Series 65 Supplement and Errata
For NASAA Study Outline effective January 1, 2010
For use with RegEd Series 65 Study Guides purchased before January 2010

Effective January 1, 2010, the NASAA Study Outline for the Series 65 NASAA Investment Adviser Competency Examination will change to reflect changes in the securities industry.

NASAA has added information on several topics, mostly involving types of accounts, such as UGMA/UTMA and 529 Plan accounts, and investments. The number of questions on legal guidelines and ethical practices has been decreased slightly, from 45 to 40. Below is a comparison of old and new outlines:

Series 65 Through 12/31/09			**Series 65 As of 1/1/10**		
Topic	Number of Questions	% of exam	Topic	Number of Questions	% of exam
Economics and Analysis	20	15%	Economic Factors and Business Information	19	15%
Investment Vehicles	26	20%	Investment Vehicle Characteristics	31	24%
Investment Recommendations and Strategies	39	30%	Client Investment Recommendations and Strategies	40	31%
Legal and Regulatory Guidelines, including Prohibition on Unethical Business Practices	45	35%	Laws, Regulations and Guidelines, including Prohibition on Unethical Business Practices	40	31%
Total	130	100%	Total	130	100%
Needed to pass	***89***	***68.5%***	***Needed to pass***	***94***	***72%***

RegEd has added the following material to our Study Guide which we believe will be valuable in helping students pass their exam.

Tax Updates for 2010

Each year, retirement plan contribution limits and some other dollar amounts related to taxation may be changed to reflect inflation. Due in large part to the weak economy in 2009, most of these limits remain unchanged for 2010. There is one change, to income thresholds for Roth IRAs, which will be discussed later.

	2008	***2009/2010***
Gift Tax Limit (to avoid gift tax)	$12,000	$13,000
Max 401k/403b/ 457 Contribution	$15,500	$16,500
401k/ 403b Catch Up Contributions	$ 5,000	$ 5,500
SEP- IRA Contributions	$46,000	$49,000
Keogh Contributions	$46,000	$49,000
Traditional IRA Contributions	$ 5,000	$ 5,000
Roth IRA Contributions	$ 5,000	$ 5,000
IRA Catch Up Contributions	$ 1,000	$ 1,000

Chapter 1: page 21

The exam is administered by FINRA on behalf of NASAA. Information about the location of testing centers and how to schedule an appointment can be found on the Web at:
http://apps.finra.org/Registration%5Fand%5FQualifications/exam/list examlocs_form.asp

This program will cover all the information you need to know in order to pass the exam. If you would like more detailed information about NASAA's Series 65 exam specifications, see:
http://www.nasaa.org/content/Files/Series65ExamSpecs.pdf

Chapter 1: Page 22

Please disregard the *Before You Test* section.

Chapter 2: Add the following information

UGMA/UTMA

Custodial accounts are usually set up under the Uniform Gifts to Minors Act (UGMA) or the Uniform Transfers to Minors Act (UTMA). These acts are designed to protect the interests of the children. The account may be set up by the child's parents, grandparents or any other interested party. When the custodial accounts are established, the securities are registered under the name of the custodian for the benefit of the child and any gifts given to fund the account are irrevocable. The custodian is an adult who acts in a fiduciary capacity (protects the interests of the child). The custodian oversees the account and is responsible for all investment decisions.

Who's the Custodian?

The custodian is typically one of the parents of the child, but could be any adult. The donor could choose to designate either parent to be custodian on the account or they could ask another individual to act as custodian for their child. There is no requirement that a custodian be a blood relative of the child.

What Type of Investments

As fiduciaries, custodians are required to protect the interests of the child. Portfolios constructed for UGMA/UTMA accounts should not be overly aggressive. Most states operate under the Uniform Prudent Investors Act (UPIA) that establishes standards for fiduciaries. Under this act, the portfolio must be invested in a prudent and diversified manner. The account is looked at as a whole, as opposed to scrutinizing the individual investments. Under UGMA/UTMA, trading on margin (with borrowed funds) is prohibited, since it would put the child in debt.

Whose Money Is It?

Any assets in an UGMA/UTMA are the property of the child and any gifts given to the child are irrevocable. The custodian may remove funds from the account to pay any taxes due or for the benefit of the child. Although his name appears in the account title, the custodian is not a co-owner of the account. UGMA/UTMA accounts are not considered to be joint accounts.

Tax Issues

Tax information for the account is reported to the IRS under the minor's social security number. Payment of any taxes due is the responsibility of the child. At whose tax rate (marginal bracket) are these taxes payable? This is a harder question. The U.S. tax code includes provisions referred to as "kiddie tax" rules. “Kiddie tax” rules apply to children under the age of 19. There is an exception whereby a student enrolled in college on a fulltime basis would be subject to these rules until age 24. Under the kiddie tax, the first $950 of earnings each year is tax-free and the next $950 is taxed at the child’s tax rate. Any additional income is taxed at the parents’ rate. Once the minor reaches age 19, all taxable income is assessed their tax rate.

Age of Majority

When the child reaches the age of majority (legal adulthood), the custodial account is closed. The legal age is determined by the state in which the child resides. All securities will be reregistered in the name of the beneficiary (former child) and transferred to a new account. Some states allow, in UTMA accounts specifically, the custodian to specify a different date for transferring assets; the custodian can use any date from age of majority up to as late as age 25.

Saving For Education

A primary concern of many investors is saving for the education of their children or grandchildren. Congress, aware of the hardships, has created tax incentives to encourage saving. We will talk about two separate vehicles. The first is a type of IRA and the second is a state sponsored qualified tuition program limited plan. The second, called Section 529 plans, may allow substantially larger contributions.

Education IRAs (Coverdell Education Savings Accounts)

For the tax years 2009 and 2010, investors may contribute up to $2,000 per year to help fund a child's education. Contributions may be made up to the child's 18th birthday and are always made on an after-tax (nondeductible) basis.

Earnings on Coverdell Education Savings Accounts are not subject to taxation provided the distribution is taken prior to age 30 and is used for qualified elementary, secondary, or higher education expenses. Although these accounts are often funded by parents or grandparents, there is no requirement that contributions be made by a blood relative of the child.

Sometimes the child decides not to pursue qualified education. In other cases, the account assets are not needed because schooling is being funded through other means, such as a scholarship. In these cases, account balances may be transferred to another relative without tax consequences.

Some individuals are unable to fund Coverdell Education Savings Accounts due to income limits. The ability to contribute phases out for individuals with AGI of $95,000 and when the individual has AGI of $110,000, they can no longer contribute into a Coverdell IRA. For joint filers with AGI of $190,000, the ability to contribute to a Coverdell IRA begins to phase out and cone the AGI is $220,000 they can no longer contribute.

Section 529 Plans

Education is very expensive. Under Section 529 of the tax code, Congress has authorized the creation of state sponsored qualified tuition programs.

Contributions to these qualified plans are considered gifts under the federal tax code and eligibility for participation is not subject to income limitations. Section 529 plans often allow for much larger contributions when compared with Education IRAs. For example, some state plans are structured to permit an individual to gift up to $65,000 in a given year without triggering federal tax liability. (The lump sum is viewed as five annual $13,000 gifts made in one calendar year.)

Contribution limits and investment choices vary from plan to plan. Some plans offer a fixed, aged-based asset allocation, while others give investors investment choices and the ability to periodically adjust the portfolio.

Although not required to do so, many investors select their home state plan to capture additional state tax advantages. Whether instate or out-of-state, investment income from all plans is free from federal taxation as long as it is used for qualified education expenses. As is the case with Education IRAs, plan assets may be transferred from one relative to another without tax consequences.

In most states, if a withdrawal is taken out of a 529 plan and is not used for higher education, the donor will pay a 10% penalty on the withdrawal plus ordinary income on any earnings. However, there are some withdrawals for reasons other than for higher education that would allow the donor to remove the funds without the 10% penalty. They include, if the beneficiary:

- receives a scholarship
- is disabled and can not attend a college/university
- is deceased

Chapter 2: Page 66

Annual Exclusion

Gifts to an individual with a value that does not exceed an annual exclusion amount are not subject to gift taxation. The annual exclusion amount is indexed for inflation and is $13,000 for 2009. The exclusion is

available for gifts given to each individual by the donor, so a single donor can give gifts that do not exceed the annual exclusion amount to any number of individuals.
A married couple may give a joint gift to an individual equal to twice the annual exclusion without triggering the gift tax. For example, if the annual exclusion is $13,000, a married couple could give $13,000 each to any recipient without incurring gift tax, for a total gift of $26,000.

Chapter 3, page 88
Investing in Foreign Securities (International Investing)

Investors are not limited to investing in ADRs but may also invest in foreign securities on foreign exchanges. There are two primary reasons why U.S. based investors would want to invest directly in foreign shares (often called ordinary shares):

1. Diversification:Investing overseas allows investors to spread investment risk among foreign companies and markets not correlated to the United States economy, and

1. Growth: Foreign markets, particularly emerging markets, can provide domestic investors with the opportunity to take advantage of economies with significantly different growth rates than those in the United States.

These advantages have to be balanced against the possibility of higher costs, sudden changes in n value, and the special risks involved international investing.

The risks involved in international investing are:
- Foreign exchange exposure. Change in exchange rates can increase or reduce the value of the investment. In addition, some countries impose exchange controls that can restrict or delay the conversion of the currency.
- Volatility. Many markets, especially emerging markets, can be extremely volatile.
- Political and economic risk. Investors must take into consideration the political, economic, and social factors that influence the price of foreign markets.
- Liquidity. Foreign markets are often less liquid. They may be open a few hours a day, may have restrictions of the amount or type of stocks that foreign investors may purchase.
- High information and execution costs. Many foreign markets charge higher commissions and executions than in the United States, and withholding taxes.

Chapter 4: Page 100
Term Bonds

Term bonds are quoted in decimals and as a percentage of par. Please note that in the past, these bonds were quoted in 1/8s. Let's look at a few examples of term bond quotes.

A bond with a price of 92 means 92% of par. Since par is always assumed to be $1,000, the bond is quoted at $920 ($1,000 x .92). A bond trading below $1,000 is known as a discount bond. If the price of this bond increased to 93, that is an increase of one point. A point represents 1% of par or $10.

A bond quoted at 103.375 means 103.375% of par. Therefore, this bond is trading at 103.375% of par. In order to get rid of the percentage sign, the decimal must be moved one place to the right, which is a price of $1,033.75. This bond is trading above $1,000 and is therefore known as a premium bond.

A bond priced at 100 is known as a par bond. A calculation is unnecessary since a price of par means its price is $1,000.

Chapter 4: Page 104
Comprehension Check Question 8

What price would be paid for a bond quoted at 103.75?

Chapter 4: Page 106
Comprehension Check Answer to Question 8

8. ***D***

The quote of 103.75 translates into $1,037.50. This is done in the following manner: 103.750% of par ($1,000) = $1,037.50 (move the decimal one place to the right to eliminate the percentage sign).

Chapter 4: Page 123
Treasury Notes and Treasury Bonds

T-notes and T-bonds have many similarities. The major difference between them is their respective times to maturity. T-notes are issued with initial maturities of 2 to 10 years, while T-bonds are issued with initial maturities exceeding 10 years. Following are the characteristics they have in common.

- Issued at par
- Pay semiannual interest
- Trade with accrued interest
- Have minimum denomination of $100 (while the US Treasury now offers these in $100 denominations, the exam will likely use a standard par value of $1,000)

Chapter 4: Page 111
Brady Bonds

Similar to Eurodollar bonds, Brady bonds are bonds which were issued by emerging market countries, particularly in Latin America, which are denominated in US dollars. These bonds are unique in that they are collateralized by US Treasury STRIPS (discussed later).

Chapter 6: Page 237
Add Rule 144 and Rule 144A information before Comprehension check

Rule 144
This regulation lays down some ground rules for sales of two types of securities: restricted stock and control stock.

- Restricted stock: As we have seen in our discussion of Regulation D, stock that is sold through a private placement is unregistered and may not be resold without either registration or an exemption. This is restricted stock, and Rule 144 provides an exemption under which it can be resold.

- Control stock: These securities have previously been registered and ordinarily could be freely resold, except for one important detail: Their owner is a control person, someone with the ability to influence the actions of the issuer. This would include officers, directors, and owners of at least 10% of the issuer's stock.

Holding Period
This first condition of Rule 144 applies only to restricted stock, not to control stock. Owners of restricted stock must hold he securities, fully paid, for at six months before selling under Rule 144. Note that this restricted period was previously 12 months.

Volume Limitation
The amount of restricted or control stock that may be sold under Rule 144 during any three-month period is the greater of:
1. 1% of the outstanding issuer securities of that class (e.g., 1% of the outstanding common stock) or
2. For listed or Nasdaq stocks, the average weekly trading volume for the past four calendar weeks.

Rule 144A
In many cases, the purchasers of private placements are institutional investors, who are hardly your average public investors. To accommodate the trading of restricted securities in which the purchaser is a sophisticated institutional investor, the SEC created Rule 144A. An investor who is qualified to buy under Rule 144A is called a qualified institutional
buyer (QIB). QIBs include the following if they control at least $100 million in securities:

- Insurance companies
- Investment companies
- Employee pension plans
- Corporations
- Partnerships
- Registered investment advisers

Chapter 6: Page 255 and 256
Listing Standards

While almost any security can be quoted in the Pink Sheets, only quotes for stocks that meet Nasdaq listing standards may be placed on the system. Nasdaq imposed standards that include tests for financial strength and minimum requirements for number of shareholders, number of shares in the hands of the public, and number of market makers. Companies that meet the minimum standards for listing are classified as *Nasdaq Capital Market* issues. Issuers who meet a second, more stringent set of listing standards are considered *Nasdaq Global Market* securities. Global Market issuers tend to be larger companies whose stock is more heavily traded than those in the Capital market. Note that the Nasdaq Capital Market was previously referred to as Nasdaq SmallCap and the Nasdaq Global Market was previously the Nasdaq National Market (NNM)

Chapter 6: Page 258
Comprehension Check Question 27

27. Stocks in which tier of Nasdaq have met more stringent listing standards?
A. Nasdaq Capital Market
B. Nasdaq Global Market

Chapter 6: Page 260
Comprehension Check Answer to Question 27

27. ***B***
To be classified as a Nasdaq Global Market security, issuers must meet more stringent listing standards than those required to be listed as a Nasdaq Capital Market security.

Chapter 7: Page 276
Correlation

If securities have a positive correlation, they tend to move in the same direction. Securities with a negative correlation tend to move in opposite directions. Correlations can range from -1 to +1. A correlation of +1.0 means the stocks move in perfect unison. Any positive number below +1.0 means the stocks move in the same direction, but the movement is less closely related. Negative correlation means the stocks tend to move in opposite directions. A 0 correlation indicates that there is no relationship between the price movements of one security and another.

Chapter 7: Page 278
Sharpe Ratio Calculation

Portfolio return - Risk-free rate of return
Standard deviation of portfolio's return

Chapter 7: Page 278
Efficient Market Hypothesis

EFFICIENT MARKETS HYPOTHESIS (EMT)

The efficient markets theory is one that relies on the various levels of information available to investors. One important assumption of the efficient market hypothesis is that new information regarding securities comes to the market in a random fashion and that security prices adjust to or reflect all new information available in the market.
The theory actually takes three forms: (1) Weak-form Efficient Market Hypothesis; (2) Semi-strong form Efficient Market Hypothesis; and (3) Strong-form Efficient market Hypothesis.

Weak-form Efficient Hypothesis
The weak-form of the EMH assumes that current security prices fully reflect all security market information, including the historical sequence of prices, rates of return, trading volume data, and other market-generated information, such as old-lot transactions, block trades, and transactions by exchange specialists. Because it assumes that current market already reflect all past returns and any other security market information, this hypothesis implies that past rates of returns and other historical market data should have no relationship with future rates of return. Therefore, this hypothesis contends that you should gain little form using any trading rule that decides whether to buy or sell a security based on past rates of return or any other past market data.

Semi-strong Form Efficiency Market Hypothesis
The semi-strong-form of the EMH suggests that the current security prices fully incorporate all publicly available information. Public information includes not only past prices, but also data reported in a company's financial statements (annual reports, income statements, filings for the Security and Exchange Commission, etc.), earnings and dividend announcements, announced merger plans, the financial situation of company's competitors, expectations regarding macroeconomic factors (such as inflation,), etc. In fact, the public information does not even have to be of a strictly financial nature. For example, for the analysis of pharmaceutical companies, the relevant public information may include the current (published) state of research in pain-relieving drugs.

The assumption behind semi-strong market efficiency is still that one should not be able to profit using something that "everybody else knows" (the information is public). Nevertheless, this assumption is far stronger than that of weak-form efficiency. Semi -strong efficiency of markets requires the existence of market analysts who are not only financial economists able to comprehend implications of vast financial information, but one should not be surprised that investment companies analyzing many of the high -tech industries have started employing experts from many non-financial areas (such as medical doctors, pharmacists, biochemists, etc.) in order to be able to assess viability of projects undertaken by high -tech companies.

Arguably, acquisition of such skills must take a lot of time and effort. In addition, the "public" information may be relatively difficult to gather and costly to process. It may not be sufficient to gain the information from, say, major newspapers and company-produced publications. One may have to follow wire reports, professional publications and databases, local papers, research journals etc. in order to gather all information necessary to effectively analyze securities.

Strong-form Efficient Market Hypothesis
The strong-form of the EMH contends that stock prices fully reflect all information from from public and private sources. The means that no group of investors has monopolistic access to information relevant to the formation of prices. Therefore, this hypothesis contends that no group of investors should be able to consistently derive above-average risk-adjusted rates of return. The strong-form of the EMH encompasses both the weak-form and the semistrong-form of the EMH. Further, the strong form of the

EMH extends the assumption of efficient markets, in which prices adjust rapidly to the release of new public information, to assume perfect markets, in which all information is cost free and available to everyone at the same time.

Implications of the Efficient Market Hypothesis
Most academic studies indicate that the stock market is highly efficient, and consequently, investors gain from active management strategies. Attempts to beat the market are not likely to be successful and can reduce returns as a result of transaction costs.

The EMH implies that although investors should follow a passive investment strategy, returns can be optimized through diversification and asset allocation, and by minimization of investment costs and taxes. In addition, the portfolio manager must choose a portfolio that is geared toward the time horizon and risk profile of the investor. The appropriate mixture of securities may vary according to the age, goals, tax bracket, employment, and risk aversion of the investor.

Chapter 7: Page 282
Comprehension Check Answer to Question 16

16. ***C***
The Sharpe Ratio is calculated as (Portfolio return - risk-free return) ÷ Standard Deviation of the portfolio's return. The numerator is the extra return the portfolio earns above the risk-free rate, while the denominator is a measure of the portfolio's risk. Another way to describe the Sharpe Ratio is to say that it measures the portfolio's risk adjusted return.

Chapter 9: Page 373
Roth IRAs: Contribution Limits

Roth IRAs are subject to the same contribution limits as the traditional IRA. Contributions to a Roth are always made on a post-tax basis and may even be made by workers after the age of 70 1/2. One major difference between the Roth and the traditional IRA is contribution eligibility. Even millionaires may contribute to a traditional plan if they have earned income, but income levels may limit an investor's eligibility to make any Roth contributions. The ability to contribute begins to phase out for individuals earning $105,000 AGI and joint filers earning $167,000. Currently, any individual earning above $120,000 AGI (couples above $177,000) is not eligible to make a contribution in that year. High-income Roth account holders are not required to liquidate their holdings, as prior contributions may remain within a previously established Roth.

Chapter 9: Page 375
Comprehension Check Question 10

10. What is the maximum annual contribution to an IRA?
A. $2,000
B. $5,000
C. $12,000

Chapter 9: Page 375
Comprehension Check Question 11

11. Mitch has an adjusted gross income for tax year 2009 of $510,000. Therefore, he cannot contribute to a traditional IRA.

A. True
B. False

Chapter 9: Page 378

Comprehension Check Answer to Question 10

*10. **B***

The current maximum annual contribution to both traditional and Roth IRAs is $ 5,000.

Chapter 9: Page 378
Comprehension Check Answer to Question 11

*11. **B***

As long as an individual has earned income, he can contribute to an IRA without regard to his level of income. The maximum that he can contribute is 100% of earned income or $5,000, whichever is less.

Chapter 9: Page 378
Comprehension Check Answer to Question 14

*14. **A***

The engineer would still be able to make a partial contribution since his income does not exceed $120,000. The retired chemist has no earned income and would not be eligible to make a contribution.

FINRA

In July of 2007, NASD merged with the member regulation, enforcement and arbitration functions of the New York Stock Exchange to create a new regulatory body: the Financial Industry Regulatory Authority, or FINRA.

Please note that while NASD no longer technically exists, it is very likely that, at the present time, Series 65 test takers may continue to see reference to NASD and NASD rules in their exams. For purposes of the Series 65, it may be helpful to think of NASD and FINRA as being interchangeable.