

# Accredited Asset Management Specialist (AAMS) Practice Exam (Sample)

## Study Guide



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**SAMPLE**

## **Questions**

- 1. What is estate planning and why is it important?**
  - A. It's the process of accumulating wealth for future generation**
  - B. It's the process of organizing how assets will be distributed after death, important for minimizing taxes and ensuring wishes are fulfilled**
  - C. It's planning for retirement income only**
  - D. It's the process of deciding insurance coverage**
- 2. Which statement is correct regarding suitability and fiduciary standards?**
  - A. Both are resolved in arbitration**
  - B. Only suitability disputes are resolved in courts**
  - C. Both standards are legally binding**
  - D. Suitability disputes are resolved in arbitration while fiduciary disputes are resolved in courts**
- 3. What is a "value stock"?**
  - A. A stock that is trading above its intrinsic value**
  - B. A stock that is considered undervalued and is trading below its intrinsic value**
  - C. A stock that pays high dividends compared to its price**
  - D. A technology-focused stock with rapid growth potential**
- 4. Which type of insurance expense is part of Ted Jones's budget?**
  - A. Homeowner's insurance**
  - B. Auto insurance**
  - C. Health insurance**
  - D. Liability insurance**
- 5. Which financial responsibility is a broker-dealer likely to protect against under FINRA regulations?**
  - A. Ensuring customer accounts are insured**
  - B. Maintaining client financial records**
  - C. Regulating employee conduct**
  - D. Monitoring investment performance**

- 6. What is a key advantage of using index funds compared to actively managed funds?**
- A. Index funds typically have higher fees**
  - B. Index funds often have lower expense ratios**
  - C. Index funds are more volatile**
  - D. Index funds require constant management**
- 7. What is a financial advisor's fiduciary duty?**
- A. To act in the best interests of their clients**
  - B. To maximize their own commission**
  - C. To ensure their clients take on high risks**
  - D. To solely focus on investment returns**
- 8. What does the term "liquidity" refer to in finance?**
- A. The ability to convert assets to cash quickly**
  - B. The rate of return on investments over time**
  - C. The diversity of investments in a portfolio**
  - D. The level of debt a company has**
- 9. Which statement accurately reflects what a higher risk investment should ideally yield?**
- A. Lower returns to compensate for increased instability**
  - B. Slightly higher returns than low-risk alternatives**
  - C. Significantly lower risk for safer investments**
  - D. Increased expected returns to account for added risk**
- 10. What is the primary purpose of rebalancing a portfolio?**
- A. To increase the number of investments**
  - B. To maintain the desired asset allocation and risk level**
  - C. To replace underperforming assets**
  - D. To focus only on fixed income assets**

## **Answers**

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1. B
2. D
3. B
4. B
5. A
6. B
7. A
8. A
9. D
10. B

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## **Explanations**

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## 1. What is estate planning and why is it important?

- A. It's the process of accumulating wealth for future generation
- B. It's the process of organizing how assets will be distributed after death, important for minimizing taxes and ensuring wishes are fulfilled**
- C. It's planning for retirement income only
- D. It's the process of deciding insurance coverage

Estate planning is the process of organizing how assets will be distributed after an individual passes away. This involves creating legal documents such as wills, trusts, and powers of attorney that specify how a person's assets should be managed and distributed according to their wishes. The importance of estate planning lies in its ability to ensure that an individual's desires regarding their assets are honored, while also minimizing estate taxes and reducing the potential for disputes among heirs. Through effective estate planning, individuals can strategically allocate their wealth to beneficiaries, provide for dependents, and choose trusted individuals to manage their affairs in the event of incapacity. This proactive approach not only helps in avoiding unnecessary taxes but also streamlines the distribution process, ultimately ensuring that the deceased's legacy is maintained as intended. Essential considerations in estate planning include addressing contingent scenarios and ensuring that all relevant legal frameworks comply with current laws and regulations, which may vary by jurisdiction.

## 2. Which statement is correct regarding suitability and fiduciary standards?

- A. Both are resolved in arbitration
- B. Only suitability disputes are resolved in courts
- C. Both standards are legally binding
- D. Suitability disputes are resolved in arbitration while fiduciary disputes are resolved in courts**

The correct answer provides clarity on the distinction between suitability and fiduciary standards in a financial context. Suitability standards require financial professionals to recommend investments that are appropriate for a client's financial situation and objectives. Disputes arising from suitability violations are typically resolved through arbitration, as many financial services agreements include arbitration clauses. On the other hand, fiduciary standards impose a higher duty, where financial advisors must act in the best interests of their clients, prioritizing their clients' needs above their own. This higher standard can lead to disputes that are more complex and often resolved in court, especially because fiduciary duty breaches can involve allegations of negligence or misconduct. This differentiation is crucial for understanding that while both standards are important in guiding financial advisors' behavior, they have different avenues for dispute resolution that reflect the severity and nature of their responsibilities. As a result, only suitability disputes tend to be resolved in arbitration, while fiduciary disputes are more likely to go to court due to their more serious implications.

### 3. What is a "value stock"?

- A. A stock that is trading above its intrinsic value
- B. A stock that is considered undervalued and is trading below its intrinsic value**
- C. A stock that pays high dividends compared to its price
- D. A technology-focused stock with rapid growth potential

A "value stock" refers to a stock that is considered to be undervalued and is trading below its intrinsic value. This means that the market price of the stock does not fully reflect the company's true worth based on its fundamentals, such as earnings, revenue, and growth potential. Investors often look for value stocks as they may represent a good investment opportunity; the idea is that the market will eventually recognize the stock's true value, leading to price appreciation. Value stocks typically have lower price-to-earnings (P/E) ratios compared to their growth-oriented counterparts, which can indicate that they are undervalued. Investors who adopt a value investing strategy seek out these stocks with the expectation that their prices will rise over time as the market corrects this undervaluation. In contrast, stocks that are trading above their intrinsic value might not fit the definition of a value stock. Additionally, while high dividend-paying stocks can be value stocks, they are not exclusively classified as such because the presence of high dividends does not guarantee that the stock itself is undervalued based on fundamentals. Lastly, technology stocks with rapid growth potential are typically categorized as growth stocks, not value stocks, as growth stocks are often priced for future growth rather than current or historic metrics.

### 4. Which type of insurance expense is part of Ted Jones's budget?

- A. Homeowner's insurance
- B. Auto insurance**
- C. Health insurance
- D. Liability insurance

The selected answer, auto insurance, is indeed an important type of insurance expense that can be included in an individual's budget. Auto insurance is crucial for protecting against financial loss in the event of accidents, theft, or damage involving vehicles. Many people budget for auto insurance to ensure they meet legal requirements and safeguard their investment in their vehicles. In the context of managing personal finances, it is common for individuals like Ted Jones to account for auto insurance as part of their monthly or annual expenses. This allows for better financial planning and ensures that he is adequately covered while on the road. Homeowner's insurance, health insurance, and liability insurance are also essential types of coverage, but depending on Ted's specific circumstances, such as whether he owns a home or has assets requiring liability coverage, auto insurance may emerge as a more immediate or pressing concern in his budget. Thus, focusing on vehicle-related expenses is a relevant decision when planning overall insurance costs.

**5. Which financial responsibility is a broker-dealer likely to protect against under FINRA regulations?**

**A. Ensuring customer accounts are insured**

**B. Maintaining client financial records**

**C. Regulating employee conduct**

**D. Monitoring investment performance**

The financial responsibility that a broker-dealer is likely to protect against under FINRA regulations is ensuring that customer accounts are insured. FINRA, or the Financial Industry Regulatory Authority, establishes rules that are designed to protect investors and ensure a fair and efficient market. In this context, customer account insurance typically refers to the protections provided by the Securities Investor Protection Corporation (SIPC). SIPC insurance helps safeguard clients' securities and cash if a brokerage firm fails. While it does not provide blanket insurance for all investment losses, it protects against the loss of securities or cash held by the broker-dealer. While maintaining client financial records, regulating employee conduct, and monitoring investment performance are important responsibilities, they primarily pertain to operational practices and compliance but do not directly relate to the insurance protections explicitly referenced in FINRA regulations. Therefore, the focus on ensuring customer accounts are insured aligns directly with the responsibilities of broker-dealers under regulatory frameworks aimed at protecting investors and their assets.

**6. What is a key advantage of using index funds compared to actively managed funds?**

**A. Index funds typically have higher fees**

**B. Index funds often have lower expense ratios**

**C. Index funds are more volatile**

**D. Index funds require constant management**

Using index funds offers a significant advantage in the form of lower expense ratios compared to actively managed funds. This is primarily because index funds are designed to track a specific benchmark or index rather than trying to outperform it through frequent buying and selling of securities. This passive management style requires far less oversight and, consequently, incurs lower operational costs, which translates to cheaper fees for investors. Investors benefit from this cost efficiency over the long term, as lower fees can compound significantly, ultimately leading to higher net returns on their investments. The focus on broad market exposure without the hefty management fees associated with active strategies makes index funds an attractive investment option for many investors looking to maximize their returns while minimizing costs.

## 7. What is a financial advisor's fiduciary duty?

- A. To act in the best interests of their clients**
- B. To maximize their own commission**
- C. To ensure their clients take on high risks**
- D. To solely focus on investment returns**

A financial advisor's fiduciary duty is fundamentally about putting their clients' best interests first. This responsibility is grounded in trust and a legal obligation, which means that the advisor must prioritize the client's needs, goals, and well-being in all financial dealings and recommendations. By acting in the client's best interest, the advisor must provide unbiased advice, disclose any potential conflicts of interest, and avoid self-serving actions that could compromise the client's financial health. This principle contrasts sharply with the other choices. Maximizing a financial advisor's own commission directly conflicts with a fiduciary duty, as this would result in the advisor prioritizing their profit over the client's needs. Similarly, encouraging clients to take on high risks does not align with the fiduciary responsibility; instead, the advisor should assess the client's risk tolerance and work towards suitable strategies that match their financial situation and goals. Lastly, focusing solely on investment returns overlooks the broader aspects of financial planning, which include risk management, client education, and holistic goal setting that considers the client's entire financial landscape. Therefore, the essence of the fiduciary duty is encapsulated in the commitment to act in the client's best interest at all times.

## 8. What does the term "liquidity" refer to in finance?

- A. The ability to convert assets to cash quickly**
- B. The rate of return on investments over time**
- C. The diversity of investments in a portfolio**
- D. The level of debt a company has**

Liquidity in finance specifically refers to the ease with which assets can be converted into cash without significantly affecting their price. Cash is considered the most liquid asset because it can be used immediately for transactions. Other assets, such as stocks, bonds, or real estate, may require more time to sell and could be subject to price fluctuations, thereby impacting how quickly cash can be obtained. Understanding liquidity is crucial for investors, as it influences their ability to meet short-term financial obligations and manage cash flow. For example, an investor needing quick access to cash might prioritize holding more liquid assets to avoid potential losses associated with selling less liquid investments at unfavorable prices. This concept is essential in risk management and financial planning, emphasizing that a balance exists between the desire for high returns and the need for access to cash.

**9. Which statement accurately reflects what a higher risk investment should ideally yield?**

- A. Lower returns to compensate for increased instability**
- B. Slightly higher returns than low-risk alternatives**
- C. Significantly lower risk for safer investments**
- D. Increased expected returns to account for added risk**

A higher risk investment is expected to yield increased expected returns to account for the additional risk. This principle is rooted in the risk-return tradeoff, which asserts that investors typically require a higher return as compensation for taking on greater risk. In financial markets, investments that carry higher risk—such as stocks or speculative assets—have the potential for significant fluctuations in value. To entice investors to accept this uncertainty, these investments generally offer the prospect of higher returns compared to lower-risk options, such as government bonds or savings accounts, which provide more stability but usually yield lower returns. This relationship is essential for investors to consider when constructing a diversified portfolio, as they balance the desire for growth (potentially achieved through higher-risk investments) with the need for capital preservation (often achieved through lower-risk assets).

**10. What is the primary purpose of rebalancing a portfolio?**

- A. To increase the number of investments**
- B. To maintain the desired asset allocation and risk level**
- C. To replace underperforming assets**
- D. To focus only on fixed income assets**

The primary purpose of rebalancing a portfolio is to maintain the desired asset allocation and risk level. Over time, the values of different investments within a portfolio can change due to market fluctuations, which can lead to an unintended drift from the initial asset allocation strategy. For instance, if stocks perform exceptionally well, they may grow to constitute a larger portion of the portfolio than originally intended, increasing the overall risk. Rebalancing involves selling portions of the assets that have increased in value and buying those that have decreased, thus realigning the portfolio with its target allocation. This process helps ensure that the investor remains aligned with their risk tolerance and investment objectives, preventing unintended overexposure to certain asset classes. The other choices do not capture this fundamental aspect of rebalancing. Increasing the number of investments does not address the risk or allocation concerns, focusing only on fixed income assets neglects the diversification principle, and replacing underperforming assets might not necessarily relate to maintaining the overall asset allocation strategy. Rebalancing is more about adjusting the mix of assets rather than strictly managing individual performance.