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FINRA Uniform Securities Agent State Law Examination

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**QUESTION 1**

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.

Correct Answer: A

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.)

QUESTION 2

MoeMoney Investment Advisers, LLC is registered in the state of Texas, and its three offices are all located in the greater Dallas-Fort Worth area. Five of its clients-all individuals-have relocated to Colorado and all have indicated a desire to retain the services of MoeMoney. In order for this to be possible,

- A. MoeMoney will need to apply for and be granted registration as an investment adviser in the state of Colorado.
- B. each client will have to write a letter to the Administrator of the state of Colorado on MoeMoney's behalf.
- C. MoeMoney will need to apply for and be granted registration as an investment adviser representative in the state of Colorado.
- D. Neither MoeMoney nor its clients need do anything.

Correct Answer: D

In order for MoeMoney to continue servicing its five individual clients who have relocated to Colorado, neither MoeMoney nor its clients need to do anything. The National Securities Markets Improvement Act of 1996 (NSMIA) established a "deminimis" exemption for investment advisers if they have no office in a state and do business with "no more than five non-institutional clients" during a one-year time frame.

QUESTION 3

Sam Shyster had his day in court-and lost. His license to do business as an investment adviser in the state has been revoked. What legitimate options does Sam have available to him now?

- A. Sam can move to another state and apply for registration as an investment adviser there.
- B. Sam has 45 days in which to file an appeal with the attorney general.



- C. Sam can register with the SEC as an investment adviser, which will exempt him from state registration requirements.
- D. Sam has 60 days to file an appeal of the decision in a court of law.

Correct Answer: D

Sam has the legitimate option of filing an appeal of the decision in a court of law within 60 days. He will not be able to register as an investment adviser with the SEC or with another state. His application will be denied when it is discovered that Sam has had his license revoked by one state.

QUESTION 4

Which of the following scenarios does not meet the definition of "custody" under NASAA Model Rules?

- A. An investment adviser is mistakenly sent a client's securities, but returns them to the sender within three business days of receipt.
- B. An investment adviser has general power of attorney for a client and is authorized to withdraw client funds or securities that are on deposit with a registered broker-dealer upon the investment adviser's request.
- C. An investment adviser receives a check from a client that is written to a mutual fund and forwards the check to the mutual fund within three business days of receipt.
- D. An investment adviser keeps a client's securities in its safety deposit box.

Correct Answer: A

If an investment adviser is mistakenly sent a client's securities, but returns them to the sender within three business days of receipt, he is not deemed to have taken custody of the securities under NASAA Model Rules. Custody is defined by the NASAA as "holding directly or indirectly, client funds or securities, or having any authority to obtain possession of them." Therefore, an investment adviser who has general power of attorney to withdraw a client's funds or securities from a broker-dealer is acting as a custodian, as is an investment adviser who keeps a client's securities in its safety deposit box. If an investment adviser receives a check from a client that is written to a third party, such as a mutual, that check must be forwarded within 24 hours of receipt, or the investment adviser is deemed to be a custodian.

QUESTION 5

Which of the following does not describe a prohibited activity by investment advisers and their representatives, according to NASAA Model Rules?

- A. A new client comes to Simon LaGree for investment advice. The client has \$25,000 to invest. Simon tells the client that it will cost the client \$5,000 to have a customized financial plan developed for him, but after that the client needs to pay only 5% of the total value of the assets under management each quarter.
- B. A 72-year-old retired social worker comes to Simon LaGree for investment advice. She has \$50,000 to invest. Simon recommends she invest half of it in an international growth mutual fund and half in a variable annuity.
- C. The agreement that Simon LaGree has his clients sign indicates that LaGree uses SecureMoney Broker-Dealers in executing trades for his clients and that, in return, LaGree receives software from the broker-dealer that allows LaGree to perform some fundamental and technical analysis.
- D. All of the above describe prohibited practices.



Correct Answer: C

It is not prohibited for LaGree to receive the software from SecureMoney in return for executing trades through that broker-dealer since LaGree has disclosed this to his clients. An investment adviser is permitted to receive soft dollars from broker-dealers in return for executing trades through them, as long as the client is informed of the arrangement and the soft dollars will benefit both the client and the adviser, which is the case in this instance since the software gives LaGree the ability to do research in order to better advise his client. Choice A is clearly prohibited since it constitutes an "unreasonable advisory fee." In Choice B, LaGree is making unsuitable recommendations to his client. A 72-year-old retired social worker is likely to have a greater-than-average need for liquidity to pay for unexpected items, such as medical bills. Variable annuities are designed to be long-term investments, not short-term investments, so they would not meet this need. They typically have high surrender penalties that the client would be subject to if she needed to make withdrawals within, say, the next 10 years. Likewise, international growth funds are not liquid investments. International growth mutual funds are invested in foreign stocks and are riskier than average, and are, thus, not suitable investment vehicles for the typical 72-year-old retired social worker.

QUESTION 6

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.

Correct Answer: C

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.

QUESTION 7

Which of the following laws deals with identity theft protection?

- A. the Bank Secrecy Act (BSA)
- B. the USA Patriot Act
- C. ERISA
- D. Regulation S-P



Correct Answer: D

Regulation S-P was enacted by the SEC to deal with identity theft. The law requires financial institutions to provide their clients with a statement of its privacy policies and practices and prohibits the disclosure of nonpublic personal information about even a prospective client to a nonaffiliated third party unless certain conditions are met, including giving the client or prospective client the right to opt out of the disclosure.

QUESTION 8

Noah Scruples, an agent with CanDo Broker-Dealers, just got a copy of the most recent report on a certain stock. The report was generated by CanDo's analyst department and is hot off the presses. It has not yet even been put on the firm's website for the firm's clients.

The analyst department has just changed its recommendation on the stock from "Hold" to "Strong Buy" based on new information that it has obtained on the company.

Can Noah rush to his office to buy shares of the stock before the analysts release their reports to CanDo's clients?

- A. Yes. The firm's analysts used publicly available information to assess the stock and make its recommendation, so Noah can buy the stock now on his own account.
- B. No. It is unethical for him to trade based on this information before the firm's clients have received the information.
- C. No. This is a prohibited activity referred to as "painting the tape."
- D. Both B and C are true statements.

Correct Answer: B

No. It is unethical for him to trade based on the information that just came from the analysts before the firm's clients have the information. This is a prohibited practice called "front running."

QUESTION 9

In accordance with the Telephone Consumer Protection Act of 1991 (TCPA), if a prospective client requests to be put on your firm's Do-Not-Call (DNC) list, the client must be kept on that list for

- A. 1 year.
- B. 2 years.
- C. 5 years.
- D. 10 years.

Correct Answer: D

If a prospective client requests being put on your firm's DNC list, you must keep that name on your list for 10 years, according to the TCPA.

QUESTION 10



Which of the following does not describe a prohibited practice for broker-dealers under the NASAA Model Rules?

I. SecureMoney Broker-Dealers has received a request from a client who wants SecureMoney to "identify a few solid firms in the Asian market and invest up to \$20,000 in them." SecureMoney executes the purchases and receives the requisite signed discretionary authorization from the client before the settlement date.

II. CanDo Broker-Dealers executes a margin transaction for a client, promptly receiving a signed, written margin agreement from the client after the transaction takes place.

III.

GetErDone Broker-Dealers receives a call from a client who wants to purchase some securities on margin. GetErDone has the client come into the office to sign a properly executed margin agreement prior to effecting the transaction.

A.

None of the selections are prohibited practices.

B.

I and III only

C.

II and III only

D.

III only

Correct Answer: C

Neither Selection II nor Selection III describes a prohibited practice for broker-dealers under the NASAA Model Rules. Broker-dealers are permitted to execute margin transactions for clients as long as they receive a signed, written margin agreement promptly after the initial margin transaction takes place. The agreement need not be signed beforehand. Discretionary authorizations do need to be signed before the broker-dealer executes any discretionary transactions for a client, so Selection I describes a prohibited practice.

QUESTION 11

The Turnover Corporation, a firm with 25,000 employees, has recently hired 50 new employees, many of whom have been hired to replace middle-level managers who have retired. Turnover has omitted this fact from its prospectus. Turnover is guilty of

A. fraud.

B. misrepresentation.

C. misusing insider information.

D. nothing. The hiring of 50 new employees by a firm with 25,000 employees is not a material fact.

Correct Answer: D

Turnover is guilty of nothing when it hires 50 new employees, but doesn't include this information in its prospectus



because this is not a material fact. Most of the employees have been hired to replace middle-level managers who have retired, and these employees wouldn't be considered significant enough to affect the price of the stock in any way. If Turnover had hired a new CEO, that would be a material fact that must be disclosed.

QUESTION 12

Which of the following scenarios would not be considered a "sale," as defined by the Uniform Securities Act (USA)?

I. Yoshito owned shares of Minnow Corporation and received shares of Whale Corporation from Whale when it merged with Minnow.

II. Olivia's uncle, an agent with SecureMoney Brokers, sold Olivia ten call options on the stock of Microsoft.

III. Hans purchased a bond of Indebted Corporation that had detachable warrants and subsequently sold the warrants.

IV.

Tom pledged some shares of stock he owned personally to secure a business loan for his company.

A.

Neither I nor II would be considered sales.

B.

Neither II nor III would be considered sales.

C.

Neither I nor IV would be considered sales.

D.

Neither III nor IV would be considered sales.

Correct Answer: C

Neither Scenario I nor Scenario IV describes sales as defined by the USA. When an investor receives securities from Company X when Company X merges with a company in which the investor owns stock, Company X is not considered to have sold those securities to the investor. Likewise, when a person uses securities he owns as collateral for a loan, the USA does not consider this to be a sale of the securities.

QUESTION 13

An investment adviser may not

A. also be registered as a broker-dealer in the state.

B. accept any kind of soft dollar compensation for using certain broker-dealers to execute trades on their clients' accounts.

C. take a position-either long or short-in securities in which any of its clients have a position.



D. recommend a stock to a client that the adviser itself holds without disclosing to the client that the adviser owns the stock.

Correct Answer: D

An investment adviser may not recommend a stock to the client that the adviser holds without disclosing to the client that it owns the stock. They are permitted to also be registered as a broker-dealer in the state and to accept certain types of soft dollars as compensation from brokers. And they can have positions in securities that their clients have positions in-just as long as this is disclosed.

QUESTION 14

Which of the following actions is the Administrator of a state empowered to take?

- A. gather evidence
- B. require restitution for the victims of a scam
- C. impose civil penalties in cases of fraud
- D. The Administrator of a state has the authority to take all of the above actions.

Correct Answer: A

The Administrator of a state can gather evidence, but it cannot impose any civil penalties, including the requirement of restitution to victims. These actions can only be performed by a court of law.

QUESTION 15

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.

Correct Answer: A

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.



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