

PRACTICE EXAM 1

QUESTIONS

- 1. Which of the following is a notice made in the financial press that formally announces a particular transaction, such as an IPO or stock placement?**
 - A. Omitting prospectus
 - B. Preliminary prospectus
 - C. Red herring
 - D. Tombstone ad

- 2. Which of the following is/are correct regarding stock splits and reverse stock splits?**
 - (1) A 3-for-1 stock split will decrease a stock's market price per share.
 - (2) A reverse stock split is intended to increase a stock's market price per share.
 - A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

- 3. Which of the following is the minimum denomination of Treasury notes that can be purchased by an investor?**
 - A. \$50
 - B. \$100
 - C. \$1,000
 - D. \$10,000

- 4. The statement of cash flows is separated into all but which of the following categories?**
 - A. Cash flow from financing activities
 - B. Cash flow from income activities
 - C. Cash flow from investing activities
 - D. Cash flow from operating activities

- 5. Which of the following are permitted investments in an IRA?**
 - (1) Real estate
 - (2) Money market funds
 - (3) Common stock
 - (4) Bond funds
 - A. (3) and (4) only
 - B. (1), (2), and (3) only
 - C. (2), (3), and (4) only
 - D. All of the above are correct.

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- 6. Which of the following statements describes a typical whole life insurance policy?**
- (1) The premiums must be paid for the insured's entire lifetime, or for a period of at least ten years.
 - (2) The cash value cannot be used as collateral for a loan.
 - (3) The difference between a policy's face amount and the reserve must be greater than the cash surrender value at all times.
 - (4) The cash value must equal the face amount of coverage by the end of the mortality table.
- A. (4) only
 - B. (2) and (3) only
 - C. (1), (2), and (3) only
 - D. All of the above are correct.
- 7. Which of the following is correct regarding a mutual fund's turnover rate?**
- A. The higher the turnover rate, the less tax efficient the mutual fund will be. Therefore, funds with high turnover rates are best positioned in taxable accounts.
 - B. The higher the turnover rate, the more tax efficient the mutual fund will be. Therefore, funds with low turnover rates are best positioned in tax-deferred accounts.
 - C. The higher the turnover rate, the less tax efficient the mutual fund will be. Therefore, funds with high turnover rates are best positioned in tax-deferred accounts.
 - D. None of the above are correct.
- 8. If an RIA has between _____ and _____ of assets under management, the RIA may register with either the applicable state(s) where the RIA maintains clients, or the SEC, at the RIA's discretion.**
- A. \$10 million, \$100 million
 - B. \$25 million, \$100 million
 - C. \$50 million, \$150 million
 - D. \$100 million, \$200 million
- 9. Which of the following are correct regarding the role of a trustee?**
- (1) A trustee is the legal owner of trust property.
 - (2) A trustee has a fiduciary duty to income beneficiaries only.
 - (3) A trustee must act at all times for the exclusive benefit of the beneficiaries or he or she may incur a legal liability.
 - (4) A trustee has a fiduciary duty to remainder beneficiaries only.
- A. (1) and (3) only
 - B. (2) and (4) only
 - C. (1), (2), and (3) only
 - D. (1), (3), and (4) only

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10. Which of the following is a system of taxation where one tax rate is applied to all personal income, with no deductions or offsets allowed?

- A. Flat tax
- B. General tax
- C. Single payer tax
- D. Value added tax

11. All but which of the following are correct regarding a bond's call provision?

- A. It protects the issuer from declines in interest rates.
- B. It will cause the investor's required rate of return to be lower.
- C. It may be included in a bond agreement.
- D. It allows the debtor to pay off the debt after a specific period of time at a predetermined price.

12. Defined benefit plans tend to favor older employees for which of the following reasons?

- A. The future value of the participant's promised benefit is greater the less time remaining until retirement.
- B. The present value of the participant's promised benefit is greater the less time remaining until retirement.
- C. The future value of the participant's promised benefit is greater the more time remaining until retirement.
- D. The present value of the participant's promised benefit is greater the more time remaining until retirement.

13. With certain exceptions, which of the following acts requires that firms or sole practitioners compensated for advising others about securities investments must register with the SEC and conform to regulations designed to protect investors?

- A. Securities Act of 1933
- B. Securities Exchange Act of 1934
- C. Investment Advisers Act of 1940
- D. Investment Company Act of 1940

14. An investor who believes that an economic recession is imminent should purchase which of the following type of stocks?

- A. Defensive stocks because they tend to underperform during economic downturns.
- B. Defensive stocks because they tend to outperform during economic downturns.
- C. Cyclical stocks because they tend to outperform during economic downturns.
- D. Cyclical stocks because they tend to underperform during economic downturns.

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- 15. Assume that an investor's portfolio has a realized return of 16%. The realized return of the S&P 500 for the same time period is 18%, and the risk-free rate is 6%. If the beta of the portfolio is 0.75, what is the portfolio's alpha?**
- A. -0.02
B. -0.01
C. +0.01
D. +0.02
- 16. Which of the following accurately describes a complex trust?**
- A. It's a trust with more than one beneficiary.
B. It's a trust that may distribute income annually.
C. It's a trust that reverts back to the grantor's estate at death.
D. It's a trust that is required to distribute all of its income annually.
- 17. Which of the following is used to determine whether an instrument qualifies as an "investment contract" for the purposes of the Securities Act of 1933?**
- A. The Howey test
B. The Knight test
C. The Lochner test
D. The Ralston test
- 18. Kappa Inc., a growing IT company based in California, plans to launch its IPO this year. The IPO will be regulated by which of the following laws?**
- A. Securities Act of 1933
B. Securities Act of 1934
C. Investment Company Act of 1940
D. SIPC of 1970
- 19. Which of the following are characteristics of Series EE bonds?**
- (1) They may be purchased for an amount equal to one-half of face value.
(2) They may be purchased for a minimum price of \$25 for a \$50 bond.
(3) The U.S. Treasury guarantees that an EE bond's value will double after 10 years.
(4) They may be purchased for a maximum price of \$5,000 for a \$10,000 bond.
- A. (1) only
B. (1), (2), and (4) only
C. (2), (3), and (4) only
D. All of the above are correct.

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- 20. Which of the following is the illegal trading practice of manipulating the market by buying and selling a security to create the illusion of high trading activity and to attract other traders who may increase the price?**
- A. Capping and pegging
 - B. Front running
 - C. Painting the tape
 - D. Trading ahead
- 21. Earnings after taxes ÷ Common stockholder equity = _____**
- A. Current ratio
 - B. Net profit margin
 - C. Operating profit margin
 - D. Return on equity
- 22. Dr. Jones, age 29, recently opened a successful dental practice. She's concerned that her young employees will leave for a more experienced dental practice once they're fully trained. In order to retain her young employees, which retirement plan should Dr. Jones adopt?**
- A. Cash balance plan
 - B. Defined benefit plan
 - C. Money purchase plan
 - D. Target benefit plan
- 23. Which of the following mutual fund share classes will charge investors a front-end load?**
- A. Class A shares
 - B. Class B shares
 - C. Class C shares
 - D. Class D shares
- 24. All but which of the following are correct regarding "notice filing" by an RIA?**
- A. Notice filing is required for an RIA to maintain its compliant registration status.
 - B. While most jurisdictions will allow for a "de minimis" number of clients before requiring notice filing, some jurisdictions may require notice filing upon taking on the first client in that jurisdiction.
 - C. Having a "place of business," as defined by applicable regulatory statutes, does not require notice filing unless the firm has 5 or more clients in the jurisdiction.
 - D. All of the above are correct.

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25. In order to be eligible to make a traditional IRA contribution, an individual must be younger than age _____ by the end of the taxable year.
- A. 59 ½
 - B. 65
 - C. 70 ½
 - D. 71
26. Which of the following are backed by the full faith and credit of the government issuing the bonds and are repaid through taxes collected by the government body?
- A. General obligation bonds
 - B. Moral obligation bonds
 - C. Private purpose bonds
 - D. Revenue bonds
27. Which of the following techniques can be used to reduce an individual's gross estate, and therefore, reduce estate taxes?
- A. Family limited partnership
 - B. Payable on death account
 - C. Living trust
 - D. Totten trust
28. Which of the following regulations governs the extension of credit by broker-dealers and controls the margin requirements for stock purchases?
- A. Regulation D
 - B. Regulation S
 - C. Regulation T
 - D. Regulation U

The following information relates to questions 29 – 31.

Alex had several capital gains and losses for the current year. His long-term capital gains were \$3,200, his long-term capital losses were \$2,800, his short-term capital gains were \$800, and his short-term capital losses were \$3,500.

29. What is the amount of net long-term capital gains?

- A. \$0
- B. \$400
- C. \$700
- D. \$2,400

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30. What is the amount of net short-term capital gains?

- A. -\$2,700
- B. -\$700
- C. -\$400
- D. \$0

31. What is the total calculated capital gain or capital loss?

- A. \$2,300 net short-term capital loss
- B. \$2,300 net short-term capital gain
- C. \$3,000 net short-term capital loss
- D. \$3,000 net short-term capital gain

32. Which of the following is a characteristic of a variable life insurance policy?

- A. Premiums and death benefits are flexible.
- B. A minimum death benefit is guaranteed.
- C. It is made up of increasing units of term insurance and a guaranteed cash value.
- D. The death benefit is linked to the performance of the S&P 500 only.

33. Which of the following rules establishes standards for the content, approval, record-keeping, and filing of communications with FINRA, and must be followed by firms when communicating with the public, including communications with retail and institutional investors?

- A. FINRA Rule 2111
- B. FINRA Rule 2210
- C. FINRA Rule 3240
- D. FINRA Rule 3270

34. Assume the next dividend for Epsilon stock will be \$3 per share, and investors require a 12% rate of return to purchase the stock. If the dividend for Epsilon stock increases by 4% each year, what price should the stock be selling for today?

- A. \$22.50 per share
- B. \$27.50 per share
- C. \$32.50 per share
- D. \$37.50 per share

35. An option that can be exercised only at its expiration date is a/an _____ style option.

- A. American
- B. Asian
- C. Australian
- D. European

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36. Which of the following is the oldest international investor protection organization and is an association of state securities administrators who are charged with the responsibility to protect consumers who purchase securities or investment advice? Its membership consists of administrators from the territories, districts, and states of the U.S., Mexico, and Canada.

- A. NAIC
- B. NASAA
- C. NASD
- D. NSCC

37. In which of the following does the donor transfer income-producing property to a reversionary trust, and then directs the trust income to be transferred to a qualified charity initially for a period of time not to exceed twenty years?

- A. Charitable lead trust
- B. Charitable remainder trust
- C. Grantor retained trust
- D. Pooled income fund

38. All but which of the following are correct regarding the Securities Exchange Act of 1934?

- A. It created the SEC.
- B. It regulates securities transactions in the secondary market.
- C. It is referred to as the "truth in securities" law.
- D. It includes provisions for other areas of securities law, including insider trading, antifraud, and proxy solicitation.

39. All but which of the following are correct regarding a "not held" order?

- A. It applies mainly to international equities.
- B. It is a market or limit order in which the customer does not want to transact automatically at the inside market, but instead has given the broker time and price discretion in transacting on a best-efforts basis.
- C. The customer is placing full confidence in the broker to execute the trade at the best price.
- D. The broker may be held liable for missing the price within the limits (limit not held) or obtaining a worse price (market not held).

40. On a company's balance sheet, assets are reported at their:

- A. discounted value.
- B. expected future value.
- C. fair market value.
- D. original cost.

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For questions 41 – 45, match the type of retirement plan with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Money purchase plan
- B. Target benefit plan
- C. Flat benefit plan
- D. SEP
- E. Cash balance plan
- F. Profit sharing plan
- G. Unit benefit plan

41. ___ A plan similar to a defined benefit plan because contributions are based on projected retirement benefits.
42. ___ A type of defined contribution plan that is not a pension plan.
43. ___ A defined benefit plan that defines the employee's benefit in terms that are more characteristic of a defined contribution plan.
44. ___ The employer calculates the contribution by multiplying an employee's years of service by a percentage of his or her salary.
45. ___ A plan that requires a fixed percentage of compensation be contributed for each eligible employee.
46. Which of the following is a fraudulent investment operation where the operator provides fabricated reports and generates investment returns for older investors through revenue paid by new investors, rather than from legitimate business activities or profits of financial trading?
- A. Pump and dump scheme
 - B. Ponzi scheme
 - C. Matrix scheme
 - D. Bucket shop scheme
47. Erin inherited shares of Beta stock that are currently valued at \$850,000. To retire and maintain her lifestyle, she requires a fixed 6% payout for life. Which of the following trusts will allow Erin to achieve her goal?
- A. Charitable remainder annuity trust
 - B. Charitable remainder unitrust
 - C. Charitable lead annuity trust
 - D. Charitable lead unitrust

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48. An investment adviser will be deemed to have custody of client assets if which of the following apply?

- A. The advisor has possession of client funds or securities and does not return them to the client within 3 days.
- B. The advisor is authorized or permitted to withdraw client funds or securities.
- C. The adviser has legal ownership or access to client funds or securities.
- D. All of the above are correct.

49. All but which of the following are characteristics of American Depository Receipts (ADRs)?

- A. They are traded on secondary exchanges.
- B. They represent ownership interest in foreign securities denominated in U.S. dollars.
- C. They involve banks collecting money in U.S. dollars and then converting into foreign currency for ADR holders.
- D. They are issued by banks in foreign countries.

50. Which of the following was adopted to update short sale regulations and to address concerns regarding potentially abusive naked short selling?

- A. Regulation BTR
- B. Regulation HFT
- C. Regulation NMS
- D. Regulation SHO

51. In 2016, Theta LLC reported total revenue of \$800,000, total expenses of \$650,000, and net income of \$150,000. If accounts receivable increased by \$90,000, then how much cash did Theta LLC receive from customers?

- A. \$560,000
- B. \$710,000
- C. \$800,000
- D. \$890,000

52. All but which of the following are correct regarding the Central Registration Depository (CRD)?

- A. It was developed by NASAA and the NASD.
- B. It consolidated a multiple paper-based state licensing and regulatory process into a single, nationwide computer system.
- C. Its computerized database contains the licensing and disciplinary histories on more than 650,000 securities professionals and 5,200 securities firms.
- D. All of the above are correct.

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53. The Russell 2000 measures the performance of _____ U.S. stocks.

- A. small-cap
- B. mid-cap
- C. large-cap
- D. blended

54. Which of the following is correct regarding commercial paper?

- A. It has a maturity of 270 days or less.
- B. It's issued in denominations of \$1,000 or more.
- C. It does not act as a viable substitute for short-term bank financing.
- D. It has less default risk than Treasury bills.

55. Which of the following is considered a hybrid security?

- A. Common stock
- B. Corporate bond
- C. Preferred stock
- D. REIT

For questions 56 – 62, match the economic indicator with the description that follows.
Use only one answer per blank. Answers may be used more than once or not at all.

- A. Leading economic indicator
- B. Lagging economic indicator

56. ___ Change in consumer sentiment

57. ___ Average prime rate charged by banks

58. ___ Change in the Consumer Price Index (CPI)

59. ___ Orders for durable goods

60. ___ Average duration of unemployment

61. ___ Change in money supply

62. ___ Housing starts

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63. Which of the following is correct regarding Coverdell Education Savings Accounts (ESAs)?

- A. Private elementary school expenses are permitted to be paid from an ESA.
- B. The maximum annual contribution to an ESA is \$5,000.
- C. Secondary school expenses are not permitted to be paid from an ESA.
- D. All of the above are correct.

64. Which of the following investment strategies is profitable in a declining stock market?

- (1) Buying a call
 - (2) Buying a put
 - (3) Selling a put
 - (4) Selling a call
- A. (1) and (3) only
 - B. (1) and (4) only
 - C. (2) and (3) only
 - D. (2) and (4) only

65. Which of the following will result if a distribution is taken from a health savings account (HSA) by an individual under age 65, and the distribution is not used to pay for qualified medical expenses?

- A. The distribution is subject to ordinary income tax only.
- B. The distribution is subject to ordinary income tax and a 20% penalty.
- C. The distribution is subject to ordinary income tax and a 25% penalty.
- D. The distribution is not subject to tax.

66. An IRA must be created and funded by _____ of the calendar year following the year in which the contribution applies.

- A. January 1
- B. April 15
- C. June 31
- D. December 31

67. Which of the following theories is based on the assumption that investors are risk averse, and they will prefer higher returns to lower returns for a given level of risk?

- A. Arbitrage pricing theory
- B. Black-scholes valuation theory
- C. Efficient market theory
- D. Modern portfolio theory

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68. What is the taxable equivalent yield of a municipal bond that has a tax-free yield of 6%? Assume the investor is in the 28% tax bracket.

- A. 4.69%
- B. 7.68%
- C. 8.33%
- D. 21.43%

69. All but which of the following are correct regarding the tenancy by entirety form of property ownership?

- A. It is an interest in property that can be held only by spouses.
- B. The property automatically passes to the surviving spouse when one spouse dies.
- C. It is an interest in property that can be held by non-spouses in an incorporated business such as an LLC, S Corp, or C Corp.
- D. In most states, it is not severable by an individual spouse.

70. Which of the following are characteristics of a zero-coupon bond?

- (1) It does not make periodic interest payments throughout the term of the bond.
- (2) It has significant reinvestment risk because no payments are made until the bond matures.
- (3) It requires taxes to be paid on accrued interest each year, even though no interest is received.
- (4) The duration of a zero-coupon bond is less than its term to maturity.

- A. (1) and (3) only
- B. (2) and (4) only
- C. (1), (2), and (3) only
- D. (2), (3), and (4) only

71. All but which of the following are characteristics of exchange-traded funds (ETFs)?

- A. They are traded on an exchange like individual securities.
- B. Their trades settle at the end of the trading day, similar to mutual funds.
- C. They have lower expenses than mutual funds.
- D. They are income tax efficient.

72. According to FINRA Rule 3240, which of the following is correct regarding borrowing and lending arrangements between an RIA and its customers?

- A. The specific borrowing/lending arrangement must meet certain conditions, such as the customer cannot be an immediate family member.
- B. Proper notification of the borrowing or lending arrangement must be given, but advanced approval is not required.
- C. The member firm must have a written policy in place regarding borrowing and lending arrangements.
- D. All of the above are correct.

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73. A stock with a beta of -1.5 and a standard deviation of 10.1 will change in which of the following ways if the stock market increases 8%?
- A. Increase by 4%
 - B. Increase by 8%
 - C. Decrease by 10%
 - D. Decrease by 12%
74. _____ risk cannot be eliminated through diversification because it affects the entire market. _____ risk may be diversified away or avoided by not investing in securities that exhibit the risk.
- A. Non-systematic, Unsystematic
 - B. Unsystematic, Systematic
 - C. Systematic, Unsystematic
 - D. Total, Systematic
75. Short-term capital gains tax rates apply if an asset is held for:
- A. 12 months or less.
 - B. less than 12 months.
 - C. 6 months or less using the half-year convention.
 - D. less than 6 months using the half-year convention.
76. The Bank Secrecy Act of 1970 requires financial institutions to assist U.S. government agencies in detecting and preventing money laundering by filing reports of cash transactions exceeding which of the following daily aggregate amounts?
- A. \$5,000
 - B. \$10,000
 - C. \$50,000
 - D. \$100,000
77. Your client is interested in participating in his company's qualified retirement plan. He has completed one year of service and assumed that he was now eligible to participate. However, his employer will not let him enroll in the plan until next year. You tell your client that eligibility may be postponed until the completion of his second year of service if which of the following conditions apply?
- A. The employer agrees to match 100% of employee deferrals up to 10% of compensation.
 - B. Contributions are made based on an age-weighted formula.
 - C. Contributions are 100% immediately vested upon eligibility.
 - D. Key employees must wait three years to enroll.

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78. Which of the following rules permits the public resale of restricted or control securities if a number of conditions are met, including how long the securities are held, the way in which they are sold, and the amount that can be sold at any one time?

- A. Securities Act Rule 144
- B. Securities Act Rule 405
- C. Securities Act Rule 433
- D. Securities Act Rule 506

79. Which of the following variables are used to calculate a stock's beta coefficient?

- (1) The standard deviation of the return for a particular security.
 - (2) The correlation coefficient between the return for a particular security and the return for the overall market.
 - (3) The standard deviation of the return for the overall market.
 - (4) The coefficient of determination.
- A. (2) only
 - B. (4) only
 - C. (1) and (3) only
 - D. (1), (2), and (3) only

The following information relates to questions 80 – 81.

Earlier this year, Pete exchanged a \$500,000 ordinary life insurance policy for an annuity. He paid \$90,000 in premiums over the life of the policy, and the cash value at the time of the exchange was \$62,000.

80. What is Pete's basis in the annuity?

- A. \$28,000
- B. \$62,000
- C. \$90,000
- D. \$152,000

81. What would be Pete's basis if he used \$25,000 of dividends to reduce the premium?

- A. \$62,000
- B. \$65,000
- C. \$90,000
- D. \$115,000

82. Which of the following corporate voting procedures entitles a shareholder to one vote per share, and votes must be divided evenly among the candidates being voted on?

- A. Accumulated voting
- B. Cumulative voting
- C. Non-regulatory voting
- D. Statutory voting

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83. A participant in a defined contribution plan is least affected by which of the following factors?

- A. Account balance
- B. Investment performance
- C. Life expectancy
- D. Pre-retirement inflation

84. Which of the following is/are correct regarding the capital structure of closed-end mutual funds?

- (1) A closed-end mutual fund has a fixed number of shares that, after original issue, trade on the secondary market.
- (2) The price an investor pays when buying shares of a closed-end mutual fund is based on supply and demand.

- A. (1) only
- B. (2) only
- C. Both (1) and (2) are correct.
- D. Neither (1) or (2) are correct.

85. Which of the following is the measure of a company's ability to pay its debt obligations?

- A. Return on debt
- B. Return on assets
- C. Times interest earned ratio
- D. Turnover ratio

For questions 86 – 88, match the dividend date with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Date of declaration
- B. Ex-dividend date
- C. Date of record
- D. Date of payment

86. ___ The date that the board of directors approves and decides that a dividend will be paid.

87. ___ The date that it is determined who owns stock in the company and is entitled to receive a dividend.

88. ___ The date that the market price of the stock adjusts for the dividend.

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- 89. Which of the following option strategies involves an investor holding a position in both a call and put for the same underlying security, with the same strike price and expiration date?**
- A. Collar
 - B. Naked call
 - C. Spread
 - D. Straddle
- 90. In 2017, the SEC adopted an amendment to the Settlement Cycle Rule under the Securities Exchange Act of 1934 that changed the standard settlement cycle for most broker-dealer transactions in which of the following ways?**
- A. The standard settlement cycle was shortened from 3 business days after the trade (T+3) to 2 business days after the trade (T+2).
 - B. The standard settlement cycle was shortened from 2 business days after the trade (T+2) to 1 business day after the trade (T+1).
 - C. The standard settlement cycle was lengthened from 1 business day after the trade (T+1) to 2 business days after the trade (T+2).
 - D. The standard settlement cycle was lengthened from 2 business days after the trade (T+2) to 3 business days after the trade (T+3).
- 91. A federal gift tax return must be filed if which of the following events occur?**
- A. A gift of a future interest in property has been made for \$5,000.
 - B. Spouses have split a \$5,000 gift of individually owned property.
 - C. The gifts from a donor to any single donee for a calendar year exceed the amount of the gift tax annual exclusion.
 - D. All of the above are correct.
- 92. SEC-registered investment advisers must deliver which of the following to each client or prospective client?**
- A. Form ADV Part 2A (brochure) only
 - B. Form ADV Part 2 (brochure supplement) only
 - C. Form ADV Part 2A (brochure) and Part 2 (brochure supplement)
 - D. Form ADV Part 1 and Part 2A (brochure)
- 93. Which of the following are profitability ratios?**
- (1) Operating profit margin
 - (2) Net profit margin
 - (3) Return on assets
 - (4) Return on equity
- A. (3) and (4) only
 - B. (1), (2), and (3) only
 - C. (1), (3), and (4) only
 - D. All of the above are correct.

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- 94. Kappa Inc., a C Corp, had a profitable year and has extra money to invest. The owners would like to maximize the after-tax income to the corporation. Which of the following investments would best help them achieve their goal?**
- A. Value stocks
 - B. Preferred stock
 - C. Municipal bonds
 - D. Highly-rated corporate bonds
- 95. Which of the following occurs when the supply of goods and services exceeds their demand?**
- A. Deflation
 - B. Inflation
 - C. Stagflation
 - D. Price stability
- 96. Which of the following is the formula to calculate an investment's public offering price (POP)?**
- A. $\text{POP} = \text{NAV} \div \text{Sales charge}$
 - B. $\text{POP} = \text{Sales charge} \div \text{NAV}$
 - C. $\text{POP} = \text{NAV} + \text{Sales charge}$
 - D. $\text{POP} = \text{NAV} - \text{Sales charge}$
- 97. Which of the following is a self-liquidating investment in real estate mortgages and mortgage-backed securities?**
- A. GIC
 - B. REIT
 - C. REMIC
 - D. UIT
- 98. Which of the following is the FINRA-developed vehicle that facilitates the mandatory reporting of over-the-counter secondary market transactions in eligible fixed income securities? All broker-dealers who are FINRA member firms have an obligation to report transactions in corporate bonds to this vehicle under an SEC-approved set of rules.**
- A. ACT
 - B. AML
 - C. CTR
 - D. TRACE

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99. Which of the following is the market value of all the goods and services produced in one year by labor and property supplied by the citizens of a country, wherever they are located?
- A. GDP
 - B. GNP
 - C. NDP
 - D. NNP
100. According to Regulation D, firms may sell private placements to how many non-accredited investors in a 12-month period?
- A. 0
 - B. 25
 - C. 35
 - D. 50
101. Which of the following are permitted distribution options from a qualified retirement plan?
- (1) Lump sum distribution
 - (2) Direct trustee-to-trustee transfer
 - (3) Payment in the form of an annuity or other periodic payment option
 - (4) Rollover of funds from one qualified retirement plan to another
- A. (1) and (3) only
 - B. (1), (2), and (4) only
 - C. (2), (3), and (4) only
 - D. All of the above are correct.
102. A call is an option to _____ a specified number of shares of stock during a specified period at a specified price. A buyer of a call option expects the price of the underlying stock to _____.
- A. buy, fall
 - B. buy, rise
 - C. sell, fall
 - D. sell, rise
103. All but which of the following are underlying assumptions of the capital asset pricing model (CAPM)?
- A. All investors have the same one-period time horizon.
 - B. All investors have the same expectations about the risk-return relationship of assets.
 - C. Investors can borrow and lend at a specific risk-free rate of return equal to zero.
 - D. There are no transaction costs, taxes, or inflation.

Practice Exam 1

- 104.** According to FINRA's eligibility requirements, statutory disqualification will result for certain misdemeanors and all felony criminal convictions for a period of _____ from the date of conviction.
- A. 5 years
 - B. 10 years
 - C. 15 years
 - D. 20 years
- 105.** Which of the following is a set of documents, including a prospectus, which a company must file with the SEC pursuant to the Securities Act of 1933 before it proceeds with a public offering?
- A. Prospectus statement
 - B. Red herring
 - C. Registration statement
 - D. Tombstone ad
- 106.** According to the principles of behavioral finance, which theory suggests that investors typically fear losses more than they value gains? As a result, investors will often choose the smaller of two potential gains if it avoids a highly probable loss.
- A. Game theory
 - B. Prospect theory
 - C. Utility theory
 - D. Zero sum theory
- 107.** If interest rates _____ following a bond issue, a sinking-fund provision will allow the issuing company to reduce the interest rate risk of its bonds as it replaces a portion of the existing debt with _____ bonds.
- A. decline, higher yielding
 - B. decline, lower yielding
 - C. rise, higher yielding
 - D. rise, lower yielding
- 108.** Which of the following is a daily publication of the National Quotation Bureau that details the bid and asked prices of corporate bonds traded in the over-the-counter market?
- A. Blue sheets
 - B. Pink sheets
 - C. White sheets
 - D. Yellow sheets

Practice Exam 1

109. The efficient market hypothesis suggests all but which of the following?

- A. Investors are unable to outperform the stock market on a consistent basis.
- B. Daily fluctuations in stock prices are a result of modern portfolio theory.
- C. The stock market's efficiency in valuing securities is rapid and accurate.
- D. Any excess returns are temporary and will regress to the mean.

110. Gamma Inc. provides the following information for the fiscal year:

Net income	\$660,000
Number of shares outstanding	40,000
Price per share	\$19.50
Total assets	\$3,250,000
Total liabilities	\$2,980,000

What is Gamma Inc.'s book value?

- A. \$78,000
- B. \$192,000
- C. \$270,000
- D. \$930,000

111. All but which of the following are correct regarding pooled income funds?

- A. A pooled income fund is generally created by a public charity, such as a private or public higher education institution or a not-for-profit hospital.
- B. A benefit of a pooled income fund is that it can invest in tax-exempt securities.
- C. In a pooled income fund, the donor's gifted property is commingled with property transferred by other donors.
- D. Additional contributions of property are permitted into a pooled income fund.

112. Which of the following are among the goals of the Federal Reserve?

- A. To achieve full employment.
- B. To minimize systematic risk.
- C. To stabilize prices.
- D. All of the above are correct.

113. Which of the following is a tax imposed in such a manner that the tax rate decreases as the amount subject to taxation increases?

- A. Corporate tax
- B. Progressive tax
- C. Regressive tax
- D. Value added tax

Practice Exam 1

114. Which of the following has the mission of protecting investors, municipal entities, and the public interest by promoting a fair and efficient municipal market, regulating firms that engage in municipal securities and advisory activities, and promoting market transparency?

- A. AMBAC
- B. FNMA
- C. GNMA
- D. MSRB

115. A large interest rate change has the most significant effect on a _____ bond.

- A. low coupon
- B. short duration
- C. high coupon
- D. short maturity

116. Which of the following lists the assets provided in the correct order from most liquid to least liquid?

- (1) Real estate
- (2) Treasury bills
- (3) Limited partnership
- (4) Investment-grade corporate bonds

- A. 2, 1, 4, 3
- B. 4, 2, 3, 1
- C. 3, 1, 4, 2
- D. 2, 4, 1, 3

117. Which of the following is/are correct regarding the objectives of ERISA?

- (1) ERISA requires retirement plan sponsors to disclose full and accurate information about qualified retirement plan activity to all participants.
- (2) ERISA guarantees future benefits at a minimum level for defined benefit plans as part of the PBGC.

- A. (1) only
- B. (2) only
- C. Both (1) and (2) are correct.
- D. Neither (1) or (2) are correct.

118. Treasury STRIPS are always issued at a:

- A. premium to par.
- B. discount to par.
- C. price equal to par.
- D. price above or equal to par.

Practice Exam 1

119. Lauren purchased a bond with a face value of \$1,000 and a coupon rate of 4.5%. Her effective tax rate is 25%. If the risk-free rate is 4%, and coupon payments are made semiannually, what is the periodic interest payment?
- A. \$16.88, paid twice per year.
 - B. \$22.50, paid twice per year.
 - C. \$45.00, paid once per year.
 - D. \$45.00, paid twice per year.
120. In addition to the federal securities laws, each state has its own set of securities laws, commonly referred to as _____, which are designed to protect investors against fraudulent sales practices and activities.
- A. Blue ocean laws
 - B. Blue sky laws
 - C. Green field laws
 - D. Open field laws
121. Which of the following is correct regarding TIPS?
- A. Investors are paid either the adjusted principal amount at maturity, or the original principal amount, whichever is greater.
 - B. They pay interest annually.
 - C. The payments increase with inflation but never decrease.
 - D. They have a final maturity up to 10 years from the date of issue.
122. Which of the following is a contract between an investor and an issuer in which the issuer guarantees payment of a stated sum to the investor at some set date in the future? In return for this future payment, the investor agrees to pay the issuer a set amount of money either as a lump sum or in periodic installments.
- A. ETN
 - B. FAC
 - C. ISO
 - D. NQSO
123. Which of the following is a theory stating that an investment company that passes all capital gains, interest, and dividends through to its shareholders shouldn't be taxed at the corporate level?
- A. Capital gain theory
 - B. Conduit theory
 - C. Passive income theory
 - D. Tax harvest theory

Practice Exam 1

- 124. Which of the following is an order to purchase a security at or below a specified price?**
- A. Buy stop order
 - B. Buy market order
 - C. Buy limit order
 - D. None of the above are correct.
- 125. All but which of the following are correct regarding advertising activities engaged in by an RIA?**
- A. Advertisements include any notice, circular, or letter addressed to more than one person.
 - B. Social media communications, such as Twitter feeds and online blogs, are not considered advertisements.
 - C. Advertisements are not permitted to use the initials "RIA" or "IAR."
 - D. All of the above are correct.
- 126. The FDIC maintains stability and public confidence in the nation's financial system by doing all but which of the following?**
- A. Insuring deposits.
 - B. Managing receiverships.
 - C. Examining and supervising financial institutions for safety, soundness, and consumer protection.
 - D. Setting minimum standards for voluntarily established pension and health plans.
- 127. Which of the following acts was intended to reshape the U.S. regulatory system in a number of areas including consumer protection, trading restrictions, credit ratings, regulation of financial products, corporate governance and disclosure, and transparency?**
- A. Patriot Act of 2001
 - B. Sarbanes-Oxley Act of 2002
 - C. Fair and Accurate Credit Transactions Act of 2003
 - D. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
- 128. Which of the following is/are correct regarding a bond's coupon rate?**
- (1) The smaller a bond's coupon, the greater its relative price fluctuation.
- (2) The smaller a bond's coupon, the greater its reinvestment risk.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

Practice Exam 1

129. Which of the following insures the interest and principal payments for municipal bonds and other public finance debt obligations?

- A. AMBAC
- B. DOL
- C. FDIC
- D. PBGC

130. All but which of the following are types of annuity settlement options?

- A. Extended term
- B. Installment refund
- C. Life with period certain
- D. Single life

ANSWER KEY

1. D

A tombstone ad is a notice made in the financial press that formally announces a particular transaction, such as an IPO or stock placement.

2. C

A 3-for-1 stock split will decrease a stock's market price per share. A reverse stock split is intended to increase a stock's market price per share.

3. B

Treasury notes are sold in minimum denominations of \$100.

4. B

The statement of cash flows is separated into the following three categories: cash flow from financing activities, cash flow from investing activities, and cash flow from operating activities.

5. D

IRAs may invest in all four types of investments, including real estate (REITs).

6. A

The cash value of a whole life insurance policy must equal the face amount of coverage by the end of the mortality table.

7. C

The higher the turnover rate, the less tax efficient the mutual fund will be. Therefore, funds with high turnover rates are best positioned in tax-deferred accounts.

8. B

If an RIA has between \$25 million and \$100 million of assets under management, the RIA may register with either the applicable state(s) where the RIA maintains clients, or the SEC. Due to legislation, exceptions may apply.

9. A

A trustee is the legal owner of trust property. A trustee must act at all times for the exclusive benefit of the beneficiaries or he or she may incur a legal liability. A trustee has a fiduciary duty to all trust beneficiaries regardless of whether they are income or remainder beneficiaries.

10. A

A flat tax is a system of taxation where one tax rate is applied to all personal income, with no deductions or offsets allowed.

11. B

A bond's call provision may be included in a bond agreement, and it allows the debtor to pay off the debt after a specific period of time at a predetermined price. It protects the issuer from declines in interest rates. If a bond is callable it will cause an investor's required rate of return to be higher.

Practice Exam 1

12. B

Defined benefit plans tend to favor older employees because the present value of the participant's promised benefit is greater the less time remaining until retirement.

13. C

With certain exceptions, the Investment Advisers Act of 1940 requires that firms or sole practitioners compensated for advising others about securities investments must register with the SEC and conform to regulations designed to protect investors.

14. B

An investor who believes that an economic recession is imminent should purchase defensive stocks because they tend to outperform during economic downturns.

15. C

$$\alpha_p = R_p - [R_f + \beta_p(R_m - R_f)]$$

$$\alpha_p = 0.16 - [0.06 + 0.75(0.18 - 0.06)] = 0.01$$

16. B

In a complex trust, income may be distributed, but it is not required. The trustee has the discretion to accumulate income. Unlike a complex trust, a simple trust must distribute all of its income annually.

17. A

The Howey test is the result of the U.S. Supreme Court case, Securities and Exchange Commission v. W. J. Howey Co. from 1946. It is used to determine whether an instrument qualifies as an "investment contract" for the purposes of the Securities Act of 1933.

18. A

The Securities Act of 1933 regulates new securities, including IPOs.

19. B

Series EE bonds may be purchased for an amount equal to one-half of face value. The minimum price is \$25 for a \$50 bond, and the maximum price is \$5,000 for a \$10,000 bond. At a minimum, the U.S. Treasury guarantees that an EE bond's value will double after 20 years.

20. C

Painting the tape is the illegal trading practice of manipulating the market by buying and selling a security to create the illusion of high trading activity and to attract other traders who may increase the price.

21. D

Earnings after taxes ÷ Common stockholder equity = Return on equity

22. C

The cash balance plan, defined benefit plan, and target benefit plan all favor older employees. Money purchase plans guarantee a contribution will be made each year and will help Dr. Jones achieve her goal of retaining her young employees.

Practice Exam 1

23. A

Class A mutual fund shares charge a front-end load.

24. C

Notice filing is required for an RIA to maintain its compliant registration status. While most jurisdictions will allow for a "de minimis" number of clients before requiring notice filing, some jurisdictions may require notice filing upon taking on the first client in that jurisdiction. Having a "place of business," as defined by applicable regulatory statutes, in a state will require notice filing regardless of the number of clients in that jurisdiction.

25. C

In order to be eligible to make a traditional IRA contribution, an individual must be younger than age 70 ½ by the end of the taxable year.

26. A

General obligation bonds are backed by the full faith and credit of the government issuing the bonds and are repaid through taxes collected by the government body.

27. A

A family limited partnership can be used to reduce an individual's gross estate, and therefore, reduce estate taxes. The other items may be used to reduce an individual's probate estate, but not his or her gross estate.

28. C

Regulation T governs the extension of credit by broker-dealers and controls the margin requirements for stock purchases.

29. B

$\$3,200 - \$2,800 = \$400$ net long-term capital gain

30. A

$\$3,500 - \$800 = \$2,700$ net short-term capital loss

31. A

$\$2,700 - \$400 = \$2,300$ net short-term capital loss

32. B

Variable life insurance policies have fixed premiums and provide a guaranteed minimum death benefit. The cash value is linked to the performance of underlying investments, which may include the S&P 500.

33. B

FINRA Rule 2210 establishes standards for the content, approval, recordkeeping, and filing of communications with FINRA, and must be followed by firms when communicating with the public, including communications with retail and institutional investors.

34. D

Price = $D_1 \div (r - g)$

Price = $\$3 \div (0.12 - 0.04) = \37.50 per share

Practice Exam 1

35. D

An option that can be exercised only at its expiration date is a European style option.

36. B

The NASAA (North American Securities Administrators Association) is the oldest international investor protection organization and is an association of state securities administrators who are charged with the responsibility to protect consumers who purchase securities or investment advice. Its membership consists of administrators from the territories, districts, and states of the U.S., Mexico, and Canada.

37. A

In a charitable lead trust, the donor transfers income-producing property to a reversionary trust, and then directs the trust income to be transferred to a qualified charity initially for a period of time not to exceed twenty years.

38. C

The Securities Exchange Act of 1934 created the SEC, regulates the securities transactions in the secondary market, and includes provisions for other areas of securities law, including insider trading, antifraud, and proxy solicitation. The "truth in securities" law is another name for the Securities Act of 1933.

39. D

With a "not held" order, the broker will not be held responsible for missing the price within the limits (limit not held) or obtaining a worse price (market not held). A "not held" order applies mainly to international equities, and it's a market or limit order in which the customer does not want to transact automatically at the inside market, but instead has given the broker time and price discretion in transacting on a best-efforts basis. The customer is placing full confidence in the broker to execute the trade at the best price.

40. C

On a company's balance sheet, assets are reported at their fair market value.

41. B

A target benefit plan is similar to a defined benefit plan because contributions are based on projected retirement benefits.

42. F

Defined contribution plans can be either pension plans or profit sharing plans.

43. E

A cash balance plan is a type of defined benefit plan that defines the employee's benefit in terms that are more characteristic of a defined contribution plan.

44. G

In a unit benefit plan, the employer calculates the contribution by multiplying an employee's years of service by a percentage of his or her salary.

45. A

A money purchase plan requires that a fixed percentage of compensation be contributed for each eligible employee.

Practice Exam 1

46. B

A Ponzi scheme is a fraudulent investment operation where the operator provides fabricated reports and generates returns for older investors through revenue paid by new investors, rather than from legitimate business activities or profits of financial trading.

47. A

A charitable remainder annuity trust (CRAT) can pay Erin a fixed percentage of the initial fair market value of the trust. With a charitable remainder unitrust (CRUT), the annual payout would be based on the fair market value of the trust revalued annually.

48. D

An investment advisor will be deemed to have custody of client assets if the advisor has possession of client funds or securities and does not return them to the client within 3 days, the advisor is authorized or permitted to withdraw client funds or securities, or the adviser has legal ownership or access to client funds or securities.

49. C

For ADRs, banks collect money in their local currency and then convert to U.S. dollars. ADRs are traded on secondary exchanges and represent ownership interest in foreign securities denominated in U.S. dollars. They are issued by banks in foreign countries.

50. D

Regulation SHO was adopted to update short sale regulations and to address concerns regarding potentially abusive naked short selling.

51. B

Cash received from customers = Revenue – Increase in accounts receivable

Cash received from customers = \$800,000 – \$90,000 = \$710,000

52. D

The Central Registration Depository (CRD) was developed by NASAA and the NASD, and it consolidated a multiple paper-based state licensing and regulatory process into a single, nationwide computer system. Its computerized database contains the licensing and disciplinary histories on more than 650,000 securities professionals and 5,200 securities firms.

53. A

The Russell 2000 measures the performance of small-cap U.S. stocks.

54. A

Commercial paper has a maturity of 270 days or less and is issued in denominations of \$100,000 or more.

55. C

Preferred stock is considered a hybrid security because it has characteristics of both common stock and fixed-income investments.

56. A

A change in consumer sentiment is a leading economic indicator.

Practice Exam 1

57. B

The average prime rate charged by banks is a lagging economic indicator.

58. B

A change in the Consumer Price Index (CPI) is a lagging economic indicator.

59. A

Orders for durable goods are a leading economic indicator.

60. B

The average duration of unemployment is a lagging economic indicator.

61. A

A change in the money supply is a leading economic indicator.

62. A

Housing starts are a leading economic indicator.

63. A

Money in a Coverdell Education Savings Account (ESA) may be used to pay private elementary and/or secondary school expenses. The maximum contribution to an ESA is \$2,000 per beneficiary per year.

64. D

Buying a put and selling a call are bearish strategies that are profitable in a declining stock market.

65. B

Distributions from a health savings account (HSA) that are not used to pay for qualified medical expenses are subject to ordinary income tax and a 20% penalty. The penalty is waived if the individual is age 65 or older.

66. B

An IRA must be created and funded by April 15 of the calendar year following the year in which the contribution applies.

67. D

Modern portfolio theory is based on the assumption that investors are risk averse, and they will prefer higher returns to lower returns for a given level of risk.

68. C

Taxable equivalent yield = $0.06 \div (1 - 0.28) = 0.0833 = 8.33\%$

69. C

Tenancy by entirety is a form of joint tenancy allowed only for married couples. The property automatically passes to the surviving spouse when one spouse dies, and in most states it is not severable by an individual spouse.

Practice Exam 1

70. A

A zero-coupon bond does not make periodic interest payments, however it requires taxes to be paid on accrued interest each year. A zero-coupon bond has no reinvestment risk, and its duration is equal to its term to maturity.

71. B

Exchange-traded funds (ETFs) may be bought or sold throughout the trading day like individual securities. They have lower expenses than mutual funds and are income tax efficient.

72. C

According to FINRA Rule 3240, borrowing and lending arrangements between an RIA and its customers requires the member firm to have a written policy in place.

73. D

$$8\% \times -1.5 = -12\%$$

A stock with a beta of -1.5 will move 150% in the opposite direction of the market. Therefore, if the stock market increases by 8%, the stock will decrease by 12%.

74. C

Systematic risk cannot be eliminated through diversification because it affects the entire market. Unsystematic risk may be diversified away or avoided by not investing in securities that exhibit the risk.

75. A

Short-term capital gains tax rates apply if an asset is held for 12 months or less.

76. B

The Bank Secrecy Act of 1970 requires financial institutions to assist U.S. government agencies in detecting and preventing money laundering by filing reports of cash transactions exceeding \$10,000 (daily aggregate amount).

77. C

An employer can make an employee wait until he or she has completed the second year of service before enrolling in a qualified retirement plan. However, the employee must become 100% immediately vested in all future contributions allocated to his or her account.

78. A

Securities Act Rule 144 permits the public resale of restricted or control securities if a number of conditions are met, including how long the securities are held, the way in which they are sold, and the amount that can be sold at any one time.

79. D

The beta coefficient is calculated by dividing the standard deviation of the return for a particular security by the standard deviation of the return for the overall market, and then multiplying the result by the correlation coefficient of the two returns.

Practice Exam 1

80. C

Pete's basis in the annuity is \$90,000, which represents his premium payments in the life insurance policy.

81. B

$$\$90,000 - \$25,000 = \$65,000$$

Pete's basis would have been equal to the premium payments (\$90,000) less the dividends used to reduce the premium (\$25,000).

82. D

Statutory voting is a voting procedure in which each shareholder is entitled to one vote per share, and votes must be divided evenly among the candidates being voted on.

83. C

The participant's retirement benefit in a defined contribution plan is based on the account balance. The account balance is affected by the investment performance. Pre-retirement inflation will likely affect salary levels and, therefore, affect the contribution amount. The participant's life expectancy does not directly affect the account balance in a defined contribution plan.

84. C

A closed-end mutual fund has a fixed number of shares that, after original issue, trade on the secondary market. The price an investor pays when buying shares of a closed-end mutual fund is based on supply and demand.

85. C

The times interest earned ratio is the measure of a company's ability to pay its debt obligations.

86. A

The date of declaration is the date that the board of directors approves and decides that a dividend will be paid.

87. C

The date of record is the date that it is determined who owns stock in the company and is entitled to receive a dividend.

88. B

The ex-dividend date is the date that the market price of the stock adjusts for the dividend.

89. D

A straddle is an option strategy that involves an investor holding a position in both a call and put for the same underlying security, with the same strike price and expiration date.

90. A

As a result of the SEC adopting an amendment to the Settlement Cycle Rule under the Securities Exchange Act of 1934, the standard settlement cycle was shortened from 3 business days after the trade (T+3) to 2 business days after the trade (T+2).

Practice Exam 1

91. D

A federal gift tax return must be filed if a gift of a future interest is made, if spouses elect to split gifts, or if the gifts from a donor to any single donee for a calendar year exceed the amount of the gift tax annual exclusion.

92. C

SEC-registered investment advisers must deliver Form ADV Part 2A (brochure) and Part 2 (brochure supplement) to each client or prospective client.

93. D

The profitability ratios are the operating profit margin, net profit margin, return on assets, and return on equity.

94. B

Corporate investors in preferred stock can generally deduct 70% of the dividends they receive.

95. A

Deflation occurs when the supply of goods and services exceeds their demand.

96. C

The formula to calculate an investment's public offering price is: $POP = NAV + Sales\ charge$

97. C

A REMIC (real estate mortgage investment conduit) is a self-liquidating investment in real estate mortgages and mortgage-backed securities.

98. D

TRACE (Trade Reporting Compliance Engine) is the FINRA-developed vehicle that facilitates the mandatory reporting of over-the-counter secondary market transactions in eligible fixed income securities. All broker-dealers who are FINRA member firms have an obligation to report transactions in corporate bonds to TRACE under an SEC-approved set of rules.

99. B

GNP (gross national product) is the market value of all the goods and services produced in one year by labor and property supplied by the citizens of a country, wherever they are located.

100. C

According to Regulation D, firms may sell private placements to 35 non-accredited investors in a 12-month period.

101. D

The permitted distribution options from a qualified retirement plan are lump sum distribution, direct trustee-to-trustee transfer, payment in the form of an annuity or other periodic payment option, and rollover of funds from one qualified retirement plan to another.

Practice Exam 1

102. B

A call is an option to buy a specified number of shares of stock during a specified period at a specified price. A buyer of a call option expects the price of the underlying stock to rise.

103. C

The underlying assumptions of the capital asset pricing model (CAPM) are that all investors have the same one-period time horizon, all investors have the same expectations about the risk-return relationship of assets, and there are no transaction costs, taxes, or inflation. The risk-free rate of return may be greater than zero.

104. B

According to FINRA's eligibility requirements, statutory disqualification will result for certain misdemeanors and all felony criminal convictions for a period of 10 years from the date of conviction.

105. C

A registration statement is a set of documents, including a prospectus, which a company must file with the SEC pursuant to the Securities Act of 1933 before it proceeds with a public offering.

106. B

Prospect theory suggests that investors typically fear losses more than they value gains. As a result, investors will often choose the smaller of two potential gains if it avoids a highly probable loss.

107. B

If interest rates decline following a bond issue, a sinking-fund provision will allow an issuing company to reduce the interest rate risk of its bonds as it replaces a portion of the existing debt with lower yielding bonds.

108. D

The yellow sheets are a daily publication of the National Quotation Bureau that details the bid and asked prices of corporate bonds traded in the over-the-counter market.

109. B

The efficient market hypothesis suggests that investors are unable to outperform the stock market on a consistent basis, the stock market's efficiency in valuing securities is rapid and accurate, and any excess returns are temporary and will regress to the mean. According to the efficient market hypothesis, daily fluctuations in stock prices are a result of a random walk pattern.

110. C

Book value = Total assets – Total liabilities

Book value = \$3,250,000 – \$2,980,000 = \$270,000

Practice Exam 1

111. B

A pooled income fund is generally created by a public charity, such as a private or public higher education institution or a not-for-profit hospital. In a pooled income fund, the donor's gifted property is commingled with property transferred by other donors, and additional contributions of property are permitted. A pooled income fund cannot invest in tax-exempt securities.

112. D

The goals of the Federal Reserve are to achieve full employment, minimize systematic risk, and stabilize prices.

113. C

A regressive tax is imposed in such a manner that the tax rate decreases as the amount subject to taxation increases.

114. D

The MSRB (Municipal Securities Rulemaking Board) has the mission of protecting investors, municipal entities, and the public interest by promoting a fair and efficient municipal market, regulating firms that engage in municipal securities and advisory activities, and promoting market transparency.

115. A

A large interest rate change has the most significant effect on a low coupon bond.

116. D

The assets ranked from most liquid to least liquid are Treasury bills, investment-grade corporate bonds, real estate, and the limited partnership.

117. A

ERISA requires retirement plan sponsors to disclose full and accurate information about qualified retirement plan activity to all participants.

118. B

Treasury STRIPS are always issued at a discount to par, like zero-coupon bonds.

119. B

Periodic interest payment = $(\$1,000 \times 0.045) \div 2 = \22.50

120. B

In addition to the federal securities laws, each state has its own set of securities laws, commonly referred to as blue sky laws, which are designed to protect investors against fraudulent sales practices and activities.

121. A

With TIPS (treasury inflation-protected securities), investors are paid either the adjusted principal amount at maturity, or the original principal amount, whichever is greater. TIPS pay interest every six months, and their interest payments increase with inflation and decrease with deflation. They have maturities of 5, 10, or 30 years.

Practice Exam 1

122. B

An FAC (face-amount certificate) is a contract between an investor and an issuer in which the issuer guarantees payment of a stated sum to the investor at some set date in the future. In return for this future payment, the investor agrees to pay the issuer a set amount of money either as a lump sum or in periodic installments.

123. B

Conduit theory states that an investment company that passes all capital gains, interest, and dividends through to its shareholders shouldn't be taxed at the corporate level.

124. C

A buy limit order is an order to purchase a security at or below a specified price.

125. B

Advertisements by an RIA include any notice, circular, or letter addressed to more than one person. It includes social media communications, such as Twitter feeds and online blogs. Advertisements are not permitted to use the initials "RIA" or "IAR."

126. D

The FDIC maintains stability and public confidence in the nation's financial system by insuring deposits, managing receiverships, and examining and supervising financial institutions for safety, soundness, and consumer protection. ERISA, not the FDIC, sets minimum standards for voluntarily established pension and health plans.

127. D

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 was intended to reshape the U.S. regulatory system in a number of areas including consumer protection, trading restrictions, credit ratings, regulation of financial products, corporate governance and disclosure, and transparency.

128. A

The smaller a bond's coupon, the greater its relative price fluctuation. The smaller a bond's coupon, the lower its reinvestment risk.

129. A

AMBAC (American Municipal Bond Assurance Corporation) insures the interest and principal payments for municipal bonds and other public finance debt obligations.

130. A

The annuity settlement options are cash, single life, life with period certain, joint-and-survivor, and installment refund.