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QUESTION 1

Painting the tape refers to

- A. the practice of buying large amounts of a security to drive its price up artificially.
- B. the illegal activity of a group of investors who buy and sell a security among themselves to create an artificially high volume of trading in hopes of luring investors to buy the security.
- C. the prohibited practice of excessively trading on a client's account that is used by some broker-dealers and/or their agents to generate more commissions for themselves.
- D. the unethical practice of investment advisers who issue "buy" recommendations for stocks that they own themselves without disclosing the fact.

Correct Answer: B

Painting the tape refers to the illegal activity of a group of investors who buy and sell a security among themselves to create an artificially high volume of trading in hopes of luring investors to buy the security. This is an attempt to manipulate the market and, as such, is illegal.

QUESTION 2

The Administrator of a state will deny the registration of a security if

- I. the mandated filing fee has not been paid.
- II. the compensation of the underwriters is excessive.
- III. the registration statement is incomplete.
- IV.

the issuer is registering the security through the registration by coordination process and has not complied with all the stipulated requirements.

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

Correct Answer: A



The Administrator of a state will deny the registration of a security under any of the situations described in Selections I, II, III, and IV-if the mandated filing fee has not been paid; if the compensation of the underwriters is excessive; if the registration statement is incomplete; or if the issuer is attempting to use registration by coordination and has not complied with all the stipulated requirements of that process.

QUESTION 3

Gazillions is an investment adviser with offices in the state that is registered with the SEC and has \$100 billion dollars under management. A client has filed a complaint asserting that the firm has been involved in fraudulent activities. In this case,

- A. Gazillions only has to answer to the SEC regarding the allegations. Since it is a federal covered investment adviser, it need not respond to any state-issued requests for information.
- B. Gazillions only has to answer to the state in which the complaint was filed.
- C. Gazillions has to answer to both the SEC and the state in which the complaint was filed.
- D. Gazillions is in trouble for not registering with both the state and the SEC given the amount of money it has under management.

Correct Answer: C

If Gazillions is operating as an SEC-registered adviser in a state, it must answer to both the SEC and the state in which the complaint has been filed, even though there is no requirement that it had to register with the state, given that it was a federal covered investment adviser. Allegations of fraud come under the state's authority as well, even if the adviser is a federal covered investment adviser.

QUESTION 4

Which of the following statements regarding an open-end investment company is not true?

- A. Its shares are bought and sold through the company.
- B. Its securities are federal covered.
- C. Its shares may sell for either net asset value or greater than net asset value, but not below
- D. Its shares are bought and sold on exchange floors.

Correct Answer: D

The shares of an open-end investment company are not bought and sold on exchange floors. An open-end investment company is a mutual fund, and its shares are bought and sold through the company. The price per share will be either at net asset value as is the case with a no load fund, or above net asset value, as is the situation with a load fund, when the price is equal to net asset value + the sales charge (load.) Open-end investment company shares are federal covered and, as such, do not need to be registered with the state.

QUESTION 5

An investment adviser suggests that his client, Arnold, a 74-year old gentleman, should consider a reallocation of the



assets in his portfolio. The adviser tells Arnold that he has far too much invested in bonds, which don't earn as much as stocks. He advises Arnold to take 80% of the money he has in bonds and invest it in an aggressive growth mutual fund that has provided an average annual return of 40% over the past three years. Arnold is impressed and follows this advice. Shortly thereafter, there is a steep drop in the market in general, and the net asset value of the aggressive growth mutual fund falls 85%.

Does Arnold have any remedies available to him?

- A. No. Arnold had the choice and got greedy. As the old saying goes, "Bulls get rich, and bears get rich, but pigs get led to slaughter."
- B. Yes. Arnold can sue for the amount of his losses, plus interest, as well as an amount assessed by the court for "pain and suffering."
- C. No. The investment adviser had no way of knowing that the market was going to fall when he provided the advice, so the adviser did not fail in his fiduciary responsibility to Arnold.
- D. Yes. Arnold can sue for the amount of his losses, plus interest, court costs, and attorneys' fees.

Correct Answer: D

If Arnold loses his money because he took the advice of his investment adviser and reallocated a large percentage of his money from bonds to an aggressive growth mutual fund, he can sue the investment adviser in civil court for the amount of his losses, plus interest, court costs, and attorneys' fees. The courts do not award damages for "pain and suffering" in these cases. The investment adviser failed in his fiduciary responsibility to Arnold in recommending that a 74-year old man reallocate a large percentage of his money from the relative safety of bonds to the much riskier investment of an aggressive growth mutual fund.

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