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**QUESTION 1**

You are an agent with a broker-dealer and have learned of limited partnership interests being sold by a small company that is planning to come out with a product that you think is going to "wow" the market. You would like to get in on the action, but the minimum investment needed is \$10,000, and you don't have that kind of dough lying around. You talk to your brother, who is also one of your clients, and get him interested in investing in the firm, too. The two of you decide to pull your money together, each putting in \$5,000, and you agree to split any profits or losses.

Is this permitted?

- A. Yes. This is permitted since the agreement is between you and a family member.
- B. Maybe. But it will require written consent from both your brother and your firm.
- C. Yes, as long as your brother provides your firm with his written consent.

Correct Answer: C

It may be permissible for you and your brother to open a joint account to invest in this partnership since he is a family member, but it will require the written consent of both your brother and your firm, and your firm is under no obligation to give its consent.

QUESTION 2

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.

Correct Answer: A

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.

QUESTION 3



A broker-dealer will be found guilty of churning an account if the account has a turnover ratio of

- A. four.
- B. five.
- C. eight.
- D. There is no specified turnover ratio assigned to the prohibited practice of churning.

Correct Answer: D

There is no specified turnover ratio assigned to the prohibited practice of churning since some investors are simply more frequent traders than others.

QUESTION 4

A bond issue has recently been registered with the state Administrator.

Which of the following statements are true?

- A. An investor can feel secure in buying the bond because it has recently been registered, which means that the state Administrator finds it to be of sound quality at this point in time.
- B. The bond may now be offered for sale in the state.
- C. The issuer may now offer this bond for sale, and any other bonds that the issuer may want to offer for sale in the future will be able to be sold after the issuer executes a notice filing.
- D. Both A and B are true statements.

Correct Answer: B

When a bond issue has been effectively registered with the state Administrator, it can be offered for sale in the state. The bond's acceptance by the Administrator simply means that the issuer has supplied enough information in order for an investor to judge the quality of the bond for himself; it in no way implies that the bond is of sound quality. It could, in fact, be a very risky security and still have met the registration requirements.

QUESTION 5

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.



Correct Answer: B

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.

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