

Cannon Financial Institute CFIRS Practice Exam (Sample)

Study Guide



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SAMPLE

Questions

- 1. Who should operations notify in addition to internal auditors during a vault audit when securities are noted as missing?**
 - A. OCC**
 - B. DTC**
 - C. SEC**
 - D. SIC**
- 2. What is a crucial component for an auditor to analyze when addressing a potential issue in the organization?**
 - A. Only the risk assessment**
 - B. The entire operational process**
 - C. The organizational culture**
 - D. The internal control framework**
- 3. When securities are sold by one investor and purchased by another investor, the transactions occur in which of the following markets?**
 - A. Money**
 - B. Primary**
 - C. Secondary**
 - D. Negotiable**
- 4. The primary focus of internal audit is to determine what aspects of an organization?**
 - A. Reasonableness of the compliance program**
 - B. Adequacy of the internal control system**
 - C. Logic of the policies and procedures**
 - D. Consistency of business practices**
- 5. A bond is convertible at 40. If the bond is currently selling at 113 and the corporation calls the bond for redemption at 107, what action is a bondholder most likely to take?**
 - A. Convert the bond into common stock**
 - B. Sell the bond**
 - C. Allow the corporation to call the bond at 107**
 - D. Convert 25 shares of stock into one bond**

- 6. What do corporate bonds represent?**
- A. Employment contracts.**
 - B. Guarantees.**
 - C. Ownership.**
 - D. Debt.**
- 7. When determining if a benefit plan is qualified, which document is crucial according to the IRS?**
- A. A written legal opinion from the drafting attorney**
 - B. A favorable determination letter from the IRS**
 - C. A written legal opinion from external counsel**
 - D. DOL certification**
- 8. Which of the following best describes the primary role of a financial institution regarding fraud?**
- A. Acting solely as intermediaries**
 - B. Liability for all unauthorized transactions**
 - C. Implementing strong authentication processes**
 - D. Monitoring financial markets for irregularities**
- 9. Which of the following is not a duty of a trustee upon termination of an account?**
- A. Determine distribution provisions in the governing instrument.**
 - B. Determine if there is a co-fiduciary appointed.**
 - C. Determine if there is any tax liability for which the account is responsible.**
 - D. Determine the fair market value (FMV) of all assets held in the account.**
- 10. Who benefits from a charitable remainder trust when it comes to income distribution?**
- A. The charity receives all income**
 - B. The beneficiaries receive income based on fixed percentages**
 - C. The grantor solely benefits until trust termination**
 - D. The trust pays no taxes on income generated**

Answers

SAMPLE

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

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Explanations

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1. Who should operations notify in addition to internal auditors during a vault audit when securities are noted as missing?

- A. OCC
- B. DTC
- C. SEC
- D. SIC**

In the context of a vault audit where securities are noted as missing, notifying the Securities Information Center (SIC) is essential. The SIC plays a critical role in the safeguarding and tracking of securities. When discrepancies occur, such as missing securities, informing the SIC allows for appropriate measures to be taken in tracking or recovering those items. The SIC is specifically designed to handle incidents involving security transactions and issues related to lost or missing securities. Their involvement is crucial for maintaining the integrity of the securities system and ensuring that necessary protocols are followed to address any potential fraud or losses. Hence, notifying the SIC is a standard and necessary action to ensure regulatory compliance and promote secure practices within the financial industry.

2. What is a crucial component for an auditor to analyze when addressing a potential issue in the organization?

- A. Only the risk assessment
- B. The entire operational process
- C. The organizational culture
- D. The internal control framework**

Focusing on the internal control framework is essential for an auditor when addressing potential issues within an organization because it encompasses the policies, procedures, and processes designed to ensure effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. By examining this framework, the auditor can identify weaknesses or gaps in controls that could lead to errors, fraud, or inefficiencies. The internal control framework serves as the foundation for risk management and provides a systematic approach to determining how risks are identified, assessed, and managed. The effectiveness of controls can directly impact the organization's ability to meet its objectives and respond to risks, making it a critical area of focus for auditors. While other aspects, like the entire operational process, organizational culture, and risk assessment, are important, they may not provide as comprehensive an understanding of where specific control weaknesses lie as the internal control framework does. This focus enables the auditor to pinpoint areas for improvement and recommend corrective actions, ensuring the organization's processes run smoothly and effectively.

3. When securities are sold by one investor and purchased by another investor, the transactions occur in which of the following markets?

- A. Money**
- B. Primary**
- C. Secondary**
- D. Negotiable**

The correct choice is the secondary market because this is the platform where previously issued securities are traded between investors. When one investor sells a security they own, and another investor purchases it, this transaction does not involve the issuing company; hence, it takes place in the secondary market. In contrast, the primary market is concerned with the issuance of new securities directly from issuers to investors. Transactions in the primary market occur when companies go public or issue additional stocks or bonds. The money market pertains to the trading of short-term debt securities and is distinctly different from transactions involving ownership of stocks, which are usually longer-term investments. The term "negotiable" relates more to the characteristics of certain financial instruments that can be transferred or sold, but it does not represent a specific market for trading securities. Thus, since the question specifies transactions between investors with no new issuance involved, the secondary market is indeed the appropriate context.

4. The primary focus of internal audit is to determine what aspects of an organization?

- A. Reasonableness of the compliance program**
- B. Adequacy of the internal control system**
- C. Logic of the policies and procedures**
- D. Consistency of business practices**

The emphasis of internal audit is predominantly on assessing the adequacy of the internal control system within an organization. This focus is crucial because the internal control system is designed to provide reasonable assurance regarding the achievement of objectives in effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations. An internal audit evaluates whether these controls are properly designed, implemented, and functioning effectively. It involves examining the procedures and processes to identify any weaknesses or deficiencies that could lead to misstatements in financial reports, risks of fraud, or non-compliance with laws. A robust internal control system helps in mitigating risks and ensuring adherence to organizational policies, thus supporting the organization's overall governance framework. While aspects like compliance programs, policies and procedures, and business practices are important, they are more specific areas that feed into the broader evaluation of internal controls. The internal audit's thorough analysis enables organizations to enhance their control environment, leading to improved operational efficacy and risk management.

5. A bond is convertible at 40. If the bond is currently selling at 113 and the corporation calls the bond for redemption at 107, what action is a bondholder most likely to take?

A. Convert the bond into common stock

B. Sell the bond

C. Allow the corporation to call the bond at 107

D. Convert 25 shares of stock into one bond

A bondholder is most likely to sell the bond when it is currently priced at 113 and the corporation has called the bond for redemption at 107. This situation creates an opportunity for the bondholder to realize a profit by selling it on the market, where it is valued higher than the call price. Selling the bond at its market price allows the bondholder to capitalize on the higher market value (113), rather than accepting the lower redemption price (107) that the corporation offers upon calling the bond. Even though the bondholder could choose to convert the bond into common stock at a predetermined rate, the bondholder gains a greater financial advantage by selling the bond at market value, given the significant price difference. This decision aligns with the bondholder's objective of maximizing returns, making selling the bond the most logical course of action in this scenario.

6. What do corporate bonds represent?

A. Employment contracts.

B. Guarantees.

C. Ownership.

D. Debt.

Corporate bonds represent a form of debt in which an investor loans money to a corporation for a specified period at a fixed interest rate. When a corporation needs to raise capital, it can issue bonds to the public, effectively borrowing funds that it agrees to repay, along with interest, over time. This arrangement allows the company to finance various projects or operational costs without giving up ownership stakes in the business. In the context of corporate finance, bonds are a common way for companies to "leverage" their operations, enabling them to invest in growth opportunities while spreading the risk among a broader range of investors. Investors who purchase these bonds are essentially lending money to the corporation, making them creditors rather than owners. This distinction is crucial for understanding the nature of corporate bonds and the financial relationships they establish.

7. When determining if a benefit plan is qualified, which document is crucial according to the IRS?

- A. A written legal opinion from the drafting attorney**
- B. A favorable determination letter from the IRS**
- C. A written legal opinion from external counsel**
- D. DOL certification**

A favorable determination letter from the IRS is essential when assessing whether a benefit plan is considered qualified. This letter serves as a formal acknowledgment from the IRS that the plan meets specific requirements under the Internal Revenue Code. It confirms that the plan is designed to provide certain tax advantages, ensuring that contributions to the plan and earnings on those contributions receive favorable tax treatment. The determination letter is a critical piece of documentation as it provides legal assurance that the plan complies with regulatory standards, protecting both the plan sponsor and the participants in terms of tax benefits. Other documents, such as a written legal opinion or certifications from the Department of Labor, may support the overall compliance and design of a plan, but they do not hold the same authoritative weight as the IRS determination letter. A determination letter directly references the intricate stipulations of the tax code and is specifically focused on the qualification status of the retirement plan, making it indispensable in evaluating the plan's qualified status.

8. Which of the following best describes the primary role of a financial institution regarding fraud?

- A. Acting solely as intermediaries**
- B. Liability for all unauthorized transactions**
- C. Implementing strong authentication processes**
- D. Monitoring financial markets for irregularities**

The primary role of a financial institution regarding fraud encompasses the implementation of strong authentication processes. These processes are essential in ensuring that transactions are conducted securely and that the identities of clients or users are verified accurately. Strong authentication methods, such as multi-factor authentication, are designed to reduce the risk of unauthorized access to accounts and sensitive information, thereby protecting both the institution and its clients from potential fraud. While financial institutions may also act as intermediaries and monitor financial markets, their proactive responsibility in preventing fraud primarily focuses on safeguarding their systems and client information through robust security measures. Additionally, while institutions can face liability for unauthorized transactions, this is more of a consequence rather than a primary role in relation to fraud management. Overall, the emphasis on strong authentication reflects a critical preventive measure in the fight against financial fraud.

9. Which of the following is not a duty of a trustee upon termination of an account?
- A. Determine distribution provisions in the governing instrument.
 - B. Determine if there is a co-fiduciary appointed.**
 - C. Determine if there is any tax liability for which the account is responsible.
 - D. Determine the fair market value (FMV) of all assets held in the account.

The correct answer revolves around the responsibilities of a trustee upon termination of an account. A trustee's duties at the time of termination include ensuring that all aspects related to the distribution of assets are handled properly, which encompasses confirming the distribution provisions stated in the governing instrument, assessing any tax liabilities related to the account, and determining the fair market value of all assets to facilitate accurate and equitable distribution. Determining whether there is a co-fiduciary appointed is not part of the trustee's duties upon the termination of an account. This aspect is typically addressed prior to or during the ongoing management of the trust rather than during its winding up. The primary focus at termination is to finalize distributions and ensure compliance with legal and financial obligations, rather than revisiting co-fiduciary appointments. This makes it clear why the determination of co-fiduciaries does not fall under the specific set of responsibilities of the trustee at that final stage.

10. Who benefits from a charitable remainder trust when it comes to income distribution?
- A. The charity receives all income
 - B. The beneficiaries receive income based on fixed percentages**
 - C. The grantor solely benefits until trust termination
 - D. The trust pays no taxes on income generated

A charitable remainder trust (CRT) is designed primarily to provide income to specific beneficiaries over a defined period, after which the remaining assets go to a designated charity. In the context of income distribution, the correct aspect is that the beneficiaries receive income based on fixed percentages. This structure allows for a predetermined percentage of the trust's value to be distributed to the beneficiaries, which can provide them with a steady and reliable income stream. The fixed percentages ensure that the distribution is calculable and can be planned for at the inception of the trust, aligning with the financial needs of the beneficiaries. This arrangement is advantageous as it enables beneficiaries to benefit from the income while also contributing to charitable causes in a structured way that ultimately supports the charity after the trust's term ends. In terms of the other options, while the charitable organization does receive the remainder of the trust's assets upon termination, they do not receive all income during the lifetime of the trust. Furthermore, the grantor may not solely benefit from the trust, as the income distribution is allocated to the beneficiaries instead. Lastly, the trust typically does have certain tax obligations, especially regarding the income generated, rather than being entirely tax-exempt.