

PRACTICE EXAM 5

QUESTIONS

- 1. Which of the following is an offering of shares to existing stockholders on a pro-rata basis?**
 - A. Private placement
 - B. Public offering
 - C. Rights offering
 - D. Tender offering

- 2. Which of the following is correct regarding open market operations?**
 - A. It is a tool used by the Federal Reserve to implement monetary policy.
 - B. It is conducted by the Trading Desk at the Federal Reserve Bank of New York.
 - C. The authority to conduct open market operations is found in Section 14 of the Federal Reserve Act.
 - D. All of the above are correct.

- 3. All but which of the following are characteristics of REMICs?**
 - A. They have a perpetual life.
 - B. They combine the predictable cash flow of a bond with the high yield of a mortgage-backed security.
 - C. Investors receive a specified cash flow from the underlying mortgages.
 - D. They are self-liquidating.

- 4. Which of the following is an order to sell a stock at a price below the current market price?**
 - A. Sell discount order
 - B. Sell limit order
 - C. Sell market order
 - D. Sell stop order

- 5. As a cyber security measure, broker-dealers should utilize a/an _____, which means that each time a user attempts to log into an investment account through an unrecognized device, the investment firm will send a unique code to the user via email or text message. Before the user can access the account, he or she must enter the code and password.**
 - A. access control
 - B. declaration of conformity
 - C. inspection certification
 - D. two-step verification process

Practice Exam 5

- 6. Justin, age 58, contributes to his employer's 401(k). In 2024, he will contribute \$25,000 to the plan through salary deferrals, and he would like to contribute to an IRA as well. If he is single and has an income of \$250,000, the maximum IRA contribution that he can make is:**
- A. \$7,000 to a deductible IRA.
 - B. \$8,000 to a deductible IRA.
 - C. \$8,000 to a non-deductible IRA.
 - D. \$8,000 to a Roth IRA.
- 7. When an investment company puts home mortgages or other loans into a pool and then sells securities representing shares of the pool, the securities sold are referred to as which of the following?**
- A. Asset-backed securities
 - B. Dark pools
 - C. Derivative-backed securities
 - D. Unit investment trusts
- 8. If the yield curve is _____, then the spread between yields of short-term and long-term bonds is _____.**
- A. flattening, decreasing
 - B. flattening, increasing
 - C. steepening, decreasing
 - D. None of the above are correct.
- 9. Which of the following is also referred to as a "red herring?"**
- A. Omitting prospectus
 - B. Preliminary prospectus
 - C. Shelf registration
 - D. Tombstone ad
- 10. Which of the following investment strategies will expose an investor to the greatest amount of risk?**
- A. Buying a covered call
 - B. Buying a naked call
 - C. Selling a covered call
 - D. Selling a naked call
- 11. A quarterly interest rate of 3.2% is equivalent to:**
- A. 1.07% monthly or 9.60% annually.
 - B. 1.07% monthly or 12.80% annually.
 - C. 6.40% monthly or 9.60% annually.
 - D. 6.40% monthly or 12.80% annually.

Practice Exam 5

12. All but which of the following are correct regarding the Federal Reserve?

- A. It derives its authority from Congress.
- B. It operates and oversees the U.S. payment system.
- C. It operates and oversees government spending.
- D. It supervises and regulates banks.

13. All but which of the following is another name for an income statement?

- A. Statement of financial performance
- B. Statement of financial position
- C. Statement of operations
- D. Statement of profit or loss

14. Which of the following is correct regarding the relationship between an investment's real return and nominal return?

- (1) Real return is an investment's rate of return after adjusting for inflation.
 - (2) Nominal return is an investment's rate of return without adjusting for inflation.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

15. Which of the following theories states that security prices in different markets will not differ for any significant period of time?

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

16. Which of the following are required to obtain a viatical settlement?

- (1) The insured must not be terminally ill.
 - (2) The insured must have owned the policy for at least one year.
 - (3) The current beneficiary of the policy must sign a release or waiver.
 - (4) The insured must sign a release allowing the viatical settlement provider access to his or her medical records.
- A. (1) and (2) only
 - B. (3) and (4) only
 - C. (2), (3), and (4) only
 - D. All of the above are correct.

Practice Exam 5

17. Which of the following is true regarding a qualified domestic trust (QDOT)?

- A. There must be at least one trustee who is a U.S. citizen or a qualifying domestic corporation.
- B. The surviving spouse must have the right to all income, as well as a general power of appointment over trust assets.
- C. The trust does not qualify for the marital deduction unless a special election is made by the trustee.
- D. Property in the trust is not subject to gift or estate taxes.

18. Which of the following are primary issuers of individual bonds?

- (1) Local government
- (2) U.S. government
- (3) An agency of the U.S. government
- (4) Corporations

- A. (1) and (4) only
- B. (1), (2), and (3) only
- C. (2), (3), and (4) only
- D. All of the above are correct.

The following information relates to questions 19 – 21.

Jennifer's income is \$80,000 and she is in the 25% tax bracket. While preparing to file her tax return, she expected to take an \$8,000 deduction through a government incentive program that she qualified for. However, she has discovered the deduction has been replaced with a \$4,000 tax credit.

19. Ignoring exemptions and other adjustments, if Jennifer had claimed the \$8,000 tax deduction, her total taxes owed would have been:

- A. \$14,000.
- B. \$16,000.
- C. \$18,000.
- D. \$20,000.

20. Ignoring exemptions and other adjustments, if Jennifer claims the \$4,000 tax credit, her total taxes owed will be:

- A. \$14,000.
- B. \$16,000.
- C. \$18,000.
- D. \$20,000.

Practice Exam 5

- 21. Ignoring exemptions and other adjustments, a tax credit of _____ would result in the same amount of taxes owed as the \$8,000 tax deduction.**
- A. \$2,000
 - B. \$3,000
 - C. \$5,000
 - D. \$6,000
- 22. Which of the following is the formula to calculate a mutual fund's turnover rate?**
- A. Turnover rate = Gross proceeds from sale of securities ÷ NAV
 - B. Turnover rate = Gross proceeds from sale of securities – NAV
 - C. Turnover rate = Gross proceeds from sale of securities + NAV
 - D. Turnover rate = NAV ÷ Gross proceeds from sale of securities
- 23. Higher inflation = _____ interest rates = _____ bond values**
- A. higher, higher
 - B. higher, lower
 - C. lower, higher
 - D. lower, lower
- 24. If a wash sale occurs, which of the following will result?**
- A. No loss deduction is allowed, and the amount of the disallowed loss is subtracted from the cost basis of the newly acquired shares.
 - B. No loss deduction is allowed, and a gain must be realized immediately.
 - C. No loss deduction is allowed, and the amount of the disallowed loss is added to the cost basis of the newly acquired shares.
 - D. The loss can be realized.
- 25. Lisa, a single taxpayer with an AGI of \$140,000, is permitted to fully deduct her IRA contribution if she's an active participant in which of the following plans?**
- A. 401(k) plan with no match
 - B. 403(b) plan with no match
 - C. 403(b) plan with match
 - D. 457 plan
- 26. If real GDP declined the last 3 quarters, how many more consecutive quarters of decline would be needed to be classified as an economic depression?**
- A. 1 quarter
 - B. 2 quarters
 - C. 3 quarters
 - D. 4 quarters

Practice Exam 5

- 27. Which of the following is the ethical barrier that is required between different divisions of a financial institution to avoid conflicts of interest?**
- A. Checks and balance system
 - B. Chinese wall
 - C. Ethical wall
 - D. Moral barrier
- 28. Preferred stock that does not have to pay missed dividends is considered which of the following?**
- A. Convertible
 - B. Cumulative
 - C. In-kind
 - D. Noncumulative
- 29. Which of the following rules addresses the registration and resale requirements for securities issued in a merger, consolidation, acquisition of assets, or reclassification of securities?**
- A. Securities Act Rule 145
 - B. Securities Act Rule 172
 - C. Securities Act Rule 238
 - D. Securities Act Rule 405
- 30. The “cooling-off period,” which transpires between the filing of a new issue’s prospectus and the actual offering of the issue, must be a minimum of how many days?**
- A. 7 days
 - B. 10 days
 - C. 20 days
 - D. 30 days
- 31. Brady bonds are typically issued by which of the following countries?**
- A. Asian countries
 - B. European countries
 - C. Latin American countries
 - D. Middle Eastern countries
- 32. Expansionary policy is characterized by which of the following?**
- A. Decreasing transfer payments
 - B. Increasing public spending
 - C. Increasing taxes
 - D. All of the above are correct.

Practice Exam 5

33. In order to maintain a SIMPLE plan, an employer may not have more than _____ employees.
- A. 25
 - B. 50
 - C. 75
 - D. 100
34. An investment-grade bond is one that is rated _____ or higher by the Standard & Poor's bond rating service. A high-yield bond is rated _____ or lower by Standard & Poor's.
- A. BBB, BB
 - B. BBB+, BB-
 - C. BBB-, BB+
 - D. BB, BBB
35. Which of the following has the most stable cash flows and the lowest prepayment risk of any class of CMO?
- A. General obligation bond
 - B. Planned amortization class bond
 - C. Targeted amortization class bond
 - D. Zero-coupon bond
36. Blue sky laws are classified as which of the following?
- A. Federal-based laws
 - B. International-based laws
 - C. Municipal-based laws
 - D. State-based laws
37. Which of the following is used by U.S. corporations (specifically, C Corps) to report income, gains, losses, deductions, and credits, and to determine their tax liability?
- A. IRS Form 1040
 - B. IRS Form 1041
 - C. IRS Form 1065
 - D. IRS Form 1120
38. Pink sheets are to unlisted stocks as _____ are to bonds.
- A. blue sheets
 - B. green sheets
 - C. white sheets
 - D. yellow sheets

Practice Exam 5

39. Which of the following acts promotes efficiency and capital formation in the financial markets, and provides for more effective and less burdensome regulation between states and the Federal Government? It also declared that any offering of a "covered security" is exempt from state registration and review.

- A. Insider Trading and Securities Fraud Enforcement Act of 1988
- B. Uniform Prudent Investors Act of 1994
- C. National Securities Market Improvement Act of 1996
- D. Sarbanes-Oxley Act of 2002

The following information relates to questions 40 – 41.

Stephanie purchased a whole life insurance policy several years ago. She has provided the following information related to the policy.

Face amount	\$250,000
Cash value	\$87,500
Paid-up additions	\$75,000
Cash value of paid-up additions	\$50,000
Annual premium	\$4,300
Annual dividend	\$1,900

40. What is the current surrender value of Stephanie's policy?

- A. \$112,500
- B. \$137,500
- C. \$162,500
- D. \$164,400

41. If Stephanie dies, a death benefit of _____ will be paid to her beneficiary.

- A. \$250,000
- B. \$262,500
- C. \$300,000
- D. \$325,000

42. An investor purchased a call option for \$3.00. The option has a strike price of \$37.00, and the stock is currently valued at \$36.00. The call option would cost \$2.50 if purchased today. Ignoring transaction costs, what is the value of the option?

- A. -\$0.50
- B. \$0
- C. \$1.00
- D. \$2.00

Practice Exam 5

43. Which of the following is a graphical representation of a security's average price over a period of time?

- A. Moving average
- B. Support and resistance average
- C. Technical average
- D. Trendline average

44. Which of the following is/are correct regarding generation skipping transfers?

- (1) A generation skipping transfer may only occur during a transferor's lifetime.
- (2) The gift tax annual exclusion may only be used to offset a lifetime generation skipping transfer.

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

45. Which of the following is a private, non-profit organization whose primary purpose is to establish and improve generally accepted accounting principles within the U.S.?

- A. FASB
- B. FDIC
- C. MSRB
- D. NSCC

46. When calculating gross domestic product (GDP), all but which of the following variables are paired with the correct description?

- A. C = Personal consumption
- B. I = Issuance of government bonds
- C. G = Government spending
- D. E = Net exports

47. Which of the following is the correct method to conducting bottom-up investment analysis?

- A. First examine a specific company, then examine a specific industry, then examine a specific economy, then examine the global economy.
- B. First examine a specific company, then examine a specific economy, then examine a specific industry, then examine the global economy.
- C. First examine the global economy, then examine a specific industry, then examine a specific economy, then examine a specific company.
- D. First examine the global economy, then examine a specific economy, then examine a specific industry, then examine a specific company.

Practice Exam 5

48. Which of the following groups may be excluded from participating in an employee stock purchase plan (ESPP)?

- A. Employees working less than 20 hours per week.
- B. Employees with less than 2 years of service.
- C. Officers of the employer.
- D. All of the above are correct.

For questions 49 – 51, 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. Business risk
- B. Tax risk
- C. Financial risk
- D. Market risk
- E. Credit risk
- F. Country risk

49. ___ The risk associated with a company's decision to use debt as part of its capital structure.

50. ___ The possibility that a bond issuer will default.

51. ___ The risk inherent in company operations.

52. Which of the following government agencies are responsible for monitoring qualified retirement plan rules and eligibility?

- A. ERISA and the IRS
- B. ERISA and the PBGC
- C. IRS and the Department of Labor
- D. IRS and the PBGC

53. Which of the following is/are correct regarding probate?

- (1) If a person dies testate, his or her property is subject to probate.
- (2) If a person dies intestate, his or her property avoids probate.

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

54. All but which of the following are characteristics of defined benefit plans?

- A. Employer contributions vary.
- B. Participant benefits vary.
- C. The employer assumes the investment risk.
- D. They favor older employees.

Practice Exam 5

55. Which of the following is correct regarding non-systematic risk?

- A. It includes risks such as tax risk and financial risk.
- B. An investor who owns five growth stocks can reduce non-systematic risk by adding a value stock to her portfolio.
- C. It is the risk associated with a particular security or company.
- D. All of the above are correct.

56. Money in a Coverdell Education Savings Account (ESA) must be used by the time the beneficiary is _____ years of age.

- A. 18
- B. 21
- C. 24
- D. 30

57. Which of the following describes the rate of return calculated by the capital asset pricing model (CAPM)?

- A. The rate of return is not reliable because CAPM fails to take risk into account.
- B. The rate of return can be used in the dividend growth model for valuing common stock.
- C. The rate of return represents the stock market's overall rate of return.
- D. The rate of return is not reliable because CAPM uses beta in its formula.

58. Alpha Inc. reports the following information at its annual shareholder meeting:

Liabilities at year-end	\$500,000
Contributed capital at year-end	\$100,000
Beginning retained earnings	\$150,000
Revenue during the year	\$300,000
Expenses during the year	\$200,000
Dividends paid during the year	\$50,000

What is the value of Alpha Inc.'s total assets at year-end?

- A. \$800,000
- B. \$900,000
- C. \$1,300,000
- D. \$1,350,000

59. Regarding the money supply, which of the following is the formula for M1?

- A. M1 = Savings accounts + Short-term time deposits
- B. M1 = Coins and currency in circulation + Money held in checking accounts
- C. M1 = Long-term time deposits
- D. M1 = Coins and currency in circulation + Short-term time deposits

Practice Exam 5

60. Which of the following is/are correct regarding tax credits?

- (1) A refundable tax credit cannot reduce a taxpayer's income tax liability below zero.
 - (2) A non-refundable tax credit can reduce a taxpayer's income tax liability below zero.
- A. (1) only
 - B. (2) only
 - C. Both (1) and (2) are correct.
 - D. Neither (1) or (2) are correct.

For questions 61 – 64, match the legislation with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Securities Act of 1933
- B. Securities Exchange Act of 1934
- C. Investment Company Act of 1940
- D. Securities Investor Protection Act of 1970

61. ___ Regulates brokerage firms.

62. ___ Regulates mutual funds.

63. ___ Regulates new securities.

64. ___ Regulates existing securities.

65. Treasury notes, Treasury bonds, and TIPS, whose interest and principal portions have been separated so they may be sold individually, are referred to as which of the following?

- A. Treasury GICs
- B. Treasury CMOs
- C. Treasury STRIPS
- D. Treasury UITs

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

- (1) Open-end mutual funds issue new shares and redeem existing shares from shareholders.
 - (2) The price an investor pays when buying shares of an open-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.

Practice Exam 5

67. Regulation A permits unregistered public offerings of up to _____ of securities in any 12-month period.
- A. \$1 million
 - B. \$5 million
 - C. \$10 million
 - D. \$20 million
68. Which of the following retirement plans require immediate vesting?
- A. Employer contributions to a 401(k) plan.
 - B. Employer contributions to a money purchase plan.
 - C. Employer contributions to a SEP.
 - D. All of the above are correct.
69. How is the net asset value (NAV) of a mutual fund calculated?
- A. NAV = (Total value of investment + Liabilities) ÷ Shares outstanding
 - B. NAV = (Total value of investment ÷ Shares outstanding) - Liabilities
 - C. NAV = (Total value of investment - Liabilities) ÷ Shares outstanding
 - D. NAV = Total value of investment ÷ Shares outstanding
70. According to the anomaly known as the “small-firm effect,” _____ companies have been shown to outperform _____ companies on a risk-adjusted basis over a period of many years.
- A. large cap, small cap
 - B. mid cap, small cap
 - C. small cap, large cap
 - D. small cap, mid cap
71. Interest earned on which of the following is a tax preference item for the alternative minimum tax (AMT)?
- A. General obligation bonds
 - B. Private activity bonds
 - C. Public purpose bonds
 - D. Revenue bonds
72. According to the Uniform Securities Act, if the Administrator issues a subpoena and the affected party fails to respond, it is referred to as which of the following?
- A. Adhesion
 - B. Contumacy
 - C. Estoppel
 - D. Rescission

Practice Exam 5

73. A research analyst provides the following economic information for Country X:

Category	Amount (\$ billions)
Consumption	11.4
Government spending	3.3
Capital consumption allowance	5.0
Gross private domestic investment	6.2
Imports	2.9
Exports	1.8

What is the gross domestic product (GDP) of Country X?

- A. \$17.9 billion
- B. \$18.6 billion
- C. \$19.8 billion
- D. \$24.8 billion

74. A corporate insider is defined as a director or senior officer of a company, as well as any person or entity that beneficially owns more than _____ of a company's voting shares.

- A. 1%
- B. 2%
- C. 5%
- D. 10%

75. Which of the following securities are backed by the full faith and credit of the U.S. government?

- A. Federal Home Loan Mortgage Corporation debentures (Freddie Macs)
- B. Federal National Mortgage Association certificates (Fannie Maes)
- C. Government National Mortgage Association certificates (Ginnie Maes)
- D. Student Loan Marketing Association notes (Sallie Maes)

76. Which of the following investments will provide tax-exempt interest if the proceeds are used to pay for qualifying education expenses?

- (1) FNMA funds
 - (2) Series EE bonds
 - (3) Treasury bonds
 - (4) Treasury bills
- A. (2) only
 - B. (1) and (2) only
 - C. (2), (3), and (4) only
 - D. All of the above are correct.

Practice Exam 5

- 77. How are the value of publicly traded stocks and bonds determined for gift and estate tax purposes?**
- A. The closing price on the date of disposition.
 - B. The opening price on the date of disposition.
 - C. The mean between the highest and lowest selling price on the date of disposition.
 - D. The mean between the highest and lowest selling price on the date prior to the date of disposition.
- 78. Which of the following is an exchange employee who is in charge of keeping a book of public limit orders on exchanges utilizing the "market-maker" system?**
- A. Designated market maker
 - B. Limit order officer
 - C. Order book official
 - D. Public order specialist
- 79. Employer contributions to a defined contribution plan must use either the _____ cliff vesting or _____ graded vesting schedules.**
- A. 3-year, 6-year
 - B. 3-year, 7-year
 - C. 5-year, 6-year
 - D. 5-year, 7-year
- 80. Which of the following is a short-term obligation that is issued for temporary financing needs by a municipality?**
- A. Bond anticipation note
 - B. Guaranteed investment contract
 - C. Tax anticipation note
 - D. Unit investment trust
- 81. Which of the following is an order to buy a stock at a price above the current market price?**
- A. Buy stop order
 - B. Buy limit order
 - C. Buy market order
 - D. None of the above are correct.
- 82. A variable life insurance policy will pay benefits that vary according to which of the following?**
- A. The flexibility of premiums paid.
 - B. The value of underlying investments.
 - C. The variability of the mortality factor.
 - D. All of the above are correct.

Practice Exam 5

83. Which of the following is correct regarding IAR registration?

- A. Individual registrations can be administered at the state level or federal level, depending on where the RIA firm is registered.
- B. All individual registrations are administered at the federal level, regardless of whether the RIA firm is registered at the SEC or state level.
- C. All individual registrations are administered at the state level, regardless of whether the RIA firm is registered at the SEC or state level.
- D. None of the above are correct.

84. Which of the following estate planning objectives can be accomplished through a will?

- A. Avoiding probate.
- B. Establishing a testamentary trust.
- C. Providing burial wishes.
- D. Providing for decisions during incapacitation.

85. An indenture agreement describes the terms and conditions of a bond, including which of the following?

- A. Call provisions
- B. Description of collateral
- C. How coupon payments are determined
- D. All of the above are correct.

86. Which of the following must be filed for each of the first three fiscal quarters of a company's fiscal year, and includes unaudited financial statements and provides a continuing view of the company's financial position during the year?

- A. Form ADV
- B. Form 8-K
- C. Form 10-K
- D. Form 10-Q

87. Which of the following is an advantage that money purchase plans have over other qualified retirement plans?

- A. Employer contributions can be omitted in certain years and must only be substantial and recurring.
- B. Forfeitures must be used to reduce future employer contributions.
- C. They are easy to explain to employees.
- D. They favor older employees.

88. A trade surplus results from which of the following?

- A. A country having a current account deficit.
- B. A country exporting more than it imports.
- C. A country exporting less than it imports.
- D. None of the above are correct.

Practice Exam 5

89. Eurodollars have which of the following characteristics?

- (1) They are foreign denominated deposits in banks located outside the U.S.
- (2) They involve deposits made at only European banks.

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

90. According to the principles of behavioral finance, which of the following terms describes an investor's tendency to look for information that supports his or her previously established decision, even if that decision was imprudent? This tendency may explain why investors are slow to sell an underperforming stock.

- A. Confirmation bias
- B. Expectation bias
- C. Hold bias
- D. Prospect bias

91. Which of the following is a computerized subscriber service that serves as a vehicle for the fourth market by permitting subscribers to display bids and offers and execute trades electronically?

- A. ECN
- B. EMMA
- C. Instinet
- D. NSCC

92. A/An _____ legal opinion means that the bond counsel has no reservations regarding the bond issue, and it is considered the most desirable for investors.

- A. binding
- B. enforceable
- C. qualified
- D. unqualified

93. Which of the following is correct regarding certificates of deposit (CDs)?

- A. They are short-term securities that may be bought or sold in the open market at a market-determined price.
- B. They typically invest in high-quality, short-term investments, such as commercial paper, Treasury bills, and money market funds.
- C. They are known as "time deposits."
- D. The financial institution typically pays a variable rate of interest for the term of the CD.

Practice Exam 5

94. In any single life private annuity transaction, if the seller outlives his or her actuarial life expectancy, the purchaser will have paid _____ for the property. If the seller does not outlive his or her actuarial life expectancy, the _____ will have made a good financial deal.

- A. too much, purchaser
- B. too much, seller
- C. too little, purchaser
- D. too little, seller

95. The annual report on _____ provides a comprehensive overview of a company's business and financial condition and includes audited financial statements.

- A. Form 6-K
- B. Form 8-K
- C. Form 10-K
- D. Form 10-Q

96. Beta Corporation sold products to customers on April 30, 2017 for a total price of \$85,000. Payment is due in 60 days. The total cost of the products was \$67,000. What is the net change in Beta Corporation's total assets on April 30, 2017?

- A. \$0
- B. \$18,000
- C. \$67,000
- D. \$103,000

97. Which of the following is/are correct regarding cyclical stocks?

- (1) When the economy is growing, demand usually strengthens and cyclical companies are able to make large profits.
- (2) When the economy is declining, cyclical companies are hurt by decreases in demand and are less profitable.

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

98. Which of the following acts, also known as the Currency and Foreign Transactions Reporting Act, requires financial institutions to assist U.S. government agencies in detecting and preventing money laundering?

- A. Bank Secrecy Act of 1970
- B. Insider Trading and Securities Fraud Enforcement Act of 1988
- C. National Securities Market Improvement Act of 1996
- D. Sarbanes-Oxley Act of 2002

Practice Exam 5

99. Which of the following plans require immediate vesting?

- (1) Money purchase plan
- (2) SEP
- (3) 401(k) plan
- (4) 403(b) plan

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

100. All but which of the following are characteristics of a REIT?

- A. It is a publicly traded open-end investment company.
- B. A mortgage REIT is a specific type of REIT.
- C. A REIT can sell at a premium or discount to its NAV.
- D. All of the above are correct.

101. Which of the following is the typical limit on the term of a loan from a qualified retirement plan?

- A. 1 year
- B. 2 years
- C. 5 years
- D. 10 years

102. Which of the following refers to taking a loss on a bond and replacing it with a substantially different bond to avoid triggering the wash sale rule?

- A. Bond conversion
- B. Bond spread
- C. Bond swap
- D. Bond yield

103. Steve sold his portfolio of ETFs and is now required to pay 15% tax on the gain. Which of the following must be true?

- (1) The ETFs were taxed at long-term capital gains rates.
- (2) Steve's marginal tax bracket was less than 25%.
- (3) Steve owned the ETFs for more than one year.
- (4) Steve's marginal tax bracket was 25% or higher.

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

Practice Exam 5

104. Which of the following will shift the Markowitz efficient frontier to the left?

- A. Taking less risk.
- B. Taking more risk.
- C. Changing the proportion of securities already invested in the portfolio.
- D. Selecting investments with lower coefficients of correlation between them.

105. Which of the following terms refers to a broker using securities in his or her possession, but owned by a customer, as collateral to raise a loan to cover a short position?

- A. Recapitalization
- B. Recollateralization
- C. Rehypothecation
- D. Securitization

106. Which of the following is the maximum prison sentence for an insider trading violation?

- A. 10 years
- B. 20 years
- C. 30 years
- D. 40 years

107. Which of the following are among the requirements for a valid S Corp election?

- (1) Only one class of stock is permitted.
 - (2) There may be no more than 75 shareholders.
 - (3) It must be a domestic corporation.
 - (4) Shareholders must be U.S. citizens or residents.
- A. (1) and (3) only
 - B. (1), (2), and (4) only
 - C. (1), (3), and (4) only
 - D. (2), (3), and (4) only

108. Which of the following are permitted investments in an IRA?

- A. A mutual fund that invests exclusively in a silver mining stock.
- B. Gold coins minted in the U.S.
- C. A real estate investment trust.
- D. All of the above are correct.

109. $(\text{Current assets} - \text{Inventory}) \div \text{Current liabilities} = \underline{\hspace{2cm}}$

- A. Current ratio
- B. Inventory turnover ratio
- C. Quick ratio
- D. Return on assets

Practice Exam 5

- 110. To calculate core inflation, which of the following categories are excluded from the calculation?**
- A. Food and energy prices
 - B. Food and utilities
 - C. Healthcare and energy prices
 - D. Technology and utilities
- 111. Investment advisers that have custody of client assets or require prepayment of advisory fees _____ or more in advance, and in excess of _____ for each client, must file an audited balance sheet with the SEC as of the end of the investment adviser's fiscal year.**
- A. 6 months, \$1,200
 - B. 6 months, \$1,500
 - C. 12 months, \$1,200
 - D. 12 months, \$1,500
- 112. Which of the following mutual fund share classes will charge investors a level load?**
- A. Class A shares
 - B. Class B shares
 - C. Class C shares
 - D. Class D shares
- 113. Investment risk is defined as which of the following?**
- A. The chance that an investment's actual return will be greater or less than its expected return.
 - B. The chance that an investment's actual return will equal its expected return.
 - C. The chance that an investment's actual return will be less than its expected return.
 - D. None of the above are correct.
- 114. All but which of the following are characteristics of sole proprietorships?**
- A. They are the simplest form of business entity.
 - B. They have no formal legal requirements.
 - C. They have a lack of continuity of business life.
 - D. They provide limited liability to owners.
- 115. Which of the following option strategies seeks to maximize an investor's profit when the price of an underlying security decreases in value?**
- A. Bear spread
 - B. Bull spread
 - C. Long straddle
 - D. Protective collar

Practice Exam 5

116. Which of the following acts allowed for the establishment of the National Association of Securities Dealers (NASD) and the U.S. domestic over-the-counter markets in securities?

- A. Maloney Act of 1938
- B. Trust Indenture Act of 1939
- C. Investment Company Act of 1940
- D. Uniform Securities Act of 1956

For questions 117 – 119, select the word that best completes the bond relationship provided. Use only one answer per blank. Answers may be used more than once or not at all.

- A. More
- B. Less

117. ___ Lower-coupon bonds are _____ affected by interest rate changes than higher-coupon bonds.

118. ___ The shorter a bond's term to maturity, the _____ its potential for relative price fluctuation.

119. ___ Long-term bonds are _____ affected by interest rate changes than short-term bonds.

120. Which of the following are correct regarding qualified personal residence trusts (QPRTs)?

- (1) A QPRT is ideal for a single parent in his 30s or 40s.
- (2) A QPRT is generally appropriate for vacation homes valued at over \$1,000,000.
- (3) After the trust term ends, the house reverts back to the grantor.
- (4) The grantor will have a taxable gift upon the creation of a QPRT.

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

121. Which of the following sections of the tax code allows individuals to make withdrawals before age 59 ½ from certain retirement accounts without penalty, as long as the SEPP (substantially equal periodic payment) regulation is met?

- A. Rule 67(e)
- B. Rule 72(t)
- C. Rule 83(b)
- D. Rule 501(r)

Practice Exam 5

122. Dawn contributed \$12,000 to a qualified retirement plan several years ago. The account balance is now \$14,500. If Dawn takes a lump sum distribution, she will owe:

- A. long-term capital gains tax on \$2,500.
- B. long-term capital gains tax on \$14,500.
- C. ordinary income tax on \$2,500.
- D. ordinary income tax on \$14,500.

123. Which of the following is required for an individual to open a health savings account (HSA)?

- A. The individual must have a high-deductible health plan (HDHP).
- B. The individual must have a low-deductible health plan (LDHP).
- C. The individual must have a flexible spending account (FSA).
- D. None of the above are required to open a health savings account.

124. Which of the following statements about property held as tenancy by entirety are correct?

- (1) The property automatically passes to the surviving co-tenant when one tenant dies.
 - (2) It is an interest in property that can be held only by spouses.
 - (3) It can be held by non-spouse business partners in an LLC.
 - (4) In most states, it is not severable by an individual tenant.
- A. (1) and (2) only
 - B. (2) and (4) only
 - C. (1), (2), and (3) only
 - D. (1), (2), and (4) only

125. Kappa Inc. provides the following information at its annual shareholder meeting:

Gross income	\$2,300,000
Net income	\$950,000
Number of shares outstanding	250,000
Price per share	\$9.10
Average total book value of equity	\$3,260,000
Total liabilities	\$2,980,000

What is Kappa Inc.'s return on equity (ROE)?

- A. 27.72%
- B. 29.14%
- C. 31.88%
- D. 33.59%

Practice Exam 5

For questions 126 – 129, match the hedging technique with the description that follows. Use only one answer per blank. Answers may be used more than once or not at all.

- A. Collar
- B. Spread
- C. Straddle
- D. Protective put

126. Purchasing a call option and selling a call option on the same stock at the same time.

127. Purchasing a put option and selling a call option on the same stock at the same time.

128. Purchasing a put option while holding shares of the underlying stock from a previous purchase.

129. Purchasing a call option and a put option on the same stock at the same time.

130. Which of the following is the official repository for information on virtually all municipal bonds, and provides free access to official disclosures, trade data, and other information about the municipal securities market?

- A. EMMA
- B. FAST
- C. MSRB
- D. TRACE

ANSWER KEY

1. C

A rights offering is an offering of shares to existing stockholders on a pro-rata basis.

2. D

Open market operations is a tool used by the Federal Reserve to implement monetary policy. It is conducted by the Trading Desk at the Federal Reserve Bank of New York, and the authority to conduct open market operations is found in Section 14 of the Federal Reserve Act.

3. A

With REMICs (real estate mortgage investment conduits), investors receive a specified cash flow from the underlying mortgages. They combine the predictable cash flow of a bond with the high yield of a mortgage-backed security. REMICs are self-liquidating and have a limited life that terminates when the underlying mortgages are repaid.

4. D

A sell stop order is an order to sell a stock at a price below the current market price.

5. D

As a cyber security measure, broker-dealers should utilize a two-step verification process, which means that each time a user attempts to log into an investment account through an unrecognized device, the investment firm will send a unique code to the user via email or text message. Before the user can access the account, he or she must enter the code and password.

6. C

Because Justin is an active participant in an employer-sponsored retirement plan, he is subject to an AGI phaseout of \$77,000 to \$87,000 in 2024. Because his income is above the phaseout range, he is not eligible to make a deductible IRA contribution. His AGI is too high to contribute to a Roth IRA, as well. The Roth IRA AGI phaseout is \$146,000 to \$161,000 in 2024.

7. A

When an investment company puts home mortgages or other loans into a pool and then sells securities representing shares of the pool, the securities sold are referred to as asset-backed securities.

8. A

If the yield curve is flattening, then the spread between yields of short-term and long-term bonds is decreasing.

9. B

The preliminary prospectus is also referred to as a “red herring.”

10. D

Selling a naked call will expose an investor to the greatest amount of risk.

Practice Exam 5

11. B

Monthly interest rate = $3.2\% \div 3 \text{ months} = 1.07\%$

Annual interest rate = $3.2\% \times 4 \text{ quarters} = 12.80\%$

12. C

The Federal Reserve supervises and regulates banks, and operates and oversees the U.S. payment system. It derives its authority from Congress.

13. B

An income statement is also referred to as a statement of financial performance, statement of operations, and statement of profit or loss. A statement of financial position is another name for a balance sheet.

14. C

Real return is an investment's rate of return after adjusting for inflation. Nominal return is an investment's rate of return without adjusting for inflation.

15. A

According to the arbitrage pricing theory, security prices in different markets will not differ for any significant period of time.

16. B

In order to obtain a viatical settlement, the insured must be terminally ill and must have owned the policy for at least two years. The current beneficiary of the policy must sign a release or waiver, and the insured must sign a release allowing the viatical settlement provider access to his or her medical records.

17. A

A qualified domestic trust (QDOT) allows property to pass to a non-U.S. citizen spouse and still qualify for the marital deduction. In order for a QDOT to be valid, there must be at least one trustee who is a U.S. citizen or a qualifying domestic corporation.

18. D

The primary issuers of individual bonds are local government, state government, U.S. government, an agency of the U.S. government, and corporations.

19. C

Taxes owed from tax deduction = $(\$80,000 - \$8,000) \times 0.25 = \$18,000$

20. B

Taxes owed from tax credit = $(\$80,000 \times 0.25) - \$4,000 = \$16,000$

21. A

Step 1: Taxes owed from tax deduction = $(\$80,000 - \$8,000) \times 0.25 = \$18,000$

Step 2: Equivalent tax credit = $(\$80,000 \times 0.25) - \$18,000 = \$2,000$

22. A

Mutual fund turnover rate = Gross proceeds from sale of securities ÷ NAV

Practice Exam 5

23. B

Higher inflation = higher interest rates = lower bond values

24. C

If a wash sale occurs, no loss deduction is allowed, and the amount of the disallowed loss is added to the cost basis of the newly acquired shares.

25. D

Regardless of income, participating in a 457 plan does not affect the deductibility of Lisa's IRA contribution. Participating in a 401(k) or 403(b) would eliminate Lisa's ability to deduct her IRA contribution because her income is over the threshold.

26. C

6 quarters – 3 quarters = 3 quarters

An economic depression is defined as a decline in real GDP for 6 or more consecutive quarters.

27. B

A Chinese wall is the ethical barrier that is required between different divisions of a financial institution to avoid conflicts of interest.

28. D

Preferred stock that does not have to pay missed dividends is considered noncumulative.

29. A

Securities Act Rule 145 addresses the registration and resale requirements for securities issued in a merger, consolidation, acquisition of assets, or reclassification of securities.

30. C

The "cooling-off period," which transpires between the filing of a new issue's prospectus and the actual offering of the issue, must be a minimum of 20 days.

31. C

Brady bonds are typically issued by Latin American countries.

32. B

Expansionary policy is characterized by decreasing taxes, increasing public spending, and increasing government borrowing.

33. D

In order to maintain a SIMPLE plan, an employer may not have more than 100 employees.

34. C

An investment-grade bond is one that is rated BBB- or higher by the Standard & Poor's bond rating service. A high-yield bond is rated BB+ or lower by Standard & Poor's.

35. B

A planned amortization class (PAC) bond has the most stable cash flows and the lowest prepayment risk of any class of CMO (collateralized mortgage obligation).

Practice Exam 5

36. D

Blue sky laws are classified as state-based laws.

37. D

IRS Form 1120 is used by U.S. corporations (specifically, C Corps) to report their income, gains, losses, deductions, and credits, and to determine their tax liability.

38. D

Pink sheets are to unlisted stocks as yellow sheets are to bonds.

39. C

The National Securities Market Improvement Act of 1996 promotes efficiency and capital formation in the financial markets, and provides for more effective and less burdensome regulation between states and the Federal Government. It also declared that any offering of a "covered security" (as defined within the Act) is exempt from state registration and review.

40. B

Surrender value = \$87,500 + \$50,000 = \$137,500

41. D

Death benefit = \$250,000 + \$75,000 = \$325,000

42. B

The call option is out-of-the-money because the strike price (\$37.00) exceeds the market price (\$36.00). Therefore, the value of the option is \$0.

43. A

The moving average is a graphical representation of a security's average price over a period of time.

44. B

A generation skipping transfer may occur during the transferor's lifetime or at the transferor's death. The gift tax annual exclusion may only be used to offset a lifetime generation skipping transfer.

45. A

The FASB (Financial Accounting Standards Board) is a private, non-profit organization whose primary purpose is to establish and improve generally accepted accounting principles within the U.S.

46. B

Gross Domestic Product (GDP) = C + I + G + E

C = Personal consumption

I = Gross private domestic investment

G = Government spending

E = Net exports

Practice Exam 5

47. A

To conduct bottom-up investment analysis, first examine a specific company, then examine a specific industry, then examine a specific economy, then examine the global economy.

48. D

All of the groups listed may be excluded from participating in an employee stock purchase plan (ESPP). These include employees working less than 20 hours per week, employees with less than 2 years of service, and officers of the employer.

49. C

Financial risk is the risk associated with a company's decision to use debt as part of its capital structure.

50. E

Credit risk is the possibility that a bond issuer will default.

51. A

Business risk is the risk inherent in company operations.

52. C

The two government agencies responsible for monitoring qualified retirement plan rules and eligibility are the IRS and the Department of Labor.

53. A

If a person dies testate or intestate, his or her property will be subject to probate.

54. B

In a defined benefit plan, employer contributions can vary but participant benefits are fixed. The employer assumes the investment risk, and they tend to favor older employees.

55. D

Non-systematic risk is the risk associated with a particular security or company. It includes risks such as tax risk and financial risk. An investor who owns five growth stocks can reduce non-systematic risk by adding a value stock to her portfolio.

56. D

Money in a Coverdell Education Savings Account (ESA) must be used by the time the beneficiary is 30 years of age.

57. B

The capital asset pricing model (CAPM) calculates the required rate of return for a stock based on its beta and the stock market's overall rate of return. That rate of return can then be used in the dividend growth model to value common stock.

58. A

Total assets = Liabilities at year-end + Contributed capital at year-end + Beginning retained earnings + Revenues - Expenses - Dividends

Total assets = \$500,000 + \$100,000 + \$150,000 + 300,000 - \$200,000 - \$50,000

Total assets = \$800,000

Practice Exam 5

59. B

M1 = Coins and currency in circulation + Money held in checking accounts

60. D

A refundable tax credit can reduce a taxpayer's income tax liability below zero. A non-refundable tax credit cannot reduce a taxpayer's income tax liability below zero.

61. D

The Securities Investor Protection Act of 1970 regulates brokerage firms.

62. C

The Investment Company Act of 1940 regulates mutual funds.

63. A

The Securities Act of 1933 regulates new securities.

64. B

The Securities Exchange Act of 1934 regulates existing securities.

65. C

Treasury notes, Treasury bonds, and TIPS, whose interest and principal portions have been separated so they may be sold individually, are referred to as Treasury STRIPS.

66. A

Open-end mutual funds issue new shares and redeem existing shares from shareholders. The price an investor pays when buying shares of an open-end mutual fund is based on the fund's net asset value (NAV).

67. B

Regulation A permits unregistered public offerings of up to \$5 million of securities in any 12-month period.

68. C

Employer contributions to a SEP require immediate vesting. A 401(k) plan and money purchase plan may use alternate vesting schedules for employer contributions.

69. C

NAV = (Total value of investment - Liabilities) ÷ Shares outstanding

70. C

According to the anomaly known as the small-firm effect, small cap companies have been shown to outperform large cap companies on a risk-adjusted basis over a period of many years.

71. B

Interest earned on private activity bonds is a tax preference item for alternative minimum tax (AMT).

72. B

According to the Uniform Securities Act, if the Administrator issues a subpoena and the affected party fails to respond, it is referred to as contumacy.

Practice Exam 5

73. C

$$GDP = C + I + G + (X - M)$$

$$GDP = \$11.4 + \$6.2 + \$3.3 + (\$1.8 - \$2.9) = \$19.8 \text{ billion}$$

74. D

A corporate insider is defined as a director or senior officer of a company, as well as any person or entity that beneficially owns more than 10% of a company's voting shares.

75. C

Only Government National Mortgage Association certificates (Ginnie Maes) are backed by the full faith and credit of the U.S. government.

76. A

Series EE bonds provide tax-exempt interest if the proceeds are used to pay for qualifying education expenses.

77. C

The value of publicly traded stocks and bonds is the mean between the highest and lowest quoted selling price on the date of disposition for gift and estate tax purposes.

78. C

An order book official (OBO) is an exchange employee who is in charge of keeping a book of public limit orders on exchanges utilizing the "market-maker" system.

79. A

Employer contributions to a defined contribution plan must use either the 3-year cliff vesting or 6-year graded vesting schedules.

80. A

A bond anticipation note (BAN) is a short-term obligation that is issued for temporary financing needs by a municipality.

81. A

A buy stop order is an order to buy a stock at a price above the current market price.

82. B

A variable life insurance policy will pay benefits that vary according to the value of the underlying investments.

83. C

Regarding IAR registration, all individual registrations are administered at the state level, regardless of whether the RIA firm is registered at the SEC or state level.

84. B

Wills do not avoid probate. Planning for incapacity is addressed through powers of attorney, not through the will. The will is often read after the decedent's funeral, therefore burial wishes should not be included. A will can be used to establish a testamentary trust.

Practice Exam 5

85. D

An indenture agreement describes the terms and conditions of a bond, including call provisions, description of collateral, and how coupon payments are determined.

86. D

Form 10-Q must be filed for each of the first three fiscal quarters of a company's fiscal year. It includes unaudited financial statements and provides a continuing view of the company's financial position during the year.

87. C

Money purchase plans are easy to explain to employees because contributions are based on a flat percentage of compensation. Money purchase plans tend to favor younger employees, and forfeitures can be reallocated to remaining employees. Contributions cannot be omitted in certain years. The "substantial and recurring" rule only applies to profit sharing plans.

88. B

A trade surplus results from a country exporting more than it imports.

89. D

Eurodollars are U.S. dollar denominated deposits in banks located outside the U.S. They do not involve deposits at only European banks.

90. A

Confirmation bias describes an investor's tendency to look for information that supports his or her previously established decision, even if that decision was imprudent. It may explain why investors are slow to sell an underperforming stock.

91. C

The Instinet is a computerized subscriber service that serves as a vehicle for the fourth market by permitting subscribers to display bids and offers and execute trades electronically.

92. D

An unqualified legal opinion means that the bond counsel has no reservations regarding the bond issue, and it is considered the most desirable for investors.

93. C

Certificates of deposit (CDs) are known as "time deposits." They are deposits made with a bank for a specified period of time.

94. A

In any single life private annuity transaction, if the seller outlives his or her actuarial life expectancy, the purchaser will have paid too much for the property. If the seller does not outlive his or her actuarial life expectancy, the purchaser will have made a good financial deal.

95. C

The annual report on Form 10-K provides a comprehensive overview of a company's business and financial condition and includes audited financial statements.

Practice Exam 5

96. B

$$\$85,000 - \$67,000 = \$18,000.$$

Accounts receivable (an asset) increases by \$85,000. The balance in inventory (an asset) decreases by \$67,000. The net increase in assets is \$18,000.

97. C

Cyclical stocks tend to prosper in growing and expanding economies, and do poorly during down business cycles.

98. A

The Bank Secrecy Act of 1970, also known as the Currency and Foreign Transactions Reporting Act, requires financial institutions to assist U.S. government agencies in detecting and preventing money laundering.

99. A

A SEP requires immediate vesting. A money purchase plan, 401(k) plan, and 403(b) plan may use alternate vesting schedules.

100. A

REITs are publicly traded closed-end investment companies that can sell at a premium or discount to its NAV. A mortgage REIT is a specific type of REIT.

101. C

The typical limit on the term of a loan from a qualified retirement plan is 5 years.

102. C

A bond swap refers to taking a loss on a bond and replacing it with a substantially different bond to avoid triggering the wash sale rule.

103. D

For the 15% capital gains rate to apply, Steve must be in a marginal tax bracket of 25% or higher. To qualify for long-term capital gains, assets must be held for more than one year.

104. D

Taking more or less risk will move the investor's position along the efficient frontier, but will not shift it. The same is true of changing the proportion of securities already invested in the portfolio. However, by selecting investments with lower coefficients of correlation, the risk will be reduced and the efficient frontier will shift upward and to the left.

105. C

Rehypothecation refers to a broker using securities in his or her possession, but owned by a customer, as collateral to raise a loan to cover a short position.

106. B

The maximum prison sentence for an insider trading violation is 20 years.

107. C

An S Corp must be a domestic corporation and may have up to 100 shareholders. All shareholders must be U.S. citizens or residents. Only one class of stock is permitted with an S Corp.

Practice Exam 5

108. D

All of the items listed are permitted investments in an IRA. These include a mutual fund that invests exclusively in a silver mining stock, gold coins minted in the U.S., and a real estate investment trust (REIT).

109. C

$(\text{Current assets} - \text{Inventory}) \div \text{Current liabilities} = \text{Quick ratio}$

110. A

To calculate core inflation, food and energy prices are excluded from the calculation.

111. A

Investment advisers that have custody of client assets or require prepayment of advisory fees 6 months or more in advance, and in excess of \$1200 for each client, must file an audited balance sheet with the SEC as of the end of the investment adviser's fiscal year.

112. C

Class C mutual fund shares charge a level load.

113. C

Investment risk is the chance that an investment's actual return will be less than its expected return.

114. D

Sole proprietorships are the simplest form of business entity, and they have no formal legal requirements. They have a lack of continuity of business life and provide unlimited liability to owners.

115. A

A bear spread seeks to maximize an investor's profit when the price of an underlying security decreases in value.

116. A

The Maloney Act of 1938 allowed for the establishment of the National Association of Securities Dealers (NASD) and the U.S. domestic over-the-counter markets in securities.

117. A

Lower-coupon bonds are more affected by interest rate changes than higher-coupon bonds. Lower-coupon bonds have more price volatility.

118. B

The shorter a bond's term to maturity, the less its potential for relative price fluctuation. Long-term bonds have more price volatility.

119. A

Long-term bonds are more affected by interest rate changes than short-term bonds. Long-term bonds have more price volatility.

Practice Exam 5

120. C

Qualified personal residence trusts (QPRTs) are commonly used for vacation homes, and homes valued over \$1,000,000. The grantor will have a taxable gift upon the creation of a QPRT.

121. B

Rule 72(t) of the tax code allows individuals to make withdrawals before age 59 ½ from certain retirement accounts without penalty, as long as the SEPP (substantially equal periodic payment) regulation is met.

122. D

Because Dawn contributed to a qualified retirement plan, the entire amount that she withdraws will be taxed as ordinary income.

123. A

To open a health savings account (HSA), an individual must have a high-deductible health plan (HDHP).

124. D

Tenancy by entirety is a form of joint tenancy allowed for married couples. It is severable only by both spouses, and the property automatically passes to the surviving spouse when the first spouse dies.

125. B

$$ROE_t = NI_t \div \text{Average BVE}_t$$

$$ROE_t = \$950,000 \div \$3,260,000 = 0.2914 = 29.14\%$$

126. B

A spread is the simultaneous purchase of one option and the sale of another option on the same side or position within the market. For example, purchasing a call option and selling a call option on the same stock at the same time is a spread.

127. A

A collar is a technique used to protect an investor's gain in a long position of stock. Specifically, an investor purchases a put option to protect against a decline in the value of an underlying stock, and sells a call option to generate premium income to cover the cost of the put option premium.

128. D

In a protective put, an investor purchases a put option while holding shares of an underlying stock from a previous purchase.

129. C

A straddle is the simultaneous purchase of a call option and a put option on the same stock at the same time.

130. A

EMMA (Electronic Municipal Market Access System) is the official repository for information on virtually all municipal bonds, and provides free access to official disclosures, trade data, and other information about the municipal securities market.

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.

Practice Exam 6

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.

Practice Exam 6

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

Practice Exam 6

- 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%

Practice Exam 6

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

Practice Exam 6

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.

Practice Exam 6

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.

Practice Exam 6

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.

Practice Exam 6

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

Practice Exam 6

- 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

Practice Exam 6

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

Practice Exam 6

- 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

Practice Exam 6

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.

Practice Exam 6

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

Practice Exam 6

- 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.

Practice Exam 6

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

Practice Exam 6

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

Practice Exam 6

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

Practice Exam 6

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.

INDEX

A

Accounting fraud, 49, 70
Accounts payable, 59, 75, 135, 151
Accounts receivable, 12, 33, 59, 75, 189
Accredited investor, 21, 37, 62, 76, 137, 152, 205, 224
Accrual basis accounting, 53
Accumulated depreciation, 226
Active participant, 53, 72, 161, 181
Activity ratio, 141, 154
Actuary/actuarial calculation, 174, 188, 198, 204, 220, 223
Adjusted basis, 169, 186, 208, 225
Adjusted gross income (AGI), 161, 181
ADV Part 1, 19, 199, 221
ADV Part 2, 19, 37
Advertising, 26, 40, 127, 132, 147, 149
After-tax return, 61, 76, 131
Age-based profit sharing plan, 101, 115
Alimony, 53, 72
Alternate physical location, 98, 114
Alternative minimum tax (AMT), 169, 186
Alternative trading system (ATS), 97, 113, 136
American depository receipt (ADR), 12, 33, 57, 74, 83, 96, 106, 113, 198, 202, 222
American Municipal Bond Assurance Corporation (AMBAC), 27, 40
American Stock Exchange (AMEX), 120, 136, 151
American style option, 211, 227
Antifraud, 10, 32
Arbitrage, 14, 48, 133, 159, 182
Assets under management, 4, 29, 45, 68
Automated Client Account Transfer Service (ACATS), 137, 139, 152
Automated Confirmation Transaction Service (ACT), 53, 72
Average collection period, 52, 141, 154, 205

B

Balance sheet, 10, 32, 46, 68, 81, 105, 124, 145, 177, 182, 190
Bank draft, 123, 145

Bank Secrecy Act of 1970, 16, 35, 65, 174, 189
Bankruptcy, 54, 73
Bear spread, 177, 190
Bearer bond, 98, 114, 122, 125, 144
Bearish strategy, 34, 47, 68
Behavioral finance, 22, 173
Beta coefficient, 17, 35
Block trading, 54, 72
Blotters, 103, 116
Blue chip stocks, 82, 92, 105, 110
Blue sky laws, 25, 39, 163, 184
Board of Governors, 54, 72, 89
Bond anticipation note (BAN), 171, 187
Bond duration, 15, 24, 35, 48, 62, 69, 76, 88, 102, 108, 115-116, 124, 130, 145, 148, 203, 223
Bond fund, 3, 129
Bond immunization, 124, 145
Bond swap, 175, 189, 205, 224
Book value, 23, 38, 140, 153, 179
Bottom-up investment analysis, 165, 185
Brady bond, 57, 60, 74, 98, 125, 162, 183
Breakpoint discount, 133, 150, 196, 219
Brochure rule, 58, 74, 123, 145
BrokerCheck, 207, 210, 225
Business continuity plan, 49, 70, 98, 114
Business cycle, 47, 54, 68-69, 72, 130, 148, 189
Business risk, 166, 185, 197, 220
Buy limit order, 26, 40, 171
Buy stop order, 26, 171, 187

C

C Corp, 15, 20, 58, 74, 132, 134, 149-150, 163, 184, 207, 225
Call loan rate, 95, 112
Call option, 21, 38, 58, 75, 164, 180, 184, 191, 198
Capital asset pricing model (CAPM), 21, 38, 51, 100, 167, 185, 216
Capital gains tax, 16, 35, 57, 74, 126, 132, 146, 149, 179
Capital loss, 8-9, 31, 51, 71, 84, 106
Capital market line, 81, 131, 208, 225

Index

- Capping, 7, 48, 56, 99, 114, 119
Carryover of basis, 122, 144
Cash balance plan, 7, 11, 30, 32, 120, 125, 134, 143, 150, 216, 229
Cash flow from financing activities, 3, 29
Cash flow from investing activities, 3, 29
Cash flow from operating activities, 3, 29
Cash flow statement, 213, 228
Cash paid to suppliers, 135, 151
Cash ratio, 64, 77
Central banking system, 50, 70
Central Registration Depository (CRD), 12, 33, 83, 96, 101, 119, 141, 143, 210
Charitable lead trust, 10, 32, 71
Charitable remainder annuity trust (CRAT), 11, 33, 52, 71, 125
Charitable remainder unitrust (CRUT), 11, 33, 52, 71, 125, 146
Charity, 10, 23, 32, 39, 52, 71, 125
Chicago Board Options Exchange (CBOE), 120, 143
Chinese wall, 65, 78, 162, 183
Churning, 119, 143
Civil penalty, 46, 68
Class A shares, 7, 31, 127, 177
Class B shares, 7, 127, 147, 177
Class C shares, 7, 127, 177, 190
Cliff vesting, 171, 187
Closed-end mutual fund, 18, 36, 91, 110, 189
Coinsurance, 199, 221
Collar (hedging technique), 19, 177, 180, 191
Collateralized mortgage obligation (CMO), 50, 70, 101, 115, 163, 183
Collectibles, 52, 71, 197, 220, 229
Commercial paper, 13, 33, 119, 143, 173, 202, 222
Commodity Futures Trading Commission (CFTC), 50, 70, 86, 107
Common stock, 3, 13, 33, 44-45, 57, 68, 87, 91-92, 110, 131, 135, 149, 151, 167, 185
Community property, 89, 94, 111, 206, 224
Complex trust, 6, 30, 196, 219
Conduit theory, 25, 40, 136, 151, 214, 228
Confirmation bias, 173, 188
Conflict of interest, 96, 112, 137, 151, 162, 183
Consolidated Quotation System (CQS), 136, 151
Consolidated tape, 63, 77
Constant dividend growth model, 100, 114
Constructive dividend, 126, 146
Consumer Price Index (CPI), 13, 34, 47, 69, 94, 111, 139, 152, 198-199, 221
Consumer sentiment, 13, 33
Contraction stage of business cycle, 47, 68, 130, 148
Contractary policy, 85, 107, 133, 135, 150-151
Contributed capital, 51, 71, 167, 185
Contumacy, 169, 186
Conversion premium, 140, 153
Convertible bond, 93, 111, 131, 149, 209, 226
Cooling-off period, 135, 151, 162, 183
Core inflation, 177, 190
Corporate bond, 13, 20, 22, 24, 37-39, 45, 68, 131, 149, 203, 217, 223
Corporate governance, 26, 40
Corporate insider, 170, 187
Correlation coefficient, 17, 35, 215, 229
Cost of goods sold, 53, 88, 108, 135, 151
Counter-cyclical stock, 130, 148
Coverdell Education Savings Account (ESA), 14, 34, 44, 67, 98, 113, 167, 185
Credit quality, 56, 73, 138, 152, 203, 223
Credit report, 99, 114
Credit risk, 166, 185, 203
Credit score, 99, 114
Cross-testing, 76, 147
Currency and Foreign Transactions Reporting Act, 174, 189
Currency Transaction Report (CTR), 20, 123, 145, 196, 219
Current ratio, 7, 93, 110, 126, 176, 204, 223
Current yield, 128, 147
Custody of assets, 12, 33, 124, 145, 177, 190
Customer Identification Program (CIP), 139, 153
Cyber security, 123, 157, 181
Cyclical stock, 5, 141, 154, 174, 189
- D**
- Dark pools, 54, 72, 97, 113, 158
Data backup, 98, 114
Date of declaration, 18, 36
Date of record, 18, 36
Death benefit, 9, 31, 99, 109, 113-114, 164, 184, 212, 227
Debenture, 50, 60, 63-64, 77, 88, 108, 126, 146, 170, 214
Debt-to-capital ratio, 87, 108, 198, 221
Default risk, 13, 45, 65, 68, 78, 87, 108, 126, 146, 203
Defensive stock, 5, 30, 88, 108, 141, 154

Index

- Deflation, 20, 37
Department of Labor (DOL), 166, 185
Depletion, 210, 226
Depreciation, 59, 75, 210, 226
Depression, 161, 183
Diluted earnings per share, 135, 151
Disallowable loss, 60, 75, 161, 183
Discount rate, 59, 75, 95, 112
Diversifiable risk, 53, 72, 126
Diversification, 16, 35, 45, 67, 205, 224
Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, 26, 40, 49, 86, 99, 107, 206
Dollar cost averaging, 99, 114
Double taxation, 58, 60, 74-75, 134, 150, 215, 228
Dow Jones Industrial Average, 82, 96, 105, 121, 144
Dow Jones Transportation Average, 212, 227
Dow Jones Utility Average, 51, 71
Duration of a bond, 15, 24, 35, 48, 62, 69, 76, 88, 102, 108, 115-116, 124, 130, 145, 148, 203, 223
- E**
- EDGAR, 63, 83, 101, 115
EE bond, 6, 30, 86, 107, 170, 187
Efficient frontier, 61, 176, 189, 196, 208, 219, 225
Efficient market hypothesis, 23, 38, 56, 74, 208, 225
Electronic Communication Network (ECN), 97, 113, 137, 140, 153, 173, 209
Electronic Municipal Market Access System (EMMA), 173, 180, 191
Emergency preparedness rule, 49, 70
Emerging markets, 57, 74
Employee stock ownership plan (ESOP), 216, 229
Employee stock purchase plan (ESPP), 92, 110, 166, 185
Equity REIT, 63, 77, 138, 152, 200, 221
ERISA, 24, 39-40, 58, 74, 86, 107, 122, 144, 166, 199, 207, 211, 221, 227
Escheat, 125, 146
Estate tax, 8, 31, 52, 160, 171, 187, 206
Eurodollar, 173, 188, 198
European style option, 9, 32
Excess contribution, 213, 228
Exchange rate risk, 65, 78, 83, 106, 197, 220
Exchange-traded fund (ETF), 15, 35, 54, 72, 96, 113, 175
Excise tax, 53, 72, 199, 213, 228
Ex-dividend date, 18, 36
Expansion stage of business cycle, 47, 69
Expansionary policy, 85, 107, 162, 183
- F**
- Face-amount certificate (FAC), 25, 40
Fair and Accurate Credit Transactions Act (FACT Act), 26, 43, 46, 68, 99, 114
Family limited partnership, 8, 31, 206, 224
Fannie Mae (FNMA), 24, 92, 110, 170
Fed funds rate, 95, 112
Federal Deposit Insurance Corporation (FDIC), 26-27, 40, 81, 94, 101, 115, 165
Federal open market committee (FOMC), 43, 50, 67
Federal Trade Commission, 138, 152
Fidelity bond, 57, 60, 75, 98, 125
Fiduciary, 4, 29, 56, 58, 74, 119, 143, 199, 221
Financial Accounting Standards Board (FASB), 165, 184
Financial Crimes Enforcement Network (FinCEN), 123, 145
Financial risk, 166-167, 185, 197, 220
FINRA Rule 2210, 9, 31, 121, 144, 209, 226
FINRA Rule 3240, 9, 15, 35
First-time home purchase, 86, 138, 152
Fiscal policy, 199, 221
529 plan, 62, 76, 131, 149, 201, 222
Fixed asset turnover ratio, 141, 154, 204
Fixed income security, 20, 37, 65, 78, 203, 223
Flat tax, 5, 29, 209
Flat yield curve, 56, 91, 109, 138, 203, 223
Flexible death benefit, 9, 99, 114
Flexible premium, 9, 99, 114
Foreign tax credit, 57, 74
Forfeitures, 91, 109, 172, 188
401(k) plan, 50, 53, 70, 72, 90, 101, 109, 115, 152, 158, 161, 169, 175, 183, 186, 189, 198, 201-202, 207, 216, 220, 223, 225, 229
403(b) plan, 44, 62, 67, 76, 94, 111, 127, 129, 147-148, 161, 175, 183, 189, 200, 207, 221, 225
457 plan, 53, 72, 161, 183
Fourth market, 65, 78, 173, 188, 212
Front running, 7, 48, 56, 69, 99, 119
Front-end load, 7, 31
Fundamental analysis, 208, 225
Future interest gift, 19, 37, 136
Futures, 50, 70, 216, 229

Index

G

General obligation bond, 8, 31, 50, 55, 73, 121, 163, 169
General power of appointment, 86, 107, 160
Generally accepted accounting principles (GAAP), 55, 73, 165, 184
Generation-skipping transfer tax (GSTT), 127, 147, 201, 222
Gift splitting, 19, 37, 89, 108
Gift tax annual exclusion, 19, 37, 44, 136, 151, 165, 184, 201, 222
Gift tax return, 19, 37
Ginnie Mae (GNMA), 24, 110, 170, 187
Global fund, 48, 69, 92, 110, 121, 144
Gold coins, 176, 190, 215, 229
Good faith deposit, 65, 78
Government borrowing, 85, 107, 133, 150, 183
Grace period, 97, 113
Gross domestic product (GDP), 21, 47, 57, 63, 69, 74, 77, 161, 165, 170, 183-184, 187
Gross national product (GNP), 21, 37, 57, 74, 139, 198
Gross profit, 88, 108, 214, 228
Growth stock, 92, 110, 167, 185, 195, 219
Guaranteed cash value, 9, 99, 114
Guaranteed investment contract (GIC), 20, 101, 171

H

Hardship withdrawal, 138, 152
Health savings account (HSA), 14, 34, 100, 114, 179, 191, 199, 221
Hedge fund, 135, 151
High-deductible health plan (HDHP), 179, 191
High-yield bond, 52, 72, 163, 183
Holding period return, 46, 68, 132, 149, 195, 219
Housing starts, 13, 34
Howey test, 6, 30, 75
Hybrid REIT, 63, 77, 200, 221
Hypothecate, 49, 70

I

I bond, 94, 111
Identity theft prevention program, 138, 140, 152-153
Incentive stock option (ISO), 25, 59, 75, 84, 106

Income statement, 159, 182
Indifference curve, 196, 219
Inferior good, 63, 77
Initial margin, 130, 148, 209
Initial public offering (IPO), 3, 6, 29-30, 57, 87, 108
Insider trading, 10, 32, 46, 68, 176, 189, 197, 204, 220, 223
Insider Trading and Securities Fraud Enforcement Act of 1988, 65, 78, 86, 99, 120, 143, 164, 174, 206
Insolvency, 63, 77
Insurance industry rating services, 87, 107
Intangible asset, 140, 153, 210, 226
Interest rate risk, 22, 38, 54, 73, 88, 108, 124, 145, 197, 203, 220, 223
Internal rate of return (IRR), 47, 69, 216, 229
Intestate, 166, 185, 205, 224
Inventory turnover ratio, 141, 154, 176
Inverted yield curve, 56, 91, 138, 152
Investment Adviser Registration Depository (IARD), 83, 96, 101, 106, 119, 141, 143, 210, 226
Investment Advisers Act of 1940, 5, 30, 201, 205, 210, 222, 226
Investment Company Act of 1940, 5-6, 64, 137, 151, 168, 178, 186, 205
Investment contract, 6, 30, 59, 75, 171

J - L

Joint tenancy, 34, 129, 148, 191
Key advisory personnel, 96, 112
"Know your customer" rule, 51, 71
Lagging economic indicator, 13, 34
Latin America, 57, 74, 162, 183
Leading economic indicator, 13, 33-34
Letter of intent (LOI), 133, 150
LIBOR, 95, 112
Life expectancy, 18, 36, 174, 188, 199, 221
Life insurance, 4, 9, 17, 29, 31, 36, 55, 73, 88, 97, 99, 108, 113-114, 129, 148, 164, 171, 187, 197, 212, 220, 227
Limit not held, 10, 32
Limited partnership, 8, 24, 31, 39, 132, 149, 206-207, 224-225
Liquidating dividend, 126, 146
Liquidation, 63, 77, 82, 105
Liquidity ratio, 204, 223
Liquidity risk, 65, 78, 203
Living trust, 8, 130, 148, 206, 224
Loss deduction, 60, 75, 161, 183
Lump sum distribution, 21, 37, 179

Index

M

- M1 of money supply, 167, 186
- M2 of money supply, 124, 145
- M3 of money supply, 44, 67
- Management fee, 54, 72
- Marginal tax rate, 85, 106
- Marital deduction, 49, 70, 160, 182
- Marital trust, 49, 83, 86, 107
- Market not held, 10, 32
- Marketability, 71, 120, 143
- Markowitz, 61, 176
- Mean, 139, 153
- Median, 139, 153
- Mode, 139, 153
- Modern portfolio theory, 14, 23, 34, 50, 70, 159, 196, 219
- Monetary policy, 43, 59, 67, 75, 81, 105, 124, 145, 157, 181, 199
- Money laundering, 16, 35, 56, 95, 112, 174, 189, 206, 224
- Money market funds, 3, 119, 143, 173, 202, 217, 222
- Money supply, 13, 34, 44, 81, 105, 124, 135, 151, 167
- Mortgage REIT, 63, 77, 138, 152, 175, 189, 200, 221
- Mortgage-backed security, 157, 181
- Moving average, 51, 71, 165, 184
- Municipal bond, 15, 20, 27, 40, 55, 65, 73, 78, 122, 144, 180, 191
- Municipal Securities Rulemaking Board (MSRB), 24, 39, 43, 56, 73, 124, 145, 165, 180

N

- Naked call, 19, 60, 75, 158, 181
- Naked short selling, 12, 33
- NASDAQ, 53, 58, 72, 74, 120, 140, 209, 226
- National Adjudicatory Council (NAC), 89, 91, 109
- National Association of Insurance Commissioners (NAIC), 10, 87, 102, 107, 123
- National Association of Securities Dealers (NASD), 10, 12, 33, 43, 91, 101-102, 109, 123, 178, 190
- National Securities Clearing Corporation (NSCC), 10, 96, 101, 113, 140, 165, 173
- Negotiable CD, 119, 143, 198, 220
- Net asset value (NAV), 20, 37, 91, 99, 110, 161, 169, 175, 182, 186, 189, 201, 222
- Net income, 12, 23, 57, 59, 74-75, 88, 108, 179

- Net profit margin, 7, 19, 37, 52, 71, 126, 205
- Net revenue, 53, 72
- Net worth statement, 46, 68
- New York Stock Exchange (NYSE), 90-91, 100, 109, 115, 120, 136, 151
- Nominal return, 119, 143, 159, 182
- Noncumulative preferred stock, 162, 183
- Nonqualified stock option (NQSO), 25, 84, 106
- North American Securities Administrators Association (NASAA), 10, 12, 32-33, 50, 91, 102, 116, 119, 143
- Notice filing, 7, 31, 82, 105, 215, 229

O

- Omitting prospectus, 3, 132, 149, 158
- Open market operations, 59, 75, 157, 181
- Open-end mutual fund, 110, 168, 186, 201, 222
- Operating profit margin, 7, 19, 37, 52, 205, 214, 224, 228
- Opportunity cost, 44, 67
- Options Clearing Corporation (OCC), 140, 153
- Order book official (OBO), 171, 187
- OTC Bulletin Board, 209, 226

P

- P/E effect, 204, 223
- Painting the tape, 7, 30, 48, 56, 99, 119
- Patriot Act of 2001, 26, 49, 86, 139, 206, 224
- Peak stage of business cycle, 47, 69
- Pegging, 7, 48, 56, 73, 99
- Penny stock, 200, 221
- Pension Benefit Guaranty Corporation (PBGC), 24, 27, 101, 122, 166, 211
- Pension plan, 11, 32, 62, 76, 134, 141, 150, 154, 206, 216, 224, 229-230
- Performance advertising, 127, 147
- Personal Service Corporation (PSC), 134, 150
- Phishing, 123, 144
- Pink sheets, 22, 163, 184
- Pipeline theory, 136, 151
- Plan sponsor, 24, 39, 119, 143
- Planned amortization class (PAC), 50, 163, 183
- Ponzi scheme, 11, 33
- Pooled income fund, 10, 23, 39, 54
- Power of appointment, 86, 107, 160
- Precious metals, 88, 108
- Pre-emptive right, 63, 77

Index

- Preferred stock, 13, 20, 33, 37, 54-55, 73, 91, 127, 147, 162, 183, 205, 212, 224, 227
Preliminary prospectus, 3, 132, 158, 181
Premature distribution, 61-62, 76, 90, 96, 109, 112, 130, 148, 198, 220
Pre-retirement inflation, 18, 36, 121, 144
Present value, 5, 30, 213, 216, 229
Pretax margin, 214, 228
Price-weighted index, 58, 82, 105, 131, 149
Prime rate, 13, 34, 95, 112
Private activity bond, 55, 73, 121, 169, 186
Private annuity, 102, 174, 188
Private placement, 21, 37, 45, 54, 57, 60, 62, 68, 74, 76, 157
Probate, 31, 83, 97, 106, 113, 166, 172, 185, 187, 224
Producer Price Index (PPI), 47, 198, 220
Profit sharing plan, 11, 32, 61-62, 76, 101, 115, 128, 134, 141, 147, 150, 154, 188, 206, 211, 216, 224, 229
Profitability ratio, 19, 37
Progressive tax, 23, 109, 209, 226
Promissory note, 123, 145, 202, 222
Prospect theory, 22, 38, 44
Prospectus, 3, 22, 38, 50, 57, 74, 132-133, 135, 140, 149, 153, 158, 162, 181, 183, 202, 214, 222
Protective put, 180, 191
Public Company Accounting Oversight Board, 49, 56, 70
Public offering price (POP), 20, 37
Public spending, 85, 107, 133, 150, 162, 183
Purchasing power risk, 65, 78, 197, 220
Put option, 14, 19, 34, 36, 47, 58, 68, 75, 82, 105, 127-128, 130, 147, 180, 191, 197, 208, 220, 226
- Q**
- Qualified dividend, 57, 74, 126, 146
Qualified domestic trust (QDOT), 160, 182
Qualified legal opinion, 83, 106
Qualified personal residence trust (QPRT), 90, 109, 178, 191, 206, 224
Qualified preretirement survivor annuity (QPSA), 195, 219
Qualified purchaser, 102, 115
Qualified terminable interest property (QTIP) trust, 49, 70, 86
Qualitative data, 121, 144, 228
Quantitative data, 144, 213, 228
Quick ratio, 52, 64, 77, 93, 176, 190, 204-205, 223
- R**
- Random walk pattern, 38
Real estate, 3, 20, 24, 29, 37, 39, 45, 68, 138, 152, 176, 181, 190
Real estate mortgage investment conduit (REMIC), 20, 37, 138, 152, 157, 181, 199
Real return, 45, 68, 119, 143, 159, 182
Recession, 5, 30, 47, 63, 68, 77, 203
Recordkeeping, 9, 31
Recourse loan, 102, 115
Red Flags Rule, 86, 107, 138, 152
Red herring, 3, 22, 158, 181, 202, 222
Refundable tax credit, 168, 186
Registration by coordination, 48, 69
Registration by notification, 48, 69
Registration by qualification, 48, 69
Registration statement, 22, 38, 101, 115, 135, 151, 211, 227
Regressive tax, 23, 39, 209
Regulation A, 45, 124, 145, 169, 186
Regulation D, 8, 21, 37, 45, 68
Regulation FD, 95, 111, 140, 216
Regulation SHO, 12, 33
Regulation S-ID, 140, 153
Regulation S-P, 216, 229
Regulation T, 8, 31, 45, 124, 130, 148, 204
Regulation U, 8, 45, 124, 204, 223
Rehypothecation, 176, 189
Reinvestment risk, 15, 26, 35, 40, 65, 78, 87, 108, 203, 223
Retained earnings, 44, 51, 71, 87, 126, 146, 167, 185
Retirement plan administrator, 119, 143
Return on equity, 7, 19, 30, 37, 126, 179
Revenue bond, 8, 55, 73, 121, 144, 169
Reverse stock split, 3, 29
Reversionary trust, 10, 32
Revocable living trust, 130, 148
Rights and warrants, 90, 109, 197, 220
Rights of accumulation, 196, 219
Risk-free rate, 6, 21, 25, 38, 96, 99, 206, 208, 225
Rollover, 21, 37
Rule 72(t), 178, 191
Rule of 72, 129, 148
Russell 2000, 13, 33, 58, 74, 96
- S**
- S Corp, 15, 58, 132, 149, 176, 189, 207, 225
S&P 500, 6, 9, 31, 58, 74, 128, 147
Safe harbor, 199, 221

Index

- Sarbanes-Oxley Act of 2002, 26, 49, 65, 70, 86, 120, 164, 174, 206
Secondary market, 10, 18, 20, 32, 36-37, 52, 71, 94, 102, 111, 116, 202
Sector rotation, 54, 72
Secured bond, 63, 77, 126, 146
Securities Act Amendments of 1975, 43, 82, 99, 120, 124, 145, 215, 228
Securities Act of 1933, 5-6, 22, 30, 32, 38, 124, 145, 168, 186, 205
Securities Act Rule 144, 17, 35, 51
Securities Act Rule 145, 162, 183
Securities Act Rule 405, 17, 51, 71, 162
Securities and Exchange Commission v. W. J. Howey Co., 30, 59, 75
Securities Exchange Act of 1934, 5, 10, 19, 32, 36, 137, 168, 186, 205, 224
Securities Investor Protection Corporation Act of 1970, 82, 105
Security market line, 81, 105, 131, 208
Self-regulatory organization (SRO), 43, 67, 90-91, 109
Sell limit order, 100, 115, 157
Sell stop order, 157, 181
Semi-strong form (efficient market hypothesis), 208, 225
SEP, 11, 62, 76, 84, 106, 127, 147, 169, 175, 186, 189, 195, 216, 219, 230
Separation from service, 109, 198, 220
Series EE bond, 6, 30, 86, 107, 170, 187
Series I bond, 94, 111
Settlement Cycle Rule, 19, 36
Shareholders' equity, 108, 198, 221
Sharpe ratio, 60, 62, 75-76, 206, 224
Shelf registration, 132, 158, 202, 211, 227
Short sale/short selling, 12, 33, 45, 54, 72
Significant business disruption, 49, 70, 98, 114
SIMPLE 401(k) plan, 101, 115, 202, 223
SIMPLE IRA, 55, 73, 101, 115, 223
Simple trust, 30, 196, 219
Skip person, 43, 67, 127, 147, 201, 222
Small-cap stocks, 13, 33
Small-firm effect, 169, 186
Social media, 26, 40, 210, 226
Soft-dollar compensation, 122, 144
Sole proprietorship, 132, 149, 177, 190
Solicitor, 64, 77, 87, 92, 110
Sovereign debt, 89, 108
Spread (hedging technique), 19, 124, 175, 177, 180, 190-191
Stagflation, 20, 61, 76
Standard deviation, 16-17, 35, 56, 60, 98, 113, 206, 215
Statement of assets and liabilities, 46, 68
Statement of cash flows, 3, 29, 46
Statement of financial performance, 159, 182
Statement of financial position, 46, 68, 159, 182
Statement of profit or loss, 159, 182
Stock bonus plan, 216, 229
Stock market anomaly, 168, 186, 204, 223
Stock split, 3, 29
Straddle (hedging technique), 19, 36, 177, 180, 191
Strong form (efficient market hypothesis), 208, 225
Subchapter M, 214, 228
Subscription privilege, 63, 77
Subscription right, 63, 77
Substantially equal periodic payments (SEPP), 61, 76, 96, 112, 148, 178, 191
Super display book system, 100, 115
Supply and demand, 18, 36, 168
Support and resistance levels, 51, 71, 132
Surety bond, 57, 60, 98, 125, 146
Surrender value, 4, 164, 184
Syndicate, 87, 108
- T**
- T+2, 19, 36
T+3, 19, 36
Tangible asset, 52, 140, 210, 226
Target benefit plan, 7, 11, 30, 32, 120, 125, 134, 143, 146, 150, 216, 229
Targeted amortization class (TAC), 50, 70, 163
Tax policy, 124, 145
Taxable account, 4, 92, 110
Taxable distribution, 43, 67
Taxable equivalent yield, 15, 34, 85, 106
Taxable gift, 90, 109, 178, 191
Tax-exempt interest, 170, 187
Technical analysis, 208, 225
Telemarketing, 48, 69
Telephone Consumer Protection Act, 492, 110
1035 exchange, 55, 73
Tenancy by entirety, 15, 34, 94, 111, 191
Testamentary trust, 172, 187
Testate, 166, 185, 205, 224
Testimonial rule, 210
Testimonials, 127, 147, 210, 224
Third market, 65, 136, 151, 211
Third-party administrator, 11

Index

- Thrift savings plan, 216, 229
Time deposit, 44, 67, 124, 145, 167, 173, 188
Times interest earned ratio, 18, 36
Tombstone ad, 3, 22, 29, 50, 132, 158, 202
Top-down investment analysis, 81, 105
Totten trust, 8, 83, 92, 106, 206, 224
Trade Reporting Compliance Engine (TRACE), 20, 37, 63, 96, 137, 139, 180
Trade surplus, 172, 188
Trading restrictions, 26, 40
Traditional IRA, 8, 31, 50
Transaction cost, 21, 38, 45, 130, 164
Treasury bill, 13, 24, 39, 44, 67, 90-91, 109, 119, 129, 143, 170, 173
Treasury bond, 44, 67, 91, 109, 119, 168, 170, 186, 202, 222
Treasury inflation-protected securities (TIPS), 25, 39, 47, 69, 103, 116, 168, 186, 199, 221
Treasury note, 3, 29, 44, 67, 81, 91, 105, 109, 168, 186
Treasury STRIPS, 24, 39, 97, 113, 134, 150, 168, 186, 200, 221
Trendline, 51, 71, 81, 131, 149, 208
Treynor ratio, 62, 76, 99, 114
Trough stage of business cycle, 47, 69
Trust Indenture Act of 1939, 64, 77, 137, 152, 178
Trustee-to-trustee transfer, 21, 37
Truth in Lending Act of 1968, 43, 67
12b-1 fee, 98, 113, 122
Two-step verification process, 157, 181
- U**
- U4, 52, 96, 211, 227
U5, 52, 71, 211
Underwriter/underwriting, 65, 78, 87, 108, 195, 219
Unemployment, 13, 34, 61, 76
UGMA/UTMA, 62, 76
Uniform Application for Securities Industry Registration or Transfer, 211, 227
- Uniform Prudent Investor Act of 1994, 50, 70
Uniform Securities Act, 43, 48, 50, 65, 69, 88, 108, 137, 139, 153, 169, 178, 186, 197, 215, 220
Uniform Termination Notice for Securities Industry Registration, 52, 71
Unit benefit plan, 11, 32
Unit investment trust (UIT), 102, 116
Universal life insurance, 99, 114
Unlisted stock, 97, 163, 184
Unqualified legal opinion, 55, 73, 83, 173, 188
Unsystematic risk, 16, 35, 53, 72, 87, 95, 108, 112, 123, 197, 220
Utility stocks, 51, 71
- V**
- Value-weighted index, 58, 74, 96, 112
Variable life insurance, 9, 31, 88, 108, 171, 187
Vesting schedule, 171, 186-187, 189
Viatical settlement, 159, 182, 199, 221
VIX, 84, 106
Volatility, 45, 67, 84, 106, 190, 203, 223
Voluntary contributions, 53, 72
Voting shares, 170, 187
- W - Z**
- Warrants and rights, 90, 109, 197, 220
Wash sale, 60, 75, 106, 161, 175, 183, 189
Weak form (efficient market hypothesis), 208, 225
Whole life insurance, 4, 29, 164, 197, 212, 220
Wilshire 5000, 58, 74, 96, 112
Yellow sheets, 22, 38, 163, 184
Yield curve, 56, 73, 91, 109, 138, 152, 158, 181, 203, 223
Yield to maturity (YTM), 47, 69, 86, 102, 116, 125, 145
Zero-coupon bond, 15, 35, 39, 48, 50, 69, 92, 110, 131, 163, 209

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