

PRACTICE EXAM 6

QUESTIONS

- 1. Colin would like to offer a retirement plan to the employees at his small retail store. He's considering either a SIMPLE or a SEP. Which of the following is a possible disadvantage to Colin if he selects a SEP?**

 - A. A SEP must provide for a qualified preretirement survivor annuity (QPSA).
 - B. Loans from a SEP are only permitted under limited circumstances.
 - C. Employer contributions to a SEP are subject to FICA/FUTA withholding.
 - D. An employee age 21 or older, earning \$8.00 per hour, who works as few as two hours per week and who has done so for three years is eligible to participate in a SEP.

- 2. Which of the following is/are correct regarding dividends paid by growth stocks and value stocks?**

 - (1) Because they are growing and expanding, growth stocks typically do not pay large dividends.
 - (2) Most of the earnings generated from value stocks are reinvested back into the company.
 - A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

- 3. Edward purchased 100 shares of Theta stock for \$55 per share. At the end of two years, he sold the shares for \$60 per share. In the first year, the stock did not pay a dividend. In the second year, the stock paid a \$4 dividend. What was the holding period return of Edward's investment?**

 - A. 10.09%
 - B. 13.21%
 - C. 16.36%
 - D. 19.18%

- 4. All but which of the following are correct regarding the process of underwriting an insurance policy?**

 - A. Underwriting refers to the process of selecting, classifying, and pricing applicants for insurance.
 - B. The underwriter is the individual who decides to accept or reject an application, and under what conditions the policy may be issued.
 - C. One of the objectives of underwriting is to generate revenue while at the same time limiting the insurance company's assumed risk.
 - D. Restrictive underwriting typically results in higher overall claims made by policy-holders.

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5. According to modern portfolio theory, an investor's optimal portfolio is located at the point of tangency of the investor's _____ and the _____ of available investment assets.
- A. indifference curve, efficient frontier
 - B. marginal utility curve, efficient frontier
 - C. marginal utility curve, indifference curve
 - D. optimal portfolio, efficient frontier
6. Which of the following is more beneficial to a taxpayer in a 28% tax bracket, a \$4,000 deduction or a \$1,000 credit?
- A. The credit will benefit the taxpayer by an additional \$120.
 - B. The deduction will benefit the taxpayer by an additional \$120.
 - C. The deduction will benefit the taxpayer by an additional \$300.
 - D. The deduction and credit will benefit the taxpayer by the same amount.
7. Which of the following allow investors to aggregate their own holdings as well as the holdings of certain related parties, such as spouses and children, toward achieving the investment thresholds at which breakpoint discounts become available?
- A. Rights of accumulation
 - B. Rights of conversion
 - C. Rights of deferment
 - D. Rights of indenture
8. A currency transaction report (CTR) must be filed by U.S. financial institutions for each deposit, withdrawal, exchange of currency, or other payment to the institution which involves a transaction in currency of more than:
- A. \$5,000.
 - B. \$10,000.
 - C. \$25,000.
 - D. \$50,000.
9. Which of the following is/are correct regarding simple and complex trusts?
- (1) A simple trust is required to pay out all of its income annually to trust beneficiaries and cannot distribute trust principal.
 - (2) A complex trust may accumulate income or make distributions from trust principal.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

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For questions 10 – 15, match the type of risk with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Systematic risk
- B. Unsystematic risk

10. Purchasing power risk

11. Business risk

12. Market risk

13. Financial risk

14. Interest rate risk

15. Exchange rate risk

16. Which of the following is the maximum criminal fine for an individual who commits an insider trading violation?

- A. \$1 million
- B. \$5 million
- C. \$10 million
- D. \$15 million

17. If \$1 is deposited in an interest-bearing account earning 8.5% annually, and the interest is not withdrawn, the account value at the end of 3 years will be:

- A. \$1.18.
- B. \$1.28.
- C. \$1.39.
- D. \$1.50.

18. Buying a _____ and selling a _____ are both bullish strategies.

- A. call, call
- B. call, put
- C. put, call
- D. put, put

19. According to the Uniform Securities Act, which of the following are classified as securities?

- A. Collectibles
- B. Fixed annuities
- C. Warrants
- D. Whole life insurance policies

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- 20. Which of the following is a weighted index of prices measured at the wholesale level?**
- A. CPI
B. GNP
C. NNI
D. PPI
- 21. Distributions from a 401(k) plan following separation from service after age _____ are not subject to the _____ premature distribution penalty.**
- A. 50, 10%
B. 50, 15%
C. 55, 10%
D. 55, 15%
- 22. All but which of the following are characteristics of defined benefit plans?**
- A. Actuarial calculations are required.
B. The employee assumes the investment risk.
C. They favor older employees.
D. None of the above are correct.
- 23. Which of the following are short-term, fixed-income securities that may be bought or sold in the open market at a market-determined price?**
- A. ADRs
B. Call options
C. Eurodollars
D. Negotiable CDs
- 24. Epsilon Inc. provides the following information in its annual report (in millions):**
- | | |
|----------------------|----------|
| Shareholders' equity | \$57,500 |
| Fixed assets | \$48,200 |
| Total debt | \$44,100 |
| Revenue | \$66,900 |
| Expenses | \$53,800 |
- What is Epsilon Inc.'s debt-to-capital ratio?**
- A. 43.4%
B. 57.3%
C. 65.9%
D. 70.8%

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25. ERISA Section 404(c) offers a/an _____ for retirement plan fiduciaries to not be liable for investment losses suffered by plan participants who self-direct their investments.
- A. excise tax
 - B. penalty
 - C. safe harbor
 - D. tax shelter
26. Viatical payments to a terminally ill insured are _____ if he or she has a life expectancy of _____.
- A. non-taxable, two years or less
 - B. non-taxable, three years or more
 - C. taxable, two years or less
 - D. taxable, three years or more
27. The U.S. government conducts _____ policy through government spending and taxation.
- A. fiscal
 - B. fiscal and monetary
 - C. open market
 - D. monetary
28. A health savings account (HSA) can be used to pay for which of the following medical expenses incurred by the account owner?
- A. Deductibles
 - B. Copayments
 - C. Coinsurance
 - D. All of the above
29. Which of the following are indexed to the rate of inflation as measured by the CPI?
- A. REITs
 - B. REMICs
 - C. TIPS
 - D. UITs
30. All but which of the following are typically included in ADV Part 1?
- A. Affiliations
 - B. Company ownership
 - C. Disciplinary history
 - D. Fee schedule

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31. Which of the following is/are correct regarding the regulation of insurance companies and broker-dealers?

- (1) Insurance company regulation occurs primarily at the state level.
- (2) Broker-dealer regulation occurs primarily at the state level.

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

32. Which of the following is correct regarding the taxation of Treasury STRIPS?

- A. Tax must be paid on accrued interest each year even though no interest is received by the investor.
- B. Tax is not paid on accrued interest each year because no interest is received by the investor.
- C. Tax must be paid at maturity only.
- D. Treasury STRIPS are not taxed.

33. Prices for goods and services will _____ when their demand exceeds their supply.

- A. deflate
- B. inflate
- C. stagflate
- D. remain unchanged

34. All but which of the following are permitted to establish a 403(b) plan for its employees?

- A. Federal government
- B. Private school
- C. Public school
- D. State government

35. All but which of the following are types of REITs?

- A. Equity REIT
- B. Hybrid REIT
- C. Mortgage REIT
- D. All of the above are correct.

36. A “penny stock” is an equity security that trades below:

- A. \$0.05.
- B. \$0.50.
- C. \$1.00.
- D. \$5.00.

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37. What is the maximum contribution a donor can make in a single year to a 529 plan if the gift tax annual exclusion is \$18,000? Assume the donor has not made previous contributions to a 529 plan.
- A. \$18,000
 - B. \$36,000
 - C. \$90,000
 - D. \$100,000
38. Pete, an elderly business owner, is interested in establishing a retirement plan that will provide the greatest retirement benefit to himself. Which of the following plans should Pete select?
- A. Defined benefit plan
 - B. Defined contribution plan
 - C. Money purchase plan
 - D. 401(k) plan
39. Which of the following is/are correct regarding open-end mutual funds?
- (1) Open-end mutual funds sell at their net asset value (NAV).
 - (2) Open-end mutual funds have a fixed capital structure.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.
40. According to Rule 206(4)-5 adopted by the SEC under the Investment Advisers Act of 1940, investment advisers are prohibited from providing advisory services for compensation to a government entity client for _____ after the adviser has made a contribution to certain elected officials or candidates.
- A. 1 year
 - B. 2 years
 - C. 3 years
 - D. 5 years
41. Which of the following is not considered a skip person for generation-skipping transfer tax (GSTT) purposes?
- (1) The transferor's spouse or former spouse, regardless of age.
 - (2) A grandchild of the transferor, if the transferor's child is deceased at the time of transfer.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

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For questions 42 – 46, match each security description with the term that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Freely traded in the secondary markets; yield and term are determined at the time of purchase.
- B. Pay a fixed rate of interest every six months until maturity; issued in terms of ten years or more.
- C. Can be redeemed at any time without penalty; objective is to earn interest for shareholders.
- D. Unsecured promissory note issued by corporations with a fixed maturity of up to 270 days.
- E. Intended to be held until maturity, but can be redeemed prior to maturity for a penalty.
- F. Dividends are declared in local currencies and paid in U.S. dollars.

42. Money market funds

43. Certificate of deposit

44. Commercial paper

45. Treasury bonds

46. American Depository Receipts

47. Which of the following is the first prospectus released for a new issue, and is intended to solicit indications of interest? It does not contain the new issue's price, and it is subject to change.

- A. Pink sheet
- B. Red herring
- C. Shelf registration
- D. Tombstone ad

48. Which of the following is/are correct regarding the early withdrawal penalty from a SIMPLE 401(k)?

- (1) Early withdrawals are subject to a 25% penalty if the withdrawals are made during the first two years of plan participation.
 - (2) After the initial two-year period, early withdrawals from a SIMPLE 401(k) are subject to a 15% penalty.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

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49. Which of the following is a measure of the timing of cash flows (i.e., the interest payments and the principal repayment) to be received from a fixed income security? It's used to assess price volatility for changes in interest rates and the reinvestment risk associated with a portfolio.

- A. Convexity
- B. Duration
- C. Term
- D. Yield

50. During a recent recession, your client, Charles, purchased high-yield corporate bonds that now face minimal default risk. However, he's now concerned that the various corporations may decide to call their bonds. You tell Charles that corporations are likely to call their bonds when:

- A. interest rates are expected to drop.
- B. the bonds are selling at a significant premium.
- C. inflation is expected to rise.
- D. interest rates have declined.

51. If an investor's brokerage firm goes out of business and is a member of the SIPC, then the investor's cash and securities held by the firm may be protected up to _____, including a _____ limit for cash.

- A. \$500,000, \$250,000
- B. \$500,000, \$500,000
- C. \$1,000,000, \$250,000
- D. \$1,000,000, \$500,000

52. Which of the following is/are correct regarding a flat yield curve?

- (1) It generally indicates an economic slowdown.
 - (2) It occurs when there is little difference between short-term and long-term yields for debt instruments of the same credit quality.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

53. Which of the following refers to the inverse relationship between bond prices and an investor's required rate of return?

- A. Credit risk
- B. Interest rate risk
- C. Liquidity risk
- D. Reinvestment risk

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- 54. Which of the following is the maximum criminal fine for a non-natural person (such as an entity whose securities are publicly traded) who commits an insider trading violation?**
- A. \$5 million
B. \$10 million
C. \$25 million
D. \$50 million
- 55. Which of the following regulations sets out certain requirements for lenders, other than securities brokers and dealers, who extend credit secured by margin stock?**
- A. Regulation S
B. Regulation T
C. Regulation U
D. Regulation W
- 56. According to the anomaly known as the P/E effect, _____ P/E stocks appear to outperform _____ P/E stocks over annual periods after being adjusted for risk and size.**
- A. average, low
B. high, average
C. high, low
D. low, high
- 57. Which of the following calculates the required amount of an employer's annual contribution to a defined benefit plan to ensure that current and future plan benefits are available to the participants?**
- A. Administrator
B. Actuary
C. Broker
D. Enrolled agent
- 58. Which of the following are liquidity ratios?**
- (1) Current ratio
(2) Debt-to-equity ratio
(3) Quick ratio
(4) Fixed asset turnover ratio
- A. (1) and (2) only
B. (1) and (3) only
C. (1), (2), and (4) only
D. (2), (3), and (4) only

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59. Which of the following acts created the SEC and empowered it with broad authority over all aspects of the securities industry?
- A. Securities Act of 1933
 - B. Securities Exchange Act of 1934
 - C. Investment Advisers Act of 1940
 - D. Investment Company Act of 1940
60. Earnings before interest and taxes (EBIT) ÷ Annual sales = _____
- A. Average collection period
 - B. Net profit margin
 - C. Operating profit margin
 - D. Quick ratio
61. When a person dies leaving a will, he or she is said to die _____. When a person dies without leaving a will, he or she dies _____.
- A. testate, intestate
 - B. intestate, testate
 - C. testate, nuncupative
 - D. intestate, nuncupative
62. All but which of the following are potential benefits of a bond swap?
- A. It can reduce an investor's tax liability.
 - B. It can provide a higher rate of return.
 - C. It can provide investment diversification.
 - D. All of the above are correct.
63. If a corporation is required to pay unpaid dividends from prior years before paying a dividend to common stockholders, the stock is considered to be:
- A. accumulated preferred stock.
 - B. convertible stock.
 - C. cumulative preferred stock.
 - D. preferred stock.
64. To be considered an accredited investor, earned income must exceed _____ (or _____ together with a spouse) in each of the prior two years, and must be reasonably expected to occur for the current year.
- A. \$200,000, \$300,000
 - B. \$300,000, \$400,000
 - C. \$400,000, \$500,000
 - D. \$500,000, \$600,000

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- 65. Assume that an investor's portfolio has a return of 15%, a standard deviation of 7%, and a beta of 2.0. If the risk-free rate of return is 4%, what is the portfolio's Sharpe ratio?**
- A. 0.06
B. 1.57
C. 1.85
D. 2.14
- 66. Profit sharing plans have which of the following characteristics?**
- A. They favor older employees.
B. They can be invested entirely in company stock.
C. They are a type of defined contribution pension plan.
D. The minimum funding standard requires the employer to make an annual contribution.
- 67. Which of the following acts provides the tools required to intercept and obstruct terrorism? Title III of this act is intended to facilitate the prevention, detection, and prosecution of international money laundering and the financing of terrorism.**
- A. Insider Trading and Securities Fraud Enforcement Act of 1988
B. Patriot Act of 2001
C. Sarbanes-Oxley Act of 2002
D. Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
- 68. Tom and Lynn Smith have lived in a community property state all their married lives. They own a house that is registered only in Lynn's name. If she dies, what will happen to the house?**
- A. The house will pass automatically to Tom.
B. The house will pass automatically to Lynn's closest family member.
C. The house will pass through Lynn's will, and the entire house will go to Tom.
D. Lynn's half of the house will pass by will. Tom already owns half under community property laws.
- 69. Nicholas, age 85, is tax sensitive and wants to pay the least amount of estate taxes at death. Which of the following techniques can he potentially use to reduce his gross estate, and therefore, reduce his estate taxes?**
- (1) Living trust
(2) Family limited partnership
(3) QPRT
(4) Totten trust
- A. (1) and (2) only
B. (2) and (3) only
C. (2) and (4) only
D. (1), (3), and (4) only

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70. Which of the following describes the difference between a 401(k) plan and a 457 plan?

- A. A 401(k) plan is a qualified plan, and a 457 plan is not a qualified plan.
- B. A 457 plan is a qualified plan, and a 401(k) plan is not a qualified plan.
- C. A 401(k) plan allows loans, and a 457 plan does not allow loans.
- D. A 501(c)(3) organization may establish a 457 plan but cannot establish a 401(k) plan.

71. A retirement plan is _____ if more than 60% of total plan benefits are in favor of key employees.

- A. ERISA certified
- B. discriminatory
- C. illegal
- D. top heavy

72. Which of the following entities will protect owners from liability beyond the amount they personally invested?

- (1) C Corp
- (2) Limited partnership
- (3) LLC
- (4) S Corp

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

73. Which of the following is a free tool from FINRA that is intended to help consumers research the professional backgrounds of brokers and brokerage firms, as well as investment adviser firms and advisers?

- A. BrokerCheck
- B. FirmCheck
- C. InvestorCheck
- D. None of the above are correct.

74. All but which of the following are characteristics of an LLC?

- A. It provides limited liability to all members.
- B. It dissolves upon the death, retirement, or resignation of a member unless the remaining members elect by majority to continue.
- C. An operating agreement is not required.
- D. Majority approval is required to transfer management or management rights.

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For questions 75 – 77, match the form of the efficient market hypothesis with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Strong form
 - B. Semi-strong form
 - C. Weak form
75. ___ Historical price data is already reflected in the current stock price and there is no value in predicting future price changes. However, fundamental analysis may generate superior performance. Technical analysis will not produce superior results.
76. ___ All historical information and industry conditions are already reflected in stock prices. Neither technical nor fundamental analysis can produce superior results over time on a risk-adjusted basis. Possessing insider information may lead to achieving returns in excess of the market.
77. ___ All public and private information is already reflected in stock prices. Neither technical nor fundamental analysis can improve the efficiency of the market to determine prices. Possessing insider information is not a factor in outperforming the overall market.
78. Which of the following is the tangent line to the efficient frontier that passes through the risk-free rate on the expected return axis?
- A. Capital market line
 - B. Security market line
 - C. Support line
 - D. Trendline
79. If \$1 is deposited each year in an interest-bearing account earning 8.5% annually, and the interest is not withdrawn, the account value at the end of 3 years will be:
- A. \$3.12.
 - B. \$3.18.
 - C. \$3.26.
 - D. \$3.44.
80. Puts are an option to _____ a specified number of shares of stock during a specified period at a specified price. A buyer of a put option expects the price of the underlying stock to _____.
- A. buy, fall
 - B. buy, rise
 - C. sell, fall
 - D. sell, rise

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- 81. Which of the following is an electronic quotation listing of the bid and asked prices of OTC stocks that do not meet the requirements to be listed on the NASDAQ stock-listing system?**
- A. ECN
B. Instinet
C. OTC Bulletin Board
D. OTC Quotation System
- 82. Which of the following is a tax imposed in such a manner that the tax rate increases as the amount subject to taxation decreases?**
- A. Flat tax
B. Progressive tax
C. Regressive tax
D. Value added tax
- 83. According to FINRA Rule 2210, "correspondence" is defined as any written (including electronic) communication that is distributed or made available to _____ or fewer retail investors within any _____ calendar-day period.**
- A. 25, 30
B. 25, 60
C. 50, 30
D. 50, 60
- 84. Carrie believes the share price of Zeta stock will decrease in the short term. She has decided to sell short 500 shares at the current market price of \$89. If the initial margin requirement is 35%, what amount must Carrie contribute as margin?**
- A. \$15,575
B. \$17,250
C. \$19,925
D. \$21,485
- 85. Which of the following is correct regarding convertible bonds?**
- A. They typically offer lower coupon rates than non-convertible bonds issued for the same term by the same issuer.
B. They typically offer higher coupon rates than non-convertible bonds issued for the same term by the same issuer.
C. They typically offer the same coupon rates as non-convertible bonds issued for the same term by the same issuer.
D. They are zero-coupon bonds issued at a discount to par.

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86. Form ADV is filed electronically through which of the following systems?

- A. BrokerCheck
- B. CRD
- C. IARD
- D. Instinet

87. Which of the following are necessary parties to a trust?

- A. Executor, decedent, beneficiary
- B. Trustee, beneficiary, administrator
- C. Trustor, trustee, beneficiary
- D. Trustor, decedent, administrator

88. Which of the following is correct regarding the SEC's guidance on the "testimonial rule" and social media?

- A. Testimonials were originally addressed in Rule 206(4)-1(a)(1) of the Investment Advisers Act of 1940.
- B. Advisers are allowed to select favorable testimonials to include on their websites only if client names are kept confidential.
- C. Advisers are allowed to select favorable testimonials to include on their websites only if they receive permission from the clients, and they post each client's full name.
- D. None of the above are correct.

For questions 89 – 91, match the cost recovery term with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Amortization
- B. Depreciation
- C. Depletion

89. ___ The process by which the tax basis of natural resources is recovered.

90. ___ The process by which the tax basis of intangible assets is recovered.

91. ___ The process by which the tax basis of tangible assets is recovered.

92. Seth owns a 12-year-old property that is worth \$339,500. If the property has depreciated at a rate of 2.5% per year, what was its original value?

- A. \$480,000
- B. \$485,000
- C. \$490,000
- D. \$495,000

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93. An option that can be exercised at any time up to and including its expiration date is a/an _____ style option.
- A. American
 - B. Asian
 - C. Australian
 - D. European
94. Which of the following forms is the “Uniform Application for Securities Industry Registration or Transfer,” which representatives of broker-dealers, investment advisers, or issuers of securities must fill out in order to become registered in the appropriate jurisdictions?
- A. Form U4
 - B. Form U5
 - C. Form U6
 - D. Form U7
95. Craig recently adopted a profit sharing plan for his business and he's unsure about the contribution rules. He'd like to know if he, as the employer, can contribute more than 25% to an employee's account in 2024. Which of the following should Craig be advised?
- A. Yes, the limit is the lesser of 100% or \$69,000.
 - B. No, the limit is 25%.
 - C. Yes, but the total company contributions cannot exceed 25% of total plan compensation.
 - D. Both A and C are correct.
96. Which of the following allows a firm to file one registration statement covering several issues of the same security? The securities can then be sold over a period of several years.
- A. Deferred registration
 - B. Omitting registration
 - C. Shelf registration
 - D. Statutory registration
97. All qualified retirement plans must satisfy the reporting and disclosure requirements as specified by _____.
- A. ERISA
 - B. the IRS
 - C. the PBGC
 - D. the SEC

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98. If an insured borrows a portion of the cash value from her whole life insurance policy, which of the following is true?
- (1) The loan can be for an amount up to 100% of the face value of the policy.
 - (2) The loan must be repaid within five years.
 - (3) The loan will not charge interest.
 - (4) Any outstanding loans must be deducted from the face amount of the policy before death benefits are paid.
- A. (4) only
 - B. (1) and (2) only
 - C. (1), (2), and (4) only
 - D. All of the above are correct.
99. Which of the following is a type of preferred stock that gives the investor the right to receive dividends equal to the normally specified rate, as well as an additional dividend based on a specific predetermined condition?
- A. Accumulating preferred stock
 - B. Dividend preferred stock
 - C. Non-participating preferred stock
 - D. Participating preferred stock
100. A diversified mutual fund cannot own more than _____ of the shares of a given company or more than _____ of fund assets in a given investment.
- A. 5%, 5%
 - B. 10%, 5%
 - C. 20%, 10%
 - D. 20%, 20%
101. Which of the following refers to the trading of exchange-listed securities in the over-the-counter market? These trades allow institutional investors to trade blocks of securities directly, rather than through an exchange, providing liquidity and anonymity to buyers.
- A. First market
 - B. Second market
 - C. Third market
 - D. Fourth market
102. The Dow Jones Transportation Average is an index comprised of _____ transportation stocks.
- A. 20
 - B. 30
 - C. 50
 - D. 100

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The following information relates to questions 103 – 104.

Alpha Corporation is investing \$900,000 in a new production facility. The present value of the future after-tax cash flows is estimated to be \$950,000. Alpha Corporation currently has 80,000 outstanding shares of stock with a current market price of \$14.00 per share.

103. What will be the value of Alpha Corporation after the investment?

- A. \$1,120,000
- B. \$1,170,000
- C. \$1,190,000
- D. \$1,204,000

104. What will be the value of Alpha Corporation's share price after the investment?

- A. \$14.63
- B. \$15.26
- C. \$15.89
- D. \$16.12

105. All but which of the following are considered quantitative data?

- A. Cash flow statement
- B. Insurance coverage
- C. Investment portfolio
- D. Lifestyle and priorities

106. Which of the following may cause a will to be considered invalid?

- (1) The testator was influenced by another person.
- (2) The testator did not have adequate mental capacity to execute a will.

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

107. If an individual contributes more to an IRA than is permitted, the excess contribution is subject to which of the following taxes?

- A. 5% excise tax
- B. 6% excise tax
- C. 10% excise tax
- D. 15% excise tax

Practice Exam 6

The following information relates to questions 108 – 110.

An analyst provides the following information for Epsilon Corporation's fiscal year:

Revenue	\$550,000
Cost of sales	\$325,000
Gross profit	\$225,000
Marketing costs	\$55,000
Operating income	\$170,000
Interest and other expenses, net	\$20,000
Earnings before taxes	\$150,000

108. What is Epsilon Corporation's gross profit margin?

- A. 27.3%
- B. 33.4%
- C. 40.9%
- D. 63.7%

109. What is Epsilon Corporation's operating profit margin?

- A. 27.3%
- B. 30.9%
- C. 51.2%
- D. 75.6%

110. What is Epsilon Corporation's pretax margin?

- A. 27.3%
- B. 40.9%
- C. 53.5%
- D. 66.7%

111. The “conduit theory,” which states that qualifying investment firms, such as REITs, should not be taxed like regular companies because interest, dividends, and capital gains are passed directly to shareholders who are then taxed on the income, is found in which of the following sections of the Internal Revenue Code?

- A. Subchapter J
- B. Subchapter K
- C. Subchapter M
- D. Subchapter S

112. Which of the following is a formal contract between a bond issuer and a bondholder?

- A. Debenture agreement
- B. Indenture agreement
- C. Prospectus agreement
- D. Tombstone agreement

Practice Exam 6

113. Which of the following imposed an obligation on the SEC to consider the impacts that any new regulation would have on competition, and empowered the SEC to establish a national market system and a system for nationwide clearing and settlement of securities transactions?

- A. Uniform Securities Act of 1956
- B. Securities Act Amendments of 1975
- C. Uniform Prudent Investors Act of 1994
- D. National Securities Market Improvement Act of 1996

114. All but which of the following are characteristics of REITs?

- A. Losses cannot be passed through to investors to deduct personally.
- B. REIT shareholders are subject to double taxation.
- C. REITs can be purchased in small denominations.
- D. All of the above are correct.

115. Which of the following will typically require an RIA firm to register or notice file in a state?

- A. The RIA firm has a physical presence in the state.
- B. The RIA firm has more than 5 clients who are located in the state.
- C. The RIA firm is actively soliciting in the state.
- D. All of the above are correct.

116. Which of the following are prohibited investments in an IRA?

- (1) U.S. minted gold coins
 - (2) Antiques
 - (3) U.S. stamps
 - (4) Art work
- A. (1) only
 - B. (1), (2), and (4) only
 - C. (2), (3), and (4) only
 - D. All of the above are correct.

117. All but which of the following are correct regarding the correlation coefficient?

- A. Two securities that have a correlation coefficient of +1 are perfectly positively correlated. The two securities will move in the exact same direction.
- B. Two securities that have a correlation coefficient of -1 are perfectly negatively correlated. The two securities will move exactly opposite each other.
- C. If two securities have a correlation coefficient of zero, there is no correlation between the price changes of the two securities.
- D. Risk is eliminated when the correlation coefficient between two securities is zero because the portfolio standard deviation will also be zero.

Practice Exam 6

- 118.** Which of the following is the rate of return that causes the net present value of all cash flows received from an investment to equal zero?
- A. CAPM
 - B. IRR
 - C. NPV
 - D. TEY
- 119.** Which of the following SEC regulations requires firms to have policies and procedures addressing the protection of customer information and records? This regulation also requires firms to provide initial and annual privacy notices to customers describing information sharing policies.
- A. Regulation FD
 - B. Regulation MA-W
 - C. Regulation N-Q
 - D. Regulation S-P
- 120.** All but which of the following are correct regarding a futures contract?
- A. It is an agreement to buy or sell a specific quantity of a commodity or financial currency at a predetermined price on a specific future date.
 - B. The holder of a futures contract cannot purchase an offsetting contract that cancels the original position, rather than receiving delivery of the commodity.
 - C. Commodities such as grains, metals, and natural gas have tradable futures contracts.
 - D. All of the above are correct.

For questions 121 – 128, 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. Profit sharing plan
- B. Pension plan

121. 401(k) plan

122. Money purchase plan

123. Stock bonus plan

124. ESOP

125. Target benefit plan

126. Thrift savings plan

127. Cash balance plan

128. SEP

Practice Exam 6

129. Last year, an investor allocated her portfolio in the following asset classes:

Asset Class	Asset Allocation (%)	Asset Class Return (%)
Domestic equities	40.0	+10.0
International equities	20.0	-4.0
Corporate bonds	30.0	+6.0
Money market funds	10.0	+2.0

What was the portfolio's weighted average return for the year?

- A. 4.8%
- B. 5.2%
- C. 5.6%
- D. 5.8%

130. Alex, age 70, has contributed \$20,000 to a Roth IRA throughout his career. The account value is now \$30,000. If Alex withdraws the entire amount, how much tax will he owe if he's in the 28% tax bracket?

- A. \$0
- B. \$1,500
- C. \$4,500
- D. \$8,400

ANSWER KEY

1. D

All employees, age 21 or older, who performed services during the current year and earned at least \$750 in three out of the past five years, must be eligible to participate in a SEP. Employer contributions to a SEP are not subject to FICA/FUTA withholding. A SEP does not need to provide for a qualified preretirement survivor annuity (QPSA), and loans from a SEP are not permitted.

2. A

Because they are growing and expanding, growth stocks typically do not pay large dividends. Most of the earnings generated from growth stocks are reinvested back into the company.

3. C

$$\text{HPR} = [(\$6,000 + \$400) - \$5,500] \div \$5,500 = 0.1636 = 16.36\%$$

4. D

Underwriting refers to the process of selecting, classifying, and pricing applicants for insurance. The underwriter is the individual who decides to accept or reject an application, and under what conditions the policy may be issued. One of the objectives of underwriting is to generate revenue while at the same time limiting the insurance company's assumed risk. Restrictive underwriting typically results in lower overall claims made by policy-holders.

5. A

According to modern portfolio theory, a client's optimal portfolio is located at the point of tangency of the investor's indifference curve and the efficient frontier of available investment assets.

6. B

$$(\$4,000 \times 0.28) - \$1,000 = \$120$$

The deduction is more beneficial because it creates the equivalent of a \$1,120 credit, which is \$120 more than the \$1,000 credit.

7. A

Rights of accumulation allow investors to aggregate their own holdings as well as the holdings of certain related parties, such as spouses and children, toward achieving the investment thresholds at which breakpoint discounts become available.

8. B

A currency transaction report (CTR) must be filed by U.S. financial institutions for each deposit, withdrawal, exchange of currency, or other payment to the institution which involves a transaction in currency of more than \$10,000.

9. C

A simple trust is required to pay out all of its income annually to trust beneficiaries and cannot distribute trust principal. A complex trust may accumulate income or make distributions from trust principal.

Practice Exam 6

10. A

Purchasing power risk is a type of systematic risk.

11. B

Business risk is a type of unsystematic risk.

12. A

Market risk is a type of systematic risk.

13. B

Financial risk is a type of unsystematic risk.

14. A

Interest rate risk is a type of systematic risk.

15. A

Exchange rate risk is a type of systematic risk.

16. B

The maximum criminal fine for an individual who commits an insider trading violation is \$5 million.

17. B

$$S^n = (1 + i)^n$$

$$S^n = (1.085)^3 = \$1.28$$

18. B

Buying a call and selling a put are both bullish strategies.

19. C

According to the Uniform Securities Act, warrants are classified as securities. Collectibles, fixed annuities, and whole life insurance policies are not classified as securities.

20. D

The PPI (Producer Price Index) is a weighted index of prices measured at the wholesale level.

21. C

Distributions from a 401(k) plan following separation from service after age 55 are not subject to the 10% premature distribution penalty.

22. B

Defined benefit plans favor older employees, and actuarial calculations are required. The employer assumes the investment risk in a defined benefit plan.

23. D

Negotiable CDs are short-term, fixed-income securities that may be bought or sold in the open market at a market-determined price.

Practice Exam 6

24. A

Debt-to-capital ratio = Total debt ÷ (Total debt + Shareholders' equity)

Debt-to-capital ratio = \$44,100 ÷ (\$44,100 + \$57,500) = 0.434 = 43.4%

25. C

ERISA Section 404(c) offers a safe harbor for retirement plan fiduciaries to not be liable for investment losses suffered by plan participants who self-direct their investments.

26. A

Viatical payments to a terminally ill insured are non-taxable if he or she has a life expectancy of two years or less.

27. A

The U.S. government conducts fiscal policy through government spending and taxation.

28. D

A health savings account (HSA) can be used to pay for the account owner's deductibles, copayments, and coinsurance.

29. C

TIPS (Treasury inflation-protected securities) are indexed to the rate of inflation as measured by the CPI.

30. D

ADV Part 1 typically includes affiliations, company ownership, and disciplinary history. It does not include a fee schedule.

31. A

Insurance company regulation occurs primarily at the state level. Broker-dealers are regulated at the federal level.

32. A

For Treasury STRIPS, tax must be paid on accrued interest each year even though no interest is received by the investor.

33. B

Prices for goods and services will inflate when their demand exceeds their supply.

34. A

A 403(b) plan may be adopted by an employer that is a state, agency of a state, nonprofit organization, public university, or private university.

35. D

The three main types of REITs are equity REITs, mortgage REITs, and hybrid REITs.

36. D

A "penny stock" is an equity security that trades below \$5.

Practice Exam 6

37. C

$$5 \times \$18,000 = \$90,000$$

A donor may contribute a total of five gift tax annual exclusion amounts on a one-time basis every five years to a 529 plan.

38. A

A defined benefit plan favors older owner/employees and would provide the greatest retirement benefit to Pete.

39. A

Open-end mutual funds sell at their net asset value (NAV) and do not have a fixed capital structure.

40. B

According to Rule 206(4)-5 adopted by the SEC under the Investment Advisers Act of 1940, investment advisers are prohibited from providing advisory services for compensation to a government entity client for 2 years after the adviser has made a contribution to certain elected officials or candidates.

41. C

A transferor's spouse or former spouse, regardless of age, is not a skip person for GSTT purposes. A grandchild of a transferor is not a skip person if the transferor's child is deceased at the time of transfer.

42. C

Money market funds can be redeemed at any time without penalty. Their objective is to earn interest for shareholders.

43. E

A certificate of deposit is intended to be held until maturity, but can be redeemed prior to maturity for a penalty.

44. D

Commercial paper is an unsecured promissory note issued by a corporation with a fixed maturity of up to 270 days.

45. B

Treasury bonds pay a fixed rate of interest every six months until maturity. They are issued in terms of ten years or more.

46. F

American Depository Receipt dividends are declared in local currencies and paid in U.S. dollars.

47. B

A red herring is the first prospectus released for a new issue and is intended to solicit indications of interest. It does not contain the new issue's price, and it is subject to change.

Practice Exam 6

48. D

The 25% penalty for early withdrawals does not apply to SIMPLE 401(k) plans. It only applies to SIMPLE IRAs. For a SIMPLE 401(k) plan, the early withdrawal penalty is always 10%.

49. B

Duration is a measure of the timing of cash flows (i.e., the interest payments and the principal repayment) to be received from a fixed income security. It's used to assess price volatility for changes in interest rates and the reinvestment risk associated with a portfolio.

50. B

If corporate bonds are selling at a significant premium, then newly issued bonds are selling with lower coupons. The corporations are likely to call their bonds and replace them with lower coupon bonds.

51. A

If an investor's brokerage firm goes out of business and is a member of the SIPC, then the investor's cash and securities held by the firm may be protected up to \$500,000, including a \$250,000 limit for cash.

52. C

A flat yield curve generally indicates an economic slowdown. It occurs when there is little difference between short-term and long-term yields for debt instruments of the same credit quality.

53. B

Interest rate risk is the risk that, as interest rates rise, bond prices will fall. Interest rate risk is measured by a bond's duration.

54. C

The maximum criminal fine for a non-natural person (such as an entity whose securities are publicly traded) who commits an insider trading violation is \$25 million.

55. C

Regulation U sets out certain requirements for lenders, other than securities brokers and dealers, who extend credit secured by margin stock.

56. D

According to the anomaly known as the P/E effect, low P/E stocks appear to outperform high P/E stocks over annual periods after being adjusted for risk and size.

57. B

An actuary calculates the required amount of an employer's annual contribution to a defined benefit plan to ensure that current and future plan benefits are available to the participants.

58. B

The liquidity ratios are the current ratio and quick ratio.

Practice Exam 6

59. B

The Securities Exchange Act of 1934 created the SEC and empowered it with broad authority over all aspects of the securities industry.

60. C

Earnings before interest and taxes (EBIT) ÷ Annual sales = Operating profit margin

61. A

When a person dies leaving a will, he or she is said to die testate. When a person dies without leaving a will, he or she dies intestate.

62. D

A bond swap can potentially reduce an investor's tax liability, provide a higher rate of return, and provide investment diversification.

63. C

If a corporation is required to pay unpaid dividends from prior years before paying a dividend to common stockholders, the stock is considered to be cumulative preferred stock.

64. A

To be considered an accredited investor, earned income must exceed \$200,000 (or \$300,000 together with a spouse) in each of the prior two years, and must be reasonably expected to occur for the current year.

65. B

Sharpe ratio = $(R_p - R_f) \div S_p$

Sharpe ratio = $(0.15 - 0.04) \div 0.07 = 1.57$

66. B

Profit sharing plans tend to favor younger employees, and they are not limited in their investment of company stock. Profit sharing plans are a type of defined contribution plan other than a pension plan. Their contributions must be substantial and recurring, but are not required annually.

67. B

The Patriot Act of 2001 provides the tools required to intercept and obstruct terrorism. Title III of this act is intended to facilitate the prevention, detection, and prosecution of international money laundering and the financing of terrorism.

68. D

Unless the house was bought by Lynn with money earned prior to marriage, or with gift or inheritance money, the house is community property. The question does not provide this information, and it cannot be assumed. Therefore, Lynn's half of the house will pass by will. Tom already owns half of the house under community property laws.

69. B

The family limited partnership and QPRT (qualified personal residence trust) can potentially reduce Nicholas's gross estate. The living trust and Totten trust will reduce the probate estate, but not the gross estate.

Practice Exam 6

70. A

A 401(k) plan is a qualified plan, and a 457 plan is not a qualified plan.

71. D

A retirement plan is top heavy if more than 60% of total plan benefits are in favor of key employees. Certain rules and conditions apply to top-heavy plans.

72. D

The LLC, C Corp, and S Corp will protect investors from liability beyond the amount they personally invested. In a limited partnership, the general partner has unlimited liability.

73. A

BrokerCheck is a free tool from FINRA that is intended to help consumers research the professional backgrounds of brokers and brokerage firms, as well as investment adviser firms and advisers.

74. C

An LLC provides limited liability to all members, and it dissolves upon the death, retirement, or resignation of a member unless the remaining members elect by majority to continue. Majority approval is required to transfer management or management rights, and an operating agreement is required to determine the management structure of an LLC.

75. C

According to the weak form of the efficient market hypothesis, historical price data is already reflected in the current stock price and there is no value in predicting future price changes. However, fundamental analysis may generate superior performance. Technical analysis will not produce superior results.

76. B

According to the semi-strong form of the efficient market hypothesis, all historical information and industry conditions are already reflected in stock prices. Neither technical nor fundamental analysis can produce superior results over time on a risk-adjusted basis. Possessing insider information may lead to achieving returns in excess of the market.

77. A

According to the strong form of the efficient market hypothesis, all public and private information is already reflected in stock prices. Neither technical nor fundamental analysis can improve the efficiency of the market to determine prices. Possessing insider information is not a factor in outperforming the overall market.

78. A

The capital market line is the tangent line to the efficient frontier that passes through the risk-free rate on the expected return axis.

79. C

$$S_n = [(1 + i)^n - 1] \div i$$

$$S_n = [(1.085)^3 - 1] \div 0.085 = \$3.26$$

Practice Exam 6

80. C

Puts are an option to sell a specified number of shares of stock during a specified period at a specified price. A buyer of a put option expects the price of the underlying stock to fall.

81. C

The OTC Bulletin Board is an electronic quotation listing of the bid and asked prices of OTC stocks that do not meet the requirements to be listed on the NASDAQ stock-listing system.

82. C

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

83. A

According to FINRA Rule 2210, "correspondence" is defined as any written (including electronic) communication that is distributed or made available to 25 or fewer retail investors within any 30 calendar-day period.

84. A

$500 \text{ shares} \times \$89 \text{ per share} \times 0.35 = \$15,575$

85. A

Because of their flexibility, convertible bonds typically offer lower coupon rates than non-convertible bonds issued for the same term by the same issuer.

86. C

Form ADV is filed electronically through the IARD (Investment Adviser Registration Depository).

87. C

The necessary parties to a trust are the trustor, trustee, and beneficiary.

88. A

Testimonials were originally addressed in Rule 206(4)-1(a)(1) of the Investment Advisers Act of 1940. In general, client testimonials are not permitted to be included on adviser websites and social media.

89. C

Depletion is the process by which the tax basis of natural resources is recovered.

90. A

Amortization is the process by which the tax basis of intangible assets is recovered.

91. B

Depreciation is the process by which the tax basis of tangible assets is recovered.

92. B

Step 1: Accumulated depreciation = 12 years \times 0.025 per year = 0.3

Step 2: Original value = $\$339,500 \div (1 - 0.3) = \$485,000$

Practice Exam 6

93. A

An option that can be exercised at any time up to and including its expiration date is an American style option.

94. A

Form U4 is the "Uniform Application for Securities Industry Registration or Transfer," which representatives of broker-dealers, investment advisers, or issuers of securities must fill out in order to become registered in the appropriate jurisdictions.

95. D

Craig can contribute more than 25% to an individual employee's account, but the contributions must remain under the IRC Section 415 limit. The total company contributions cannot exceed 25% of total plan compensation.

96. C

Shelf registrations allows a firm to file one registration statement covering several issues of the same security. The securities can then be sold over a period of several years.

97. A

All qualified retirement plans must satisfy the reporting and disclosure requirements as specified by ERISA.

98. A

Any outstanding policy loans must be deducted from the face amount of a life insurance policy before death benefits are paid. Insureds can typically borrow an amount up to the cash value of the policy, not the face value.

99. D

Participating preferred stock gives the investor the right to receive dividends equal to the normally specified rate, as well as an additional dividend based on a specific predetermined condition.

100. B

A diversified mutual fund cannot own more than 10% of the shares of a given company or more than 5% of fund assets in a given investment.

101. C

Third market refers to the trading of exchange-listed securities in the over-the-counter market. These trades allow institutional investors to trade blocks of securities directly, rather than through an exchange, providing liquidity and anonymity to buyers.

102. A

The Dow Jones Transportation Average is an index comprised of 20 transportation stocks.

103. B

$(\$14.00 \text{ per share} \times 80,000 \text{ shares}) + (\$950,000 - \$900,000) = \$1,170,000$

Practice Exam 6

104. A

Step 1: $(\$950,000 - \$900,000) \div 80,000 \text{ shares} = \0.63

Step 2: $\$14.00 + \$0.63 = \$14.63$

105. D

Insurance coverage, a cash flow statement, and an investment portfolio are considered quantitative data. Lifestyle and priorities are qualitative data.

106. B

A will may be considered invalid if the testator did not act of his or her own free will, or if the testator did not have adequate mental capacity to execute a will. Simply being influenced by another person does not cause a will to be considered invalid.

107. B

If an individual contributes more to an IRA than is permitted, the excess contribution is subject to a 6% excise tax.

108. C

Gross profit margin = Gross profit \div Revenue

Gross profit margin = $\$225,000 \div \$550,000 = 0.409 = 40.9\%$

109. B

Operating profit margin = Operating income \div Revenue

Operating profit margin = $\$170,000 \div \$550,000 = 0.309 = 30.9\%$

110. A

Pretax margin = Earnings before taxes \div Revenue

Pretax margin = $\$150,000 \div \$550,000 = 0.273 = 27.3\%$

111. C

The "conduit theory," which states that qualifying investment firms, such as REITs, should not be taxed like regular companies because interest, dividends, and capital gains are passed directly to shareholders who are then taxed on the income, is found in Subchapter M of the Internal Revenue Code.

112. B

An indenture agreement is a formal contract between a bond issuer and a bondholder.

113. B

The Securities Act Amendments of 1975 imposed an obligation on the SEC to consider the impacts that any new regulation would have on competition, and empowered the SEC to establish a national market system and a system for nationwide clearing and settlement of securities transactions.

114. B

REITs can be purchased in small denominations, and losses cannot be passed through to investors to deduct personally. REIT shareholders are not subject to double taxation.

Practice Exam 6

115. D

An RIA firm will be required to register or notice file in a state if the RIA firm has a physical presence in the state, or if it has more than 5 clients who are located in the state, or if the firm is actively soliciting in the state.

116. C

Collectibles that are prohibited investments in IRAs include antiques, stamps, art work, rugs, metals, gems, stamps, and coins. There is an exception for U.S. minted gold coins.

117. D

Risk is eliminated when the correlation coefficient between two securities is -1. If two securities have a correlation coefficient of zero, there is no correlation between the price changes of the two securities.

118. B

The internal rate of return (IRR) is the rate of return that causes the net present value of all cash flows received from an investment to equal zero.

119. D

Regulation S-P requires firms to have policies and procedures addressing the protection of customer information and records. This regulation also requires firms to provide initial and annual privacy notices to customers describing information sharing policies.

120. B

A futures contract is an agreement to buy or sell a specific quantity of a commodity or financial currency at a predetermined price on a specific future date. The holder of a futures contract may purchase an offsetting contract that cancels the original position, rather than receiving delivery of the commodity. Commodities such as grains, metals, and natural gas all have tradable futures contracts.

121. A

A 401(k) plan is a type of profit sharing plan.

122. B

A money purchase plan is a type of pension plan.

123. A

A stock bonus plan is a type of profit sharing plan.

124. A

An ESOP is a type of profit sharing plan.

125. B

A target benefit plan is a type of pension plan.

126. A

A thrift savings plan is a type of profit sharing plan.

127. B

A cash balance plan is a type of pension plan.

Practice Exam 6

128. B

A SEP is a type of pension plan.

129. B

$$R_p = w_1R_1 + w_2R_2 + w_3R_3 + w_4R_4$$

$$R_p = (0.40 \times 0.10) + (0.20 \times -0.04) + (0.30 \times 0.06) + (0.10 \times 0.02)$$

$$R_p = 0.04 - 0.008 + 0.018 + 0.002 = 0.052 = 5.2\%$$

130. A

Roth IRA contributions are made with after-tax dollars and grow tax-free. Alex will not owe taxes when he takes the distribution.

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