1. (C) The licenses of all agents, broker-dealers, investment advisers, and investment adviser representatives expire each year on December 31st and must be renewed at that time to remain effective. Renewal is accomplished by paying a filing fee. The fact that the registration fee was paid in October or that the broker-dealer went out of business in September is not relevant. If a registration fee is paid in the middle of the year, the fee is usually not prorated.

2. (B) Every applicant whether an agent, broker-dealer, investment adviser, or investment adviser representative must pay a registration fee. This fee is paid when an applicant files the initial application as well as when the license expires each year on December 31. If a registration fee is paid in the middle of the year, the fee is usually not prorated.

3. (A) Advisers with assets of $30 million or more must register with the federal government and are known as federal covered advisers. Advisers with assets between $25 and $30 million may register with the federal or state government. Those with fewer assets generally fall under state jurisdiction. Although states may not require registration of a federal covered adviser, advisers are required to pay both an initial and renewal filing fee in the states in which they transact business.

4. (B) If a firm meets the definition of a broker-dealer, it is generally required to register in any state in which it effects transactions in securities. The term broker-dealer, however, does NOT include:
   - Agents
   - Issuers
   - Banks, savings institutions, and trust companies (though banks, holding companies, or bank subsidiaries are not excluded from the definition)
   - A person that has no place of business in the state AND only transacts business with issuers, other broker-dealers, financial institutions, or institutional buyers
   - A person that has no place of business in the state AND is licensed where the person maintains its place of business and sells only to existing clients who are not residents of the state

   There is no de minimis exemption for broker-dealers with no place of business in a state and a limited number of noninstitutional clients. There is also no exemption based on the type of securities in which the broker-dealer transacts business in a state.

5. (C) Since the statute of limitations for civil liabilities under the USA is limited to three years from the occurrence of the sale or within two years of discovery, whichever comes first, any surety bond required must be maintained to enforce any liability under the Act. Under the registration requirements, when a surety bond is required, the administrator will stipulate that the bond must provide for any suit brought by a client even though the registrant is no longer in business.

6. (D) Under the provisions of the Uniform Securities Act, every cause of action survives the death of any person who might have been a plaintiff or defendant. The client may file the suit in State A and need not file the civil suit in the state where the firm is headquartered. The statute of limitations for civil liabilities under the USA is three years from the sale or rendering of investment advice, or within two years of discovery. Therefore, the suit may be filed and the customer may recover damages. (The client still has one year left to file.)
7. **(D)** Under the Uniform Securities Act, banks, trust companies, and saving institutions are specifically exempt from the definition of investment adviser. There is no specific exemption for insurance companies.

8. **(B)** Under the Investment Advisers Act, the following persons are exempt from the definition of investment adviser:
   - A bank or any bank holding company that is not an investment company
   - Any lawyer, engineer, accountant, or teacher whose advice is incidental to her profession
   - Any broker-dealer whose advisory services are incidental to its business as a broker or dealer
   - Any bona fide publisher
   - Any person whose advice is limited to securities that are direct obligations of the U.S. government or guaranteed by the government

   A bank holding company that is an investment company is not exempt from the definition of an investment adviser.

9. **(A)** According to SEC Release 1092, the professional exclusion provided by the Advisers Act is only available to lawyers, accountants, engineers, and teachers. A person engaged in any other profession who performs investment advisory services would be considered an investment adviser, whether or not the performance of investment services is incidental to the practice of her profession. However, other exemptions under the Act may be available to professionals, e.g., accountants and lawyers. The Act does not provide a specific exemption to a marketing firm. For example, a firm that markets financial planning services does not have an exemption from the definition of investment adviser and may be required to register.

10. **(B)** Submission of Form ADV-E with the SEC is required if the adviser has custody of client funds and securities. The form is filed by an independent public accountant hired by the adviser who has audited the adviser’s records. Form ADV-H is filed by an adviser seeking an exemption for a temporary or continuing hardship. Form ADV-NR is filed by a nonresident general partner or nonresident managing agent of a U.S. registered investment adviser. Form ADV-W is filed by an adviser that is either seeking a partial or full withdrawal from registration.

11. **(C)** Submission of Form ADV-E with the SEC is required if the adviser has custody of client funds and securities. The form must be filed by an independent accountant, not the adviser, within 30 days after the completion of the audit.

12. **(C)** Under the USA, the term broker-dealer does NOT include any person that has no place of business in the state AND only transacts business with issuers, other broker-dealers, financial institutions, or institutional buyers. If a firm has an office in State B, it would meet the definition of a broker-dealer in State B regardless of the clients it sells securities to or conducts business with. Whether or not the other broker-dealers or institutional clients have an office in State B is irrelevant, since XYZ has an office in State B. There is no exemption from the definition of broker-dealer in a state if you sell securities to high net worth individual investors since they are not considered institutional buyers.
13. (A) Under the USA, the term broker-dealer does NOT include any person that doesn’t have a place of business in the state AND only transacts business with issuers, other broker-dealers, financial institutions, or institutional buyers. Since CMP is opening an office in North Carolina, the firm would need to be registered in that state regardless of the clients it sells securities to or conducts business with. Since the broker-dealer will be registered in North Carolina, any agent of that broker-dealer effecting transactions in that state would also need to be registered.

14. (B) Books and records must be maintained in an easily accessible place for five years. During the first two years, the records must be maintained in an appropriate office of the investment adviser. Records may be preserved on microfilm, microfiche, or any similar device. They may also be kept on various electronic storage media such as CD-ROMs, provided the disks are tamper-evident (write once read many). This means that any attempt to alter the records would become obvious and easily determined upon examination. These files do not need to be password-protected, but the adviser must be able to limit access to the records to authorized personnel and regulators.

15. (D) Books and records must be maintained in an easily accessible place for five years. During the first two years, the records must be maintained in an appropriate office of the investment adviser. Records may be preserved on microfilm, microfiche, or any similar media. They may, but are not required to, be kept on various electronic storage media such as CD-ROMs, provided the disks are tamper-evident—i.e., the information cannot be easily altered. This means that any attempt to alter the records would be easily determined upon examining them. These files do not need to be password-protected, but the adviser must be able to limit access to the records to authorized personnel and the regulators.

16. (C) Any investment adviser subject to the registration provisions of the Advisers Act is also required to keep certain records. Some of the records required include a copy of each written statement sent to a client, a copy of the investment adviser’s code of ethics, and a memorandum of each order to purchase or sell a security. There is no requirement to keep a copy of each prospectus sent to a client.

17. (D) Any investment adviser subject to the registration provisions of the Advisers Act is also required to keep certain records. Some of them include a record of any violation of the investment adviser’s code of ethics, all written agreements entered into by the investment adviser and clients, and originals of all written communication sent by the adviser relating to recommendations. The adviser is required to keep a copy of each notice, circular, advertisement, investment letter, or other communication that is circulated to 10 or more persons. If the communication recommends the purchase or sale of a specific security but does not state the reason for it, a memorandum must be prepared indicating the reason for the recommendation.

18. (C) Under the Uniform Securities Act, the term broker-dealer does NOT include any person that has no place of business in the state AND only transacts business with issuers, other broker-dealers, financial institutions, or institutional buyers. Since Big Chill will no longer have an office in North Carolina, the firm would not need to be registered in that state unless the clients it sells securities to or conducts business with are noninstitutional investors. Since the broker-dealer will not be registered in North Carolina, any agent of that broker-dealer effecting transactions in that state would not need to be registered.
19. (C) NSMIA, the National Securities Markets Improvement Act, was created to eliminate some of the dual requirements of federal and state securities law. The federal government and the states have a division of responsibility when regulating investment advisers. In general, an adviser must be registered with either the SEC or with one or more states. There is no requirement to register at both the federal and state levels. The basis for the federal/state division is usually the amount of assets under management, not the type of clients the adviser has. Advisers with assets of $30 million or more must register with the federal government, while those with fewer assets fall under state jurisdiction. (Note: An IA may also choose to register with the SEC if it has between $25 million and $30 million under management.) An adviser registered with the SEC is referred to as a federal covered adviser and is exempt from state registration. Investment advisers with less than $25 million of assets under management are generally exempt from federal or SEC registration and are required to register at the state level. If the state in which the adviser conducts business does not provide for the registration of investment advisers, the IA must register with the SEC.

20. (A) Any investment adviser subject to the registration provisions of the Advisers Act is required to keep certain records. Ledgers are used by the firm for accounting purposes. E-mail is used as a means of communication between the firm and clients. Trade tickets are used to record all orders for the purchase and sale of securities. There is no requirement that an investment adviser or broker-dealer retain a copy of a client’s tax return.

21. (B) Under the Uniform Securities Act, agent means any individual (other than a broker-dealer) who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities. Excluded from the definition is an individual who represents an issuer in effecting transactions in certain exempt securities or who represents an issuer in exempt transactions. If you represent an issuer and sell commercial paper in denominations of at least $50,000 that matures within nine months of the date of issuance, you are exempt from the definition of agent. There is no specific exemption if you represent an issuer and sell corporate debt or equity securities. If you represent an issuer and sell securities to institutional investors or fiduciaries, you would not meet the definition of agent.

22. (D) Under the Uniform Securities Act, agent means any individual (other than a broker-dealer) who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities. Excluded from the definition is an individual who represents an issuer in effecting transactions in certain exempt securities or who represents an issuer in exempt transactions. Since Zack is representing an issuer and selling a certain type of exempt security (securities issued by a federally chartered bank), he would not meet the definition of agent under any circumstances (whether selling to institutional and/or retail investors).

23. (D) According to SEC Release 1092, lawyers who hold themselves out to the public as providers of financial planning services would meet the definition of an investment adviser. In these circumstances, the advice provided by the lawyers would no longer be incidental to their law practice.

24. (A) Applying the three-part test for an investment adviser, Robin is giving clients investment advice. She is recommending that they buy variable annuities, which are securities. She is in the business of providing this advice. (It does not matter that she only works part-time; she is performing this activity on a regular basis.) She is receiving compensation for these services in the form of fees for creating these financial plans. However, Robin is performing these activities as an employee of Jon and Jamie Financial Planning. Presuming that her firm is registered as an investment adviser, Robin would be defined as an investment adviser representative, while Jon and Jamie Financial Planning would be the investment adviser.
25. (D) Morg must register in Maine and Massachusetts since a firm must register in any state in which it maintains an office regardless of the number of clients it has. Morg must also register in every state in which it has more than five retail clients—it has six retail clients in Vermont. It does not need to register in New Hampshire since only four of its clients there are retail investors—the other six are institutions and the firm does not maintain an office in that state.

26. (C) Under NASAA’s Statement of Policy on Unethical Practices of Investment Advisers, it is unethical to misrepresent the qualifications of the adviser or any employee. Advisers must consider how the wording of their ads will be interpreted by the public and how it could be misleading. Since the advertisement states that the partners, not all employees, have earned their CFP certification, this is acceptable since the statement is true.

27. (B) The initials IAR (investment adviser representative) may not be used. The abbreviation could signify that the individual has met some type of regulatory qualification. The use of the designation IAR (investment adviser representative) is improper since it is not a designation approved by any professional organization. An IAR only needs to file with the state administrator. A CPA (certified public accountant) and a CFP (certified financial planner) may be abbreviated since this qualification requires a person to meet specific standards and pass a number of examinations. MBA (Master’s of Business Administration) may also be abbreviated since the person has obtained a degree from a college or university.

28. (A) The initials IAR (investment adviser representative) or RIA (registered investment adviser) may not be used. The abbreviation could signify that the individual has met some type of regulatory qualification. A registered investment adviser only needs to file with the SEC or the state administrator. An investment adviser representative only needs to file with the states with which he is required to be registered.

29. (C) Failure to notify a superior of a written customer complaint is an unethical business practice, rather than an illegal activity, even though the allegation in the letter is of an illegal activity. A careful reading of choice IV shows that the IAR of the investment adviser provided material public information to a client. It would be insider trading if the information supplied was not available to the public. There is nothing unethical or illegal in providing this information. The intentional misrepresentation of a registered person’s qualifications with the intent to deceive constitutes fraud. It would be a more subjective case if the agent had only described himself as an expert in the field. In the case described, displaying a fictitious certification with the intent to deceive and to induce an action creates a fraudulent condition. Common law deceit is the broadest described form of fraud. It is derived from English common law.

30. (D) Regarding specific standards, investment adviser advertising may not refer, directly or indirectly, to any testimonials about the adviser or its services. A testimonial is an advertisement in which an individual recommends the investment adviser’s services based on personal experiences with the adviser. Testimonials are prohibited whether or not the client signs any document, the advertisement is filed with a regulator, or any disclosure is made concerning the persons quoted in the testimonial.
31. (A) Advertising by investment advisers is expected to meet the standards set out in the rules under the Uniform Securities Act. Investment adviser advertising may not:

1. Contain a testimonial of any kind
2. State that any report, analysis, or other service will be furnished free or without charge, unless these items are, in fact, free and are furnished entirely without any condition or obligation
3. Contain untrue statements of material fact, or be false or misleading in any way.

IAs may include a list of all of their recommendations with the name of the security, the date, any bias in the recommendation (buy, sell, or hold), the market price at the time the recommendation was made, and the current market price of the security. A top-20 list would not meet these criteria.

Since the clients of the firm will receive free research without spending a specific amount of money, this would be permissible. Choice (C) is not permitted since the adviser would be listing its best, not all, recommendations.

32. (C) Regarding specific standards, investment adviser advertising may not refer, directly or indirectly, to any testimonials about the adviser or its services. A testimonial is an advertisement in which an individual recommends the investment adviser’s services based on personal experiences with the adviser. Testimonials are prohibited whether or not the clients consented to allowing their names to be disclosed. There is no prohibition against listing the name(s) of clients or employees of the adviser along with their professional designations.

33. (B) NASAA’s Statement of Policy on Unethical Business Practices of Investment Advisers states that investment advisers may accept verbal authorization to exercise discretionary authority over client accounts for up to 10 days. However, written discretionary authorization must then be received from the client within the 10-day period. If it is not obtained, the adviser may not continue to exercise discretion. Since the trip is longer than 10 days she needs to provide written authorization prior to her return. There is no requirement to provide written authorization for each order for an account in which written authorization has been signed by a client.

34. (D) NASAA’s Statement of Policy on Unethical Business Practices of Investment Advisers states that any notice, circular, or report is considered advertising whether or not it is delivered by written or electronic means. An adviser is permitted to include a listing of all recommendations provided the following conditions are met. The adviser furnishes a list of all recommendations it has made within the immediately preceding period of not less than one year and (i) states the name of each such security recommended, the date and nature of each such recommendation (e.g., whether to buy, sell, or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each such security as of the most recent practicable date, and (ii) contains the following cautionary legend on the first page: “It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.”

Advertising does not need to be filed with the SEC or the state prior to being disseminated and may be sent to both existing and potential clients.

35. (A) Before taking steps to evaluate the investment (such as checking the general partner’s track record), you must determine whether the product is being sold legally under the Securities Act of 1933. Choices (B), (C), and (D) address this issue. The manager also should be concerned about whether the rules regarding private securities transactions have been followed.
36. (A) Effecting client transactions that are not recorded on the books and records of the agent’s employer is a prohibited practice, regardless of the type of security or client involved. These are securities transactions outside the regular course or scope of an agent’s employment with a broker-dealer. The agent must provide written notice to Integrated indicating the nature of the transaction. Integrated must approve her participation and acknowledge that she will be paid a fee. Since the agent is receiving compensation, Integrated must record the transaction on its books and properly supervise the agent’s activities.

37. (C) Certain provisions are required in investment advisory contracts. One provision requires the adviser to notify clients of any change in the membership of the partnership within a reasonable period. Whether or not the partners manage Carrie’s assets is not relevant to the notification provision. It would be a good business practice for Closter to notify Carrie if the person that manages her assets leaves the firm, but it is not required since that person is not a partner.

38. (D) An investment advisory contract may not be assigned without the client’s consent. Assignment is defined if there is a change in the management or control of the adviser. The death or resignation of a majority of the partners or partnership would result in an assignment. Assignment is also defined as a change in the majority of the voting stock, such as another firm purchasing a majority of the stock of the advisory firm. If an IAR leaves the firm or passes away, this would not be considered a change in control and the contract may be assigned without the client’s consent.

39. (D) If a broker-dealer represents that a security is being offered at a price that represents the current market price, the broker-dealer must have reasonable grounds for making this statement to a client. If the broker-dealer claims it is a top market maker and the security is traded on the bulletin board, this may not be considered the current market price. If a broker-dealer made this statement to a client without proper disclosure of this fact, it would be considered an unethical business practice. If the security is listed on the NYSE or Nasdaq, the fact that a broker-dealer is not a market maker is not relevant since this will still represent the current market price.

40. (B) An investment advisory firm must keep all information concerning its clients confidential. It may release the information only if required to do so by law or with the client’s approval. The SEC and IRS are regulatory agencies that could obtain the information from the adviser without the client’s approval. The Financial Planning Association is a trade association and not a regulatory agency.

41. (B) It is considered fraudulent for a broker-dealer to fail to notify a client of larger-than-ordinary commissions or costs. Purchases or sales of a small amount of securities can often lead to larger than ordinary costs because of minimum charges assessed for transactions. This can lead to commissions that are large as a percentage of the purchase price. It is not illegal to assess such charges, but it is illegal not to inform the client about them. Charging a client an unreasonable commission is prohibited.

42. (A) It is considered an unethical business practice for a broker-dealer to charge an unreasonable fee for transactions or services performed. A small service fee might be acceptable but not one that is twice the amount of the commission. While there is no requirement to receive the client’s permission or to notify the client in writing prior to the trade, the fee should be disclosed on the confirmation.
43. (D) NASAA’s Statement of Policy on Unethical Business Practices provides that the entering into, or renewal of, an investment advisory contract would need to include disclosure of:

- All fees and services provided
- The term of the contract
- A formula for computing the advisory fee
- The amount of prepaid fees to be returned in the event of an early termination of the contract
- The fact that no assignment of the contract will be made without the consent of the client
- Whether the contract grants discretionary power to the adviser
- The fee for managing equity securities may be higher than for fixed-income securities

Choice II is true since the contract may be assigned with the consent of the client. Choice III is not true since some amount of prepaid fees should be returned if the contract is terminated.

44. (C) Investment advisory contracts must provide that:

- The adviser will not be compensated on the basis of a share of the capital appreciation of the account.
- The adviser may not assign client contracts without the consent of the client.
- If the adviser is a partnership, clients will be notified of changes in the partnership within a reasonable period.

It is perfectly acceptable to refund advisory fees if an advisory contract is terminated and to charge a fee based on the total value of the account ($150,000). There is no requirement to notify clients if three new portfolio managers (who are not partners or owners) are hired by the firm.

45. (B) The Advisers Act allows an investment adviser to pay a fee to an unaffiliated person for the solicitation of advisory clients if certain conditions are met. The adviser must be registered, not the solicitor, and there must be a written agreement between the solicitor and the investment adviser. The agreement between the adviser and solicitor must describe the solicitation activities and compensation arrangement. The solicitor disclosure document must give the names of the adviser and solicitor, the nature of the relationship, the terms of the compensation, and any amount charged to the customer above the adviser’s normal fee to pay for the solicitation of the account. Ted needs to disclose the amount of compensation he will be receiving. The amount of compensation paid by the client who is introduced by a solicitor may be higher than that paid by a client who comes directly to the adviser as long as it is disclosed.

46. (D) In a soft-dollar arrangement, an investment adviser sends client transactions to a particular broker-dealer even though that broker’s commissions may not be the lowest ones available in the market. In return, the investment adviser receives research or other services from the broker-dealer. In these arrangements, the clients of the investment adviser should be able to benefit by using the services of this broker-dealer as compared to a broker-dealer charging lower commissions. There is no requirement for the adviser to reduce its fee or obtain the client’s prior written consent.
47. **(A)** Concerning soft-dollar arrangements, the SEC interprets research and brokerage services to include research as well as anything that helps the investment adviser to effect securities transactions or to perform related functions such as clearance, settlement, and custody. The key is that the service that the adviser receives as part of a soft-dollar arrangement must benefit its clients. Some examples of allowable services include traditional research reports and other related publications, discussions with research analysts concerning the securities they cover, portfolio analysis software, attendance at a conference or seminar where corporate executives discuss their company’s performance, market and economic data services, and certain trading software. The permissible uses of soft dollars do not include accounting fees, advertising and marketing expenses, the adviser’s travel expenses, meals or entertainment, overhead and administrative expenses, employee salaries, marketing, professional licensing fees, computer terminals, and the correction of trading errors.

48. **(C)** Failing to furnish a client that has purchased shares of a new issue with a prospectus is an unethical and/or dishonest business practice by a broker-dealer and/or an agent. The responsibility to furnish this document falls on the broker-dealer that sold the security to the client.

49. **(B)** An agent of a broker-dealer that will be marketing a new issue of securities must provide any potential client with a preliminary prospectus and any additional documentation that the issuer files with the appropriate regulators. The additional information is sometimes referred to as a prospectus supplement. There is no requirement to provide a client with the underwriting spread (the difference between the public offering price and the proceeds to the issuer). The new issue is not priced until the effective date and the final prospectus will disclose the underwriting spread.

50. **(D)** Failing to disclose that a broker-dealer is affiliated with or controlled by an issuer of securities is considered a dishonest and/or unethical business practice. The agent would need to disclose the affiliation before entering into any contract with a customer to buy or sell securities. The disclosure may be made verbally prior to the trade if written disclosure is made at or before the completion of the transaction (usually the settlement date). The disclosure would need to be made to any account of a broker-dealer.

51. **(A)** Failing to disclose that a broker-dealer is affiliated with or controlled by an issuer of securities is considered a dishonest and/or unethical business practice. The agent would need to disclose the affiliation before entering into any contract with any client that will be purchasing the variable annuities. The disclosure may be made verbally prior to the trade if written disclosure is made at or before the completion of the transaction (usually the settlement date). The broker-dealer or insurance company is not required to refund any fees charged to clients.

52. **(D)** Failing to disclose that a broker-dealer is affiliated with or controlled by an issuer of securities is considered a dishonest and/or unethical business practice. The agent would need to disclose the affiliation before entering into any contract with a customer to buy or sell securities. The disclosure may be made verbally prior to the trade if written disclosure is made at or before the completion of the transaction (usually the settlement date). The disclosure would need to be made to any account of a broker-dealer.
53. (C) It is considered an unethical business practice by a broker-dealer to fail to make a bona fide offering of securities when acting as an underwriter or member of a selling group in the distribution of securities. Selling part of an oversubscribed offering to employees of the broker-dealer may be considered a failure to make a bona fide offering. Clients should receive an allocation on an oversubscribed offering prior to employees of broker-dealer W. Municipal securities can be suitable for:

- Nonresidents of a state
- Retail investors, whether or not they are residents of the state
- Institutional investors

54. (D) It is considered an unethical business practice by a broker-dealer to fail to make a bona fide offering of securities when acting as an underwriter or member of a selling group in the distribution of securities. None of the broker-dealers would be allowed to exclusively offer its allotments to hedge funds since this would exclude all other investors and would not be considered a bona fide offering.

55. (B) According to the Investment Advisers Act of 1940, every registered adviser is required to have written policies and procedures that reasonably prevent violation of the Act. Although the written policies and procedures will vary depending on the nature of the adviser’s business, some of the issues that should be addressed include preventing the misuse of material nonpublic information, trading practices including allocation of trades to client accounts and best execution, safeguarding the privacy of client records and information. There is no reason why an adviser would need to have a policy that prohibits its employees from providing tax advice. The advice would need to be suitable for the client.

56. (A) According to the Investment Advisers Act of 1940, every registered adviser is required to have written policies and procedures that reasonably prevent violations of the Act. One of the policies must include the prevention of misuse of material nonpublic information. This would include having prohibitions against trading portfolio securities based on information acquired by other fiduciaries employed by the investment adviser.

It would be acceptable for an employee of an adviser (a portfolio manager) to buy the same security as a fund she manages after the shares are purchased for the fund. Buying the shares for a personal account prior to buying shares for the fund, or buying the shares for a fund after learning that affiliated persons will be buying shares would be a violation of the Act.

57. (B) According to the Investment Advisers Act of 1940, every registered adviser is required to have written policies and procedures that reasonably prevent violations of the Act. One of the policies must include the prevention of misuse of material nonpublic information (insider trading). There is no exemption if the adviser is also a broker-dealer, or only manages funds investing in exempt securities.

58. (D) Any investment advisory contract that attempts to bind any person to transactions that are not permitted under the Act is null and void. Even if the client signs the contract, and the transactions are disclosed, the contract is void.

59. (A) A client purchasing mutual funds is required to pay taxes on the distributions regardless of whether they are reinvested in additional shares. The amount of tax will be determined based on the current tax rate on dividends and capital gains applicable to the client.
60. (C) Although many people view Treasury securities as risk-free, they are not totally free of all types of risk. Treasuries have no credit risk since they are backed by the U.S. government. They are subject to inflationary (purchasing power) risk as well as market risk. The value of Treasuries could increase or decrease prior to maturity based on changes in interest rates.

61. (C) This case is an example of a contingent fee, which generally includes any arrangement in which the adviser’s fee depends on attaining a specific level of capital gains or appreciation (or avoiding capital losses or depreciation). The SEC considers contingent fees a type of performance fee, which are generally prohibited in advisory contracts. Exceptions include contracts for clients who have at least $750,000 under management with the adviser, or clients who have a net worth in excess of $1,500,000. Since the client has a net worth of $2,000,000, she would qualify for this exception.

62. (C) Under the Investment Advisers Act of 1940, performance fees are generally prohibited. Exceptions include contracts for clients who have at least $750,000 under management with the adviser or who have a net worth in excess of $1,500,000. There is also an exception if the client is an executive, a partner, or a knowledgeable employee of the adviser. The amount of funds under management is not a factor for these clients. The type of account—individual, joint, or IRA—is also not a factor.

63. (D) Under the Investment Advisers Act of 1940, performance fees are generally prohibited. Exceptions include contracts for clients who have at least $750,000 under management with the adviser or who have a net worth in excess of $1,500,000. They would be defined as qualified clients. Registered investment companies, clients that are not U.S. residents, and certain employees of the adviser may also be charged performance-based fees. The SEC does not need to approve the method used to calculate the fee, but it must be disclosed to clients.

64. (A) The adviser is not charging a performance-based fee in this question. Under the Investment Advisers Act of 1940, an advisory contract may provide for compensation based on the total value of a fund or account over a definite period. The fee the client paid increased, not because the fee percentage increased, but due to the assets or total value of the account increasing. No violation has occurred. If the fee percentage increased due to the performance of the account (a performance fee), it would be allowed only if this information was properly disclosed and the account was held by a qualified client.

65. (D) An adviser is permitted to use a broker-dealer to execute transactions in exchange for certain services. The term is referred to as soft dollars and it is defined as a means of paying brokerage firms for their services through trade commissions. The key here is that the services that the adviser receives as part of a soft-dollar arrangement must benefit its clients. Some examples of allowable services would include traditional and third-party research reports and other related publications, discussions with research analysts concerning the securities they cover, portfolio analysis software, attendance at a conference or seminar where corporate executives discuss their company’s performance, market and economic data services, and certain trading software. The permissible uses of soft dollars do not include compliance or administrative assistance, advertising and marketing, the adviser’s travel expenses, meals or entertainment, overhead and administrative expenses, employee salaries, marketing, professional licensing fees, computer terminals, and the correction of trading errors.
66. (B) An adviser is permitted to use a broker-dealer to execute transactions in exchange for certain services. The term is referred to as soft-dollars and it is defined as a means of paying brokerage firms for their services through trade commissions. The key here is that the services that the adviser receives as part of a soft-dollar arrangement must benefit its clients. The broker-dealer is permitted to pay for the cost of the conference that an adviser attends concerning securities within an industry in which the adviser will be invested. Travel costs and any costs that should be paid by the adviser (e.g., salaries of the adviser’s internal research staff) are not covered under a soft-dollar arrangement. Whereas the cost of the computer terminals could not be paid for with soft dollars, the cost of the data services would be covered by soft dollars.

67. (A) Under the USA, a nonissuer transaction may be exempt from registration if the issuer is engaged in business, whether or not the company is profitable. The USA specifically states that this exemption is not available if the issuer operates a blank-check, blind-pool, or shell company whose primary business plan is to engage in a merger or business combination. The answer here is not suggesting that a transaction in a security of an unprofitable company is exempt from registration; however, the other choices are definitely not considered exempt transactions.

68. (B) This is an example of an exempt transaction since it is considered a nonissuer transaction executed by a registered broker-dealer where the security is listed on a national securities exchange. If the issuer were selling securities that were listed on a national securities exchange, this might qualify as an exempt security.

69. (D) In all four choices, the broker-dealer would be required to register in Pennsylvania. A nonissuer transaction of a security listed on a national securities exchange is an exempt transaction and a municipal security is an exempt security. A broker-dealer executing a transaction in an exempt security or exempt transaction is required to register, unless it is exempt from the definition of a broker-dealer in that state. Since the broker-dealer either has an office in Pennsylvania or is transacting business with residents of that state, it would be required to register.

70. (C) Under the Uniform Securities Act, any offer to an investment company or other institutional investor, a transaction by an executor of an estate, or a trustee involved in a bankruptcy, would be defined as an exempt transaction. An unsolicited nonissuer transaction may qualify as an exempted transaction.

71. (B) A nonissuer transaction of a security that is regularly quoted on the OTC Bulletin Board would not qualify as an exempt transaction. The OTCBB does not have specific listing criteria, whereas national exchanges such as the NYSE and Nasdaq have minimum standards to which issuers must adhere. All the other choices are specifically defined under the USA as exempt transactions.