the order.

#### Explanation

If an error has been made in the notice of execution and reported to a customer, the customer must pay for the shares at the correct price. The correct price, is the price at which the order was actually executed, either on the exchange or in the market where the execution occurred.

**Reference:** 9.1.1.3.1 in the License Exam Manual

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### Question #141 of 210

Question ID: 786030



Broker to broker confirmations must be sent no later than

- ☐ A) end of day on the date of the trade
- ☐ B) trade date plus two business days
- ☐ C) regular way settlement date
- ☒ D) next business day

Explanation

Confirmations between brokers (broker to broker confirms) must be sent no later than the next business day following the transaction (T + 1).

**Reference:** 9.1.2.5.2 in the License Exam Manual

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**Question #142 of 210**

Question ID: 606548

Closed-end investment company shares can be purchased and sold:

- ☐ A) only over the counter.
- ☐ B) from the closed-end company.
- ☒ C) in the secondary market.
- ☐ D) from the sponsor.

Explanation

A closed-end company share is bought and sold in the secondary market.

**Reference:** 10.1.1.3.1 in the License Exam Manual

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**Question #143 of 210**

Question ID: 606578

Which of the following two are TRUE of a leveraged exchange traded fund (ETF)?

- I. The leveraged ETF may be purchased on margin.
- II. Securities within the leveraged fund portfolio may be purchased on margin.
- III. The leveraged ETF may never be purchased on margin.
- IV. Securities within the leveraged fund portfolio may never be purchased on margin.

- ☐ A) II and III.
- ☐ B) III and IV.
- ☒ C) I and II.
- ☐ D) I and IV.

Explanation

Because an exchange traded fund is purchased and sold on an exchange, the rules generally applying to all exchange products such as purchasing them on margin, would apply. Leveraged funds can use a number of different securities types including derivative products, and trading techniques such as trading on margin as a means of attaining the leveraged returns they promise.

**Reference:** 10.10.2 in the License Exam Manual

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**Question #144 of 210**

Question ID: 606558

Which of the following is true regarding a "summary section" and a "statement of additional information" for management investment companies?

- ☐ A) Both must be included in the prospectus of a management company.
- ☒ B) A statement of additional information (SAI) need not be included in the prospectus of a management company.
- ☐ C) Neither are required to be in the prospectus of a mutual fund.
- ☐ D) A summary section need not be included in the prospectus of a mutual fund.

Explanation

A statement of additional information (SAI) need not be in a prospectus but available for both open and closed-end investment companies. It consists of information not necessarily needed to make an informed purchase decision but still useful to the investor. The SEC however mandates that "enhanced disclosure" in the form of a summary section be included in the prospectus of open-end investment companies (mutual funds). It must be written in plain language and the SEC mandates the order of, and the items to be addressed in the summary.

**Reference:** 10.2.1.3 in the License Exam Manual

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### Question #145 of 210

Question ID: 606547

According to the Investment Company Act of 1940, a diversified mutual fund may hold, at *most*, what percentage of a corporation's voting securities?

- X **A)** 50%.
- ✓ **B)** 10%.
- X **C)** 75%.
- X **D)** 5%.

#### Explanation

To be considered a diversified investment company, a mutual fund can own no more than 10% of a target company's voting securities. Additionally, no diversified investment company may invest more than 5% of its portfolio in a single company's securities.

**Reference:** 10.1.1.3.3 in the License Exam Manual

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### Question #146 of 210

Question ID: 606598

Which of the following is TRUE about a sales agreement between a principal underwriter and a member, which enables the member to receive a discount from the public offering price?

- I. It must be in writing.
- II. It must provide for a 45-day right of refusal.
- III. It must provide that the member will sell at NAV only when selling to the public.
- IV. It must provide for a refund of the concession by the member to the underwriter if the shares are redeemed within 7 business days of the sale.

- ✓ **A)** I and IV.
- X **B)** I and III.
- X **C)** II and III.
- X **D)** II and IV.

#### Explanation

All sales agreements must be in writing, provide for a 7-day refund of the concession, and include a stipulation that the member will maintain the public offering price, not the NAV.

**Reference:** 10.7.6.1 in the License Exam Manual

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### Question #147 of 210

Question ID: 606675

The practice of dollar cost averaging requires the investor to:

- X **A)** buy a security in a falling market and sell it in a rising market.
- ✓ **B)** buy a security in a falling market and buy it in a rising market.
- X **C)** sell a security in a falling market and buy it in a rising market.
- X **D)** sell a security in a falling market and sell it in a rising market.

#### Explanation

Dollar cost averaging requires the investor to invest a fixed amount of money on a regular basis regardless of whether the stock market is rising or falling.

**Reference:** 10.9.1.1 in the License Exam Manual

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### Question #148 of 210

Question ID: 606662

Unrealized gain in a mutual fund portfolio does which of the following?

- I. Increases the dividends paid to shareholders.
- II. Represents the undistributed income and the growth in market value of securities held in the portfolio.
- III. Is realized by shareholders only when they redeem their shares.
- IV. Has no effect on shareholders until the annual long-term capital gains distribution is paid.

✓ **A) II and III.**

X **B) I and III.**

X **C) I and IV.**

X **D) II and IV.**

#### Explanation

Unrealized gains result from asset appreciation and undistributed income. This increase in value is reflected in an appreciation of the mutual fund shares. Investors realize this appreciation only by selling their shares.

**Reference:** 10.8.1.3 in the License Exam Manual

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### Question #149 of 210

Question ID: 606553

Which of the following is true regarding exchange traded funds (ETFs)?

- I. The SEC has classified them as mutual funds.
- II. The SEC has classified them as a type of open-end fund.
- III. They have operating costs and expenses that are higher than most mutual funds.
- IV. They have operating costs and expenses that are lower than most mutual funds.

✓ **A) II and IV**

X **B) I and IV**

X **C) I and III**

X **D) II and III**

#### Explanation

The SEC has classified exchange traded funds as a type of open-end fund but not a mutual fund. ETFs traditionally have operating costs and expenses that are lower than most mutual funds because they do not have to purchase and sell holdings within the portfolio to accommodate investors purchasing shares or redeeming shares, as is the case with mutual funds.

**Reference:** 10.1.1.3.4 in the License Exam Manual

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### Question #150 of 210

Question ID: 606551

Customers could pay a commission, rather than a sales charge, for shares of a(n):

- ✓ **A) closed-end investment company.**
- X **B) front-end load fund.**
- X **C) mutual fund.**
- X **D) open-end investment company.**

#### Explanation

Sales charges could be paid on all types of open-end funds. Commissions are paid on securities traded in the secondary market, such as closed-end investment company shares.

**Reference:** 10.1.1.3.1 in the License Exam Manual

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### Question #151 of 210

Question ID: 606669

Net asset value per share for a mutual fund can be expected to decrease if the:

- ☐ **A)** fund has experienced net redemption of shares .
- ☒ **B)** fund has made dividend distributions to shareholders .
- ☐ **C)** securities in the portfolio have appreciated in value.
- ☐ **D)** issuers of securities in the portfolio have made dividend distributions.

Explanation

The NAV per share will rise or fall relative to the value of the underlying portfolio. If dividends are distributed to shareholders, the fund's assets decrease and their per-share value will decline accordingly. Appreciation of the portfolio and dividends received will increase the value. Redemption of shares will have no impact on the NAV per share as the money paid out is offset by a reduced number of shares outstanding.

**Reference:** 10.8.1.1 in the License Exam Manual

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**Question #152 of 210**

Question ID: 606579

The net asset value of an international bond fund can be expected to increase if:

- I. interest rates rise abroad.
- II. interest rates fall abroad.
- III. the U.S. dollar strengthens.
- IV. the U.S. dollar weakens.

- ☐ **A)** I and III.
- ☒ **B)** II and IV.
- ☐ **C)** II and III.
- ☐ **D)** I and IV.

Explanation

If interest rates fall, bond prices will rise, thus increasing the NAV of a bond portfolio. If the U.S. dollar weakens, the value of other currencies will rise. This would also increase the NAV for a portfolio of international bonds.

**Reference:** 10.5.1.4 in the License Exam Manual

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**Question #153 of 210**

Question ID: 606682

A 3× leveraged inverse exchange-traded fund means:

- ☐ **A)** There is no risk if the targeted index rises.
- ☒ **B)** The goal of the fund is to have the shares go up by 3 times the amount that the targeted index falls.
- ☐ **C)** The fund may not use more than 3 leverage producing derivative products within its fund portfolio like options or futures.
- ☐ **D)** The fund shares cannot be purchased on margin by investors.

Explanation

A leveraged inverse fund attempts to produce returns opposite of the targeted index in the amount designated by the leverage multiplier; in this case, three times. If the targeted index rose, the inverse fund would fall by the leverage multiplier and in that regard substantial risk must be recognized due to the leverage. Leveraged funds will utilize derivative products like options and futures to help meet the desired goal and can use investment strategies such as margin to purchase securities for the fund portfolio as well. Lastly, because the fund shares are exchange-traded, they can be purchased on margin by investors.

**Reference:** 10.10.3 in the License Exam Manual

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**Question #154 of 210**

Question ID: 606684

If an index is up 2%, a 3X leveraged inverse ETF tracking that index should be

- ☐ **A)** up 2%
- ☐ **B)** up 6%
- ☐ **C)** down 3%
- ☒ **D)** down 6%

### Explanation

Inverse or reverse funds attempt to deliver returns that are the opposite of the index they are tracking. If the index is up, the inverse fund should be down. A leverage fund attempts to deliver returns that are a multiple of the index it is tracking. Therefore, an inverse 3X leveraged fund should be down 3X as much as the index is up if it performs as it should. In this example, down 6% (3 X 2%).

**Reference:** 10.10.3 in the License Exam Manual

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### **Question #155 of 210**

Question ID: 606539

An investment company that holds which of the following does NOT meet the definition of a diversified investment company under the 1940 Investment Company Act?

- ✓ **A)** 33% of its assets in securities issued by a small-cap new issue.
- X **B)** 80% of its assets in securities of 50 health care companies.
- X **C)** 8% of a given corporation's voting stock in its portfolio.
- X **D)** 4% of its assets invested in stock of a major publicly held corporation.

### Explanation

An investment company that has invested 33% of its assets in any issue, small-cap or not, exceeds the limits set in the 75-5-10 test. This test requires that 75% of the assets be invested in securities issued by companies other than the investment company (regardless of the type of companies) so that no more than 5% of total assets are invested in any one company, and no more than 10% of an outside corporation's voting securities are owned by the investment company.

**Reference:** 10.1.1.3.3 in the License Exam Manual

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### **Question #156 of 210**

Question ID: 606580

Mutual fund shares represent an undivided interest in the fund, which means that:

- X **A)** the number of shares outstanding is limited to a predetermined maximum.
- X **B)** investors can only purchase full shares.
- X **C)** the fund can only hold securities of certain companies .
- ✓ **D)** each investor owns a proportional part of every security in the portfolio.

### Explanation

Each mutual fund shareholder owns an undivided interest in the investment company's portfolio. Because each share represents one class of voting stock, the investor's interest in the fund is reflected by the number of shares owned.

**Reference:** 10.5 in the License Exam Manual

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### **Question #157 of 210**

Question ID: 606535

When speaking to a customer about exchange-traded funds (ETFs), a registered representative could CORRECTLY state that these funds

- X **A)** cannot be purchased using traditional limit or stop orders
- X **B)** cannot be bought on margin
- ✓ **C)** do not have the same potential tax consequences as mutual funds, such as making capital gains distributions annually
- X **D)** can be purchased only by paying a sales charge added to the NAV

### Explanation

With ETFs, portfolio turnover rate is minimized because they do not have to buy and sell shares within their portfolio to accommodate shareholder purchases and redemptions. This can affect the potential tax consequences. While an ETF can make a capital gains distribution, they generally do not, unlike a mutual fund which generally would make such distributions on an annual basis. ETFs can be traded like other exchange products using traditional stock trading techniques and are priced by supply and demand. Customers pay commissions, not sales charges.

**Reference:** 10.1.1.3.4 in the License Exam Manual

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### Question #158 of 210

Question ID: 606590

A mutual fund's expense ratio is found by dividing its expenses by its:

- ☐ A) income.
- ☒ B) average annual net assets.
- ☐ C) dividends.
- ☐ D) public offering price.

#### Explanation

A mutual fund's expense ratio is calculated by dividing its expenses by its average annual net assets.

**Reference:** 10.6.2.2 in the License Exam Manual

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### Question #159 of 210

Question ID: 606628

The exchange privilege offered by open-end investment companies allows investors to:

- ☐ A) purchase new fund shares from dividends.
- ☐ B) exchange personally owned securities for shares of the investment company.
- ☒ C) exchange shares of one open-end fund for another in the same fund family at a net asset value basis.
- ☐ D) delay the payment of taxes on shares.

#### Explanation

Exchange privileges allow an investor to convert the value of shares held in one fund for those of an equal value in the same family. Remember that conversion is a taxable event; if the shares converted have increased in value, capital gains taxes will be due.

**Reference:** 10.7.5.4.1 in the License Exam Manual

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### Question #160 of 210

Question ID: 606530

Which of the following persons must sign a stock or bond power to effect good delivery of securities sold from an account set up under the Uniform Transfer to Minors Act?

- ☐ A) Minor.
- ☐ B) Parent.
- ☐ C) Donor.
- ☒ D) Custodian.

#### Explanation

The custodian must sign securities in a custodial account to effect good delivery.

**Reference:** 9.2.2.3 in the License Exam Manual

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### Question #161 of 210

Question ID: 606555

An open-end investment company may do all of the following EXCEPT:

- ☐ A) continuously offer shares.
- ☐ B) redeem shares.
- ☐ C) borrow money.
- ☒ D) issue bonds.

#### Explanation

A mutual fund may not issue any senior securities, although it may purchase almost any type of security for its portfolio.

**Reference:** 10.2.1.1 in the License Exam Manual

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### Question #162 of 210

Question ID: 606692

Holding Company Depository Receipts (HOLDRs) are

- I. traded on exchanges in round lots
- II. redeemable by the issuer, just as mutual funds shares are redeemable by an investment company
- III. investments that will distribute the cash dividends of the companies held in the portfolio directly to the investor
- IV. investments that allow no flexibility in managing the tax consequences related to holding shares of the companies within the portfolio

- ☐ A) II and III
- ☐ B) II and IV
- ☐ C) I and IV
- ☒ D) I and III

#### Explanation

HOLDRs are exchange-traded investments and trade in round lots (100 shares). They are not redeemable by their issuer like mutual fund shares are. Additionally, HOLDRs distribute cash dividends generated by the companies held in the portfolio directly to the owners of the HOLDR shares. These exchange-traded products allow great flexibility in managing the tax consequences of the investment because the securities can be unbundled and traded individually, thus taking losses when advantageous and deferring gains when advantageous.

**Reference:** 10.12.1 in the License Exam Manual

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### Question #163 of 210

Question ID: 606657

If an investor has received dividends and capital gains distributions on mutual fund shares she has held for 4 months, the investor will pay:

- ☐ A) long-term or short-term capital gains rates, depending on the length of time the customer has held the fund shares.
- ☐ B) ordinary income tax rates on the capital gains and dividends.
- ☒ C) capital gains rates on capital gains distributions and ordinary income rates on dividends.
- ☐ D) no tax until she liquidates the shares.

#### Explanation

Capital gains distributions are taxed as capital gains, with their holding status depending on how long the fund has held the securities, not how long the investor has held the mutual fund shares. Dividend distributions are taxed as ordinary income.

**Reference:** 10.8.1.3 in the License Exam Manual

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### Question #164 of 210

Question ID: 606602

When is the sales charge deducted from purchases of mutual fund shares made under a letter of intent?

- ☒ A) When each purchase is made.
- ☐ B) When each letter of intent is completed.
- ☐ C) Annually.
- ☐ D) Monthly.

#### Explanation

When the customer makes the first investment under a letter of intent, the reduced sales charge applies immediately and to each subsequent investment. With each additional investment, the same reduced charge is deducted. If the customer does not invest the amount stated in the letter, the full sales load applies retroactively to the total investment.

**Reference:** 10.7.5.1.1 in the License Exam Manual

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### Question #165 of 210

Question ID: 606605

A letter of intent for a mutual fund does NOT contain which of the following provisions?

- ☒ A) The fund can halt redemption during the period of time the letter of intent is in effect.

- X **B)** The letter can be backdated 90 days to include a previous deposit.
- X **C)** The time limit is 13 months.
- X **D)** The fund will keep some of the initially issued shares in an escrow account to ensure payment of the full sales load.

Explanation

A letter of intent is not binding on the client in any way. Should the client decide to liquidate the account before completing the letter, the company will reduce the redemption by the amount of shares held in escrow.

**Reference:** 10.7.5.1.1 in the License Exam Manual

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**Question #166 of 210**

Question ID: 606502

A member firm receives a signed proxy from a customer who failed to indicate how his shares held in street name are to be voted at the annual shareholder's meeting. Under NYSE rules, the member firm:

- X **A)** cannot vote the shares.
- X **B)** may vote the shares as it sees fit.
- ✓ **C)** must vote the shares as recommended by management of the issuer.
- X **D)** may vote the shares as it sees fit only if a principal attends the meeting.

Explanation

If the beneficial owner of street name stock returns a signed proxy statement but fails to indicate how the shares are to be voted, the member must vote the shares as recommended by management of the issuer.

**Reference:** 9.1.3.3 in the License Exam Manual

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**Question #167 of 210**

Question ID: 721452

A stock mutual fund wishes to advertise itself as diversified. To be able to do so, the fund must invest:

- X **A)** so that it holds no more than 10% of the voting stock of any one company.
- ✓ **B)** All of these.
- X **C)** at least 75% of its assets in securities other than its own.
- X **D)** no more than 5% of its assets in any one target company.

Explanation

All of these choices comprise the 75-5-10 rule for diversified investment companies under the Investment Company Act of 1940. At least a minimum of 75% of the total assets must be invested in securities other than those of the investment company. Of the assets invested, no more than 5% of the fund's total assets can be in any one company nor can the percentage ownership of any one company be more than 10%.

**Reference:** 10.1.1.3.3 in the License Exam Manual

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**Question #168 of 210**

Question ID: 606647

An agent has recommended investments in the XYZ fund family to his customers for 10 years. He is referred by one of his customers to a prospect who has inherited \$500,000 as beneficiary of a life insurance policy. The prospect tells the agent she has never invested in the market before, is risk averse, and wants safety of principal to be the first priority with liquidity second. The agent recommends the following investments:

XYZ government bond fund, B shares \$200,000  
XYZ large-cap growth and Income B shares \$150,000  
XYZ liquid reserve money market \$150,000

The recommendation is:

- ✓ **A)** unsuitable because it does not address the customer's two primary objectives.
- X **B)** suitable because it addresses the customer's safety objective.



- X **C)** suitable because it addresses the customer's liquidity objective.
- X **D)** suitable because he recommended conservative investments.

Explanation

The customer's objectives of safety and liquidity are not satisfied by these recommendations. The government bond fund and large-cap growth and income fund are both subject to market risk and, as Class B shares, are subject to a contingent-deferred sales charge in the event the customer wishes to access the funds before the back-end load expires. The back-end load is not consistent with the customer's liquidity objective.

**Reference:** 10.7.5.5 in the License Exam Manual

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**Question #169 of 210**

Question ID: 606668

SEC rules require that open-end management companies distribute dividends to their investors from the firm's:

- X **A)** portfolio earnings.
- X **B)** capital gains.
- ✓ **C)** net investment income.
- X **D)** gross revenue.

Explanation

Dividends must be paid from the net investment income.

**Reference:** 10.8.1.1 in the License Exam Manual

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**Question #170 of 210**

Question ID: 606623

Each of the following investors may take advantage of breakpoints EXCEPT:

- X **A)** Individual.
- X **B)** Corporation.
- X **C)** Trust.
- ✓ **D)** Investment club.

Explanation

Breakpoint discounts are available only to legal persons. An investment club is not considered a legal person, but trusts and corporations are.

**Reference:** 10.7.5.1 in the License Exam Manual

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**Question #171 of 210**

Question ID: 606596

A customer invests \$18,000 in a mutual fund and signs a letter of intent for \$25,000 in order to qualify for a breakpoint. One year later, the shares are valued at \$25,100 even though he has made no new investments. Which of the following statements regarding the above situation is TRUE?

- ✓ **A)** The representative should remind the customer that he signed a letter of intent 12 months ago.
- X **B)** The investment no longer qualifies for a breakpoint.
- X **C)** Shares held in escrow will be liquidated at the appreciated value.
- X **D)** The letter of intent is considered to be fulfilled.

Explanation

A letter of intent must be met with dollars invested within 13 months. The customer needs to invest an additional \$7,000 to fulfill his letter of intent. The representative should remind the customer of his intention to qualify for the reduced sales charge.

**Reference:** 10.7.5.1.1 in the License Exam Manual

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**Question #172 of 210**

Question ID: 606593

If a registered representative is comparing two mutual funds for a customer, which of the following comparisons would NOT be permissible?

- X **A)** Comparing two equity funds with slightly different investment objectives, even if the differences and their consequences are carefully explained.
- ✓ **B)** Comparing an equity growth fund to a money market fund with the intention of convincing an investor to purchase the growth fund.
- X **C)** Comparing diversified growth funds from two different fund families.
- X **D)** Comparing a long-term bond fund to a shorter-term bond fund to demonstrate the trade-offs that exist between risk and return.

Explanation

A characteristic of money market funds is that they deliberately avoid growth. Thus, for the growth investor, a comparison of a money market fund to a growth fund is an unfair comparison.

**Reference:** 10.6 in the License Exam Manual

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**Question #173 of 210**

Question ID: 606616

A customer buys AC Growth Fund and enjoys a substantial paper capital gain. When he believes the market has reached its peak, he switches into AC Income Fund within the AC family of funds. He incurs a small service fee but is not charged an additional sales charge. What is the tax effect?

- X **A)** Any gain or loss is deferred until he liquidates the AC Income Fund.
- X **B)** The tax basis of AC Income Fund is adjusted to reflect the gain in AC Growth Fund.
- ✓ **C)** Any gain in AC Growth Fund is taxable because the exchange is treated as a sale and a purchase.
- X **D)** It is a tax-free exchange.

Explanation

The exchange is treated as a sale of the growth fund shares followed by a purchase of the income fund shares. The gain or loss is determined by comparing the cost basis of the growth fund shares with the net asset value at the time of exchange. Any difference is a capital gain or loss, even though the proceeds were immediately used to purchase the income fund.

**Reference:** 10.7.5.4.1 in the License Exam Manual

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**Question #174 of 210**

Question ID: 606528

Which of the following is NOT good delivery for 470 shares of stock?

- X **A)** 4 100-share certificates and 1 70-share certificate .
- X **B)** 47 10-share certificates.
- X **C)** 8 50-share certificates, 1 40-share certificate, and 1 30-share certificate.
- ✓ **D)** 2 100-share certificates and 3 90-share certificates.

Explanation

Shares must add up to 100 or be in multiples of 100, with the exception of odd lots.

**Reference:** 9.2.1.3 in the License Exam Manual

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**Question #175 of 210**

Question ID: 606540

All of the following terms apply to municipal unit investment trusts EXCEPT:

- X **A)** redeemable.
- X **B)** regulated.
- X **C)** registered.
- ✓ **D)** managed.

#### Explanation

Municipal UITs buy bonds and hold them until redemption or call. The bonds are not actively traded so the portfolio is not managed but is overseen by a trustee.

**Reference:** 10.1.1.2 in the License Exam Manual

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### Question #176 of 210

Question ID: 606608

XYZ Technology Fund permits rights of accumulation. A shareholder has invested \$9,000 and signed a letter of intent for a \$15,000 investment. If his reinvested dividends during the 13 months total \$720, how much money must he contribute to fulfill the letter of intent?

- ✓ **A)** 6000.
- X **B)** 15000.
- X **C)** 5280.
- X **D)** 9000.

#### Explanation

The shareholder must contribute the full \$15,000, so he owes an additional \$6,000. Reinvested dividends and changes in the NAV do not count toward a breakpoint during the period of a letter of intent.

**Reference:** 10.7.5.2 in the License Exam Manual

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### Question #177 of 210

Question ID: 606503

When a customer enters a sell order and the customer is in possession of the certificates, a broker/dealer must determine all of the following EXCEPT:

- X **A)** the location of the securities.
- ✓ **B)** whether the transfer agent has accepted the securities.
- X **C)** whether the client can make delivery promptly .
- X **D)** whether the securities are in deliverable form.

#### Explanation

A firm must make an affirmative determination and be reasonably sure the client can make prompt delivery. Conversely, approval of the transfer agent is not a factor when accepting a sell order.

**Reference:** 9.1.1.1 in the License Exam Manual

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### Question #178 of 210

Question ID: 606501

If a member firm acting as a proxy solicitor for LRK Corporation is given a shareholder list by LRK, which of the following statements is TRUE?

- X **A)** The member can use the list only to solicit new business with the written consent of LRK.
- ✓ **B)** The member firm cannot use the list for any purpose other than to solicit proxies.
- X **C)** The member firm can use the list to solicit new business.
- X **D)** The member can use the list only to solicit new business with the written consent of FINRA.

#### Explanation

A member given a shareholder list can use the list only to solicit proxies. It can be used for no other purpose.

**Reference:** 9.1.3.3 in the License Exam Manual

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### Question #179 of 210

Question ID: 606685

Leveraged index funds

- I. can be exchange-traded (ETFs)
- II. can never be exchange-traded (ETFs)

- III. can be inverse or reverse funds
- IV. can never be inverse or reverse funds

- ✓ **A)** I and III.
- X **B)** I and IV.
- X **C)** II and III.
- X **D)** II and IV.

#### Explanation

Leveraged funds, those attempting to deliver a multiple of (ex: 2X, 3X) the returns delivered by the index they track, can be exchange-traded (ETFs), and can be inverse (reverse) funds as well. Inverse funds attempt to deliver returns the opposite of those realized by the index they track.

**Reference:** 10.10.3 in the License Exam Manual

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### Question #180 of 210

Question ID: 606621

A customer has been following several investment company quotes in the newspaper. She notices that the GEM Fund has an NAV of \$12 and a POP of \$12.50, and that the ABC Fund has an NAV of \$11.50 and a POP of \$10.98. The customer should conclude that:

- X **A)** both are open-end funds.
- ✓ **B)** GEM may be an open- or closed-end fund and ABC is a closed-end fund.
- X **C)** ABC and GEM are both unit investment trusts.
- X **D)** ABC is an open-end fund and GEM is a closed-end fund.

#### Explanation

The price for open-end funds is determined by adding the sales charge to the NAV. An open-end fund can never have a POP less than its NAV, therefore ABC cannot be an open-end fund.

**Reference:** 10.7.4 in the License Exam Manual

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### Question #181 of 210

Question ID: 786029

In an interdealer trade, if the seller delivers before the settlement date, which of the following statements is TRUE?

- X **A)** The buyer must accept delivery.
- X **B)** The seller has violated the Uniform Practice Code.
- ✓ **C)** The buyer may accept the stock or may refuse it without prejudice.
- X **D)** The buyer must only accept delivery if the seller gave advance notice of his intention.

#### Explanation

In a regular way trade, the firm is not obligated to accept securities delivered before settlement date (2 business days after the trade date) but may do so if it wishes.

**Reference:** 9.1.2.1 in the License Exam Manual

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### Question #182 of 210

Question ID: 606541

The capital structure of an open-end investment company can include:

- X **A)** only debt issues with no bank borrowing allowed.
- X **B)** preferred stock, common stock, and bonds.
- X **C)** preferred and common stock with no bank borrowing allowed.
- ✓ **D)** one issue of common stock and limited bank borrowing.

#### Explanation

Open-end investment companies may only issue redeemable common stock. Preferred stock, bonds, and other forms of senior securities are not allowed. Bank borrowing is allowed subject to certain limitations.

**Reference:** 10.1.1.3.2 in the License Exam Manual

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### Question #183 of 210

Question ID: 786020

Written notice of intent to deliver before an agreed to settlement date is required in which of the following transactions?

- ☐ A) In a delayed delivery
- ☐ B) In a Regulation T delivery
- ☒ C) In a seller's option
- ☐ D) In regular way settlement

#### Explanation

A seller's option trade gives the seller a specified settlement date that exceeds the regular way delivery date to deliver the securities. If the seller wishes to deliver them before the agreed on settlement date, he must provide 24-hour notice to the buyer.

**Reference:** 9.1.2.3 in the License Exam Manual

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### Question #184 of 210

Question ID: 606542

Exchange traded funds:

- I. pass on capital gains to investors annually.
- II. can be bought and sold throughout the trading day.
- III. have high expense ratios.
- IV. have low expense ratios.

- ☐ A) I and IV.
- ☒ B) II and IV.
- ☐ C) I and III.
- ☐ D) II and III.

#### Explanation

Noted advantages of Exchange Traded Funds (ETFs) are that they have low operating costs and thus low expense ratios and can be bought and sold throughout the trading day.

**Reference:** 10.1.1.3.4 in the License Exam Manual

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### Question #185 of 210

Question ID: 606513

Sell order tickets must be:

- ☒ A) marked as either long or short.
- ☐ B) marked only if they are long sales.
- ☐ C) executed in accordance with the appropriate rules, but not necessarily marked.
- ☐ D) marked only if they are short sales.

#### Explanation

Every sell order must be marked as either a long sale or a short sale.

**Reference:** 9.1.1.2 in the License Exam Manual

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### Question #186 of 210

Question ID: 606603

For a mutual fund that collects a 12b-1 fees, which of the following statements are TRUE?

- I. The fund may use the money to pay for mailing sales literature.
- II. Advertising materials must always state that the fund is no-load.
- III. The fund may use the money to pay for commissions on portfolio transactions.

IV. The fund's prospectus must disclose the fee.

- X **A)** II and III.
- X **B)** III and IV.
- X **C)** I and II.
- ✓ **D)** I and IV.

Explanation

12b-1 fees may be used only to cover promotional and other distribution expenses for funds that are distributors of their own shares; fee amounts must be disclosed in the prospectus. The fund may not use the term "no-load" in any communications with the public if the 12b-1 fee and other service fees exceed .25% of average net assets.

**Reference:** 10.7.4.5 in the License Exam Manual

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**Question #187 of 210**

Question ID: 606600

The POP for a mutual fund as quoted in the financial press reflects:

- X **A)** no sales charge because the offering price depends on the quantity purchased.
- ✓ **B)** the maximum sales charge the fund distributor collects.
- X **C)** the minimum sales charge the fund distributor collects.
- X **D)** the average sales charge for the preceding 3 months.

Explanation

The public offering price for a quoted mutual fund includes the maximum sales charge the fund distributor can assess.

**Reference:** 10.7.2 in the License Exam Manual

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**Question #188 of 210**

Question ID: 606670

A customer owns shares in ACME Income Fund and decides to exchange them for shares in ACME Growth Fund within the same family of funds. Which of the following statements is TRUE?

- ✓ **A)** The exchange is a taxable event.
- X **B)** The exchange results in a deferral of tax.
- X **C)** Tax or loss on the exchange cannot be determined until ACME Growth Fund is sold.
- X **D)** The exchange is a nontaxable swap.

Explanation

The IRS deems an exchange to be a sale and repurchase of shares. On any sale of securities, capital gains or losses are realized; as such, exchanges are a taxable event.

**Reference:** 10.8.1.6.3 in the License Exam Manual

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**Question #189 of 210**

Question ID: 606588

A registered representative speaking to a customer is explaining registered funds that invest in nonregistered hedge funds. Which of the following statements would NOT be correct?

- X **A)** These funds generally allow purchases with an initial investment that is lower than what would be required to invest directly in a hedge fund.
- ✓ **B)** These funds, called funds of hedge funds, eliminate all of the risks associated with hedge funds.
- X **C)** To divest of your fund of hedge fund investment, the shares will need to be redeemed by the mutual fund issuer.
- X **D)** Hedge funds are directly available to sophisticated (accredited) investors, while funds of hedge funds allow all investors to invest in hedge funds indirectly.

Explanation

Because the portfolio of the registered fund consists of shares of nonregistered hedge funds, virtually all of the risks associated with hedge funds are transferred to the mutual fund. Funds of hedge funds allow all investors, not just accredited investors, to have access to hedge fund investments, and they are likely to have lower initial investment requirements, making that access even easier. To divest of fund of hedge fund shares, the issuer would have to redeem them from the investor, as is the case with all registered mutual funds.

**Reference:** 10.5.1.8 in the License Exam Manual

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### Question #190 of 210

Question ID: 606620

FINRA rules require that, if a customer redeems mutual fund shares within 7 business days of purchase:

- ☐ **A)** the fund must report the redemption promptly to the SEC.
- ☐ **B)** the customer is entitled to receive the original NAV or the current NAV, whichever is higher.
- ☒ **C)** the member firm must forfeit the concession earned.
- ☐ **D)** the representative who sold the shares will be subject to a Code of Procedure hearing.

#### Explanation

If a customer redeems mutual fund shares within 7 business days of purchase, any concession earned by the member firm that sold it to him must be returned to the underwriter. The same rule applies to variable annuities.

**Reference:** 10.7.6.1 in the License Exam Manual

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### Question #191 of 210

Question ID: 786025

All of the following statements regarding customer confirmations are true EXCEPT

- ☐ **A)** the confirmation must disclose commissions if the firm acted as agent
- ☒ **B)** the customer must receive the confirmation no later than the business day after the trade
- ☐ **C)** the confirmation must disclose whether the broker/dealer is a market maker in the security sold
- ☐ **D)** the confirmation must disclose if a control relationship exists

#### Explanation

The customer must be sent or receive a confirmation from the broker/dealer no later than completion of the transaction (on or before settlement date).

**Reference:** 9.1.1.4 in the License Exam Manual

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### Question #192 of 210

Question ID: 606577

If a client prefers mutual fund investments in companies that primarily generate capital appreciation to companies that pay a steady dividend, what type of mutual fund and associated investment objective would you recommend?

- ☐ **A)** An index fund.
- ☒ **B)** A growth fund.
- ☐ **C)** A growth and income fund.
- ☐ **D)** An income fund.

#### Explanation

A growth mutual fund invests in stocks that are growing rapidly and stresses capital appreciation rather than income. The key is that the growth and appreciation are synonymous.

**Reference:** 10.5.1.1.1 in the License Exam Manual

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### Question #193 of 210

Question ID: 606641

All of the following may receive breakpoint discounts EXCEPT:

- ☐ **A)** an investor in an individual retirement account .

- X **B)** a pension plan trustee .
- X **C)** a husband and wife in a joint account.
- ✓ **D)** an investment club .

Explanation

Breakpoints are not available to investment clubs.

**Reference:** 10.7.5.1 in the License Exam Manual

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**Question #194 of 210**

Question ID: 606587

A mutual fund portfolio consists entirely of stocks of companies with either new products just released in the market place or companies holding patents pending. This mutual fund is best described as a:

- ✓ **A)** special situation fund.
- X **B)** combination fund.
- X **C)** index fund.
- X **D)** dow theory fund.

Explanation

Special situation funds buy securities of companies that are considered to be in a position to benefit from special nonrecurring situations. Those could be; new management, new products, patents pending, takeover or turnaround situations.

**Reference:** 10.5.1.1.5 in the License Exam Manual

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**Question #195 of 210**

Question ID: 606576

If a couple has a long-term growth objective and is willing to accept a reasonable amount of risk, which of the following mutual funds is *most* suitable for them?

- X **A)** Municipal bond fund.
- X **B)** Money market fund.
- ✓ **C)** Common stock fund.
- X **D)** Corporate bond fund.

Explanation

A common stock fund will help the couple meet their long-term growth objective.

**Reference:** 10.5.1.1 in the License Exam Manual

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**Question #196 of 210**

Question ID: 606687

Which of the following funds is most likely to contain within its portfolio securities of issuers who have NOT specified the use of the capital they are raising?

- ✓ **A)** Hedge fund containing blank-check and blind-pool offerings in its portfolio
- X **B)** No-load fund offered by a no-load mutual fund company
- X **C)** Exchange-traded growth fund
- X **D)** Income fund offered by an investment company registered under the 1940 Investment Company Act

Explanation

Blank-check and blind-pool securities are offerings where the issuer has not specified the use of the capital it is raising. While these securities are available individually to investors, some hedge funds will either target them or include them within their portfolios. The unique risks of these companies, coupled with the unique risks of hedge funds in general, must be considered in terms of suitability.

**Reference:** 10.11.2 in the License Exam Manual

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### Question #197 of 210

Question ID: 606622

A mutual fund has a net asset value (NAV) of \$7.80 per share, and the fund pays its underwriter a concession of \$0.12 per share. If the fund has a sales load of \$0.50 per share and an administrative fee of \$0.15 per share, how much does the investor pay per share to purchase a Class A share of this fund?

- ✓ **A)** 8.3.
- X **B)** 8.57.
- X **C)** 8.42.
- X **D)** 7.8.

#### Explanation

The investor pays the public offering price (POP) when purchasing mutual fund shares. For a Class A share upon purchase, the POP is the NAV plus the sales charge.

**Reference:** 10.7.4.6 in the License Exam Manual

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### Question #198 of 210

Question ID: 606659

Which of the following statements are TRUE of mutual fund dividend distributions?

- I. The fund pays dividends from net investment income.
- II. A single taxpayer may exclude \$100 worth of dividend income from taxes annually.
- III. An investor is liable for taxes on distributions, whether taken in cash or reinvested in the fund.
- IV. An investor is not liable for taxes if he automatically reinvests distributions.

- ✓ **A)** I and III.
- X **B)** III and IV.
- X **C)** II and IV.
- X **D)** I and II.

#### Explanation

Mutual funds pay dividends from net investment income, and shareholders are liable for taxes on all distributions, whether reinvested or taken in cash.

**Reference:** 10.8.1.1 in the License Exam Manual

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### Question #199 of 210

Question ID: 606666

Customer A and Customer B each have an open account in a mutual fund that charges a front-end load. Customer A has decided to receive all distributions in cash, while Customer B automatically reinvests all distributions. How do their decisions affect their investments?

- I. Receiving cash distributions may reduce Customer A's proportional interest in the fund.
- II. Customer A may use the cash distributions to purchase shares later at NAV.
- III. Customer B's reinvestments purchase additional shares at NAV rather than at the offering price.
- IV. Due to compounding, Customer B's principal will be at greater risk.

- X **A)** I and IV.
- X **B)** II and IV.
- ✓ **C)** I and III.
- X **D)** II and III.

#### Explanation

If the customer elects to receive distributions in cash while other investors purchase shares through reinvestment, his proportional interest in the fund will decline. The option to have distributions automatically reinvested allows those purchases to be made at NAV but a purchase made later would be made at the POP like any other new purchase.

**Reference:** 10.8.1.3.4 in the License Exam Manual

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### Question #200 of 210

Question ID: 606557

Financial information CANNOT be used in a mutual fund prospectus if the information is older than:

- X **A)** 60 days.
- X **B)** 9 months.
- X **C)** 12 months.
- ✓ **D)** 16 months.

Explanation

A mutual fund prospectus may not contain information that is more than 16 months old.

**Reference:** 10.2.1.4 in the License Exam Manual

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**Question #201 of 210**

Question ID: 606606

To qualify for the quantity discount, which of the following may NOT be joined together under the definition of "any person" ?

- X **A)** Father and son in an UTMA account.
- X **B)** Husband and wife investing in a joint account.
- ✓ **C)** Father and his 35-year-old son investing in separate accounts.
- X **D)** Trust officer working on behalf of a single trust account.

Explanation

For the purpose of qualifying for breakpoints, the definition of "any person" includes family units, but only minor children. Adults, other than a husband and wife, are separate persons.

**Reference:** 10.7.5.1 in the License Exam Manual

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**Question #202 of 210**

Question ID: 721448

In a contested proxy (proxy contest) solicitation, all those soliciting proxies from shareholders must register with

- X **A)** NSCC
- X **B)** FINRA
- ✓ **C)** SEC
- X **D)** FRB

Explanation

In a contested proxy solicitation all those soliciting proxies from shareholders must register with the Securities Exchange Commission (SEC).

**Reference:** 9.1.3.2 in the License Exam Manual

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**Question #203 of 210**

Question ID: 606572

Your married customers, ages 48 and 50, have a combined annual income of more than \$200,000. They are concerned about the effects of rising inflation, and since they are heavily invested in bonds, they seek to invest a portion of their portfolio in a fund that will provide additional diversification. Which of the following mutual funds is the *most* suitable for these customers?

- X **A)** ABC Investment-Grade Bond Fund.
- X **B)** XYZ Government Income Fund.
- X **C)** NavCo Tax-Free Municipal Bond Fund.
- ✓ **D)** ATF Overseas Opportunities Fund.

Explanation

Investment in an overseas equity fund will provide diversification not necessarily subject to U.S. inflation. The tax-free fund will not provide additional diversification or the best hedge against inflation. A high-grade bond fund will not add diversification.

**Reference:** 10.5.1.1.7 in the License Exam Manual

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### Question #204 of 210

Question ID: 606564

The transfer agent of a mutual fund:

- I. redeems shares.
- II. sells shares.
- III. holds custody of fund securities.
- IV. handles name changes of mutual fund ownership.

- ☐ A) II and IV.
- ☐ B) I and III.
- ☒ C) I and IV.
- ☐ D) II and III.

#### Explanation

The transfer agent redeems shares of a mutual fund at the price calculated after receiving a request for redemption. The transfer agent also handles the transfer of account ownership for such transactions as an inheritance or gift.

**Reference:** 10.3.4 in the License Exam Manual

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### Question #205 of 210

Question ID: 606676

The open-end investment company share price quoted in the newspaper is the:

- ☐ A) dealer's price.
- ☐ B) confirmed price.
- ☐ C) underwriter's concession.
- ☒ D) bid price.

#### Explanation

Newspaper quotes of mutual fund shares always show the net asset value (NAV), often referred to as the bid price.

**Reference:** 10.10 in the License Exam Manual

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### Question #206 of 210

Question ID: 606562

An investment adviser's contract must be approved by:

- ☐ A) the FINRA district committee.
- ☐ B) the SEC.
- ☐ C) FINRA's National Adjudicatory Council.
- ☒ D) the fund's board of directors or outstanding shares.

#### Explanation

An investment adviser's contract is approved annually by the board of directors or by a majority vote of the outstanding shares.

**Reference:** 10.3.2 in the License Exam Manual

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### Question #207 of 210

Question ID: 606591

Potential investment company clients should be advised to investigate a fund by looking at which of the following?

- I. Investment policy.
- II. Number of shares outstanding.
- III. Custodian bank.
- IV. Portfolio.

- ☐ A) I and III.

- X **B)** II and IV.
- X **C)** II and III.
- ✓ **D)** I and IV.

Explanation

Investment policy, track record, portfolio, and sales load should all be researched when assessing a fund. The identity of the custodian bank for the fund, or number of shares outstanding, does not bear on its performance or suitability.

**Reference:** 10.6 in the License Exam Manual

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**Question #208 of 210**

Question ID: 606571

Which of the following mutual funds should an investment adviser representative recommend to a corporate client whose objective is current income with moderate risk?

- X **A)** High-yield bond fund.
- X **B)** Money market fund.
- ✓ **C)** Preferred stock fund.
- X **D)** Aggressive growth fund.

Explanation

Preferred stock generates current income in the form of dividends. Aggressive growth funds strive for capital appreciation rather than current income. Money market funds have low yields, not the high yields that an income investor wants. While high-yield bonds provide current income, they entail a high, rather than a moderate, degree of risk.

**Reference:** 10.5.1.1.2 in the License Exam Manual

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**Question #209 of 210**

Question ID: 606619

If the ABCD mutual fund has a \$25,000 breakpoint on its Class-A shares where the sales charge decreases from 5% to 4%, which of the following purchases would likely represent a breakpoint sale?

- X **A)** 32000.
- X **B)** 18000.
- X **C)** 26000.
- ✓ **D)** 24000.

Explanation

A breakpoint sale occurs just below a breakpoint where the customer could realize a reduced sales charge. Selling mutual fund shares to a customer just below a breakpoint (to share in the higher sales charges applicable to those sales) is a rules violation.

**Reference:** 10.7.5.1.2 in the License Exam Manual

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**Question #210 of 210**

Question ID: 606655

Mutual fund shareholders are NOT taxed on:

- ✓ **A)** unrealized capital gains.
- X **B)** capital gains distributions.
- X **C)** reinvested dividends.
- X **D)** interest distributions.

Explanation

Interest, dividends, and realized capital gains are all taxed. However, unrealized capital gains are not taxed. Unrealized gains contribute to NAV appreciation and to a shareholder's capital gain upon redemption.

**Reference:** 10.8.1.3 in the License Exam Manual