

Securities Training Series 7 Practice Test (Sample)

Study Guide



Everything you need from our exam experts!

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SAMPLE

Questions

- 1. Which of the following describes the breakeven point accurately?**
 - A. It lies above the lower strike price for a vertical spread**
 - B. It is typically found at the midpoint of two strike prices**
 - C. It always occurs at the higher strike price**
 - D. It can vary and is not predictable**
- 2. Which type of pricing does the 5% policy cover?**
 - A. Only agency transaction pricing**
 - B. Only principal transaction pricing**
 - C. Both agency and principal transaction pricing**
 - D. Only negotiating transaction pricing**
- 3. What is the minimum maintenance requirement for a short account if the stock is trading above \$5?**
 - A. 25% of the market value**
 - B. 50% of the market value**
 - C. 30% of the market value or \$5 per share**
 - D. 10% of the market value**
- 4. What is the typical duration for bond anticipation notes?**
 - A. Long-term**
 - B. Medium-term**
 - C. Short-term**
 - D. Indeterminate**
- 5. Under what condition would a cash dividend received by a retail investor be taxed at a preferred rate?**
 - A. If the investor holds the stock for at least 30 days surrounding the ex-dividend date**
 - B. If the investor holds the stock for at least 60 days surrounding the ex-dividend date**
 - C. If the investor holds the stock for at least 90 days surrounding the ex-dividend date**
 - D. If the investor holds the stock for at least 120 days surrounding the ex-dividend date**

- 6. How long can the Letter of Intent be backdated for practical purposes?**
- A. 1 month**
 - B. 2 months**
 - C. 3 months**
 - D. 4 months**
- 7. What do oil and gas income programs primarily pass through to investors?**
- A. Tax credits and incentives**
 - B. Depletion allowances**
 - C. Exploration risk**
 - D. Royalty fees**
- 8. How much excess equity is created for every \$1.00 increase in portfolio value?**
- A. 25 cents**
 - B. 50 cents**
 - C. 75 cents**
 - D. 1 dollar**
- 9. How is a credit spread created by an investor in options trading?**
- A. By selling the near expiration and buying the distant expiration**
 - B. By selling the distant expiration and buying the near expiration**
 - C. By buying calls and selling puts simultaneously**
 - D. By purchasing options with different strike prices**
- 10. What is the purpose of Regulation SHO?**
- A. It eliminates the need for margin accounts**
 - B. It ensures broker-dealers can borrow the securities for short selling**
 - C. It restricts trading of penny stocks**
 - D. It regulates insider trading practices**

Answers

SAMPLE

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

SAMPLE

Explanations

SAMPLE

1. Which of the following describes the breakeven point accurately?

A. It lies above the lower strike price for a vertical spread

B. It is typically found at the midpoint of two strike prices

C. It always occurs at the higher strike price

D. It can vary and is not predictable

The breakeven point in a vertical spread can indeed be described as lying above the lower strike price. In a vertical spread strategy, which involves buying and selling options of the same class but at different strike prices, the breakeven point is determined based on the net premium received or paid. When calculating the breakeven for a debit vertical spread (where you pay more for the option you buy than the option you sell), the breakeven is at the lower strike price plus the net premium paid. For a credit vertical spread (where you receive more for the option you sell than what you pay for the option you buy), the breakeven would be at the higher strike price minus the net premium received. In both cases, the breakeven point is above the lower strike price, as it needs to account for the cost of entering the trade, hence making option A an accurate description. The other choices provide incorrect contexts or define the breakeven point in ways that do not apply universally to vertical spreads. For instance, the breakeven point is not reliably found at the midpoint of the strike prices, nor does it strictly occur at the higher strike price for most configurations of vertical spreads. Additionally, while the breakeven

2. Which type of pricing does the 5% policy cover?

A. Only agency transaction pricing

B. Only principal transaction pricing

C. Both agency and principal transaction pricing

D. Only negotiating transaction pricing

The 5% policy is a guideline established by the Financial Industry Regulatory Authority (FINRA) that provides a framework for fair pricing in securities transactions. This policy is applicable to both agency transactions, where a broker acts on behalf of a client to execute a trade, and principal transactions, where a broker buys or sells securities for their own account. The essence of the 5% policy is to ensure that the markups or markdowns are reasonable and do not exceed 5% of the total transaction value. This means it aims to prevent excessive charges in both types of transactions, promoting transparency and fairness in the market. The context of the other options is important for understanding why this comprehensive approach is necessary. Agency transactions involve brokers executing trades for clients, while principal transactions include brokers trading from their own inventory. Thus, to ensure that all clients, regardless of the transaction type, are treated fairly in terms of pricing, the policy covers both categories, making the correct answer comprehensive and inclusive.

3. What is the minimum maintenance requirement for a short account if the stock is trading above \$5?

- A. 25% of the market value**
- B. 50% of the market value**
- C. 30% of the market value or \$5 per share**
- D. 10% of the market value**

The minimum maintenance requirement for a short account when the stock is trading above \$5 is determined by the guidelines established by regulatory bodies. For stocks priced at or above \$5, the maintenance requirement is set at the greater of either 30% of the market value of the short position or \$5 per share. In the context of the chosen answer, if the stock is valued at a price higher than \$5, the maintenance requirement will be calculated as 30% of the market value, but it cannot drop below \$5 per share. This ensures that there is sufficient margin to cover any potential increases in stock price that would result in losses for the short seller. Thus, the selected answer reflects the correct understanding of this requirement and provides the necessary cushion for risk management in short selling scenarios.

4. What is the typical duration for bond anticipation notes?

- A. Long-term**
- B. Medium-term**
- C. Short-term**
- D. Indeterminate**

Bond anticipation notes are typically issued for short-term financing needs, which makes the duration of these instruments around one to three years, though they are often less than one year. These notes are essentially a temporary borrowing mechanism used by municipalities to raise funds in anticipation of the forthcoming issuance of long-term bonds. Since they are aimed at addressing immediate cash flow needs and are designed to be paid off quickly once long-term financing is secured, the short-term characteristic is crucial. This allows issuers to bridge funding gaps without committing to the long-term obligations that would come from issuing bonds immediately. Therefore, the correct answer accurately reflects the nature and purpose of bond anticipation notes.

5. Under what condition would a cash dividend received by a retail investor be taxed at a preferred rate?

A. If the investor holds the stock for at least 30 days surrounding the ex-dividend date

B. If the investor holds the stock for at least 60 days surrounding the ex-dividend date

C. If the investor holds the stock for at least 90 days surrounding the ex-dividend date

D. If the investor holds the stock for at least 120 days surrounding the ex-dividend date

A cash dividend received by a retail investor is taxed at a preferred rate, specifically the qualified dividend rate, when certain holding period requirements are met. The holding period is crucial because the Internal Revenue Service (IRS) stipulates that to qualify for this preferred tax rate, the investor must hold the stock for a minimum period surrounding the ex-dividend date. In this case, holding the stock for at least 60 days surrounding the ex-dividend date is the correct threshold to qualify for the lower tax rate on the dividend. This period ensures that the investor maintains a genuine investment in the stock rather than engaging in short-term trading strategies to capture dividend payments without having a long-term investment perspective. The ex-dividend date is the cutoff date for when new buyers of the stock will not receive the declared dividend, and the surrounding holding period includes both a 30-day period before and a 30-day period after the ex-dividend date. Holding the stock for this duration qualifies the dividend as a qualified dividend, thus allowing it to be taxed at the favorable capital gains rate, which is typically lower than ordinary income rates.

6. How long can the Letter of Intent be backdated for practical purposes?

A. 1 month

B. 2 months

C. 3 months

D. 4 months

A Letter of Intent (LOI) in the context of mutual funds and certain investment accounts allows investors to commit to investing a specific amount over a period of time while receiving the benefits of a lower sales charge. For practical purposes, the LOI can typically be backdated for a maximum of three months before the date of the LOI. This three-month backdating is significant because it allows the investor to count any investments made during this time towards the total commitment of the LOI. This flexibility incentivizes larger upfront investments, enabling investors to take advantage of reduced sales charges sooner. Hence, identifying the correct backdating period as three months aligns with regulatory standards and practices in the investment industry, ensuring that investors can effectively utilize their contributions while benefiting from the cost savings associated with higher total investments.

7. What do oil and gas income programs primarily pass through to investors?

A. Tax credits and incentives

B. Depletion allowances

C. Exploration risk

D. Royalty fees

Oil and gas income programs primarily pass through depletion allowances to investors because these allowances represent a tax deduction that reflects the reduction in the value of the mineral resource being extracted. Depletion allowances allow investors to recover their investment in the natural resources as these resources are depleted over time. This mechanism not only encourages investment in the industry but also provides a way for investors to offset income generated from these programs, making them more attractive. While other aspects like tax credits, exploration risk, and royalty fees relate to oil and gas ventures, they do not primarily characterize what is passed through to investors in income programs. Tax credits and incentives can vary widely and are not a guaranteed part of income programs. Exploration risk is inherent to the sector but does not represent a tangible financial benefit passed through to investors. Royalty fees do provide income but are typically paid to landowners or mineral rights holders and do not directly translate to what income programs distribute to their investors.

8. How much excess equity is created for every \$1.00 increase in portfolio value?

A. 25 cents

B. 50 cents

C. 75 cents

D. 1 dollar

In the context of financial securities and portfolio management, the increase in the value of a portfolio is often associated with the concept of excess equity, which is influenced by margin requirements and the use of leverage. When a portfolio value increases, the additional equity created is contingent upon the margin and the leverage ratio used. In this scenario, for every \$1.00 increase in portfolio value, excess equity is typically calculated based on a specific margin requirement. If the margin requirement is set at 50%, this means that an investor is allowed to borrow up to 50% of their portfolio value, effectively using leverage. Under this condition, when the portfolio value rises by \$1.00, only half of that increase would need to be paid back if using borrowed funds, therefore creating 50 cents of excess equity. This is aligned with typical margin lending rules where the return on equity rises as the portfolio appreciates, and traders may not be required to develop their entire equity stake every time there's a marginal increase in asset value. Thus, this understanding directly supports why a 50-cent increase in excess equity is accurate with a dollar rise in portfolio value.

9. How is a credit spread created by an investor in options trading?

- A. By selling the near expiration and buying the distant expiration
- B. By selling the distant expiration and buying the near expiration**
- C. By buying calls and selling puts simultaneously
- D. By purchasing options with different strike prices

A credit spread in options trading is created when an investor sells an option with a higher premium and buys an option with a lower premium, resulting in an initial net credit to their account. This typically involves the sale of a distal expiration option and the purchase of a nearer expiration option, allowing the investor to profit from the differential in premiums. In this context, when an investor sells the distant expiration option, they are generally taking on more risk compared to the option they buy that has a nearer expiration. The intent is to capture the premium difference while controlling risk exposure. The trade-off lies in managing the timing of options expiration, where the sold option may expire worthless if the market behaves favorably, while the bought option can hedge against adverse price movements. Understanding the mechanics of credit spreads is crucial for options traders, as it helps them leverage their positions while also managing risks effectively. This strategy is also useful for generating income when market conditions are favorable and can be adapted using various strike prices and expiration dates based on the investor's outlook on the underlying asset.

10. What is the purpose of Regulation SHO?

- A. It eliminates the need for margin accounts
- B. It ensures broker-dealers can borrow the securities for short selling**
- C. It restricts trading of penny stocks
- D. It regulates insider trading practices

Regulation SHO primarily focuses on short selling of securities, and its purpose is to establish requirements that ensure broker-dealers can borrow the securities they need for short selling transactions. This regulation is critical because short selling involves selling stocks that the seller does not currently own with the expectation that the price will decline. In order for a broker-dealer to facilitate this process, they must be able to borrow the security to deliver to the buyer. To maintain market integrity and prevent potential abuse in short selling, Regulation SHO imposes rules that require broker-dealers to locate and borrow the securities before executing a short sale. This "locate" requirement aims to reduce the risk of "naked" short selling, where a sale is made without ensuring that the securities can be borrowed. By ensuring broker-dealers have access to the necessary securities, Regulation SHO contributes to a more orderly marketplace and reduces the chance of settlement failures. Therefore, the essence of Regulation SHO is closely tied to its role in facilitating responsible short selling practices within the financial markets.