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Exam : **Series63**

Title : Uniform Securities Agent State
Law Examination

Vendor : FINRA

Version : DEMO

NO.1 Which of the following would be an unsuitable recommendation for your 68-year-old client?

- A. a Treasury Inflation Protected Security (TIPS)
- B. a deferred annuity
- C. an S&P 500 Index mutual fund
- D. a high quality corporate bond fund

Answer: B

Explanation

A deferred annuity would be an unsuitable recommendation for your 68-year-old client. These annuities charge significant penalties for early withdrawals-and "early" can mean before 10 years, or even longer. A

68-year-old client may have the need to withdraw his money early to make medical payments.

NO.2 Your client calls you with a market order to purchase 500 shares of the stock of Oracle and asks when payment will be due. If today is Wednesday, September 15th, you inform the client that payment is due on

- A. Monday, September 20th.
- B. Thursday, September 16th.
- C. Friday, September 17th.
- D. Saturday, September 18th.

Answer: A

Explanation

If your client places an order to purchase 500 shares of Oracle on the open market on Wednesday, September

15th, payment will be due on Monday, September 20th. The settlement date for stock transactions is T + 3, which means the third business day after the trade. Saturday is not a business day.

NO.3 Which of the following is an example of commingling?

- A. Sly is an agent with a broker-dealer who recently executed a stock purchase for his client and had the client make the check for the purchase out to Sly for deposit in Sly's broker-dealer account.
- B. In order to generate more commissions for herself Ms. Fox makes trades on some of her client's accounts and has the trade confirmations sent to a P.O box she owns.
- C. Mr. Hawk encourages his clients to leave their securities in "street name" with the broker-dealer for which Mr. Hawk works.
- D. All of the above are examples of commingling.

Answer: A

Explanation

When Sly has his client pay for a stock purchase by making the check out to Sly himself, he has engaged in the prohibited practice of commingling. Ms. Fox is also engaged in a prohibited practice, but she is engaged in making unauthorized transactions. Mr. Hawk is doing nothing wrong. It is typical for clients to leave securities on deposit with their broker-dealers in what is called "street name." This makes it easier for the client to sell the securities later on since he physically will not have to deliver the securities to the broker, for one thing.

NO.4 Which of the following persons would not be required to register with the state as an agent

under the guidelines of the Uniform Securities Act (USA)?

- A.** Keith is a salaried employee of Middlesex County in Massachusetts who sells revenue bonds issued by the county to the public.
- B.** John is employed by TrustUs Corporation to sell shares of the firm's stock to the firm's employees and receives a commission on the shares he sells.
- C.** Stefan is a sales representative for SecureMoney Broker-Dealers and sells only mutual fund shares.
- D.** Preetham is part-owner of SecureMoney Broker-Dealers and executes the purchase and sale of securities for the firm's customers.

Answer: A

Explanation

Keith would not have to register as an agent since he is a salaried employee of a county in Massachusetts selling county-issued bonds to the public. He is not representing a broker-dealer; he is not receiving a commission on the bonds he sells; and he is selling exempt (government-issued) securities. John receives a commission on his sales, so he is considered to be an agent. Stefan is a sales representative employed by a broker-dealer, which makes him an agent under USA guidelines. Even though Preetham is part-owner of the broker-dealer for which he is effecting transactions, he is acting as an agent in doing so.

NO.5 Iggy recently started his own company. He soon discovered it required more cash to keep it going than he had anticipated. He ran an ad in the local paper for investors and got a response. He found a template for a promissory note on the internet, filled in the requisite information specific to the agreement he and the investor had worked out, and printed it out. On it, he promised to make monthly interest payments of 2% on the loan and to repay the principal amount at the end of 18 months. A few months after the arrangement, Iggy read an article in a small business publication that indicated that promissory notes had to be registered with the state unless they were sold in an exempt transaction, such as one enacted with a financial institution, prior to being offered for sale. The article indicated that a seller who had sold an unregistered note in error could remedy the situation by sending the buyer a formal offer to buy the security back, with interest. Iggy turned to the computer once again, found a form that could be used for a formal offer of rescission, filled it out, and sent it to the investor. Having done this,

- A.** Iggy cannot be sued for civil damages if the investor fails to respond to the offer within 30 days.
- B.** Iggy must follow up with a second notice sent via registered mail if he has not heard from the investor within 30 days.
- C.** Iggy must wait 6 months for a response from the investor. If no response is received by the end of 6 months, Iggy is off the hook.
- D.** Iggy will not be assessed any penalties by the Administrator of the state, but the investor can still sue for damages in civil court.

Answer: A

Explanation

Since Iggy realized the promissory note he had sold to the investor required state registration and sent a formal offer of rescission to the investor, he cannot be sued for civil damages if the investor has not responded to the offer within 30 days. The investor has 30 days to accept or reject the offer. If he either rejects it or fails to accept it by not responding to the offer at all, the investor has lost the right to sue for damages.

NO.6 Erin is a registered agent who works for SecureMoney Brokers-dealers. One of her clients, Mrs. McTurk, is a recently-widowed woman who relies on Erin for advice about her investment portfolio. Mrs. McTurk reminds Erin of her own grandmother, and she is happy to provide guidance within the sphere of her own knowledge.

Based on these facts, which of the following statements is true?

- A.** SecureMoney Broker-dealers must register as an investment adviser since one of its employees is providing investment advice.
- B.** Erin must register as an investment adviser since she is providing investment advice.
- C.** SecureMoney Broker-dealers must register as an investment adviser since one of its employees is providing investment advice, and Erin must register as an investment adviser representative as the firm's employee.
- D.** Neither SecureMoney Broker-dealers nor Erin must register as an investment adviser based on the facts provided.

Answer: D

Explanation

Neither SecureMoney Broker-dealers nor Erin must register as an investment adviser based on the facts provided since neither the broker-dealer nor Erin is receiving any compensation for the advice Erin is giving Mrs. McTurk. In this instance, the advice provided is considered incidental to the broker-dealer business.

NO.7 To say a security is "exempt," means that

- I.** it is exempt from the state's anti-fraud laws.
- II.** it is exempt from state registration requirements.
- III.** any transaction involving it is considered to be an exempt transaction.

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

Answer: D

Explanation

To say a security is "exempt" means only that the security is exempt from state registration requirements. It is not exempt from the state's anti-fraud laws and may or may not be part of an exempt transaction. That is defined by the transaction.

NO.8 Which of the following is not a method that can be used to register securities with the state?

- A.** registration by exception
- B.** registration by notification
- C.** registration by coordination
- D.** registration by qualification

Answer: A

Explanation

Registration by exception is not a method that is used to register securities with the state. Registration by notification is a method available for those securities that meet a certain set of criteria and requires the least amount of paperwork. Registration by coordination is the method used

for most securities. Registration by qualification is the most burdensome method, requiring a voluminous amount of paperwork.

NO.9 When selling shares of an investment company to a client, an agent must provide the client with

- I. the fund's prospectus, which provides information on any loads or other fees as well as historical return information.
- II. information about any breakpoints if it is a load fund along with an explanation of a letter of intent
- III. information regarding the investment adviser used by the fund
- IV. an explanation of the various loads and fees outlined in the fund's prospectus

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

Answer: D

Explanation

When selling shares of an investment company to a client, the agent must provide the client with the fund's prospectus and provide the client with an explanation of the various loads and fees and any breakpoints that, if reached, will result in a lower load charge for the client, along with information on a letter of intent, which the client can execute. The agent need not provide any information regarding the investment adviser used by the fund although that information is contained in the prospectus as well.

NO.10 You are an investment adviser to Mr. Crochety, an elderly man who lives solely on his social security income although he managed to accumulate an investment portfolio worth about \$100,000 over the years. Mr.

Crochety recently got his hands on a business publication and read about the tax-free interest paid by municipal bonds. He calls you and instructs you to sell his other investments and invest all his money in a municipal bond portfolio, so that "the government doesn't get any more of my hard-earned money." You tell Mr. Crochety that you don't believe this is a wise move because he's in such a low tax bracket that municipal bonds are not a good investment for him, but he is insistent. Based on these facts, you should

- A. ignore Mr. Crochety's instruction since it is not in his best interest.
- B. require Mr. Crochety to sign an affidavit of liability waiver, indicating that you will not be held responsible for any adverse consequences of this decision.
- C. have Mr. Crochety sign a statement of investment policy that indicates that this transaction is being executed on the client's instructions and that you have advised the client against it.
- D. call Mr. Crochety's relatives and suggest they have him examined for mental instability.

Answer: C

Explanation

Given that you have advised Mr. Crochety that this is not a wise move and he still insists on it, you should protect yourself by getting it in writing. In no case, however, can you require a client to sign an affidavit of liability waiver, nor can you refuse to follow his adamant instructions.

NO.11 Mr. Bigwig, CEO of HiGrowth Corporation, meets with the president of BigFee Investment

Bankers and arranges for BigFee to underwrite an Initial Public Offering (IPO) for the firm. When the IPO comes to market, GetErDone Broker-Dealers is part of the selling group, which handles the sale of the stock to the public.

In this scenario, which party is the broker?

- A. HiGrowth Corporation
- B. Mr. Bigwig
- C. BigFee Investment Bankers
- D. GetErDone Broker-Dealers

Answer: D

Explanation

GetErDone Broker-Dealers is the broker in this scenario. GetErDone is simply finding buyers for the securities and receives a commission for doing so. GetErDone is not itself purchasing the securities in the scenario described. It would be considered unethical for the broker-dealer to do so since they are required to make a bona fide public offering of all of the securities allotted to them for distribution under NASAA Model Rules.

NO.12 Switch Advisory is a small investment adviser partnership registered in a single state. A larger investment adviser firm, Bait Investment Adviser, is registered in the same state as well as two other states. Bait has offered to buy out three of Switch's partners who want to retire. This will give Bait a 60% ownership in Switch Advisory.

Which of the following statements are true?

- I. Switch Advisory must obtain the approval of its clients before the partners can sell their interests to Bait.
- II. Switch Advisory must notify the state Administrator of this event.
- III. Switch Advisory must notify their clients of this event, but does not need the clients' approval.
- IV. Switch Advisory must notify the SEC of this event.

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

Answer: B

Explanation

Only Selections I and II are true. Switch must obtain the approval of its clients before the partners can sell their interests, and Switch must notify the state Administrator of this event. Whenever a change in partnership will result in new ownership of the business, which is the case when an external entity acquires a 60% interest, an investment adviser must get its clients' approval. As a state-registered investment adviser, switch also needs to notify the state Administrator. The SEC does not require notification since Switch is not a federal covered investment adviser.

NO.13 Under the guidelines of the Bank Secrecy Act (BSA), the Treasury Department now requires broker-dealers to obtain and keep certain information relating to clients that make or receive funds transfers that involve

- A. \$3,000 or more.
- B. \$10,000 or more.

- C. \$5,000 or more.
- D. \$100,000 or more.

Answer: A

Explanation

Under the guidelines of the BSA, the Treasury Department now requires broker-dealers to obtain and keep information relating to clients that make or receive funds transfers that involve \$3,000 or more. If the transaction is a cash transaction over \$10,000, the same rules apply, and a Currency Transaction Report must be filed with FinCEN. Under the USA Patriot Act, if the broker-dealer thinks that a transaction of \$5,000 or more is suspect, the broker-dealer must file a suspicious activity report (SAR.)

NO.14 Penny Swyne, an agent employed by Bear Broker-Dealers, has received a written complaint via e-mail from Mr. Wolf regarding her performance as his agent.

What are Ms. Swyne's legitimate options?

- A. Ms. Swyne can call Mr. Wolf and offer to meet him for a romantic dinner and try to convince him to revoke the complaint.
- B. As illegal as it may sound, since the complaint was via e-mail, Ms. Swyne can hit the delete button and make it all go away.
- C. Ms. Swyne must forward the complaint to the state Administrator.
- D. Ms. Swyne must provide Bear Broker-Dealers with a copy of the complaint.

Answer: D

Explanation

Ms. Swyne must provide Bear Broker-Dealers with a copy of the complaint sent by Mr. Wolf. Bear Broker-Dealers is required to respond to this complaint in writing and keep a record of it. E-mails are treated the same as snail-mails.

NO.15 Ken Con is an agent with Blue Sky Broker-Dealers. He gets up early each morning so that he can study any late-breaking news that may affect the markets and figure out ways to incorporate this news into conversations with select clients in order to pressure them to restructure their portfolios by selling holdings they have in one particular industry to invest the money in another particular industry.

Ken has been very successful with this strategy and executes more trades for his clients than any other agent with the firm, but is he in danger of losing his license?

- A. Yes. Ken is engaging in churning, a prohibited practice and can have his license revoked or suspended.
- B. It depends. If his clients have lost money, Ken may lose his license; but if a review indicates that his clients' accounts earn profits, then his license is safe.
- C. Yes. Ken is guilty of the prohibited practice of "tailgating."
- D. No. Ken is just a successful sales person who is working harder than the other agents in the firm.

Answer: A

Explanation

Yes. If Ken is getting up each morning in order to collect news that he can use to pressure his clients to buy and sell their securities, Ken is engaging in churning and can have his license revoked or suspended for this prohibited practice. A lot of the news might have a short-term effect on a particular industry, but any profits gained by trying to time the market will often not be sufficient to

cover the commissions that the investor had to pay on the transactions and the taxes they may have to pay on the short-term capital gains they realized when they sold securities. Regardless, it doesn't matter whether his clients' accounts show a profit or not.

NO.16 Kevin has a pair of season tickets to the Boston Red Sox games. He and his wife can't attend all the games themselves, so Kevin has created "packages" of eight games each that he is listing for sale on Craig's List.

Do these "packages" meet the definition of securities, and, if so, does Kevin need to register them with the state before offering them for sale?

A. If Kevin will be profiting from the sale of the packages, the packages are defined to be securities, but since he's selling the packages to only a few people, he will not have to register them with the state.

(Kevin may, however, be guilty of violating ticket scalping laws.)

B. Only if Kevin will be selling the packages at or below cost are the packages not considered to be securities, in which case Kevin will not have to register them with the state.

C. The packages are not considered to be securities since each package is merely a purchase and sale agreement between Kevin and another person. There is no third party involved. Because they do not meet the definition of securities, Kevin does not need to register them with the state.

D. Statements A and B are both true statements.

Answer: C

Explanation

The packages are not considered to be securities since each package is simply a purchase and sale agreement between Kevin and another person, with no third party involvement; and since they are not securities, Kevin need not register them with the state. A buyer of one of the packages is not expecting to earn a profit on this investment "solely through the efforts of others," which is one of the defining characteristics of a security, as ruled by the U.S. Supreme Court in 1946.

NO.17 The Administrator of a state can deny an application if

A. the application is missing information.

B. the registrant has been enjoined from engaging in activities involving securities in another state.

C. the Administrator determines the applicant is not financially solvent.

D. any of the above is true.

Answer: D

Explanation

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

NO.18 Newbie Corporation is considering the possibility of an interstate initial public offering (IPO) of its stock. In the initial meetings with BigFee Investment Bankers, Newbie has learned that the underwriting spread will be

15%. Although the actual offering price won't be set until Newbie's registration statement is approved by the SEC, BigFee has indicated that the offer price will probably be between \$3 and \$4 a share and that the stock will initially be listed on the OTC Bulletin Board.

What methods for state registration does Newbie have available?

- I. registration by coordination
- II. registration by notification
- III. registration by qualification

A. Newbie may elect to register by any one of the above methods although registration by qualification would be the most burdensome choice.

- B.** Method I only
- C.** Methods I and III only
- D.** Method II only

Answer: C

Explanation

Newbie may apply for state registration using either the registration by coordination or the registration by qualification method, although the latter method is the most burdensome of the three. The firm is not eligible to register by notification. To be eligible, the offer price of the IPO would have to be at least \$5, and the underwriting spread would need to be no greater than 10%.

NO.19 Under the Uniform Securities Act (USA), the term "investment adviser" does not apply to

- I. an investment advisory firm owned and operated by a sole proprietor.
- II. a bank or savings institution.
- III. an investment adviser representative.
- IV. a broker-dealer or its agents if the advice is incidental to the business although there is a nominal charge for any specific investment advice given.

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

Answer: C

Explanation

The term "investment adviser" does not apply to Selections II or III. The term "investment adviser" does not apply to a bank or savings institution or to an investment adviser representative. Those persons are specifically excluded from the definition provided by the USA. Any investment advisory firm, regardless of whether it is owned and operated by a sole proprietor, is considered to be an investment adviser. A broker-dealer that charges for its investment advice, even if it claims that the advice is incidental to its business, would be considered an investment adviser due to the special remuneration the firm receives for its advisory services.

NO.20 Don is a state-registered agent with GetErDone Broker-Dealers. He has three other friends who are licensed agents-Huey, Dewey, and Louie. Huey is also an agent with GetErDone Broker-Dealers. Dewey is an agent with a different firm in the same city, CanDo Broker-Dealers. Louie works for a Broker-Dealer with an office just across the state line.

Don can enter a commission-splitting agreement with

- A.** Huey only
- B.** either Huey or Dewey or both
- C.** Dewey only
- D.** Either Huey, Dewey, or Louie or any combination of the three

Answer: A

Explanation

Don can enter a commission-splitting agreement with Huey only since he is the only one who is also working for GetErDone Broker-Dealers. It is considered unethical to split "commissions, profits or other compensation.

. .with any person not also registered as an agent for the same broker-dealer," under NASAA Model Rules.

NO.21 An investment adviser or its representative may

A. only exercise any discretionary power in the purchase or sale of securities for a client's account after receiving written authority prior to the execution of the transactions.

B. exercise discretionary power in the purchase or sale of securities for a client's account as long as it receives written discretionary authority over the account within 10 business days of the first discretionary transaction placed, assuming oral authority has already been given.

C. exercise discretionary power in the purchase or sale of securities for a client's account as long as.

D. exercise discretionary power in the purchase or sale of securities for a client's account only after.

Answer: B

Explanation

An investment adviser or its representative may exercise discretionary power in the purchase or sale of securities for a client's account as long as it receives written discretionary authority over the account within 10 business days of the first transaction placed, assuming oral authority has already been given.

NO.22 Which of the following describes a prohibited practice in the sale of shares of investment companies?

I. Sandy Slacker hands her client the fund's prospectus and tells him that the prospectus will provide him all that he needs to know about loads and fees associated with the fund.

II. Elliot Eager tells a client who has an investment objective that includes current income that a certain bond fund has a current yield of 8% and provides the client with a prospectus so that the client can peruse the average annual returns that the fund has generated in past years when the client has the time.

III. After explaining all the fees and loads involved in two different bond funds as well as the difference between current yield and total return, Patty shows the client the data on the average annual returns that the two bond funds provided. She explains to the client that the municipal bond fund has a lower yield than the similar-risk corporate bond fund because the interest income the client will receive from the municipal bond fund will be free from federal taxation, while the interest income on the corporate bond fund is fully taxable.

A. All the choices describe prohibited practices in the sale of shares of investment companies.

B. I only

C. I and II only

D. I and III only

Answer: C

Explanation

Only the scenarios described in Selections I and II represent prohibited practices. The NASAA rules state that it is not enough to hand a client a prospectus, but that the agent must fully explain all sales

charges and also to explain the difference between current yield and total return to the client and present that client with the fund's most recent average annual returns over the past year, 5-year, and 10-year periods. Sandy and Elliot have not done this in the scenarios described. In Selection III, Patty has done so and has also provided the client with accurate and useful information regarding why a municipal bond offers a lower yield than a corporate bond fund.

NO.23 Once a person has filed an application with the Administrator, and in doing so has truthfully disclosed every material fact, how long does the Administrator have after the effective date of the registration to commence a proceeding to deny, suspend, or revoke that person's license based on those facts?

- A. 30 days.
- B. 60 days.
- C. 90 days.
- D. one year.

Answer: C

Explanation

If a person has appropriately and truthfully disclosed every material fact on its application for registration, the Administrator has 90 days after the registration becomes effective to commence a proceeding to deny, suspend, or revoke the license. If the Administrator has known about the fact for longer than this, he may not begin a proceeding against that person according to the Uniform Securities Act.

NO.24 Ms. Muffet is employed by Spyder Broker-Dealers. Her job duties include providing price quotes and executing purchases and sales for the firm's clients. She is paid a salary plus commission. Ms. Muffet is

- A. a broker-dealer.
- B. an agent.
- C. an investment adviser.
- D. an investment adviser representative.

Answer: B

Explanation

As an employee of Spyder Broker-Dealers who executes trades for clients, Ms. Muffet is an agent who works for the broker-dealer Spyder. She does not provide investment advice for a fee, so she is neither an investment adviser nor an investment adviser representative.

NO.25 Which of the following does not describe a prohibited practice for investment advisers?

- I. The adviser sells its non-institutional clients securities that it has issued.
 - II. The adviser makes a discretionary trade for a client after receiving verbal authorization only and does not receive written authorization from the client within 10 business days of doing so.
 - III. The investment adviser requires an advisory fee of \$300 to be paid in advance at the beginning of each quarter.
- A. None of the selections describe prohibited practices.
 - B. I only
 - C. I and III only
 - D. II and III only

Answer: D

Explanation

Selections II and III do not describe prohibited practices. If an adviser makes a discretionary trade for a client after having received verbal authorization to do so and does not receive written authorization from the client within 10 business days of doing so, the adviser is limited to making recommendations to the client and executing unsolicited trades only, but he has not engaged in a prohibited practice, and this is the scenario described in Selection II. There is no provision that prohibits an adviser from requiring an advisory fee to be paid in advance as long as it is reasonable, as described in Selection III. An adviser is not permitted to sell its non-institutional clients securities it has issued itself because of the significant conflict of interest involved.

The exception is if the client is an institution that is in the business of lending money, but Selection I specifically indicates "non-institutional clients."