

100% Money Back
Guarantee

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Law Examination

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QUESTION 1

A margin transaction refers to a transaction

- A. that is illegal under the guidelines of the Uniform Securities Act.
- B. in which the client borrows some of the money that he is investing.
- C. in which a registered agent makes trades on a customer's account without that customer's knowledge.
- D. Both A and C are true statements.

Correct Answer: B

A margin transaction refers to a transaction in which the client borrows some of the money that he is investing. It is a recognized practice.

QUESTION 2

As an agent, which of the following statements about the Securities Investor Protection Corporation (SIPC) can you legitimately make to your client?

- A. The SIPC is the FDIC of the stock and bond markets."
- B. "The SIPC was established to restore funds to investors when the brokerage firm they have been using is bankrupt or in financial distress."
- C. "The SIPC is a government agency created by an Act of Congress to combat fraud."
- D. "The SIPC is a government agency that was created by an Act of Congress to protect investors against losses in the stock and bond market."

Correct Answer: B

The statement that you can legitimately make about the SIPC to your client is that it was established to restore funds to investors when the brokerage firm they have been using is bankrupt or in financial distress. The SIPC does not insure investors against losses in the stock and bond markets like the FDIC does bank deposits, and it does not combat fraud.

QUESTION 3

Which of the following statements would not be in violation of NASAA rules regarding the sale of investment company shares?

- I. "Investing your money in shares of this money market mutual fund is identical to putting your money in a savings account at a bank, except the money market fund provides a higher return."
- II. "Our U.S. government bond fund is invested only in government bonds issued by the S. government and is, therefore, a risk-free investment."
- III.

"You are investing \$22,000 in this fund today. The fund has a 5% load at this investment level, but if you sign a letter of intent to invest another \$3,000 within the next 13 months, your load will be reduced to 4%. If something comes up and you can't invest the extra \$3,000 within 13 months, you will only need to pay the difference in the two loads."

- A.
I only
- B.
I and II only
- C.
III only
- D.
I, II, and III

Correct Answer: C

Only Selection III would not violate NASAA rules regarding the sale of investment company shares because it is the only true statement. If a fund has a breakpoint at \$25,000 that triggers a reduced front-end load and allows an investor to receive the reduced load charge if the investor signs a letter of intent stipulating that the additional investment will be made within 13 months, the only penalty to the investor who doesn't meet the breakpoint is payment of the difference in the two loads. Investing in shares of a money market mutual fund is not identical to putting money in a savings account at a bank. The bank account is insured by the FDIC in most cases; the money market mutual fund is not insured by the FDIC, and the investor can lose money (although, to date, money market mutual funds have covered any losses that they've experienced and not passed those losses onto their investors.) A U.S. government bond fund that is invested only in U.S. government bonds is free from default-risk, but it is still subject to interest rate risk. If interest rates increase, the value of the bonds in these funds-and therefore the fund itself-will decrease.

QUESTION 4

Which of the following is not considered to be a person, as defined by the Uniform Securities Act?

- A. a 16-year old cheerleader
- B. a law firm that is organized as a partnership
- C. a corporation
- D. a school district

Correct Answer: A

A minor is not considered to be a person, as defined by the Uniform Securities Act. However, partnerships, corporations, and governmental subdivisions, such as school districts, are included in the definition.

QUESTION 5

When a customer files a complaint with a broker-dealer,

I. the broker-dealer must submit the complaint to the firm's compliance department.

II. the broker-dealer must provide a prompt written response to the complainant.

III.

the broker-dealer must temporarily suspend the activities of any agent named in the complaint.

A.

I, II and III

B.

I and II only

C.

I and III only

D.

II and III only

Correct Answer: B

Only Selections I and II are true. When a customer files a complaint with a broker-dealer, the broker-dealer is required to submit the complaint to the firm's compliance department, if any, and to provide the complainant with a prompt written response. It is not necessary to suspend the activities of an agent named in the complaint.

QUESTION 6

Constance is an investment adviser representative. She told one of her clients that he should put at least 15% of his investment monies in a U.S. government bond mutual fund.

She explained that she believed that he required this percentage to meet his liquidity needs, and U.S. government bond funds are risk-free. A few months later, the client needed to sell some of his fund shares in order to pay some medical

bills and was surprised to discover that he lost money on the sale because the net asset value of the fund had dropped.

Was Constance guilty of any securities violations?

A. Yes. Constance is guilty of fraud. She misled the client into thinking he couldn't lose any money if he invested the money in a U.S. government bond mutual fund.

B. Yes. Constance should never recommend that a client invest such a high percentage of his investment monies in a U.S. government bond mutual fund.

C. No. U.S. government bonds are often referred to as risk-free investments, so Constance made no misstatement of fact in telling her client this.

D. It depends. If Constance realized that the client could lose money in a U.S. government bond fund, then she is guilty of fraud, but if she did not herself realize that, then she is merely misinformed.

Correct Answer: A

Yes. Constance is guilty of fraud. She misled her client into thinking he couldn't lose money if he invested the money in a U.S. government bond fund. Although U.S. government bonds are referred to as risk-free, this just means they are considered free from default risk. The value of the bonds-and, therefore, the U.S. government bond funds-will change with changes in interest rates. As an investment adviser representative, Constance should know this. Regardless of whether or not she does, she is guilty of fraud simply by providing the misleading information. If she knew it and deliberately misled the client, she is guilty of criminal fraud.

QUESTION 7

Trevor is currently a registered agent in the state of Connecticut where he has been employed by Connect and Company, a broker-dealer that is registered in Connecticut and has subsidiary operations in Massachusetts, New Jersey, and New York. Trevor has moved to Massachusetts and is now associated with one of Connect's subsidiaries, a broker-dealer registered in the state. Trevor has applied to the Administrator of Massachusetts for registration as an agent.

Can Trevor execute purchases and sales for clients while his registration is still pending?

- A. No. Until he is informed by the Administrator of Massachusetts that his application has been accepted, Trevor may not affect any securities transactions in Massachusetts.
- B. Yes. Because Trevor is a registered agent in another state and is affiliated with a broker- dealer that is registered in the state of Massachusetts, he is not restricted from executing trades.
- C. Yes. Trevor can execute trades for new clients he solicits, but only for sixty days while his registration is pending.
- D. It depends. Trevor can execute some purchases and sales, but only for clients that he already had who may have recently relocated to Massachusetts and only for sixty days while his registration is pending.

Correct Answer: D

It depends. Because he is a registered agent in another state and the broker-dealer he is now affiliated with is registered in the state of Massachusetts, Trevor can execute purchases and sales, but only for existing clients while his registration with the Massachusetts Administrator is still pending and only for sixty days. This assumes, of course, Trevor has no violations that would restrict him from registering in Massachusetts.

QUESTION 8

The Administrator of a state can deny an application if

- A. the application is missing information.
- B. the registrant has been enjoined from engaging in activities involving securities in another state.
- C. the Administrator determines the applicant is not financially solvent.
- D. any of the above is true.

Correct Answer: D

The Administrator of a state can deny an application if the application is missing information, if the registrant has been enjoined from engaging in activities involving securities in another state, or if the Administrator determines the applicant is not financially solvent.

QUESTION 9

Under the NASAA Model Rules, which of the following must an investment adviser provide its clients with at least once a year?

- A. the total number of agency cross transactions completed for the client during the period
- B. the total amount of commissions or other compensation that the investment adviser received or expects to receive in connection with agency cross transactions performed for the client during the period
- C. the number of any complaints that each of its investment adviser representatives has received during the period
- D. both A and B

Correct Answer: D

Under NASAA Model Rules, an investment adviser must provide its clients with the total number of agency cross transactions completed for the client during the period as well as the total amount of any commissions or other compensation that the investment adviser received or expects to receive in connection with agency cross transactions performed for the client during the period.

QUESTION 10

Which of the following is not one of the criteria for a security to be eligible for registration by notification?

- A. The issuer must have preferred stockholders as well as common stockholders.
- B. The issuer must have a net worth of \$4 million, or its net income before tax for at least two of the
- C. The issuer must never have defaulted on any bond or long-term lease obligation.
- D. If the security to be issued is an equity interest in the firm, its offer price has to be at least \$5 a

Correct Answer: A

The issuer does not have to have both preferred stockholders and common shareholders in order to be eligible for registration by notification. If, however, the issuer does use preferred stock financing, it must not have missed a preferred stock dividend payment.

QUESTION 11

Which of the following trades is illegal?

- A. a short sale
- B. a margin transaction
- C. a market-not-held order
- D. the sale of a mutual fund if the purchaser hasn't received a prospectus

Correct Answer: D

It is illegal to sell a mutual fund if the purchaser hasn't received a prospectus. The purchaser must receive this no later than the date on which the trade confirmation is due. Short sales, margin transactions, and market-not-held orders are all legitimate.

QUESTION 12

Which of the following persons falls under the definition of "broker-dealer," as defined by the Uniform Securities Act (USA)?

- A. Marge is a loan officer at Treadwater Bank and Trust.
- B. Juan is employed by TrustUs Corporation to sell shares of the firm's stock to the firm's employees and receives a commission on the shares he sells.
- C. Michaela is employed by GetErDone broker-dealers and sells both exempt and non- exempt securities to GetErDone's clients.
- D. MyTrades is a sole proprietorship owned by Nathan Newmoney, who has established the firm solely to make trades on his own account, thereby avoiding the commissions he would have to pay a middleman.

Correct Answer: D

MyTrades falls under the definition of "broker-dealer," as defined by the Uniform Securities Act since Nathan Newmoney is engaged in trading on his own account. The USA defines a broker-dealer as any person that conducts securities transactions on its own account or for others. Both Juan and Michaela are "agents" under the USA definition, and agents are specifically excluded from the definition of a broker-dealer. Marge is also excluded from the definition since she is a loan officer at a bank.