



TESTGEEK EXAM PREP, LLC

YOUR PARTNER FOR SUCCESS

ADDRESSING THE NEEDS OF
INDIVIDUALS WHO NEED TO PASS THEIR LICENSING EXAMS THE FIRST
TIME

SERIES 7 CLASS NOTES

Please visit: testgeekexamprep.com

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FINRA RULES & REGS.

SALES LITERATURE/ADVERTISING

RETAIL

- Market letters
- Seminars
- Research reports
- Form letters (>25 persons)
- Reprints
- 3 year record retention

Prior principal approval

INSTITUTIONAL

Non-retail

post principal approval

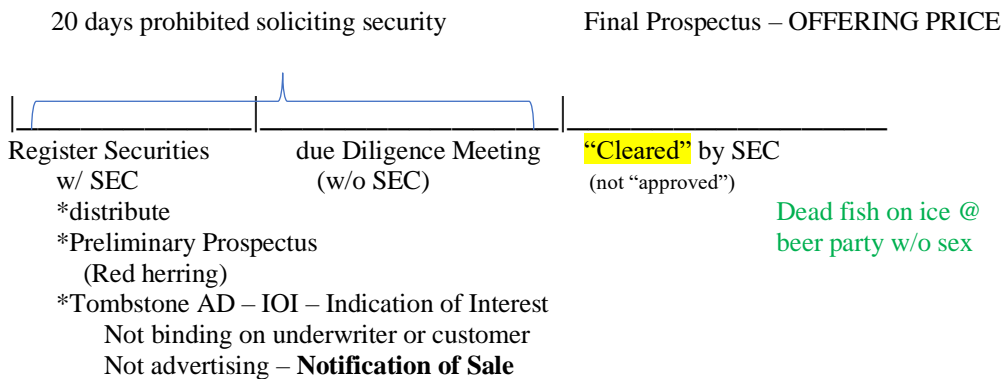
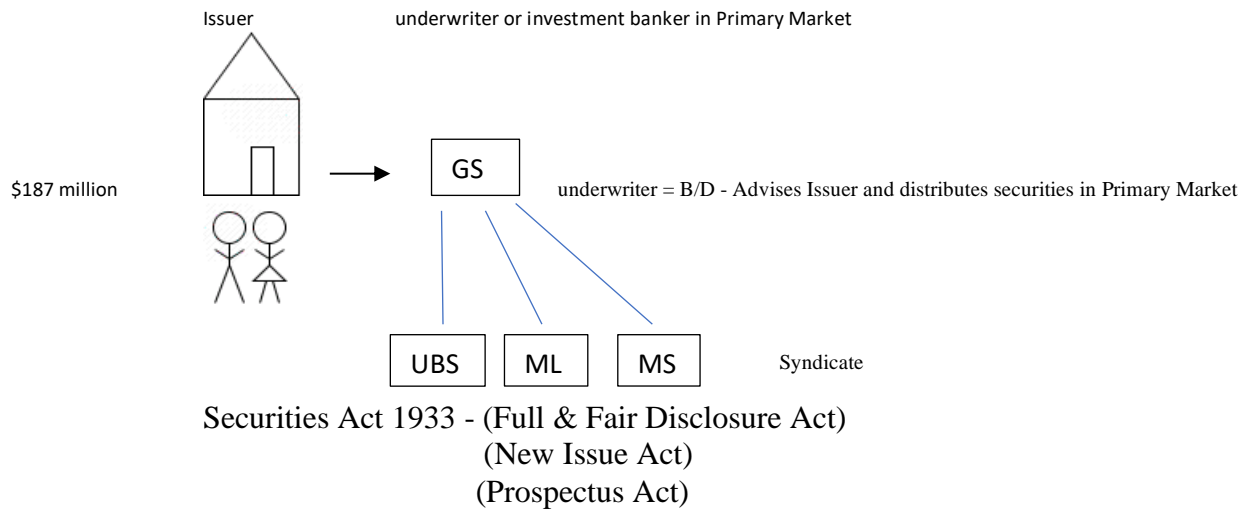
CORRESPONDENCE

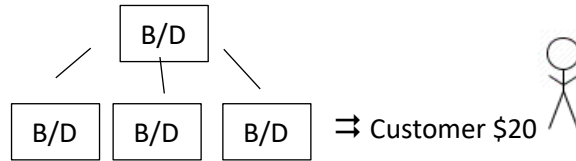
WRITTEN/ELECTRONIC

- personal communications
- email/I.M.
- form letters (25 or fewer w/in 30 days)

No prior approval required

Issuing (u/w) Securities





*** Best Efforts**

Underwriters take on no \$ liability for unsold shares

*** Firm Commitment**

(\$ liability) pay Mom & Pa \$187 million

Issuer pay spread

Get paid the SPREA

Shares sold \$20 IOP. \$1.00 spread. How much does issuer get paid? \$19.00

Offering Price – determined by:

Price to Earning (PE) of comparable companies

Indication of interest (IOI)

Difference between the price and proceeds \$ to the issuer = underwriting spread

Issuer pays spread (not customer)

Offering price is paid by the retail customer without commission.

Spread is negotiated before happens

.10	mgr fee – who wrote it	}	SPREAD
(.65)	concession – who sold share (always apply to underwriter)		
(.25)	underwriting fee – only paid for taking on <u>risk</u> (to syndicate members only)		

Types of accounts

Who signs new account form? Principal only (not customer!)

JTWROS (spouses) joint acct. holder receives assets from decedent (avoids probate).

JTIC (non-spouses) decedents assets got to estate

CORPORATE – resolution - cash accts., resolution & by-laws – margin accts.

PARTNERSHIP – resolution and agreement – cash or margin

DISCRETIONARY - authorization signed by customer AND approved by manager

NUMBERED – signature card on file

UGMA/UTMA – irrevocable gift, age of majority/ up to age 25

Suitability = based on stated investment objective

Which is the most important information to make suitable recommendation?

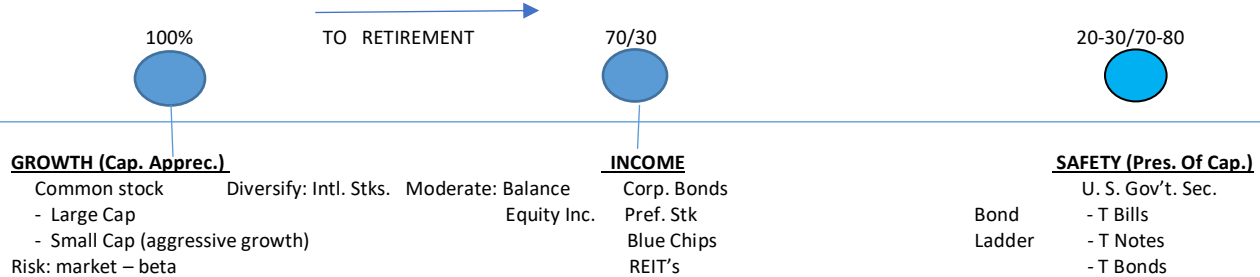
- A. age
- B. Risk
- C. Investment objective (keep your eye on the prize)
- D. Annual income

A 68-year-old woman is unemployed and receives social security. She has \$250k to invest and her primary concerns are moderate growth & income. As RR, which would you recommend?

- A. Diverse Portfolio of Stocks & Bonds
- B. Laddered bond portfolio
- C. A laddered treasury portfolio
- D. A blend of domestic & international stocks.

(growth = stocks, income = bond)

PORTFOLIO: Equity/Debt



Special Situations: Liquidity (down payment on home) - Money Market
Tax Advantages (High Tax Bracket) - Municipal Bonds
Long-Term college saving – Zero Coupon

If no stated objective is given, use portfolio allocation models:

Your clients, retired and in their late 60's, would like you to review their portfolio. As their R.R, you would most likely recommend which of the following

- A. 30% domestic equities, 30% bonds, 30% international equities, 10% cash
- B. 50% domestic equities, 50% international equities
- C. 25% domestic equities, 60% bonds, 15% cash
- D. 10% domestic equities, 40% bonds, 40% international equities, 10% cash

Retirement Plans

Qualified – pre-taxed contributions (cost basis=0)

Non-qualified – after-tax contributions (taxed > cost basis)

For those who turn 73 in 2023 through 2032, the starting age for RMDs is 73 and the first RMD must be taken no later than April 1 of the year following the year they turn 73.

IRA'S -

Traditional

Roth

403b –

KEOGH –

E.R.I.S.A. 1974

Margin Accounts (3-5 question/ 1-2 calculations)

Margin – may be hypothecated (used as collateral)

Paperwork-

Margin Agreement

Hypothecation Agreement – pledge securities as collateral

Consent to Loan Agreement – “optional” create short sales
(doesn't HAVE to be signed)

Credit Agreement – Interest Rate

Bank Employee opens a margin account. AOF would be required to be signed except:

- A. Margin Agreement
- B. Hypothecation
- C. Approval of/from bank manager
- D. Credit Agreement

Eligible Securities (Marginable, Able to be used as collateral)

- Listed (stocks & bond) on EXCHANGE
 - ETFs
 - NASDAQ – stock/bond included on
 - Other OTC – FRB approved list
 - IPO’s
 - Investment Company Shares (mutual funds)
- } only after 30 days
} from issue day

Are IPO’s and mutual funds *marginable*? (Used as collateral)

IPO & MF – new issue have prospectus

Ineligible Securities

- Options
 - Loan value of options = \$0
- Other OTC – not FRB (penny stock)

1000 Share XYZ @ \$40
 Reg T deposit = 50%
 Borrowing from
 Reg U - Banks (rehypothcation) –

Long Market Value	LMV - \$40,000	recalculate daily
Debt Balance (owes)	<u>DR - \$20,000</u>	
	Equity- \$20,000	

CMV=\$50	LMV- \$50,000	
	<u>DR- \$20,000</u>	
	Equity-\$30,000	
	<u>Loan value \$25,000</u>	loan value = 50% of market value
	Excess equity \$5000	(Reg. T value)
		(EE= Amount of customer’s equity above loan value)

“line of Credit” – amount allowed to borrow SMA – never goes away unless you use it.
 “Merrill Lynch” credit card

Buying Power = 2x	SMA = \$5000
Withdrawn as cash = 1x	

CMV = \$30	LMV- \$30,000		
	<u>DR- \$20,000</u>	} Eq.%=33%	FINRA minimum maintenance requirement = 25%
	Equity-\$10,000		
	<u>Loan value \$15,000</u>		
	Excess equity \$0		
	SMA= \$5000		

MV @ min maintenance = $\frac{DR}{.75}$ (At what value may market drop before we get to min. maint.?)

$\frac{20k}{.75} = \$26,666$ If long market value dropped to: \$26,666
 Dr = \$20,000
 Equity = \$6,666 } 25%

If customer sells stock, all monies used to reduce Dr. (SMA is increased by half of the sales proceeds): Sell \$2000 –

LMV - \$28,000
 DR - \$18,000
 EQ - \$10,000
 Loan Val. - \$14,000
 EE - 0
 SMA - \$6000

Your customer has the current values in their margin account:

LMV \$150k
 DR \$70 k
 EQ \$80k
 SMA \$5k

Customer sells \$18k then purchases \$21k of new stock. What is the required deposit?

- A. \$0
- B. \$5000
- C. \$10,000
- D. \$20,000

In a new margin account, customer buys 100 sh XYZ @ \$18. What is the required deposit?

- A. \$900
- B. \$1000
- C. \$1800
- D. \$2000

FINRA min deposit: \$2000/100%

Short Account



Sale proceeds: \$8000
Required Reg T deposit: \$4000 +
 CR= \$12,000
SMV= \$8000 value of stock
 Equity= \$4000

Value goes down to \$70
 Sale proceeds: \$8000
 + Reg T \$4000
 CR \$12000
 -SMV \$7000
 EQ \$5000 rises

Equity value increases
 with decrease in market value

Value does up to \$90

Sale proceeds: \$8000
 + Reg T \$4000
 CR \$12000
 -SMV \$9000
 EQ \$3000

33%

Short: FINRA minimum maintenance requirement 30%

In a new margin acct., customer sells short 100sh. @ \$18. What is required deposit?

- A. \$900
- B. \$1000
- C. \$1800
- D. \$2000

Short Acct. – min. deposit = \$2000

Combined Equity

10	LMV= \$10k	CR= \$12k	12
<u>6</u>	DR= \$6k	SMV = \$9k	<u>9</u>
4	SMA = \$2k	SMA = \$1k	3

Combine Equity: \$7k
 LMV + CR – SMV- DR= Equity

In a combined margin account, customer's LMV increase, while a same time SMV decreases.
 The combined EQ will:

- A. Increase (both positive events)
- B. Decrease
- C. Remains the same
- D. CBD (cannot be determined) never pick – never the right answer

Fundamental Analysis – financial statements

Balance Sheet -

$$\text{Assets} = \text{liabilities} + \text{owner's equity}$$

Current Assets

Fixed Assets

Other

Current liabilities

Long term liabilities

Common stock

Earnings

Declared- cash dividends come out of earnings. Earnings decrease, current liability increase

Pays - cash dividend = current assets ↓
current liabilities ↑

Income Statement

Sales

- cost

Gross Profits

- Income

- Tax

- Pref Div

Earnings = \$9 mil

outstanding shares 1mil = EPS \$9.00

PE (Price to earnings) $15 = \frac{\text{CMV } \$135}{\text{EPS } \$9.00}$ (S&P avg. value usually 15x above EPS)

EQUITY SECURITIES – ownership



Mom & Pop Flower Shop

1. Common stock

Authorize -# of shares *COULD* distribute

Issue- # share *HAS* distributed

(IPO – Initial Public Offering)

Outstanding – Public’s Hands

(Profit – Sometimes paid out in the form of dividends. Roughly, only 4% of companies regularly payout dividends – “Blue Chips”)

Treasury Stock- Company repurchases stock. Less stock available makes stock more valuable.

← privately owned companies stop here

Issue - Treasury Stock = Outstanding Stock

Which of the following debt instruments do not pay interest?

- A. Treasury Bills (doesn’t pay interest)
- B. Treasury Notes
- C. Treasury Bonds
- D. Treasury Stock (doesn’t pay interest but isn’t debt)

All of the following are backed by the full faith & credit of the gov’t except:

- A. Treasury Bills
- B. Treasury Notes
- C. Treasury Bonds
- D. Treasury Stock

Customer places an order to buy 100sh IBM @ \$90. B/D places the trade and executes the order.

Is the customer now the owner?

Ownership = Settlement Day

“Regular Way”

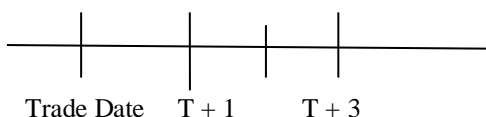
Settlement Day T+1= Transfer of Ownership

Payment & Ownership are two different things

Payment due T+3 FRB (Federal Reserve Bank) extension of credit

What regulation of FRB requires payment by T+3? Reg T

Ownership + Payment
T+1 T+3 (4 business days to pay)



Failure to pay by T+3:

- Request Extension (by Broker/Dealer)

OR

- Sell out (liquidate)

↪ 90 Days Freeze on extension of credit (privilege of credit)
Cleared fed funds required for purchases
(\$ upfront to buy)

EQUITY - OWNERSHIP

Rights of Shareholders

Voting Rights:

- Directors
- Recapitalization (issue add'l securities, stock splits)
- Mergers & Business reorganization

EXCEPT: Dividends, officers (VP, Director of Marketing, CEO)

officers are appointed by directors

Shareholders have the right to vote on all of the following, except:

- A. Directors
- B. Recapitalization
- C. Merger & Business Reorganization
- D. Officers

Right to receive dividend *IF* declared

Board announces a \$.75 cash dividend:

- Declaration date 12/7
- Record Date 1/7
- Payable date 2/7

What would be the last day to buy the stock and receive the dividend?



Ex-Dividend = Record Date

1/7 – “too late” = Same day as Record Date

Because it takes 1 days for ownership to change hands (settlement), investor would have to buy 1 business day prior to the record date in order to receive the dividend.

WARNING – BE CAREFUL OF HOLIDAYS – Jan. 1, July 4, Dec. 25

Board of Directors determines all of the following dates, except:

- A. Declaration Date (BOD declares A, C, D)
- B. Ex-Div. Date (FINRA/NYSE) T+2
- C. Record Date
- D. Payable Date

Dividends

- Cash (taxed as ordinary income – 1040)
- Stock (Capital Gain/Loss at time of sale)
– using adjustable cost basis

Investor owns 100sh of XYZ at \$50

Company announces a 10% stock dividend. How many additional shares will they receive?

- A. 5
- B. 10
- C. 100
- D. 110

100 share @ \$50

10% stock dividend

Add'l shares = 10

100 shares @ \$50

100% stock div. (2:1 split)

200 shares @ \$25

Sell @ \$30

Profit/capital gain

100% stock dividend (2:1 split)

25% stock dividend (5:4 split - 1 add'l share for every 4)

50% stock dividend (3:2 split)

Reverse Split (1:5)

Increase share price

Generally occurs when stock falls below \$1 – not a good thing – and is in danger of being delisted/kicked off exchange.

Selling Dividend (recommendation)

XYZ is trading at \$45/sh. XYZ announces a \$.75 cash dividend. The day before the ex-date, a R.R. recommends to his customers they buy the stock the day before the ex-date before it's too late. THIS IS PROHIBITED! YOU'LL LOSE YOUR LICENSE.

The stock price is adjusted by the amount of the dividend on the ex-date therefore there is no benefit to buying prior to the ex-date.

Under FINRA rules, which is prohibited practice? Recommendations to customers purchasing prior to the Ex-Div date (Selling the Dividend).

Property Dividend

- receiving product
- Shares of stock from another company (subsidiary * Spin off)

XYZ Inc pays to its existing shareholders, shares of stock in ABC Inc. This is known as:

- A. Arbitrage**
- B. Spin off**
- C. Illegal**
- D. Day Trading**

Pre-Emptive Rights

CMV - \$10

1,000,000 shares outstanding

Customer owns 50,000 shares (5%)

Company issues additional: 1,000,000 shares – The company must offer shares to existing shareholders first

Rights offering – 5% = 50,000 @ \$8(Below CMV=value)

↳ Security

- trade
subscription price
- exercise
- expire (30-45 days)

value:

CMV-

rights + 1

Has value b/c it's offered @ less than Market Value- VERY short term

****Only 10 questions will use calculator – math is not ambiguous – words are!****

2. Warrants –

right to buy stock @ specific price/time

Long-term (3-7 years)

Usually offered @ \$ above CMV (Current Market Value) that's why it's long term

Warrants are often issues through ESOP's – Employee Stock Option Plans or sometimes attached to new bond or stock offerings as enticements to make the new issues more marketable to investors.

When issued, warrants offer:

- A. intrinsic value
- B. time value
- C. both intrinsic value and time value
- D. neither intrinsic value nor time value

Rights – short term, below CMV

Warrants – long term, above CMV

3. Preferred Stock

Objective: Income

Acts like a bond – pays fixed income

Pays fixed, stated dividend.

Risk: Interest Rate

Interest Rates ↑

Market price of Preferred stock ↓ - less attractive



COMPARISON OF COMMON STOCK AND PREFERRED STOCK

Common Stock

Objective: Growth/Capital Appreciation

Income (blue chip)

Risk: (Systematic) Market Risk
(Unsystematic) Business Risk

Beta

1.0 = overall market

Volatility of the market – your stock in the market

Systematic Risk

S& P 500	↑	10%
Stock	↑	12%
Beta		1.2 = 120%

What does a Beta of 1.0 mean?

Equals the overall market (from which all other stocks compared).

MSFT Beta – was 1.001

Now 1.3 > .3 **ALPHA** – measured business risk.

- CEO resigns

- new product

Difference between historical & current Beta

Which of the following effect Alpha?

- A. Market index goes up
- B. CEO Resigns
- C. Market goes down
- D. Interest rates

Preferred Stock -

XYZ, Inc 6%
Par value = \$100
Income = \$6

Fixed doesn't mean guaranteed.

Types -

- Straight Preferred (IBM)
- Cumulative (Airline stock – all over the place)
 - ARREARS - Make up back dividends
- Participating – Additional Dividends (if declared)
 - Young companies (just starting out/growth) ... additional dividends above & beyond stated rate
- Convertible – convert to common stock
 - Fixed income produce income until market rises and can provide growth.

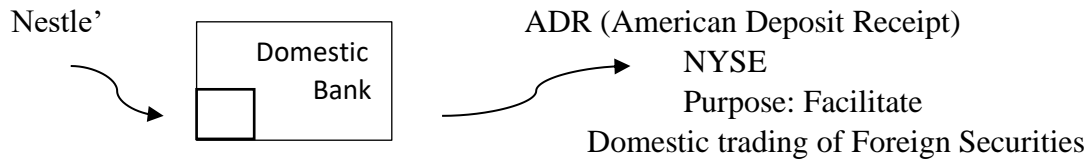
Which of the following would be least interest rate sensitive?

- A. Straight Preferred
- B. Cumulative Preferred
- C. Participating Preferred

D. Convertible Preferred

4. ADR's

– Diversify with International investment

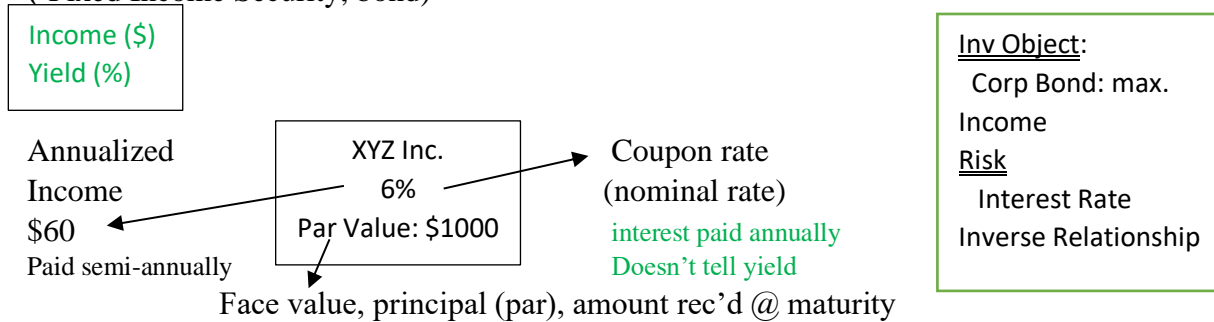


We could lose value simply
 Between currency exchanges rate

RISK:
 Currency Risk

DEBT SECURITIES – Fixed Income - Creditors loaning company money

(Fixed Income Security, bond)



Interest rates affect market price of the bond.

Buy a bond @ discount or premium, how does it **affect income**? It doesn't, **income is** fixed. It affects return on investment-yield

$$\text{Annual Income/CMY} = \text{current yield}$$

JQP owns 10m XYZ Inc 6% '25 purchased @ 92. Current yield?

$$\frac{60}{920} = 6.5\%$$

Common stock

Could have a current yield if they pay dividends.

Current income = dividends or interest

XYZ Inc reports \$3 in earnings and pays a \$0.25 quarterly dividend. If it trades @ \$20/sh, what is current yield?

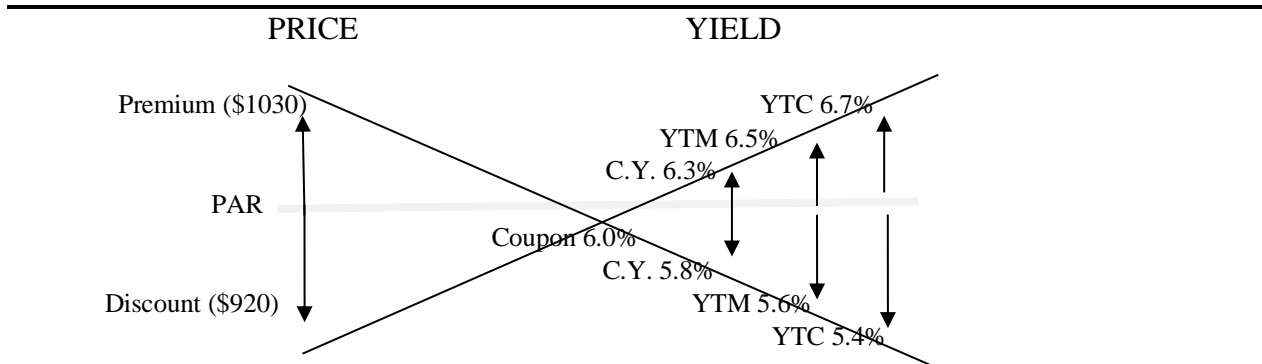
$$\frac{1}{20} = 5\%$$

XYZ, Inc. was trading @ \$50, it's now @ \$80.

If the current yield is 5%, what is quarterly dividend? $\$1.00 \quad 4/80=5\%$

When adding/subtracting profit/loss when held to maturity = Yield to Maturity

When adding/subtracting profit/loss when called away = Yield to Call



B/D's required to disclose –“Yield to Worst” between YTM & YTC. Lowest possible yield an investor could receive.

Call Provisions

Issuer (of Bond) – Refunding (refinancing)

Highest interest rate and lowest cost is most likely to be refunded

9% nominal maturing 2020, callable @ par (Time is irrelevant for the test)

(rate)

(cost)

Which is most likely to be refunded?

- A. 9% nominal, maturity 2020, call @ par
- B. 9% nominal, maturity 2021, call @ 101 ½
- C. 7.5% nominal, maturity 2020, call @ par
- D. 7.5% nominal, maturity 2021, call @ 101 ½

Investor

(calls not good) –

1. Call Risk is reinvesting PRINCIPAL @ lower interest rate
2. YTC

Reinvestment Risk is
Reinvestment of interest
Payment @ lower rate
EXCEPT: Zero Coupons

Forms of Bonds

Bearer Bonds (haven't been issued in 20 years)

Fully Register

Book_Entry (Journal)– (all data – no physical certificate)

Majority – US Gov't 100% this way

1. Term - Corporate = Dollar Bond (easily converted to dollars)

Quoted % of par

\$2,000,000 1/1/10 94 = \$940

\$2,000,000 1/1/20 103 ½ = \$1035

Some muni's

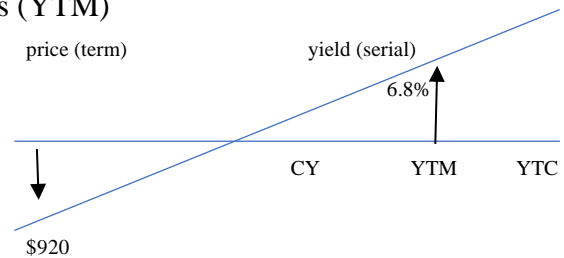
2. Serial = Only muni's are serial

1/1/10 \$2,000,000

Quoted: 6.80% Basis (YTM)

Matures over a series of years

- '15
- '16
- '17
- '18
- '19
- '20



Interest – Zero Coupon – (used to pay for college tuition)

Buy @ deep discount – hold to maturity to make money

Typically ½ face value – long term investment

“Difference” between discount & face value is the interest you earn

FV \$1000

Buy \$500

Taxed - as ordinary income

- annually – 1099

– Straight Line Accretion

(Opposite of amortization)

Risk: **Inflation** (Fixed Return)

Most interest rate sensitive

All bonds have reinvestment risk except: Zero Coupon

Have most interest rate sensitivity: Zero Coupon

Suitability – Saving for college tuition

Who is most suitable for a long-term zero coupons?

A. 67 yearold cardiologist, \$250k

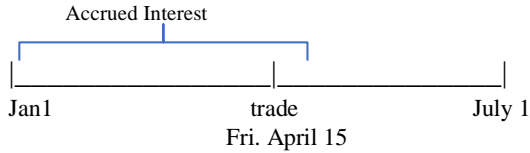
B. 36 yr old, Single Women, 2 young kids

C. 75 yr. old retiree

D. 28 yr. old, trying to create down payment on home in 10 years

Accrued Interest

10 m XYZ 8s '25 101 ½ 7.93% J.J. bond
(\$10,000) (8%) (2025) (\$1015) (Current yield)



Buyer of Bond owes interest to seller – added to price

Corp/Muni

Accrues

-30/360

- up to day before settlement (T+1)

Gov't Securities

- Actual Days

- up to day before settlement (T+1)

Test – Feb always has 28 days

Settlement doesn't include weekends. Accrued interest does!

Interest on Gov't Securities will accrue up to and including, which of the following:

- A. First Date
- B. Settlement Date
- C. Trade Date
- D. Independence Date

Which of the following bonds trade flat:

- A. Bond trading @ par
- B. Bond not trading
- C. Bond trades without accrued interest
- D. Suspended trading

Flat - zero coupon/
- bond in default

Flat Bond – refers to interest not price

All of the following bonds trade “and interest” except:

- A. XYZ Bond
- B. US trade Bond
- C. Zero
- D. Muni

(w/accrued interest)

look for bond trading flat

RISKS

Interest Rate

Long Term Bonds vs Short Term

Most volatile – Zero Coupon (bc longest duration)

Equal Maturity

Most Volatile – Price furthest from par
 Doesn't matter if its premium or discount

Credit Risk (default) test calls it **CREDIT RISK**

What would a high yield bond's greatest risk be? **CREDIT RISK**

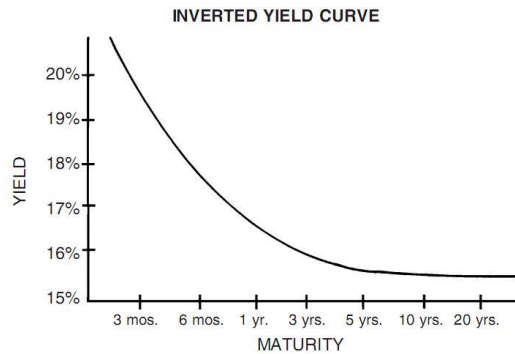
Moody's	S&P	
Aaa	AAA	Investment Grade – “Bank”
:	:	
:	:	
Baa	BBB	
<hr/>		
Ba	BB	
:	:	Non-Investment Grade – “Junk Bonds”
D	D	“high yield”

Test – If rating starts with B
 – needs 3 letters to be investment grade

According to officer of Comptroller of Currency, which of the following is considered Bank Grade?

- A. Ba3
- B. BB+
- C. BBB-
- D. B++

Yield Curves



Rapid DECLINE of interest rate
 Interest rates fall
 Temporary situation
 Precursor to recession

Which is most senior in the liquidation priority?

- A. Subordinate Debenture
- B. Preferred Equity Holder
- C. 2nd mortgage bond
- D. Common stock

Liquidation Priority (Bankruptcy)

1. Wages – pay the employees
2. IRS – taxes
3. Creditors
 - Secured
 - Unsecured/General
4. Equity
 - Preferred
 - Common

Eurodollar CD

Euro = “non US” - to do with Europe or Euros
 Attract US investors, all in American \$ -- interest & principal in US \$

Eurodollar Bond

Bond issued by non-US -- principal & interest in U.S. \$

Euro Bonds

Issued by anyone – Paid in foreign currency (currency risk to U.S. investors)

Which of the following represent currency risk to US investors?

- I. Eurodollar CD
- II. Eurobond Kingdom of Norway – Foreign Tax credit on US tax form 1099
- III. Eurodollar bond
- IV. A.D.R.

Kingdom of Norway a Bond subtracts Norwegian taxes from U.S. investor’s interest payments. Investor is eligible for a Foreign Tax credit on US tax form.

Which would be affected by a down grade in a Moody’s rating?

- A. ETF Stock
- B. ELN Bond
- C. ABC
- D. BFD

ELN- Equity Linked Notes = Debt – (NOTE) Instrument

Convertible Bonds

(CMV is not fixed) CMV = 110

XYZ Inc. 6% Convertible Price @ \$25 Par Value: \$1000

\$25	\$25
\$25	\$25
\$25	\$25

Parity= equal value
 Bond ↑; stock ↑

Bond ↓; stock ↓

: :

Conversion ratio – 40 shares

If bond price appreciates to 110 (% of bond par +10%) what is parity price of the stock?
stock $25 \times 10\% = \$27.50$

Parity Price = % increase of one security - apply the same percentage to the other

JQP owns XYZ Inc 8% convertible debenture with conversion \$50. The market declines to 90. The stock is currently trading 2 points below parity. What is the current price of the stock?

Convertible $50 \downarrow 10\% = 45 - 2 = 43$

A. \$50

B. \$48

100 } -10%
90 }

C. \$45

D. \$43

Forced Conversion – Company announces a call on a convertible bond to force investors to convert to the stock.

JQP owns a XYZ, INC 8% convertible bond with a conversion price of \$50. B.O.D.'s announce a call in 30 days at 103. CMV of the bond is 101. If the stock is trading at \$55/share, which should a R.R. recommend?

A. Sell the bond at the current price

B. Convert

C. Tender the bond at the call

D. Sell short against the box

Bond price is up only 1%, call price is up 3%, stock price is up 10%. Stock is more valuable.

TEST TIP – If a convertible bond is called – ALWAYS PICK CONVERT!

US Gov't Securities

Length of term

short

intermediate

long term

T Bill

T Notes

T Bonds

shortest - 1 yr or less

2-10 years

Greater than 10 years

Bill

Knows

Bonds

T Bill – 1 year or less
 1, 3, 6, 12 months
 4, 13, 26, 52 weeks
 (double on the back end)

All are T-Bill maturities except:
 A. 4 week
 B. 8 week
 C. 26 week
 D. 52 week

Notes & Bonds – similar to Corps. & Muni's
 \$1000 Par, semi-annual interest, quoted as % of par
 \$1000 JJ 94.08 → 94 8/32

What is the \$ difference between:

Bid Ask
 96.10 (10/32) 96.25 (25/32)

Bond Quotes with “.” Separates whole # from fraction 1/32

Bid Ask
 95.10 (10/32) 95.25 (25/32)

\$

15/32

.46875

\$4.68

Turn decimal into fraction, move decimal 1 place.

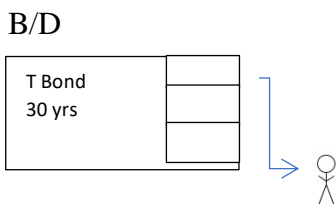
T STRIPSs backed by US Gov't
 Striped from Interest & Principal

T receipts backed by B/D, banks

Zero's

difference is who issued them/
 Who backed them

Suitability:
 no income
 Fixed income
 Yrs future/ college tuition



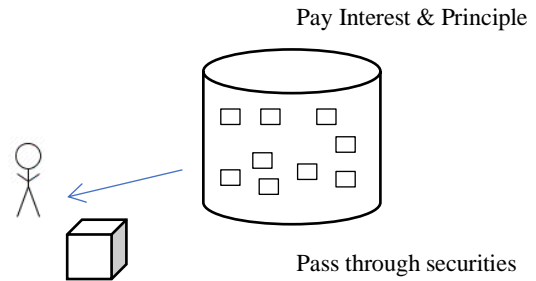
Risk:

Gov't. Agencies – (not government issued)

“Uncle Sam’s relatives”

- GNMA backed fully by US Gov't
- FNMA
- FHLMC mortgage backed securities

- **Interest Fully taxable**



GNMA

Backed by full faith US Gov't (still fully taxable)
Interest paid monthly

CMO's - Derivatives

What collateralizes a CMO?

- A. Mortgages
- B. Real Properties
- C. Equity Securities
- D. Asset Back Securities

Pay Interest Monthly

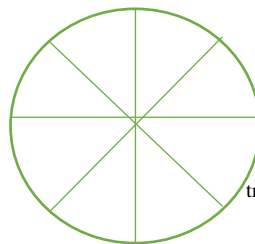
TAC – long term tranche

Most risk
Highest yield

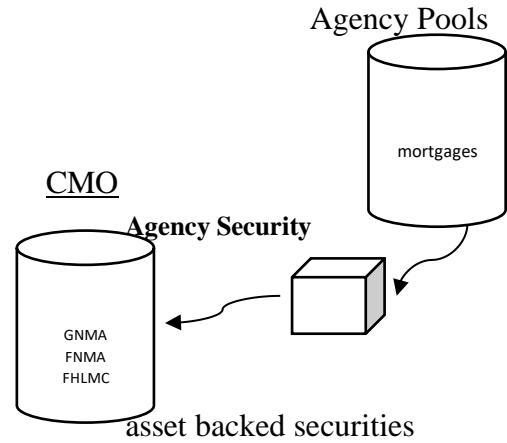
PAC – shortest term

Least risk

Prepayment & Extension Risk



tranches – divided by when we calculate mortgage to be estimated to be paid



Private label CMOs vs Agency CMOs

- | | |
|--------------|---------------|
| B/D | GNMA |
| Banks | FNMA |
| | FHLMC |
| lower rating | higher rating |

higher risk

lower risk

Asset backed Securities

- Private label could be - mortgages
- Car loans
- Credit loans

Municipal Securities

Interest – Muni’s - federally Tax Exempt (U.S. Govt’s are state Tax Exempt)
 - State exempt (for residence)

Suitability – Investors in the highest tax brackets

1. GENERAL OBLIGATION (GO) safer than revenue

- Back from taxes
- State – income, sales, driver’s fees
- Other (county) – Ad Valorem (Property)

Requires Voter Approval

Debt Limits

Other GO

Double Barrel (hybrid)

Revenue then taxes

City or County

2. REVENUE

User fees – tolls, concession

Leases

Self-supporting

No voter approval

bit more risk

Trust Indenture – included to make bond more marketable (have more risk)

(Bond Contract) – Protective Covenants

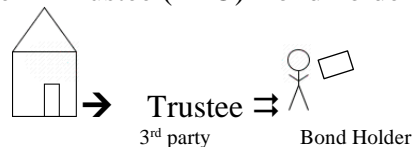
TRUST INDENTURE ACT ‘39

All Corp Bonds > \$50 mill (Prospectus for Bond)

Not required for munis

Non-exempt

Contract: Issuer + Trustee (FBO) Bond holders



Trustee – 3rd party acting for another.

Covenants (promises & obligations)

Rate – User fee

- Maintenance
- Insurance
- Principal & interest

Add'l Bonds – yes w/ caveat:

Open ended – add'l bonds test – is the revenue sufficient to cover both bonds
Close ended – subordinate - “junior” in claim
2nd in payment to 1st bond (pays 1st bond, then 2nd)

Call Provisions

Whole
Partial (call any part of serial offers, selected at random)
Catastrophes – condemn (legally)

Flow of Funds

<u>Gross Pledge</u>	<u>Net Revenue Pledge</u>
1. Debt service (Prin. & Int.)	1. Operating Expenses
2. Operating Expenses	2. Debt Services

What is the priority of payment under gross rev pledge?

- I. Operating Expenses
- II. Debt Service
- III. Sinking Fund (left over reserve account)

Other Revenue

IDR's (Industrial Development Revenue)

“Private Purpose” Lease-backed/Corp

Interest maybe taxable – AMT (Alternative Minimum Tax)

Which one is least suitable to a client subject to AMT?

- A. Private purpose
- B. General Obligation
- C. US Bond
- D. XYZ Debenture

Special Tax – alcohol, tobacco, excise (gas)

Moral Obligation – no voter approval

From state legislature, if revenue doesn't cover, then state pays.

STATE Legislature's moral obligation

Which is required to issue a moral obligation bond?

- A. 2/3 voter approval
- B. Majority
- C. Anti-tax advocate approval
- D. No voter approval

Madison, Wisc. issues a bond to build a new bridge and charges a toll to pay the interest and principal. If the tolls are insufficient, the city of Madison will back the bond with its full faith and credit. This is which type of bond?

- A. Limited Tax bond
- B. Double barrel bond
- C. Moral obligation bond
- D. Special Assessment bond

Moral obligation = state legislature

Double barrel = city, county

BAB's – Building America Bonds (no longer issued)

Issued: Muni's (state, city, county) INTEREST – taxable (Federal Tax Credit)

Backed by US Gov't

ARS – Auction Rate Security - alternative to money market

Money Market most known for liquidity

Lost money these days in real return on MM

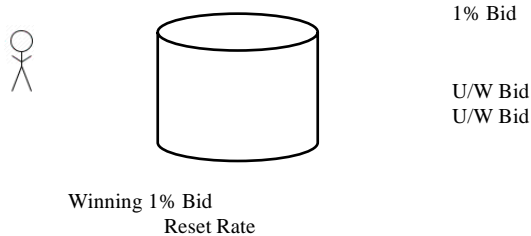
Auction Rate Securities

vs Money Market

RISK = Failed Auction

No one showed up to bid/no demand - worthless

Dutch Auction



Highest bid wins & becomes new reset rate

3. Muni Notes

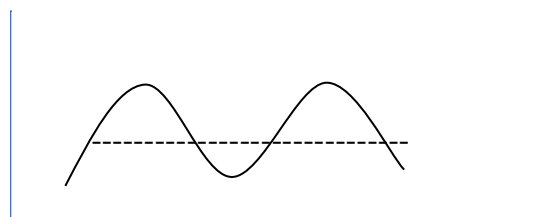
Short term

TAN, BAN, RAN

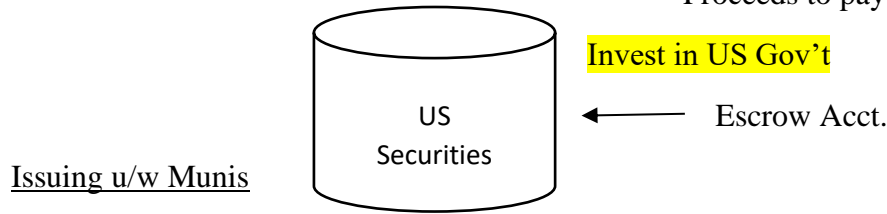
Creates bridge (loan)

Purpose: Cash flow

Interest at Maturity



3% issue new bond today (who knows interest rate tomorrow)
 Proceeds to pay



King Co
 (Exempt from Act '33)

Syndicate orders

Order Priority (Pro Golfers Don't Miss)

- Pre-Sale
- Group
- Designated
- Member

Bond Counsel/ Bond Attorney

Underwriters:

Official Statement (OS) no rules to require them
 Like prospectus (used to help sell bonds/marketing)
 Prepared by underwriter with help from Issuer
 Approved by muni principal

Rules to use & retention – 3 yrs

Bond Attorney's:

Legal Opinion

attest to:

1. Authority of Issuer
2. IRS
(interest federally tax exempt)
3. '33 exempt
Don't need to be registered SEC
No prospectus

SERIES 7 Hall of Fame Question:

Qualified or **UNQUALIFIED**

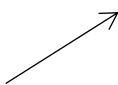
Find nothing wrong – no doubt
 Comes without contingencies

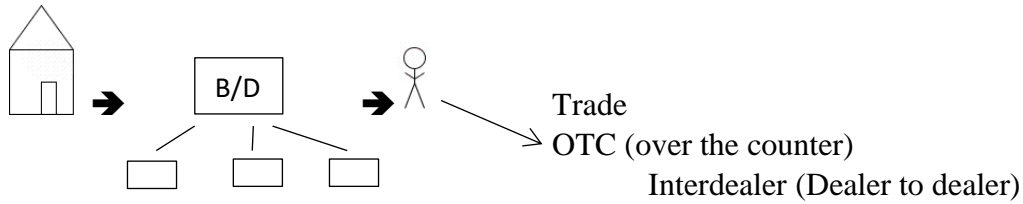
Where would you find info on a new muni bond rating?

- A. Legal opinion
- B. Prospectus
- C. Official Statement
- D. Coverage Ratio

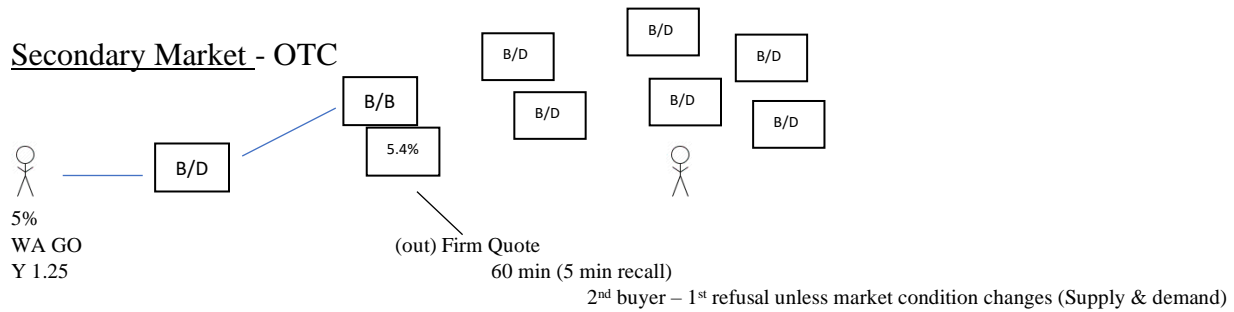
Secondary Trading

Secondary Trade (no supply & demand)
 Exchange (NYSE) not listed/doesn't trade





Secondary Market - OTC

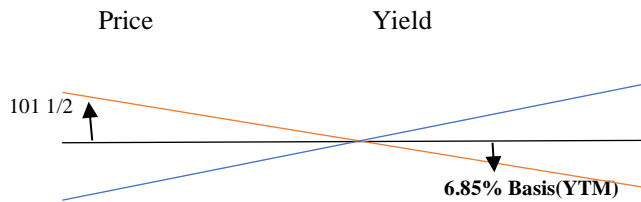


Broker/Dealer - dealer buys & sells from inventory
 Brokers/Broker – broker doesn't own any inventory
 Supplies list of buyers & sellers to those subscribed

Muni dealer purchases 7% muni @ par reoffer to public fair quote:

- I. 6.85% less 1/2
- II. 4.70% net
- III. 101 1/2 + 1/2 point
- IV. 108

- A. I & III
- B. I & IV
- C. II & III
- D. II & IV



According to the MSRB, dealer quotes are required to be:

- A. Best Available
- B. Lowest possible
- C. Average of at least 3 dealers
- D. Fair & Reasonable

Taxation of Muni's

1. U.S. Territories - Puerto Rico, Guam, Virgin Isl.

Interest – Fed, State, local tax exempt – for all US Residents

Capital Gains

Buys @ 110 (% of par), held to maturity, receive 100 (% of par)

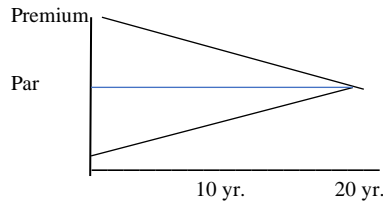
- A. \$10 loss
- B. \$100 loss
- C. \$10 gain
- D. \$0

Buys @ 110 (% of par), matures in 20 years, sell after 10 years @ 106 (% of par).

- A. \$4 loss
- B. \$40 loss
- C. \$10 gain
- D. \$0

Investor buys muni @ 110 (% of par), sells after 10 yrs @ 106(% of par). What method is used to determine capital gains?

- A. Constant Interest Amortization
- B. Straight Line Amortization
- C. Constant Interest Accretion
- D. Straight Line Accretion



Straight Line Amortization – to kill off the premium

Customer purchases a muni @ 108(% of par) that matures in 20 years and sells after 10 years @ 102(% of par). For tax purposes, what is the gain or loss?

- A. \$10 gain
- B. \$20 loss
- C. \$60 loss
- D. \$0 gain or loss

½ way to maturity adjust ½ premium

1. PREMIUM BOND – Held to MATURITY = 0

SOLD PRIOR TO MATURITY – STRAIGHT LINE AMORTIZATION

2. DISCOUNT BOND (2nd market)

cost vs. sale (No adjustment)

3. ORIGINAL ISSUE DISCOUNT (O.I.D.)
- held to maturity – 0 gain/loss
 - sold prior to mat. - Straight Line Accretion (taxable Cap. Gain/Loss)

Remember:

<p>\$1000 \$500</p>	<p>Zero Coupon Taxed Ord. income annually –Straight Line Accretion (taxable interest)</p>
-------------------------	---

Tax Equivalent Yield

A customer indicates they would like highest after- tax income possible. As the RR, which would you inquire?

- A. What state do you live in?
- B. Who’s your mama, Chris?
- C. Do you not like the gov’t?
- D. What is your tax bracket?

Muni suitability – highest tax bracket
#1 priority

A customer currently owns 5% muni and would like highest after- tax income possible. They are in the 34% tax bracket. What yield would they have (on corp bond) to receive to equal the tax-free muni?

<p><u>Muni yield</u> = equivalent taxable (corp) yield</p> <p>100%-TB</p>	<p>$\frac{5\%}{.66} = 7.5\%$</p>
---	---

Corp Yield (100-TB) = Tax Free Yield

MSRB Rules – make but can’t enforce

All of the following may enforce MRSB rules, except

- A. MSRB
- B. FINRA
- C. SEC
- D. Office of Comptroller of Currency (OCC)

whoever oversees you!

Confirmation (BOND)

- Interest payment dates
- Maturity Date
- Option if any (call dates)
- Dated Date – new muni’s
 - date when interest first accrues

CUSIP (ID & Tracking)
Capacity: Agency/Principal
“Yield to Worst”
Conflicts of interest - Control

Suitability

Customer refuses to disclose financial information
MSRB = no recommendations!

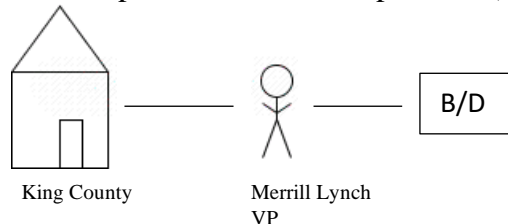
Unsuitable trade

UNSOLICITED (allowable - but mark unsolicited)

All of the following must be considered before recommending to customer except:

- A. Muni Security Rates
- B. Tax Status
- C. State of Residence
- D. Muni Coverage Ratio (Doesn't have to do with suitability)

Control Relationship – someone who represents (has authority over) issuer & B/D



B/D Must Disclose on confirm

Rule G37 MFP – Municipal Financial Professional
(Muni underwriting department)

Max political contribution = \$250

Part owner of joint checking account = 100% contribution

Firm invites municipal officials to a golf tournament. Firms give \$69 driver to each official. According to the MSRB, which is allowed?

- A. Tourney only
- B. \$69 driver only
- C. Both allowed
- D. Neither.

Financial Advisor

u/w – prohibited (conflict of interest)

acting as municipalities financial advisor

Information Sources -Bond Buyer (daily)

New issue Muni's

G.O. Index

Test: Revenue Bond Market – REVDEX

25 Revenue bonds/ 30 years maturity

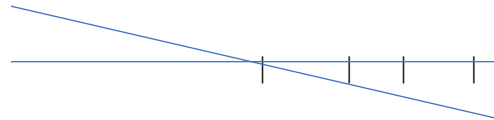
30 day Visible Supply – all new munis to be issued within the next 30 days

Placement = $\frac{\$ \text{ amount sold}}{\$ \text{ amount offered}}$ (weekly)
Ratio

Municipal Practice Questions -

Which must be disclosed YTC on customer confirm?

- A. 6 ½% nominal, 7 % basis 2014
- B. 6 ½% nominal, 7 % basis 2010
- C. 5 ½% nominal, 5 % basis 2010
- D. 5 ½% nominal, @ par 2014



All of the following muni's are quoted on yield (basis) except:

- A. Secured
- B. Serial
- C. Term
- D. Tax anticipation notes

MSRB are authorized to adopt rules on all of the following except:

- A. Sale of new issue
- B. Form & content of new quotes
- C. Regulate muni advertising
- D. Info to be provided by muni issuers

oversees B/D Reps

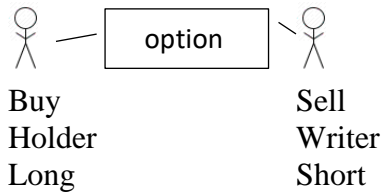
Not Specifically Muni Issuers

OPTIONS –

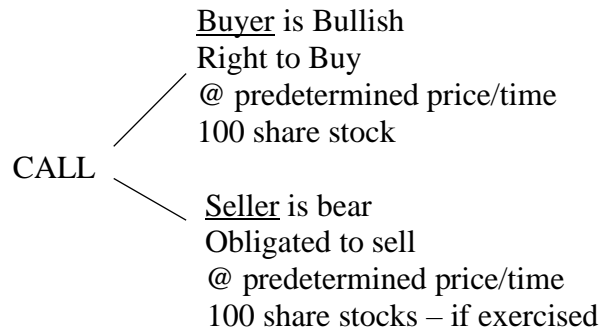
Goals: Recognize Strategies & Solve Strategies

Is the market price of option fixed? No

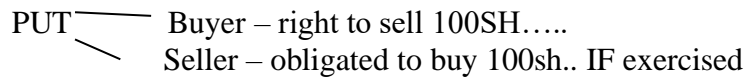
Market may move up or down more than 5% in one year – 1-2x yr on average



Lease in real estate is a call



Exercising options doesn't serve purpose 92% of the time.
Options are for leverage



Your customer buys 1 XYZ June 40 call @ 2 when XYZ is trading @ \$36/sh.

Premium = time value + intrinsic value
 more time = more valuable
 more time = ↑ premium

At expiration, XYZ is now trading @ \$46/sh.

Intrinsic value = “in the money” (reflected in premium \$ for \$)
 Calls: intrinsic value
 Stock price is greater than strike price
 Stock Price > Strike price (Regardless of side you are on)

What will the investor do?

- Exercise
- Expire
- Trade (closes the position)

Your customer closes their position. What is their profit or loss?

(Buy) (Sell)
<u>Out</u> <u>In</u>
-\$200
_____ + \$600
_____ \$ 400

Bull **Investor buys 1 IBM July 90 call @ 3, when IBM is trading @ \$85. IBM is now @ \$98. Investor closes their position. What is profit/loss?**

	<u>OUT</u>		<u>IN</u>
	-300		
	_____		+800
			+ 500
Max gain – unlimited			
Max loss – limited (premium) \$300			
BE – SP + Premium			

Bear **Your customer sells 1 IBM Jul 90 call @ 3, when IBM is trading @ \$85. At expiration, IBM is now \$98. Customer closes their position. What is profit/loss?**

	<u>OUT</u>		<u>IN</u>
			+ 300
			-800
			-500
Max gain – limited to premium			
Max loss – unlimited			
Sell stock you don't own is "uncovered" or "naked" call			

Bear **Investor buys 1 XYZ Aug 30 put @ 2, when stock is trading @ \$33. Intrinsic value: CMV < strike price. Put more valuable when stock goes down.**

Bear **At expiration, XYZ is now trading @ \$21. Investor closes the position. What is profit/loss?**

	<u>OUT</u>		<u>IN</u>
	-200		
	_____		+900
			+700
Max Gain = SP – premium (00)			
Max Loss = premium (limited)			
BE = SP – premium			
* Buying options - most you can lose is the premium.			

Bull **Customer sells 1 XYZ Aug 30 put @ 2, trading at \$33. At expiration, XYZ is now trading @ \$21, close position. What is profit/loss?**

	<u>OUT</u>		<u>IN</u>
			+200
			-900
			-700
Max loss = SP-premium			
Max gain = premium			
BE = SP – premium/share			

MOST COMMON ON TEST:

HEDGES – investing in stock and using an option to either:

1. Protect (guard against risk, hedge)

-or-

2. Profit

		<u>Out</u>		<u>In</u>
Bull	Chester buys 100 shares IBM @ \$90.	-200		
	Buy 1 IBM Jul 90 put @ 2.	-9000		
		-9200		

BE = T = 92

	<u>Out</u>		<u>In</u>
Lester buys 100 share IBM @ \$90			+300
Sells IBM July 95 call @3	-9000		
BE = 87	-8700		

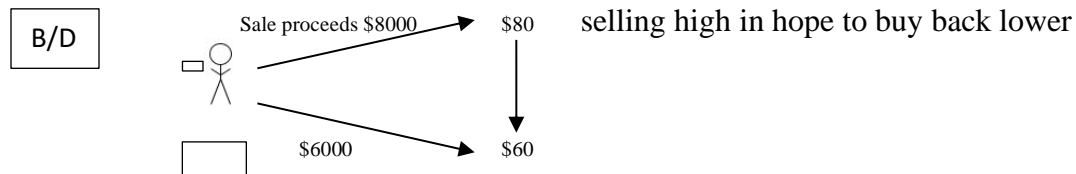
“Covered call” he owns the stock.

Sally is long 100 shares XYZ @ \$50. She fears a near term correction but overall she remains bullish. As her RR, which would you recommend to profit from this situation:

- A. Buy \$50 call
- B. Buy \$50 put
- C. Sell \$55 call
- D. Sell \$55 put

always - buy for protection
- sell for profit

Sell Short (stock) selling stock you don't own



UNLIMITED RISK/LOSS

Uncovered call
Sells short stock

<u>OUT</u>		<u>IN</u>
-200		+ 8000
		+ 7800

Investor sells short 100 XYZ @ \$80, buy 1 XYZ Jun 80 call @ 2.

Stock goes to \$347 exercise call – only costs \$200 premium.

* Primary objective: stock floors out.

Sell short 100 shares XYZ @ \$80 & simultaneously writes 1 XYZ \$75 put @ 3. BE? 83

BUY | SELL

$$\begin{array}{r} | + 8000 \\ | + 300 \\ \hline | + 8300 \end{array}$$

The stock declines to \$72 & put is exercised. For tax purposes, what is gain or loss?

- | | |
|--------------------|-----------------|
| A. \$1100 gain | <u>Out In</u> |
| B. \$800 gain | + 8300 |
| C. \$300 loss | <u>-7500</u> |
| D. Unlimited loss. | + 800 |

Buy 300 shares XYZ @ \$50, sell 3 XYZ 55 calls @ 3. What's BE?

Multiple lots & multiple contracts have NO effect on BE.

Solve as if they were 1.

Unless net profit or loss.

	<u>Out In</u>
CMV = 58	-5000 +5500
Call exercised	<u> </u> +300
Profit/loss	+800 (x3) =2400

Buy 300 shares XYZ @ \$50, Sell 5 XYZ 55 call @ 3. What is max loss?

TEST: Ratio Write 2 uncovered calls = unlimited loss

Short calls to long stock

STRADDLES (1-3 questions on test)

Buying both types (call/put)	<u>out/in</u>
Or	-400
Selling both types	<u>-200</u>
	-600

↑ Long 1 XYZ Sept 40 call @ 4 - BE is \$46

↓ Long 1 XYZ Sept 40 put @ 2 - BE is \$34

Long Straddle – volatility (unsure of direction of market):

Anticipate news (earnings, new product – new drug in pharmaceuticals)

BE = SP + BOTH premiums

Max Gain = goes up unlimited, goes down \$3400

Max Loss = both premiums (limited)

Short Straddle – Stable market (0 movement)

↓ Short 1 XYZ Sept 40 call @ 4

↑ Short 1 XYZ Sept 40 put @ 2

BE= SP ± BOTH PREMIUMS = 46

= 34

Max gain= ltd to premium

Max loss = unlimited, \$3400

Goes up, goes down

COMBINATION (a straddle w/ different strike prices)

Long 1 XYZ Jun 60 call @ 4

Long 1 XYZ Jun 65 put @ 2

BE?

I. 71

II. 66

III. 64

IV. 59

Sally writes a combination. She is:

A. Bullish

B. Bearish

C. Neutral

D. Consolidated

SPREADS (a lot on test)

Buying and selling SAME type.

Call Spread

Call Option – lower SP is more dominant = higher premium

Bull Call Long 1 XYZ Nov 30 call @ 4

buy | sell

↑ Short 1 XYZ Nov 40 call @ 1

out | in

-400 |

_____ | +100

-300 |

Net premium = Spread

Bought the spread – look at net premium = Know market attitude

Only acts as if there is one – as told by net premium ↑

BE= 33

Max loss= \$300 (premium)

Max gain = \$700

\$10

Always difference between 2 strike prices

BE= Call spreads Add net premium Lower SP (CAL)

Buy 1 XYZ Jan 20 call @5	<u>out in</u>	
Write 1 XYZ Jan 30 call @ 3	- 5	Net Debit-Bought call = bull
BE= 22	<u> +3</u>	higher premium - Bull
Max Gain: \$800	-2	
Max Loss: \$200		

	<u>out in</u>	
Buy 1 XYZ 40 call @ 3	-3	
Sell 1 XYZ 30 call @ 7	<u> +7</u>	
bearish BE= 34	+4	Net Credit -Sell Spread
call spread Max gain: \$400		sell Call = bear
Max loss: \$600		

Put Spread

Put shares Subtract Higher SP (PSH)

Higher premium dominate – determines attitude

	Out In
Long 1 XYZ 30 put @ 4	4
Short 1 XYZ 20 put @ 2	<u> 2</u>
Bear ↓ BE= \$28	2
Max Gain: \$800	
Max Loss: \$200	

	Out In
Buy 1 XYZ 60 put @ 3	3
Sell 1 XYZ 70 put @ 6	<u> 6</u>
Bull ↑ BE: \$67	3
Gain: \$300	
Loss: \$700	

Dominant:

Call – lower SP = higher premium

PUT – higher SP = higher premium

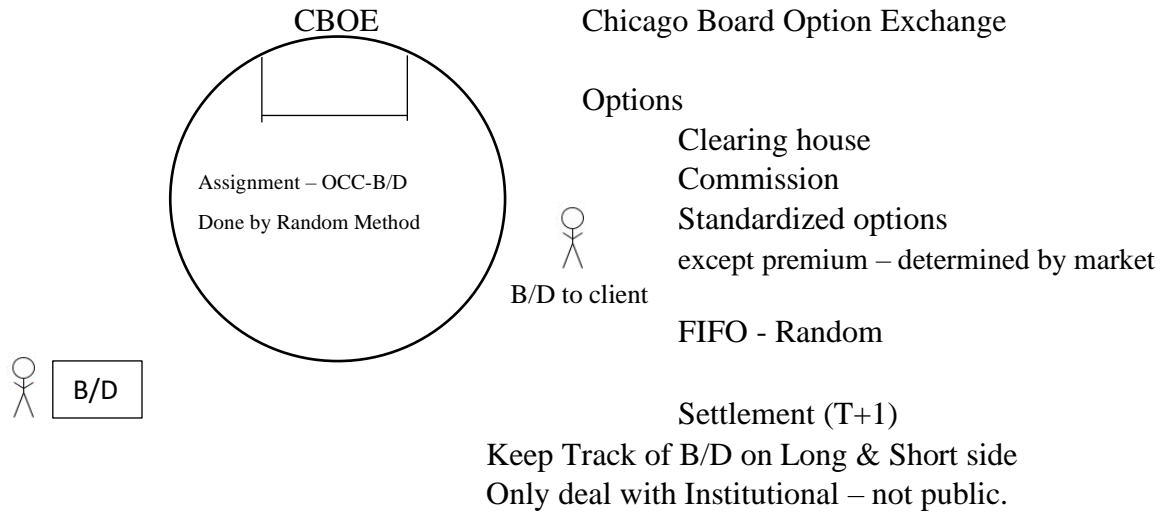
Your customer is long 1 XYZ \$50 call and short 1 XYZ \$60 call. Which are true?

- I. Bullish
- II. Bearish
- III. Debit
- IV Credit

Customer writes 1 XYZ 80 put @4 and buys 1 XYZ 70 put @ 2. Which are true?

- I. Bullish
- II. Bearish
- III. Debit
- IV Credit

Doesn't sign/return – closing transaction only.



Customer buys option, settles T+1. 3 weeks later, customer exercises the option. It settles when? T+2

What method does OCC use to assign exercise notice to B/D?

- A. FIFO
- B. LIFO
- C. Random
- D. Largest position

What method does B/D use to assign exercise notice to customers?

- I. FIFO
- II. LIFO
- III. Random
- IV. Largest position

Cease Trading

3rd Friday (4pm EST) of expiration month

Exercise option (5:30 EST) Stock Trans.

OCC automatically exercises ALL option IN THE MONEY

Forces you to close.

Options Expire

11:59 pm Friday

Greatest Advantage to options – LEVEAGE

Position Limits

75k contracts (made up #)

On “same side of the market” (market attitude) = Aggregated

Bull: Buy 50k call

Bull: Sell 40k puts

Which of these option positions would be aggregated to determine position limits?

I. ___ buy calls. ___ sell calls

II. ___ buy calls. ___ sell puts

III. ___ buy puts. ___ sell puts

IV. ___ buy puts. ___ sell calls.

An investor currently holds a XYZ call @3 when XYZ is trading @ \$48. Customer wants to liquidate their position. The RR would enter an order ticket:

- A. Opening sale
- B. Opening purchase
- C. Closing sale
- D. Closing purchase

Investor buys XYZ 40 call @ 4.50 when XYZ is trading @ \$42. What is its time value?

XYZ
40
Call

Premium = Time Value + Intrinsic Value (difference in CMV & SP)

\$4.50 = 2.50 + 2

<u>Buy Sell</u>
<u>4.5 2</u>
-2.5

Buy 1 XYZ Apr 40 call @ 4.45

Sell 1 XYZ Apr 50 call @ 1.50

- I. Bull
- II. Bear
- III. Vertical
- IV. Horizontal (Calendar spread)

Horizontal Time Spread?

- A. Different S.P., same exp.
- B. Same S.P. different exp.

- C. Different S.P., Different exp.
- D. Same S.P., same exp.

Debit Call Spread	↑	Long 30 call @ 3 Short 40 call @ <u>1</u> -2
Credit Call Spread	↓	Long 40 call @ 1 Sell 30 call @ <u>3</u> +2
Debt Put Spread	↓	Buy 50 put @ 3 Sell 40 put @ <u>1</u> -2
Credit Put Spread	↑	Buy 40 put @ 1 Sell 50 put @ <u>3</u> +2

OPTIONS ARE **NOT** AFFECTED BY CASH DIVIDENDS!!

Taxes

9 months on options – short term Capital Gains

Buy 40 call @ 3 when XYZ is trading @\$36. At expiration, with XYZ now @ \$48, Investor exercises her call option. For tax purposes, what is the cost basis?

- A. \$40/sh
- B. \$43/sh
- C. \$48/sh
- D. \$51/sh

<u>buy</u> sell
3
<u>40</u>
43

Buy 100 Sh @ 50
June 30 '13

Buy Apr 50 put @ 2
Nov 30 '13

holding period suspended
when buying put

Sell 100 sh @ 60
Jul 30 '14

therefore this is short term,
not long term gain

Married Put – If purchased on the same day -Long puts will NOT effect holding period on stock

STAOCK DIVIDENDS

1 XYZ 30 call

2 for 1 split (even)

Anything not “for 1” is uneven

Even – effects contracts

Uneven – effects shares

Like stock splits – strike price changes too

(3:2)

JQP owns 1 XYZ 30 call. BOD of XYZ announces 12% stock dividend. On ex-Dividend Date, JQP will own:

A. 1 XYZ 100 shares 28.50 call

(uneven)

B. 2 XYZ 100 shares 28.50 call

C. 1 XYZ 112 shares 28.50 call

D. 2 XYZ 112 shares 28.50 call

Non-Equity Options – (No Stock)

Index

S&P 500 (SPX)

S&P 100 (OEX)

Exercise= settles in cash (not shares)

Buy 1 OEX 425 call @ 12 *bullish

Index rises to 450 in the money

Exercises – cash \$ equal to intrinsic Value

A. \$1200

B. \$1300

C. \$2500

Exercise=\$=Intrinsic Value (no premium)

D. Share each stock in underlying index

VIX – Volatility Index (Fear Index) helps option buyers know volatility & price options.

VIX mimics volatility of:

A. S&P 100

B. DJIA

C. Russell

D. S&P 500

American (exercise anytime) vs. European (exercise only @ expiration)

Concerned about timing – Nov call – American exercises any time

(before end of year could cause capital gains)

European – April – now on next year taxes

Foreign Currency Options

Boeing imports raw materials from Tokyo with payment in Yen in 30 days. To protect:

- A. Buy yen call
- B. Buy yen put
- C. Buy us call don't exist
- D. Buy us put don't exist

Risk= ↓US \$

XYZ exports wool hats to London CO with payment in pounds in 30 days.

- A. Buy pound call
- B. Buy pound put
- C. Buy us call don't exist
- D. Buy us put don't exist

Risk= ↑ US \$

US Corps only:

- Exporters buy
- Puts
- Imports buy
- Calls
- (EPIC)

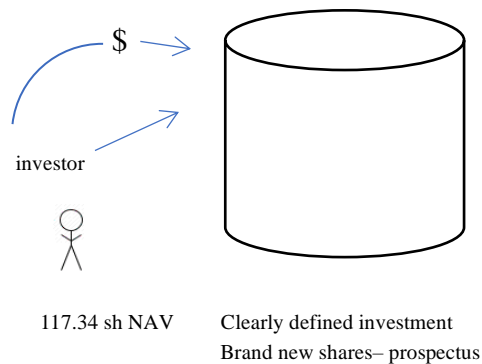
Non US companies:

- Exporters buy
- Calls
- Imports buy
- Puts
- (ECIP)

INVESTMENT COMPANIES

- Capital appreciation – common stock
- Aggressive growth – small cap stock
- Tax Free income – muni

Net assets in pool/ share outstanding = NAV
Portfolio of investment



TYPES

1. Unit Investment Trust (UIT) – passive –

2. Open End Management Company – active management
(mutual funds) Brand new shares, prospectus, priced as NAV, redeemable

3. Closed end Management Company
active management

Investment Pool – IPO, prospectus > NYSE, OTC, supply & demand
Often trades @ less than NAV

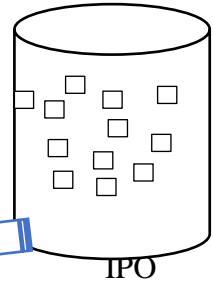
4. ETFs - passive
(Exchange Traded Funds)

Most popular vehicle today

Always tracks index

Benefit: ETF or open-ended buy entire market.
Performance will match market.

NYSE - OTC



IPO
Prospectus

Leveraged ETFs

(attempting to get 2x-3x underlying index)

- Margin, options

Buy on margin

If index goes up 2% this year,

Will the 200% ETF will go up 4%? **NO** Pretty much a “guarantee”

200%, 300% attempted but on a **daily** basis

Low cost – depends on

Index cheaper than managed

Leveraged ETF – 200%

CMV = \$50

Day 1 Index up 5% x2 = 10% \$55

Day 2 index flat - \$55

Day 3 index down 10% x2 = 20% \$44

Assuming ETF achieve objective, what is current market price after 3rd day?

\$44

Reverse ETF (short ETF) – the same as if you were shorting the index

IF market value of underlying index goes down, the reverse ETF will:

A. Increase

B. Decrease

C. Same

D. CBD

Open - End Management Co

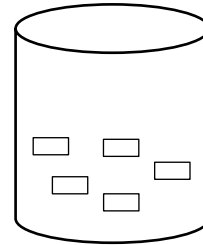
(mutual funds)

1. Board of Directors

40% “non-interested”

Not otherwise employee by the investment company to give non-biased opinion
(has nothing to do with financial interest)

- 2. Investment Advisor (Firm)
 - % of AUM (largest expense)
 - Manage portfolio
 - Buy & sell



- 3. Custodian (Safe keeping) - Assets actual held at custodial bank

\$12 mill

- 4. Transfer Agent

-\$2 mill liabilities

Customer Service, # of shares outstanding, issues and redeems shares

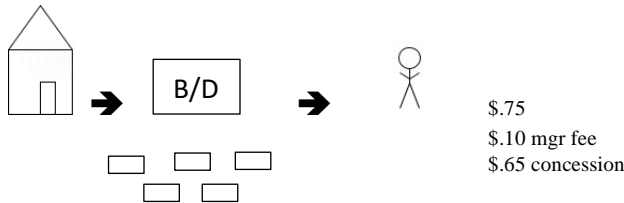
\$10 mill Net Assets

/1 mill outstanding

\$10 mill-NAV Share

Distribution

Distributors (Fund Sponsors)
Underwriters



\$10
(NAV)

\$\$.75 sale load
charge

\$10.75
(offer) POP

Class A front load – (Pay up - front sales charges)

Class B back end – (buy @ NAV, charge sales charges only if sell)

redemption fee: CDSC

Break Points – no standard break points

Breakpoints

0-24k 8%

24-44k 7%

50-74k 6%

75-99k 5%

All are eligible for breakpoints (Quantity Discounts) except,

Single entities

Individual

Custodial accounts

Joint Accounts

(parent single entity)

Business

Investment clubs – not eligible

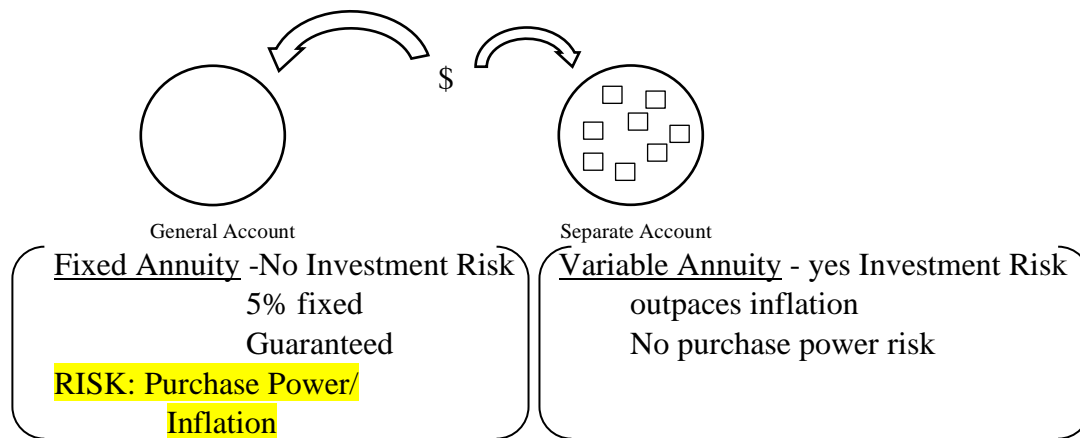
John Doe Jr. age 31 & John Doe Sr. age 62

Rep wants to diversify customer's \$100k investment and places \$ in 7 different fund companies with the same objective & risk profile?

Break point sale – rep maximize sale charges (Illegal)

Hedge Funds – Private investment company – not mutual funds. Open enrollment/1x yr, unregistered. High net worth clients, accredited investors. **RISK: Liquidity**

Module 12 - Variable Annuities

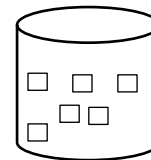


(Non-Qualified) Variable Annuities

Customer concerned with, adverse to, inflation risk. As RR, what would you recommend?

- A. Fixed annuity
- B. Variable annuity outpaces inflation
- C. Bank CD
- D. Money Market

Grow tax deferred
< 59 ½ yr old (10% penalty)



How are distributions taxed?

- A. Ordinary Income
- B. Cap gains
- C. OI & CG
- D. Not taxed

Upon distribution, how is variable annuity taxed?

- A. FIFO
- B. LIFO IRS wants money before you go.
- C. SHID
- D. Random

Customer invested \$20,000 into a non-qualified variable annuity.

At age 60, the annuity is now worth \$40,000 and the customer takes a random withdrawal of \$25,000. How much is taxable?

- A. \$5k
- B. \$20k
- C. \$25k
- D. \$0

Annuitize - (Income for life)

Accumulation units vary during accumulation phase – become annuity units and remain fixed.

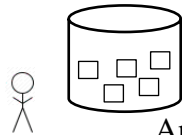
Value – NAV comparable to A.I.R. (2 things in play)

AIR – Assumed Investment Right

Vs.

Performance of Assets

Annuitizes (income for life)



Annuity Units:

- # units fixed forever
- Value= AIR vs performance

Which is true about variable annuities?

- A. Withdrawals prior to 59 ½ are prohibited.
- B. Number of units during accumulation phase varies
- C. Returns are guaranteed
- D. The value of payments is determined by the value of assets in separate acct during annuitization stage.

Who would be most suitable for Variable Annuities?

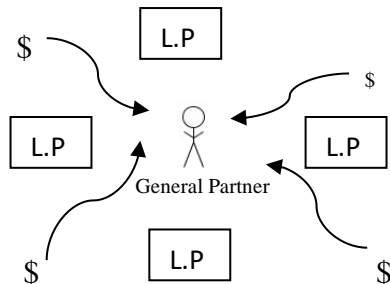
- A. 57 yr old about to retire
- B. 75 yr old wants fixed income
- C. 36 yr old max out qualified plan has money to invest tax deferred
- D. 28 yr old want down payment on house in 10 years.

Payout Options

1. Life Only (largest monthly income)
2. Life only with period of certain (guaranteed **at least**)
3. Joint with last survivor
4. Unit Refund

Module 7 - Direct Participation Program (D.P.P)

Limited Partnership – Business Entity



Responsibilities –

Limited Partners (Investors) - Provide capital only. They do not take on any managerial role. In exchange, receive limited liability (extent of investment).

General Partner – Manages the partnership’s assets. Takes full liability

Your customer has taken a 10% interest in a DPP for \$100,000. Two years later, the DPP goes bankrupt. Upon liquidation of the assets, they have \$2,000,000 in assets as well as a \$5,000,000 outstanding, non-recourse loan. What is your customer’s total liability?

- A. 0
- B. \$100,000
- C. \$300,000
- D. \$400,000

Liquidation Priority: All Creditors, Limited Partner, General Partner

Subscription Agreement – Limited Partner attests to their net worth and that they understand the risks. Effective only when the **G.P. signs** off.

SUITABILITY:

- Real Estate – New construction
- Existing Properties
- Raw (undeveloped) land
- Low-Income/Historic

Oil and Gas – Exploratory (Wildcatting)

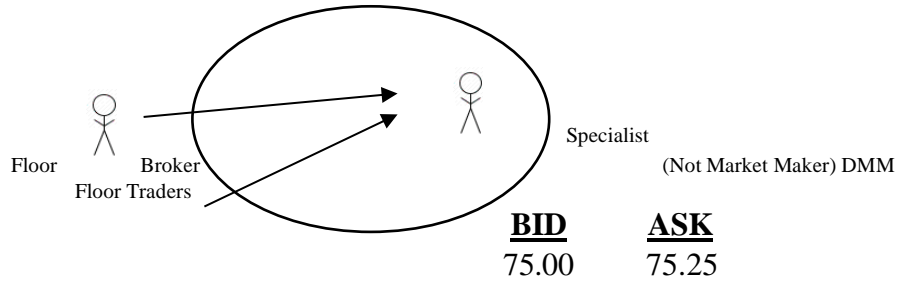
Developmental
Income

Investment Consideration – Profit motive must be first priority (not tax benefits)

Module 10 - TRADING SECURITIES

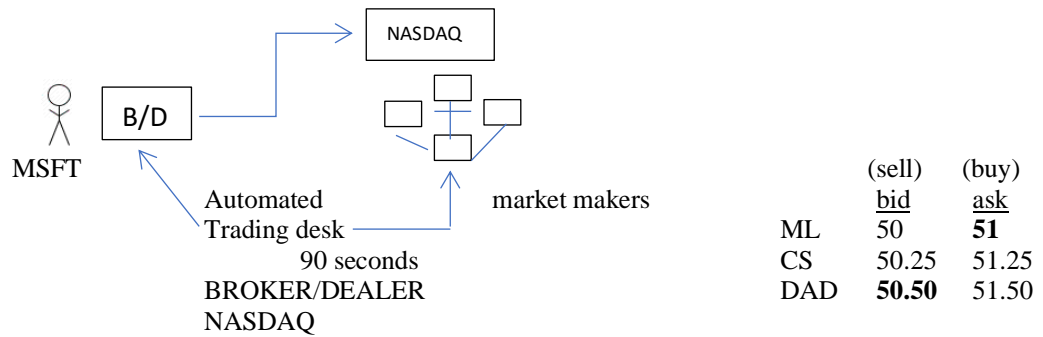
Markets

Exchanges – listed (auction)



OTC – unlisted (Interdealer - Dealer to dealer)

Before FINRA ('08)
Was NASD



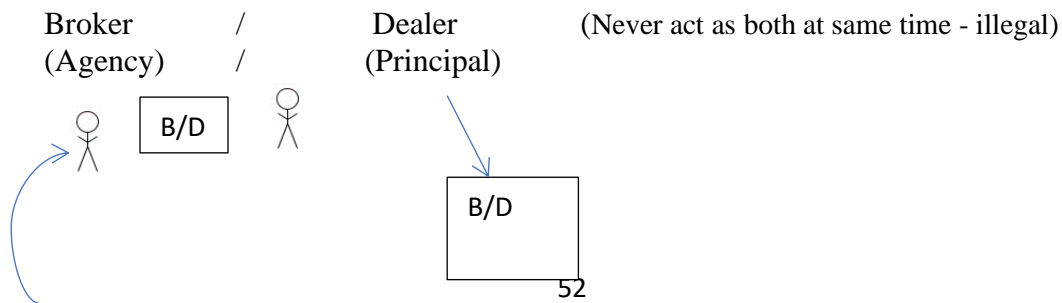
NASDAQ - Display Quotes from Market Makers/ Only belongs in OTC

Doesn't facilitate trades

Highest bid & lowest ask - inside market or **INSIDE QUOTE**

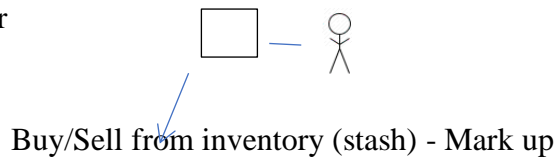
50.50 x 51.00

Best available to public

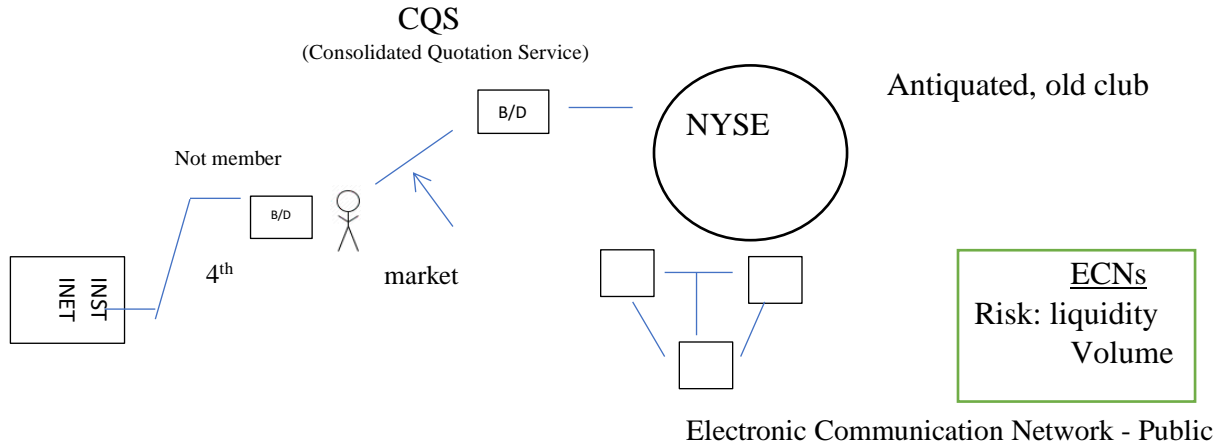


Broker facilitates buyer/seller

Commissions



3rd Market, 4th Market & ECN's



Specialized Orders

SL BS
---CMV---
BL SS

- 1) Determine if they Own it (sell) or Want it (buy)
- 2) What do they anticipate? ↑Or ↓(Market Attitude)

Your customer is long a stock with a large gain and is concerned the market may go down. As the RR, which would you recommend?

- A. Buy Stop
- B. Buy Limit
- C. Sell Stop
- D. Sell Limit

Your customer has been following a stock that has been moving sideways and would like to take advantage if the stock should break through resistance. Which would you recommend?

- A. Buy Stop
- B. Buy Limit
- C. Sell Stop
- D. Sell Limit

Customer has buy limit of @ \$49.50 when CMV \$50. The Board of Directors of XYZ declares and pay \$1 dividend. Which orders would a specialist automatically adjust for a dividend?

- I. Stop Limit
- II. Buy Stop
- III. Buy Limit
- IV. Sell Stop

Hint: - Only those orders that are placed below the market price-

Which order may accelerate a bear market?

-Sell Stop

If the market hits or passes through certain price then – Stop order triggers

It then becomes a market order to buy/sell at the next price. **Whatever** the price is!

Stops –Accelerates the Market

Accelerate bull market?

-Buy stop

Customer places an order – Sell 100 shares 43.50 Stop

43.78 43.65 43.52 43.55 43.50 43.45 43.57 43.40

At what price is the order executed?

- A. 43.52
- B. 43.50
- C. 43.45
- D. 43.57

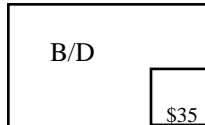
FINRA 5% Mark up Policy

Applies to both agency (commissions) & principal(markups) transactions.

Agency	/	Principal
Broker	/	Dealer
Commission	/	Mark-up

- Prospectus offerings exempt from 5% markup policy.
 (IPO's \$ Investment
 Co.)

- Based on current Inside Quote (Current Market price)



\$52 net (\$1)

	sell	buy
	<u>bid</u>	<u>ask</u>
ML	50	51
CS	50.25	51.25
BoA	50.50	51.50

Page 4

C. FINRA states all recommendations must be based upon stated objective

A. moderate growth and income = stocks and bonds

C. A 25/75 portfolio is most appropriate

Page 5

C. B/d's do not require approval from a customer's employer

Page 7

A. With the sale, SMA increase by half the sale and then used to purchase the new stock

C. Minimum deposit is \$2000 or 100% of the purchase

Page 8

D. Minimum deposits in short accounts is always \$2000

Page 9

D. Increases in LMV and decreases in SMV would both cause the equity to rise

Page 10

A. T Bills are issued at a discount

D. Common stock is issued by corporations, not the U.S. Gov't.

Page 11

D. Shareholders don't vote for the CEO or any other officer

Page 12

B. Ex-dividend dates are determined by FINRA/NYSE

B. 10% of 100 shares

Page 13

B. A distribution of a subsidiary

Page 14

B. Warrants are issued above the cmv and would not have intrinsic value until the stock goes above the exercise price

Page 15

B. Management and new products would affect the alpha of a stock

Page 16

D. Since it is convertible into stock, investor's would be less concerned about interest rates

Page 17

A. Highest rate and lowest cost is most likely refundable. Maturity date is irrelevant here.

Page 19

B. Best for saving for college tuition

C. Gov't. bonds settle T+1 therefore accrues interest up to the trade date.

C. Bonds that trade without accrued interest are said to trade flat

C. All of these bonds would trade with accrued interest except zero coupon bonds

Page 20

C. If it starts with a letter "B", it has to have 3 letters.

Page 21..

II and IV Eurobonds and ADR's

B. ELN's are a debt instrument affected by bond ratings

Page 22

D. The parity price of the stock is \$45. 2 points (\$) below parity is \$43

B. ALWAYS convert to stock with a callable, convertible bond. (The stock value is 10% above par and the cmv of the bond and the call price are only 1 and 3% above)

Page 24

II, I, III Gross pledge pay interest and principal first

A. IDR's or private purpose bonds are subject to AMT

D. Moral Obligation bonds are revenue bonds

B. City or county are Double Barrel Bonds, State are Moral Obligation

Page 26

A. School bonds are General Obligation Bonds

D. G.O. or Revenue does not add to diversification

Page 27

C. Official Statements are similar to a prospectus delivered by the underwriter

Page 28

A. A reasonable markup would be 101 ½ with a basis quote (YTM) of 6.80%

D. MSRB rules require B/D quotes to be fair and reasonable

Page 29

D. Adjusted cost is par

C. Adjusted cost is 105

B. Premium bonds use straight line amortization

B. Adjusted cost is 104

Page 30

D. High tax bracket is most suitable

A. MSRB does not have enforcement power

Page 31

D. Coverage ratios are used for analysis, not suitability

C. They do not violate the gift rule

Page 32

C. YTC would be the worst yield on discount bonds

C. Term bonds would be quoted as a % of par

D. The MSRB does not regulate issuers (States, cities, counties)

Page 35

C. Short calls could enhance the profit of a long stock

Page 37

C. Short straddles (combination) anticipate a stable market

Page 38

I and III The long 50 call is more dominant

I and IV The short 80 put is more dominant

Page 39

D. A short put is bullish and would bring money into the account

I and III To maximize the profit of a Debit spread, you want the spread to widen and exercise both options

C. 15 days from account approval

Page 40

C. The OCC is required to assign exercise notices to B/D's on a random basis

I and III B/D's may use FIFO or random when assigning notices to customers

Page 41

II and IV Option positions on the same side of the market (bullish or bearish)

C. Long investors enter a closing sale. Short investors enter a closing purchase

I and III Different strike prices is a vertical spread

B. A calendar or time spread is different expirations

Page 43

C. For an uneven split/dividend, on the shares change. The number of contracts remain the same

C. Intrinsic value is \$25 (x 1000) Intrinsic Value does not include the premium

D. The VIX tracks the volatility of the S&P 500

Page 44

A. U.S. Importers buy Calls

B. U.S Exporters buy Puts

Page 45

A. Inverse ETF's are shorting the market

Page 47

B. Limited partners liability is their initial investment

Page 49

C. Because they believe the market will drop, the only sell order below the market is a sell stop

Page 50

A. The only buy order above the market

III and IV Only those orders below the market are automatically adjusted

C. It takes 2 orders to execute. It's triggered at 45.50 and executed at the next price. Whatever price that is.

SERIES 7 ADDENDUM -

ACCREDITED INVESTORS The definition of accredited investor was amended in August 2020. "the amendments allow investors to qualify as accredited investors based on defined measures of professional knowledge, experience or certifications in addition to the existing tests for income or net worth. The amendments also expand the list of entities that may qualify as accredited investors, including by allowing any entity that meets an investments test to qualify." Among other categories, the SEC now defines accredited investors to include the following: individuals who have certain professional certifications, designations or credentials; individuals who are "knowledgeable employees" of a private fund; and SEC- and state-registered investment advisers.

RMD's – The SECURE ACT (I DOUBT IF ANY OF THIS IS TESTED AT THIS POINT)

RMD's are no longer required before age 70 ½. Required minimum distribution is now at age 73. (The RMD requirement is currently suspended during the COVID pandemic)

Beginning in 2020, individuals are now allowed to continue making contributions to their IRAs no matter what their age, as long as they have earned income.

Contact Person - Number of business days a trusted **contact person** needs to be notified that an account has been temporarily held for a senior investor and how long an account can be temporarily held for – 2 days to notify, 15 business days max held

Spoofing - is the act of disguising a communication from an unknown source as being from a known, trusted source. **Spoofing** can apply to emails, phone calls, and websites

Interval Funds (who they are suitable for and a definition question)

-What are they? [Interval funds](#) aren't a strategy – they're a structure. It's just a way to describe a type of closed-end fund that continuously offers new shares for sale, but buys back existing shares only during specified periods, or intervals.

Because interval funds offer only periodic liquidity – usually at 3, 6, 9 or 12 months – investors must be mindful that their investment dollars will not be available to them in the way an exchange-traded stock or bond investment may be. In general, the risk specific to the structure of interval funds is that they lack daily liquidity and **can expose investors to liquidity risk.**

SERIES 7 PRACTICE FINAL

1. A customer has \$100,000. He wants specific monthly income and has lost money in the market so he's concerned with the protection of his principle. Which of the following would you recommend?

- A. ETF
- B. fixed annuity
- C. Mutual fund
- D. Variable annuity

2. Which of the following is true about a variable annuity?

- A. Withdrawals are not allowed during the accumulation period
- B. the number of units in the separate account varies during the accumulation phase
- C. Returns are guaranteed
- D. The value of the separate account determines the amount of the monthly payments received during the annuity phase.

3. Which of the following would be suitable to purchase a variable annuity?

- A. 45 year old man, wants to purchase with \$50,000 in non-qualified funds; he is in the 35% tax bracket, wants to minimize tax effects, and has already maximum funded his retirement program through work.
- B. 20 year old who wants to use the money to purchase a home in 10 years), risk tolerance
- C. 70 year old interested in capital preservation),
- D. 30 year old of modest means who just lost his job).

4. An investor owning an option contract liquidates the position. On the order ticket, the R.R. would enter

- A. An opening sale
- B. An opening purchase
- C, A closing purchase
- D. A closing sale

5. An RR recommends a variable annuity with an income rider to a client. Customer agrees and tells you he will surrender his other non-qualified variable annuity he has with a life insurance company to purchase the variable annuity RR is recommending. The RR should do which of the following?

- A. Complete the paperwork to transfer the funds using a 1035 so there will be no tax consequences.
- B. Tell the client he will need to use cash or cash equivalents from another source.
- C. Reevaluate whether the recommendation for the variable annuity is still suitable.
- D. Call the existing life insurance company to instruct them to surrender the policy immediately.

6. An investor informs you that he wants to save for retirement. His main investment objective is to avoid purchasing power risk and to be paid income that may outperform inflation. As a RR you recommend

- A. Variable Annuity
- B. Fixed Annuity

- C. series EE bond
- D. Money Market

7. A customer purchases a non-qualified annuity for \$10,000. Ten years later he takes a lump sum withdrawal from the policy of \$30,000 to close the account. What is the tax reporting?

- A. \$30,000 capital gain
- B. \$20,000 capital gain
- C. \$30,000 ordinary income
- D. \$20,000 ordinary income

8. An elderly man requests to purchase a position. He gets confused during the interview. What does the RR do in regard to his requested purchase?

- A. Make the purchase
- B. Call the firm to discuss what protocols should be followed with working with an elderly prospect with early onset of dementia
- C. Tell him the sale is not suitable
- D. Speak with a family member regarding the purchase

9. A 17 year old, whose birthday is next month, wants to open an account with his wages from his part time position. Do you open the account?

- A. Call parents to obtain verbal authorization
- B. Open the account
- C. Refuse to open the account
- D. Get permission from the office manager to open the account

10. Investor owns the following positions in his account:

- \$150,000– long position
- \$70,000– DR
- \$80,000 – Equity

He sells XYZ for \$18,000 and, at the same time, buys ABC for \$20,000. How much is he required to deposit?

- A. Zero
- B. \$500
- C. \$4,000
- D. \$10,000

11. Bruce is funding his 401k at 4%, he is 40 years old and he makes 35,000 a year. He came in to an inheritance of 50k and wants to save it for retirement. How should he best invest the money?

- A. fixed immediate annuity at 6 1/2%,
- B. variable deferred annuity at 5 1/2%,
- C. variable immediate annuity at 6%,
- D. max out 401k contributions

12. 80 year old customer has 100,000 and he is looking for safety for his principal and some income would be nice.

- A. Immediate fixed annuity period certain 5%,
- B. Immediate fixed annuity straight-life 7 1/2%,
- C. immediate variable annuity life with period certain

D. 6%, Treasury bond ladder

13. Which two of these are considered retail "*Sales Literature?*"

- I. Unlimited number of emails sent to current customers
- II. More than 25 emails sent to prospects
- III. 25 or less emails sent to prospects
- IV. 1 text message sent to a current customer

- A. I and II
- B. I and IV
- C. II and III
- D. III and IV

14. A customer opens an individual account and buys 100sh of stock and tells the rep to watch the stock. The rep notices the stock is dropping. The rep calls the customer and finds out the customer is out of the country. As the R.R, he should

- A. Take instructions from the customer's spouse
- B. Buy the stock from the customer for his own account.
- C. Sell the stock using discretion.
- D. Wait for the customer to return even though the stock is losing value.

15. Contrasting Agency CMOs to private label CMOs, all of the following statements are true, except

- A. Agency CMO's usually have higher credit ratings
- B Private Label CMO's may contain mortgage securities other than U.S Agency issues
- C Agency CMO's are created by Investment Banks
- D. Private Label CMO's usually have lower credit ratings

16. What you should warn a customer about if they want to do ECN trading after hours.

- A. Liquidity and pricing may be an issue
- B. You might not be able to receive a confirmation statement
- C. Electronic trading is risky
- D. The R.R. will not receive a commission

17. Which of these agency bonds are backed by the US Government

- A. FHLMC bonds
- B. GNMA bonds
- C. FNMA bonds
- D. Federal Intermediate Credit Bank bonds.

18. A MFP writes a check from a joint account that is for political contributions, and he says that his interest in the joint account is less than 50%. How much of the check is attributable to him as a political donation.

- A. none
- B. his proportionate share of the joint account
- C. half of the check amount
- D. all of the check amount.

19. An RR had already given a customer a \$50 flower bouquet for her birthday earlier in the year and the client just got a promotion, so which of these could the RR give:

- A. a \$60 bouquet of flowers
- B. a \$75 restaurant gift card
- C. Two tickets to a show for the customer and their spouse worth \$65
- D. Take the client to dinner with the cost of the meals being \$150.

20. How often do CMO's pay dividends?

- A. Annually
- B. Semi-Annually
- C. Monthly
- D. At Maturity

21. What should a Registered Rep do if their client wants to make speculative purchase in an UTMA account?

- A. Make the purchase
- B. Decline and let the Principal know
- C. Discuss with the Principal
- D. Have conversation with client about the risks involved

22. Where would you see trading in the 3rd Market?

- A. Off trading floor
- B. Between Institutional Investors
- C. Foreign markets
- D. After Primary Issue

23. A client is 50 years old and has a non-qualified variable annuity. If he were to take distributions from the annuity, the distributions are taxed/subject to:

- I. Ordinary income tax
 - II. 10% Penalty
 - III. No Tax
 - IV. Capital Gain or Loss
- A. I
 - B. I and II
 - C. III
 - D. II and IV

24. A fund portfolio is made up of the following mix:

20% Bonds

40% Preferred Stock

40% Equity

This portfolio could best be described as:

- A. Equity Fund
- B. Growth Fund
- C. Fixed Income
- D. Asset Allocation Fund

25. Registered Rep must disclose what if a customer wants to buy a Fund of Hedge Funds?
- A. This is a Special Fund
 - B. The fund is made up of different Hedge Funds
 - C. No need to make any disclosures
 - D. This is a prohibited transaction
26. A client wants to trade through an ECN after hours. What must the RR disclose?
- I Limited Volume
 - II Limited Liquidity
 - III Unlimited hours
 - IV Unlimited commissions
- A. I and II
 - B. I and III
 - C. II and III
 - D. II and IV
27. John has capital gains of \$10,000 and capital losses of \$15,000. How much of a capital loss may John use to offset earned income this year?"
- A. \$3,000
 - B. \$5,000
 - C. \$0
 - D. \$15,000
28. Treasury bill interest would be taxed at which level?
- A. State only
 - B. State and Federal
 - C. Federal only
 - D. Neither State nor Federal
29. Your client list the following sources of income. Which group includes only earned income?
- A. wages, rental income, alimony
 - B. social security, wages, child support
 - C. wages, alimony, child support
 - D. wages, alimony
30. Which of the following would be most sensitive to interest rate changes?
- A. XYZ Inc. 6% Ba debenture maturing in 10 years
 - B. 8% U.S. Treasury Bond maturing in 5 years
 - C. ABC Inc. 5% AAA bond maturing in 5 years
 - D. MNO Inc. Zero Coupon maturing in 10 years
31. In an additional offering, an underwriter purchases shares above the current market price. This would be
- A. legal stabilization if disclosed in the Prospectus
 - B. illegal stabilization since it was purchased above the offering price.
 - C. legal if purchased for a customer

D. Not enough information to determine if it was legal or illegal

32. Which of the following would be adversely affected if the issuer's credit rating were to decline?

- A. ETF
- B. A growth mutual fund
- C. ELN
- D. U.I.T.

33. You're golfing with your client on Sunday morning and he tells you to sell 100sh at the market. As his RR, what do you do?

- A. Refuse the order
- B. Tell your client per FINRA rule 1545 you're not permitted to take orders on non-business days.
- C. Place the order on Monday morning and mark the ticket to appear like the order was taken that day.
- D. Place the order on Monday morning but use Sundays date and time as when the order was taken.

34. Your clients, retired and in their late 60's, would like you to review their portfolio. As their R.R, you would most likely recommend which of the following

- A. 30% domestic equities, 30% bonds, 30% international equities, 10% cash
- B. 50% domestic equities, 50% international equities
- C. 25% domestic equities, 60% bonds, 15% cash
- D. 10% domestic equities, 40% bonds, 40% international equities

35. In a new margin account, your customer places an order to buy 100 sh. of XYZ. The trade is executed at \$18/sh. As their RR, you would inform your customer they would be required to deposit

- A. \$900
- B. \$1000
- C. \$1800
- D. \$2000

36. A customer would like to provide their R.R. with authorization over their account. They have signed the documents and have sent them in the mail. The customer then leaves down and the R.R. notices their stock dropping. Which action may the R.R. take?

- A. Sell the stock immediately since the document has been signed
- B. Do nothing
- C. Obtain principal approval before selling the stock
- D. Place a sell limit at a price that is reasonable

37. According to FINRA rule 5130, all of the following are restricted from purchasing a new issue, except

- I wife of the CEO of the issuer
- II officer of the underwriter
- III employee of the Issuer
- IV employee of the underwriter

- A. I and III
- B. I and IV

- C. II and III
- D. II and IV

38. An investor is long 1 OEX December 420 call for \$1200. When the current market is at 445 the investor exercises is option. He would receive:

- A. The difference between the strike price and the market value times a multiplier of 100
- B. 100sh of stock in the underlying security for a cost of \$420
- C. The net difference between \$1200 and \$445
- D. The difference between the strike price and the market value times a multiplier of 100 less the premium

39. Your customer is 42 years old and is seeking income to diversify his portfolio but is concerned about rising interest rates. As their RR you mention that equity investments usually do well in a rising interest rate environment. The customer is a bit uncomfortable about investing in stocks at this time. Which of the investments would be least interest rate sensitive?

- A. A corporate bond with 5 years to maturity
- B. A municipal general obligation bond
- C. A convertible preferred stock
- D. A CMO

40. Which of the following bonds would a B/D be required to disclose yield to call on the customer's confirmation?

- A. 9% nominal, maturing 2020, trading at a 9.5% basis
- B. 9% nominal, maturing 2025, trading at a 9.0% basis
- C. 7.5% nominal, maturing 2020, trading at a 8.5% basis
- D. 7.5% nominal, maturing 2025, trading at a 6.5% basis

41. Which customer would be most suited to invest \$20,000 in a long-term zero coupon bond?

- A. 50 year old cardiologist making \$200,000
- B. 30 year old single mother of 2 young children
- C. 25 year old college student wanting to purchase a home in 5 years
- D. 68 year old retired couple with a pension and social security income

42. Your customer notices that the value in the underlying index of an Inverse ETF has decreased in value. As the R.R., you would inform the customer that the value of the ETF would

- A. Increase in value
- B. Decrease in value
- C. Have no effect on the ETF
- D. There's not enough information to know its effect on the ETF

43. If a RR mother-in-law wants to purchase shares of an IPO that his firm is u/w he should?

- A) Purchase the funds on the company's books and transfer them to her account after they go public
- B) Put an Indication of Interest for the IPO in his mother-in-laws account
- C) Tell his mother-in-law to purchase the shares when they become available in the 2nd market
- D) Purchase the shares at the IPO for the mother-in-law's account

44. If a client asks you, his RR, to help him raise capital for a new golf course in which the investors will have ownership. By doing so, you will not be paid but will be able to play the course any time you would like for free. What would you do?

- A. Tell your Principal what you plan to do and let him know you will not be paid for it.
- B. Write a letter to your firm asking permission to take part in this with your client
- C. Let your Principal know after you have helped the client with this
- D. No permission is required as you are not being paid to help this client

45. Data Tech imports raw material from their Tokyo supplier with payment in Yen expected in 30 days. However, Data Tech fears the value of the dollar will decline in the near future. To hedge their purchase they may:

- A. Buy Yen Calls
- B. Buy Yen Puts
- C. Buy U.S. Dollar Calls
- D. Buy U.S. Dollar Puts

46. A customer asks you to send duplicate confirms and statements to an outside Investment Advisor. What should you do?

- A. Note that on the Account form with his name and address
- B. Deny the request, as this would need a power of attorney in place to be possible
- C. Send the request to the registration and processing department for execution
- D. Get prior approval with each separate confirm & statement before they are sent

47. Your customer owns a leverage ETF whose goal is 200% of the underlying Index. Both the Index and the ETF are valued at 50. If the Index goes up 10% the first day and down 20% the second day, what is the value of the ETF if it achieves its objective?

- A. 45
- B. 44
- C. 36
- D. 35

48. A member firm completes an agency transaction. Which terms best describes this transaction?

- I receives a markup
- II receives a commission
- III a broker transaction
- IV a dealer transaction

- A. I and III
- B. I and IV
- C. II and III
- D. II and IV

49. What would be the result of a shareholder's equity if a 10% stock dividend is paid?

- A. 10% increase
- B. 10% decrease
- C. 9% increase
- D. no change

50. In a new margin account, an investor sells short 100 shares at \$34/share. What is the required deposit?

- A. \$1500
- B. \$1700
- C. \$2000
- D. \$3400

51. A customer purchases a security and holds it in their account with for 18 months. With no other transactions, how often would a B/D be required to send account statements?

- A. Monthly
- B. Quarterly
- C. Semi-annually
- D. Annually

52. A B/D completes a trade involving a book entry security. When does it clear and transfer?

- A. with good delivery and payment
- B. with journal entry
- C. on the trade date
- D. with payment

53. An Investment Banker is underwriting a new issue with the following:

Shares being held for sale by supporting banks: 100,000

Price per share: 10.00

Manager's fee: .10

Concession: 0.50

Underwriters Allowance: 0.70

Amount Paid to Issuer: 9.20

How much does the underwriter pay to the syndicate members for the additional risk of selling new securities?

- A. \$10,000
- B. \$20,000
- C. \$50,000
- D. \$70,000

54. What interest rate does the FRB use to affect monetary policy?

- A. Prime Rate
- B. Broker Call Rate
- C. Discount Rate
- D. Fed Funds Rate

55. Your investor purchased a State of Tennessee General Obligation Bond at 108. It matures in 20 years and your customer sells after 10 years at 102. For tax purposes, what is the gain or loss?

- A. \$20 loss
- B. \$60 loss
- C. \$20 gain

D. \$60 gain

56. A municipality wants to call in an outstanding Revenue Bond. It may do so under all of the following conditions, except

- A. The municipality has reached its statutory debt limit.
- B. A provision in its sinking fund agreement calling for a partial call
- C. The facility supporting the bond has been condemned
- D. Interest rates have fallen

57. The attorney's for a new municipal bond offering have concluded that the bond has no contingencies as to the authority of the issuer, its tax status or that the security need not be registered with the SEC. In other words, the attorney's opinion is deemed

- A. In good faith
- B. Qualified
- C. Exceptional
- D. Unqualified

58. All of the following debt securities trade "add interest" except:

- A. Treasury bond
- B. Corporate bond
- C. Treasury bill
- D. Muni bond

59. Your customer has mentioned that, despite the fact their child most likely will not be going to college, they would like to invest for their child's education. As their R.R, which would you recommend?

- A. Coverdell because it allows use for both primary and secondary education
- B. SEP-IRA
- C. UGMA because it allows the custodian to remove the gift if they do not go to college.
- D. H.R. 10 Plan

60. Your customer has stated they would like to be able to trade during the day and, if possible, to purchase below the NAV. You would recommend

- A. ETF
- B. Open end mutual fund
- C. Closed end mutual fund
- D. U.I.T.

61. An investor who is fairly conservative is seeking income and doesn't think the market will rise. As a R.R., which would you recommend?

- A. A credit call spread
- B. A long straddle
- C. Buy a put
- D. covered calls

62. An investor is long 1 XYZ April 40 call and short 1 XYZ July 40 call. Which of the following best describes his position?

- I Bullish
- II Bearish
- III Calendar spread
- IV Vertical spread

- A. I and III
- B. I and IV
- C. II and III
- D. II and IV

63. Your customer, invested in an Oil & Gas D.P.P., was informed that the partnership is to be dissolved and is concerned about their liability for outstanding debts. Upon liquidation of the D.D.P., there are \$2,000,000 in assets and an outstanding \$5,000,000 non-recourse loan. The R.R. would inform their customer that their liability will be

- A. A proportionate interest of \$3,000,000
- B. A proportionate interest of \$5,000,000
- C. A proportionate interest of \$2,000,000
- D. no additional liability beyond their initial investment

64. A municipal security legal opinion covers which of the following?

- I. Feasibility of public works projects.
- II. Creditworthiness of the issuing municipality.
- III. Tax status of the municipal debt.
- IV. The constitutionality and legality of the municipal debt.

- A. III and IV.
- B. I and IV.
- C. I and II.
- D. II and III.

65. A customer has indicated to her R.R. that she doesn't believe the market will move much in the near term. The most appropriate strategy the R.R. would recommend would be

- A. Sell a spread
- B. Buy a spread
- C. Sell a combination
- D. Buy a combination

66. A new customer wants to open a cash account under his company's name. As the R.R., what paperwork would you be required to fill out?

- I a new account form
- II Corporate resolution
- III Corporate By-laws
- IV Margin agreement

- A. I and IV
- B. II and III
- C. I and II
- D. II and IV

67. An R.R. is discussing a possible investment in several growth funds from several different investment companies in order for the customer to be better diversified. This strategy could possibly lead to

- A. A better overall return for the customer
- B. Reduced risk through diversification
- C. Greater exposure to market risk
- D. Increased sales charges from illegal breakpoint sales

68. An institutional customer is considering investing in a CMO your company sponsors and has indicated they are most concerned with repayment risk. Which would be most appropriate?

- A. PAC
- B. TAC
- C. BAC
- D. Zero Tranche

69. Which of the following orders could potentially accelerate a bear market?

- A. Buy Limit
- B. Buy Stop
- C. Sell Limit
- D. Sell Stop

70. Your customer informs you that news is expected on Data Tech, Inc. that she believes will have a big impact on the stock. Unfortunately she is unsure if the news is good for the company or will be damaging. As her RR, you inform her that she could take advantage of this if she

- A. Buys a call
- B. Sells a put
- C. Buys a spread
- D. Buys a straddle

71. Your customer has a long stock position with a substantial gain and is concerned the market may reverse itself in the near future and he would lose his large gain He would like to be prepared to sell stock and receive a certain price. As his R.R., you would recommend a

- A. Placing a sell stop order
- B. Buying a put option on the stock
- C. Selling his position immediately
- D. Inform him that the market will continue to rise

72. All of the following securities are backed by the full faith and credit of the U.S. Government, except

- A. Treasury Bills
- B. Treasury Notes
- C. Treasury Bonds
- D. Treasury Stock

73. A customer purchased a new issue Municipal bond at a discount several years ago and would like to sell the bond in the secondary market. To determine their cost basis they would be required to use which method?

- A. Constant interest amortization
- B. Straight line amortization
- C. Original cost
- D. Accretion

74. The Investment Company Act of 1940 requires the Board of Directors to contain at least 40% non-interested Board members. A non-interested member is one that

- A. would be prohibited from investing in the fund
- B. Is not otherwise employed by the investment company
- C. Is not permitted to attend any board meetings
- D. May not vote on any matters brought before the board

75. A customer is currently invested in a D.P.P that provides her with significant passive income. She would like to find an additional D.P.P. that would help to offset this income. As her R.R., you might recommend

- A. A real estate program that specifically invests in undeveloped land
- B. An oil and gas income program
- C. A program that develops low income housing
- D. A program that invests only in equipment leasing

76. A customer has noticed that the beta on a particular stock is 1.0. This means

- A. The performance of the stock historically is more volatile than the overall market
- B. The performance is equal to the overall market
- C. The performance is less volatile than the overall market
- D. The performance of the stock is 10% above the market

77. An investor, age 53, would like to maximize income with moderate risk. He makes \$75,000/year and has invested for the past 15 years. Which investment would be most appropriate for this customer?

- A. A mutual fund invested in intermediate-term Government securities
- B. A stock that has the potential to grow over time
- C. A money market fund
- D. A real estate investment trust that trades on an exchange

78. You have learned that your customer is subject to the IRS Alternative Minimum Tax. Which investment would be least appropriate?

- A. State of New York General Obligation bond
- B. U. S. Treasury bond
- C. Data Tech, Inc. debenture
- D. Dillon, Mich. Business Development Revenue bond

79. In discussions with your customer, he tells you he wants to buy 1000 shares of an internet related stock. As the R.R. for the account you would

- A. Place the trade immediately
- B. Obtain signed, discretionary authority
- C. Get approval from your principal
- D. Recommend a better suited investment

80. Which of the following is required to sign a new account form?

- A. Customer
- B. Registered Representative
- C. Principal
- D. Customer and Principal

81. Which of the following best describes Rule 144a?

- A. Sale of restricted stock by institutions
- B. Sale of restricted stock by accredited investors
- C. Sale of stock by insiders
- D. Sale of stock by all investors

82. The economic theory that believes that a decrease in taxes will increase government revenues is known as

- A. Classical Theory
- B. Keynesian Theory
- C. Supply-side Theory
- D. Demand-side Theory

83. An investor owns a XYX 6% convertible debenture currently trading at 90. It is convertible into XYZ's common stock at \$50/share. If the common stock is currently trading 2 points below parity, what is its current market price?

- A. \$50/share
- B. \$48/share
- C. \$45/share
- D. \$43/share

84. An officer of XYZ, Inc. currently owns common stock in her company that was purchased in a private placement. In order for her to sell her shares, she would be required to do all of the following, except

- A. Be subject to a 6 month holding period
- B. File Form 144
- C. Sell only to other officers of XYZ, Inc.
- D. Be subject to volume limits on the amount of stock she may sell

85. A R.R. is analyzing the trading history of ABC, Inc. stock when she notices a classic head and shoulders bottom formation appearing on the graph. According to technical analysis, this would indicate

- A. An interruption in a trend
- B. Reversal of trend
- C. The end of a trend
- D. A beginning of a trend

86. The Federal Reserve Board's most common tool when affecting Monetary Policy is

- A. Raising or lowering all interest rates
- B. Printing more money in the basement of the Treasury Department
- C. Buy or sell Treasury Bills through the Federal Open Market Operations
- D. Closing all banks for one day

87. An investor considering purchasing high yield bonds would be most concerned with which of the following?

- A. Interest rate risk
- B. Credit risk
- C. Market risk
- D. Business risk

88. An investor is considering diversifying their portfolio by including international stocks. You recommend that they consider ADR's as an efficient way to invest internationally. All of the following statements concerning ADR's are true, except

- A. They facilitate domestic trading of foreign securities
- B. Besides market risk, they should also be concerned with currency risk
- C. an ADR is a domestic security issued by domestic institutions
- D. Liquidity is a risk

89. An investor purchases stock, regular way, in their cash account. When would this transaction settle?

- A. Same day
- B. Next business day
- C. Second business day
- D. Fourth business day

90. A new customer is concerned with anonymity and request the account be identified by number rather than by name. As the R.R., you would inform the customer

- A. It is permitted so long as the customer has a signed signature card on file
- B. Will be allowed if we don't tell the principal
- C. Is prohibited under any circumstance
- D. Cannot be done for IRS purposes

91. An investor has opened a new options account at your B/D. A signed options agreement must be signed and return by the customer

- A. within 15 days of the first trade
- B. at the same time they receive the Options Disclosure Document
- C. Prior to discussing option strategies
- D. within 15 days of account approval by the R.O.P.

92. A customer wishes to invest in an oil and gas D.P.P. but is adverse to risk. As the R. R., which program would be least suitable?

- A. An Income Program
- B. A Wildcatting Program
- C. A Developmental Program
- D. A Fractal Income Program

93. Your customer is long 1 XYZ Nov. 30 call when she learns that XYZ has announced a 3 for 2 split and wants to know how this will affect her option. As her RR, you tell her on the ex-dividend date she will own:

- A. 1 XYZ 20 call (100 shares)
- B. 2 XYZ 20 calls (100 shares)
- C. 1 XYZ 20 call (150 shares)
- D. 2 XYZ 20 calls (150 shares)

94. Your customer has just purchase common stock of Hop To the Moon Brewery in a Rule 147 offering and has mentioned he has a friend that would also like to purchase the stock. As the R.R., you would inform him of which of the following

- I the stock may be purchased by anyone as long as it is suitable
- II The stock is restricted to state residents only
- III It may be purchased by out of state residents 6 months after the offering
- IV There are no restrictions on residency

- A. I and III
- B. I and IV
- C. II and III
- D. II and IV

95. A U.S. Treasury bond is currently quoted Bid 94.08 Ask 94.16. What is the dollar amount of the difference between the bid and ask?

- A. \$0.80
- B. \$2.50
- C. \$8
- D. \$25

96. A customer, currently in the 34% tax bracket, owns a State of Alabama 5% Sewer Revenue bond and is concerned with receiving as much after tax income as possible and is considering a higher yielding corporate bond. What is the equivalent tax yield?

- A. 3.7%
- B. 5%
- C. 6.3%
- D. 7.5%

97. The VIX mimics the volatility of stocks that underlie options. Known as the "fear index", the VIX tracks which index?

- A. S&P 100
- B. Wilshire 5000
- C Russell 2000
- D. S&P 500

98. The city of Portsmouth, Va. Is considering building a new bridge and want to issue a new bond to pay for its construction. The principal and interest will be paid for by tolls. However, if the tolls are insufficient, the city will back the bond with its full faith and taxing authority. This type of bond is referred to as:

- A. Limited Tax Bond
- B. Double Barrel Bond
- C. Moral Obligation Bond
- D. Special Assessment Bond

99. Your institutional client would like to sell their stock they purchased in a private placement one year ago. As their R.R., you would inform them they:

- A. must file Form 144
- B. have a holding period of 2 years
- C. may freely sell the stock
- D. must file Form 144a

100. A R.R. in analyzing the common stock of Data Tech, Inc., notices the alpha has changed. The most likely cause of this would be

- A. The overall market has gone up significantly
- B. Interest rates has risen.
- C. Inflation rate has dropped
- D. the CEO has resigned

101. You have noticed that Data Tech, Inc. has announced an increase in their quarterly dividend. The Board of Directors will determine all of the following dates, except

- A. Declaration Date
- B. Ex-Dividend Date
- C. Record Date
- D. Payable Date

102. Your customer is interested in opening a margin account at your firm and is concerned about the interest charged on amount borrowed. As the R.R., you would direct them to

- A. Credit Agreement
- B. Hypothecation Agreement
- C. Consent to Loan Agreement
- D. Disclosure document

103. Which one is senior to claims in a corporate liquidation?

- A. Common Stock
- B. Preferred stock
- C. Mortgage bond
- D. Subordinate debenture

104. A R.R. holds a seminar with 100 attendees. She hands out a flyer to all of the attendees. This would be considered

- A. Retail sales literature
- B. Correspondence
- C. Institutional sales literature
- D. Non-descript sales literature

105. A married couple, in their early thirties, have 50,000 to invest for a down payment on a new house in the city. They currently have \$100,000 in various domestic stocks and bonds and understand the fundamentals of investing. The most suitable recommendation would be

- A. a mutual fund that invests in international stocks since they need diversity
- B. Delaware Cash Reserve Fund
- C. an ETF so they can get in and out easily since they will need access to their money
- D. Columbia Intermediate-term Income Fund

106. In analyzing a new school bond about to be issued by the local school district, a R.R. would be concerned about which of the following?

- I Estimate of additional taxes necessary for construction
- II Flow of Funds
- III Legal Limits
- IV Voters attitude

- A. I and III
- B. I and IV
- C. II and III
- D. II and IV

107. Which of the following bonds would be most likely called?

- A. 9% coupon, maturing 2020, callable at par
- B. 9% coupon, maturing 2021, callable at 101 ½
- C. 7 ½% coupon, maturing 2020, callable at par
- D. 7 ½% coupon, maturing 2021, callable at 101 ½

108. A customer purchases 1 XYX April 50 call for 3 when the stock is trading at \$46/sh. When the stock reaches \$60, she exercises the option to purchase the shares. For tax purposes, what is her cost basis?

- A. \$5000
- B. \$5300
- C. \$6000
- D. \$6300

109. While at a restaurant, a R.R. overhears that XYZ will report bad earnings in the morning. When she arrives at her office the next morning, she should

- A. use the information only in her own account
- B. use the information only for her institutional accounts
- C. contact her legal/compliance department immediately
- D. contact the trading desk immediately

110. A married couple, just recently retired, has a pension they receive from their respective employers that enable them to pay all of their bills and have a little left over for emergencies. They have an additional \$100,000 they would like to invest for traveling and their hobbies. They are not adverse to some risk but consider themselves to be moderate risk-takers. As their R.R., which would be most suitable?

- A. Soguard Oversees Opportunity Fund
- B. Hendley Growth Fund
- C. Bennett Equity Income Fund
- D. Delaware Cash Reserve Fund

111. An investor is long 1 ABC May 40 call for \$600 and is short 1 ABC May 50 call for \$200. To maximize his profit, he would:

- I want the spread to widen
 - II Want the spread to narrow
 - III Exercise both options
 - IV Allow both options to expire
- A. I and III
 - B. I and IV
 - C. II and III
 - D. II and IV

112. Jane Doe, custodian for Johnny Doe in an UGMA. What is the limit on the amount of gift Jane may give to Johnny under UGMA?

- A. \$5,500 if Jane is over age 59 1/2
- B. \$14,000 in any one year
- C. \$100,000 depending on Johnny's residence
- D. unlimited

113. Jim, a customer in a joint account with his wife, calls to liquidate a stock in the account and requests to deposit the proceeds in his wife's individual account, also located at your firm. He states she will need the proceeds to pay for health insurance premiums on a policy in both of their names. As the R.R., you would

- A. Be prohibited from liquidating and depositing without authorization from Jim's wife unless the R.R. is licensed in health insurance
- B. Follow all instructions and liquidate the security and deposit the proceeds in Jim's wife's account
- C. Liquidate the security but may not deposit in Jim's wife's account without authorization from the wife.
- D. Contact your supervisor immediately

114. A R.R. receives notice from a customer's son that his father has passed away. The son informs the R.R. that he has power of attorney over his father's account. The son requests that all assets in the account be liquidated. The R.R. would be required to do all of the following, except

- A. Follow all instructions from the son since he has power of attorney
- B. Cancel any open orders and mark the account deceased
- C. Freeze the account
- D. Await proper documents from the executor of the estate

115. All of the following would be eligible to receive a breakpoint from an Investment Company, except

- A. Jane Doe, Custodian for Johnny Doe
- B. John Doe, Inc.
- C. A customer that has signed a Letter of Intent in which they deposit over 18 months
- D. John Doe

116. A customer, age 40, currently has a 401k from his employer and wants to invest additional assets for retirement. With the 401k, as well as, social security, the additional investment would be used only for emergencies and, therefore, does not want to be required to take distribution. Which should the R.R recommend?

- A. Keogh
- B. Roth IRA
- C. Traditional IRA
- D. 403b

117. A new customer, age 50, would like to open an account. All of the following deposits may indicate money laundering, except

- A. Bearer Securities
- B. Money order
- C. Traveler's Cheque
- D. Personal check

118. A customer owns a XYZ, Inc. 6% debenture that pays interest on a JJ basis. The customer believes interest rates will rise in the near-term and places an order to sell his bond on Friday April 15th. He asks whether or not he will receive any accrued interest. As the R.R., you would inform your customer of all of the following, except

- A. interest accrues on an actual day basis
- B. accrued interest will be added to the price of the bond
- C. interest accrues up to the day before settlement
- D. he will receive 109 days of interest

119. An investor wants to invest internationally to hedge the U.S. economy. He would like relatively good quality but is adverse to currency risk. Which of the following would you NOT recommend?

- A. Eurodollar CD's from a top-rated foreign bank
- B. BBB rated Eurodollar Bond
- C. Aa rated domestic debenture
- D. An ADR from a blue-chip foreign company

120. A high net worth, high tax bracket investor currently owns a Puerto Rico 3% General Obligation bond. She is concerned that the interest is taxable since she is a resident of New York. Her R.R should tell her

- A. Interest is only federally tax exempt
- B. Interest is both federally and State tax exempt
- C. Interest is only State exempt
- D. Interest is fully taxable

121. Investor writes a call in July but it expires in January of next year. When is it taxed?

- A. When the investor receives the money
- B. When the option expires
- C. When the option is sold
- D. On the settlement date

122. Which of the following would be least suitable investment for investor seeking conservative monthly income:

- A. Columbia Intermediate term bond fund
- B. Spence Short term Government bond fund
- C. CDs
- D. Leveraged bond index fund

123. Which bond would be subject to AMT?

- A. Public use revenue bonds
- B. Private use revenue bonds
- C. U.S. Government bonds
- D. Corporate debentures

124. A 15 year treasury bond is quoted 98.16 – 98.20. What is the dollar amount of the spread?

- A. \$0.04
- B. \$1.25
- C. \$12.50
- D. \$40

125. A R.R. has learned that her customer has inherited a large stock portfolio from his recently deceased aunt. The first step the R.R. would want to take is:

- A. Determine what the original cost basis is for the stock on the original purchase date
- B. If the inheritance is contested
- C. If the customer have any children
- D. Determine the cost basis for the stock on the date the aunt passed away

ANSWERS AND RATIONALE

1. B. Fixed, guaranteed income
2. B. During the accumulation phase, units (or shares) vary as you invest and/or reinvest. During the annuity phase, the monthly income is determined by the separate account performance AND the A.I.R.
3. A. Since variable annuities are used as a non-qualified retirement plan, it is MOST appropriate for those who have maxed out their qualified plans and still have monies they wish to invest tax-deferred.
4. D. The R.R. is closing a long option position, the order would be a closing sale

5. C. Since the RR was unaware of a pre-existing annuity, it would be appropriate to reevaluate the recommendation.
6. A. The only choice that could be equity based and thus outpace inflation.
7. D. Since annuities are non-qualified, the \$10,000 has already been taxed. Therefore, only the earnings (\$20,000) would be taxed. And like all retirement funds, are taxed as ordinary income.
8. B. Extra care should be taken to ensure elderly clients aware of the objectives and risks of their investments.
9. C. Accounts cannot be opened for minors.
10. A, before the transactions, the customer had \$5000 in SMA. After the transaction, half the sale proceeds are credited to SMA giving them \$14,000. Since their buying power is 2x the SMA, no cash deposit would be required.
11. D. Always max out the qualified plans first before opening a non-qualified plan.
12. D.
13. A. Correspondence vs. sales literature. 25 or less is correspondence.
14. D. NO discretion without authorization
15. C. Agency CMO's, as the name implies, are created by Gov't. Agencies and have higher credit ratings relative to private CMO's, created by investment banks.
16. A. After hours trading through ECN's can have very limited trading.
17. B. GNMA are the only agency issue backed by the full faith and credit of the U.S. Gov't.
18. D. It doesn't matter if the check is from a joint account.
19. D. The RR must be present to be considered a legitimate business expense.
20. C. Like some mortgage-backed securities, they pay interest monthly.
21. C. Extra prudence should be taken in Custodial accounts.
22. A. 3rd market transactions are done interdealer (OTC).
23. B. Distributions prior to 59 ½ are penalized 10% and earnings above cost basis are always taxed as ordinary income
24. D. The assets are invested in BOTH equity and debt
25. B. This is the definition of a fund of hedge funds.
26. A. After hours trading has far fewer trading
27. A. You may write off no more than \$3000 in losses per year
28. C. Gov't securities are state tax exempt
29. D. rental income, social security and child support are not considered earned income.
30. D. Zero's are always the most volatile because of greater bond duration.
31. B. Stabilizing bids must be at, or below, the offering price.
32. C. The credit rating affects a bond rating. The only debt instrument is Equity Linked Note.
33. D. Must indicate the date of the order.
34. C. A 25/75 portfolio is most appropriate.
35. C. FINRA's minimum deposit in a new margin account is \$2000 or 100% of the transaction, whichever is less
36. B. A discretionary account requires trading authorization be signed by the customer and the account approved by the principal.
37. A. Employees of B/D's are restricted persons. Employees of the Issuer or their wives are not.
38. A. Upon exercising a non-equity option, the investor would receive the intrinsic value (cmv > Strk.Pr.)
39. C. Convertible securities are ultimately interested in the common stock and not so interested in the income or the interest rate.
40. D. With a 6.5% basis (YTM), the bond is trading at a premium and thus YTC is the worst yield.
41. B. Zero's are best for saving for college tuition. Limited Partnership has limited liability. Limited to your initial investment.

42. A. An inverse ETF works in reverse of the underlying index. Investments with the same investment objective into different fund companies would lead to larger sales charges. FINRA rule prohibits these types of recommendations.
43. C. As an immediate family member, she would be prohibited from purchasing the IPO and would be permitted to purchase the security in the secondary market only.
44. A. Outside business activity without compensation requires notification only.
45. A. To hedge increasing Yen, buy Yen calls. (Remember, U.S. dollar options don't exist!)
46. C. Notification to the processing dept.
47. C. The ETF will go up 20% the first day and down 40% the second day (2x the index). From a value of 50, up to 60, down to 36.
48. C. A broker/agency transaction charge commissions, dealer/principal transaction charges markups.
49. D. A 10% increase in shares to the investor is proportionate to the increase in the number of shares outstanding, therefore, no change in ownership.
50. C. The minimum deposit in short account is always \$2000.
51. B. Account statements must be sent no less than quarterly.
52. B. With no certificate, the trade is cleared with proper journal entry.
53. B. Total allowance is 0.70 and the concession is 0.50. Therefore the U/W fee, the compensation for taking on risk is 0.20.
54. C. The only interest rate the FRB directly controls is the Discount Rate.
55. A. Using straight line amortization, the adjusted cost basis would be 104. Since the investor sold the bond at 102, it would be a \$20 capital loss.
56. A. Revenue bonds are not under statutory debt limits. Only G.O.'s are
57. D. A legal opinion that has no conditions or contingencies is deemed to be unqualified. An opinion that is without qualifications.
58. C. T Bills do not pay interest. They are bought by the investor at a discount (like a zero) and therefore trades flat (without accrued interest). All of the other bonds pay regular interest and investors would have to pay accrued interest which is "added" to the market price.
59. A. Coverdell's allow for primary as well as secondary education whereas, UGMA contributions are irrevocable.
60. C. Closed end funds traded in the secondary market based on supply and demand and often trade below their NAV.
61. D. Covered calls are an excellent way to generate income in neutral to slightly bearish markets.
62. C. Since the strike prices are the same but the expirations are different, this is a calendar (horizontal) spread. Since the short call has the longer expiration, it would have more time value and therefore a higher premium and thus make the short call more dominant. And short calls are bearish.
63. D. Limited Partnership has limited liability. Limited to your initial investment.
64. A. The legal opinion attests to 3 things: legal authority of the issuer, IRS authority of Federal tax-exempt interest and that the security is exempt from the Securities Act of 1933.
65. C. Short straddles are most appropriate for stable/neutral markets.
66. C. For a cash account, a new account form and a resolution are the only documents required. For a margin account, the corporate by-laws would be required as well.
67. D. Investments with the same investment objective into different fund companies would lead to larger sales charges. FINRA rule prohibits these types of recommendations.
68. A. Planned Amortization Class are the shortest tranches and are least volatile.
69. D. If a large quantity of sell stops accumulate in the market and are then triggered into market orders, they could create a large drop in the stock.
70. D. A long straddle attempts to profit from a big move in the stock but are unsure of the direction.
71. B. A put option allows the investor to sell the stock at the strike price.

72. D. Treasury stock is common stock a corporation has repurchased in the secondary market.
73. D. Original Issue Discounts (O.I.D.) must be accreted.
74. B. Non-interested board members are brought in from outside of the company to represent the views of the shareholders and, therefore, are not otherwise employees of the Investment Co.
75. C. A low income partnership creates tax credits that would help offset passive income.
76. B. A beta of 1.0 equals the market.
77. D. Remember, investment objective is the first factor. REITs would pay the highest income of these choices.
- D. Only Industrial Development Revenue bonds are subject to the AMT. Corporate bonds are fully taxable no matter what so are not an issue for AMT.
79. B. A R.R. must know the amount, the action (buy or sell), and the name of the asset. Without all 3 of these, the R.R. would be required to have discretionary authority.
80. C. Under FINRA rule, only the principal is required to sign the new account form.
81. A. Form 144 is for control persons. Form 144a is for institutions.
82. C. The Laffer Curve is the premise behind Supply-side Theory.
83. D. Since the bond price has fallen by 10%, the stock price would have to fall by 10% to remain at parity (\$45/sh.). The stock, trading 2 points (dollars) below parity, is trading at \$43
84. C. Securities purchased by control persons in a private placement are restricted for 6 months. They are required to file Form 144 and are under volume limitations but can sell to anyone in the open market.
85. B. Head and shoulders indicate a reversal of trend.
86. C. Buying or selling securities to or from member banks is the most common method for affecting monetary policy.
87. B. Credit risk is the risk of default. High yield = low rating = default risk.
88. D. Since ADRs trade on NYSE, there is no liquidity risk.
89. C. It doesn't matter which type of account, cash or margin. Regular way settlement is T + 2.
90. A. It is possible to open an account registered by number rather than by name if there is a signature card on file.
91. D. Option Agreements must be signed and return by the customer within 15 days of account approval.
92. B. Exploratory Oil and Gas Programs, also known as wildcatting, are the riskiest.
93. C. In a 3 for 2 (uneven) split, the number of contracts remain the same but the number of shares in the contract changes. There is only one answer that satisfies these two conditions.
94. C. Rule 147 offerings are intrastate offerings sold only to state residents and are restricted to out of state buyers for 6 months.
95. B. Treasury bonds are quoted in 32ths. Bid: 94 $\frac{1}{4}$, Ask: 94 $\frac{1}{2}$. If 1 bond point is 1% of par (\$10), then $\frac{1}{4}$ of a bond point is \$2.50.
96. D. The tax equivalent yield formula: $\text{muni yield}/100\% - \text{Tax bracket}$ (5/0.66)
97. D. The VIX tracks the volatility of the S&P 500 index.
98. B. Double barrel bonds are issued by counties or cities. Moral Obligation bonds are issued ONLY by the state with the backing of the state legislature.
99. D. Institutions are required to file Form 144a when selling restricted stock
100. D. Alpha measures business risk which is affect by management changes
101. B. The ex-dividend date is determined by FINRA/NYSE calculated from the record date.
102. A. The credit agreement contains the scale for interest charged on margin balances.
103. C. Secured debt has the highest priority amongst investors (after employees and the IRS).
104. A. Literature handed to the general public is retail.
105. B. A money market is most appropriate for liquid assets of less than a year.

106. B. General Obligation bonds require voter approval and are backed by taxes.
107. A. Highest rate at the lowest cost is most likely to be called. Ignore the maturity!!
108. B. The cost of the option is added to the cost of the stock.
109. C. It isn't illegal to "overhear" information. It is illegal to use it.
110. C. The key to this is "moderate" investors.
111. A. D.E.W. Debit spreads, Exercise, Widen. Keep it simple! **Deb** needs to **Exercise** or she will **Widen**.
112. D. Don't be confused with the gift tax rule! There is no law that limits how much you can give someone.
113. C. Jim has authority in the joint account but no authority in his wife's account.
114. A. Power of attorney ceases upon death.
115. C. A Letter of Intent must be satisfied within 13 months.
116. B. Roth IRA's do not require a minimum distribution at 70 ½.
117. D. All of these answers are "cash" like except a personal check.
118. A. Interest on corporate and municipals accrue on a 30/360 basis up to the day before settlement. Settlement does not include weekends but accrued interest does. The day before settlement is Monday April 19th.
119. D. Euro dollar CD's and Eurobonds pay interest in U. S. dollars. ADR's are subject to currency risk.
120. B. Interest from U.S. territories is federally and State tax exempt for all U.S. residents.
121. B. The gain or loss is realized once the option expires.
122. D. A leveraged index fund could lose twice or three times the loss of the underlying index.
123. B. Private purpose (Industrial Development Revenue bond) is the only bond subject to the AMT.
124. B. Gov't. bonds are quoted in 32ths so a difference of 4/32 (1/8th of a bond point) is \$1.25.
125. D. For tax purposes, stock inherited receives a step-up in cost basis to the fair market value at date of death.