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**Exam** : **AFP-Exam-1**

**Title** : Applied Financial Planning  
Certification Exam 1 (AFP)

**Vendor** : CSI

**Version** : DEMO

**NO.1** Todd, a financial planner, is meeting with Vanessa, a new client, to review her investment goals and objectives. During the meeting, Vanessa states that she believes the markets are very efficient and should reflect all available information in the price of securities. She is looking for an investment option that will reflect a similar level of risk and return characteristics as the Canadian market. What investment option should Todd recommend with Vanessa that would reflect her opinions?

- A. Canadian neutral balanced fund.
- B. Canadian value mutual fund.
- C. Canadian exchange-traded fund.
- D. Canadian hedge fund.

**Answer:** C

Explanation:

Vanessa's belief points directly to passive market exposure. If she accepts that markets are efficient and wants risk and return characteristics similar to the Canadian market, an exchange-traded fund tracking a broad Canadian equity index is the most consistent recommendation. An ETF can provide diversified Canadian market exposure, transparent holdings, intraday liquidity, and typically lower management cost than many actively managed strategies. A Canadian value mutual fund is an active or style-biased mandate and may depart materially from total market characteristics. A neutral balanced fund includes fixed income and therefore will not mirror the Canadian equity market. A hedge fund may use leverage, short positions, derivatives, or absolute-return strategies, which do not match her stated view. Todd must still confirm KYC information and suitability, but among the options, the Canadian ETF best operationalizes an efficient-market philosophy. Study Guide focus: passive investing, ETFs, diversification, efficient markets, and investment objective alignment. The recommendation should still be framed inside Vanessa's KYC profile rather than presented as a universal market rule.

**NO.2** In which life cycle stage would a financial planner identify his client to be if they have a high mortgage balance and an unstable or lower income, and are willing to take on investment risk because of their longer time horizon?

- A. Financial independence.
- B. Accumulation.
- C. Consolidation.
- D. Gifting.

**Answer:** B

**NO.3** Kendrick, age 55, owns a successful small business, ZXC Inc., valued at \$800,000. Kendrick has extensive savings outside of the business and would like to pass the company onto his son at some point in the future.

Kendrick expects the business to increase in value \$25,000 per year. If Kendrick decides to use an estate freeze to reduce the amount of taxes he will be required to pay, his financial planner should recommend that he implement the estate freeze at which point in relation to gifting the business to his son?

- A. To take effect at the time of his passing.
- B. One month prior to gifting the company.
- C. Immediately.

D. At the same time as gifting the company.

**Answer:** C

**NO.4** A retiree holds most of her investments in interest-bearing GICs inside a non-registered account while her TFSA is invested in cash. She has unused TFSA room and wants to improve after-tax efficiency without increasing total portfolio risk materially. What should the planner consider?

A. Withdrawing RRIF minimums and gifting them immediately.

B. Holding more interest-bearing assets inside the TFS

C. Moving all assets into speculative equities.

D. Borrowing to invest in the non-registered account.

**Answer:** B

**NO.5** Matias is working on estate planning recommendations for his client Cynthia. After a recent meeting, Matias is confident that an estate freeze would be the best option for her. Which factor would have determined that the estate freeze was the best recommendation for him to give Cynthia?

A. Her children have higher marginal tax rates than her.

B. The economy is about to enter a period of hyper-inflation.

C. She requires flexibility in updating beneficiaries.

D. She can afford to live on a fixed stream of income.

**Answer:** D

Explanation:

An estate freeze is suitable only if Cynthia can live on the fixed economic interest she retains. The freeze typically converts her growth interest into fixed-value preferred shares and transfers future growth to children, a trust, or other successors. That structure is poor planning if she still needs flexible access to future growth for lifestyle, health-care costs, or retirement security. The children's higher marginal tax rates would not support a freeze for income-splitting purposes. Hyperinflation actually increases the risk that a fixed income stream becomes inadequate. A need for flexibility in changing beneficiaries may point away from a rigid freeze unless a trust is carefully designed. The answer is therefore D: Cynthia's ability to live on a fixed stream of income is the factor that makes the freeze viable. Study Guide focus: estate-freeze suitability, retained preferred shares, income sufficiency, growth transfer, and estate planning risk. The planner should stress-test retirement income, health costs, and inflation before concluding that the freeze is affordable.

**NO.6** Dianna is visiting with Karen, her Financial Planner, and is excited to report that she has just bought her dream home. She has also let Karen know she is meeting with an insurance representative to purchase a whole life insurance to cover her 20-year mortgage. Why might Karen suggest Dianna consider term life insurance instead?

A. The client's health may deteriorate as she gets older.

B. The term policy has a cash value, which can be borrowed against.

C. It is better suited for long term insurance needs.

D. The cost of premiums is lower than whole life.

**Answer:** D

Explanation:

Karen's recommendation should match the insurance product to the liability. Dianna's need is

temporary: a 20-year mortgage balance that would create financial hardship if she died before the debt was retired. Term life insurance is designed for temporary capital needs and normally provides the largest amount of death benefit for the lowest initial premium because it contains no cash-value savings component. Whole life can be appropriate for permanent estate liquidity, final taxes, charitable objectives, or lifetime dependency needs, but those facts are not present. Option A may be true as a general underwriting concern, but it does not explain why term is better for this mortgage need. Option B is false because term insurance does not build cash value.

Option C describes permanent needs, not a 20-year mortgage. The AFP planning conclusion is that term coverage should be considered where the risk period and capital need are limited. Study Guide focus: needs-based insurance analysis, term versus permanent insurance, mortgage protection, and product suitability.

**NO.7** A client believes that security prices quickly reflect public information and wants broad Canadian equity exposure with low cost and minimal manager discretion. What investment best matches this view?

- A. Canadian index exchange-traded fund.
- B. Sector-specific hedge fund.
- C. Portfolio of five selected mining stocks.
- D. One-year cashable GIC.

**Answer:** A

Explanation:

The client's belief is consistent with efficient-market thinking: if prices already reflect public information, paying for active security selection may add cost without reliable excess return. A Canadian index ETF offers broad market exposure, transparent holdings, intraday liquidity, and generally low management cost. Option B relies on active or alternative management and may involve leverage, shorting, concentration, or complex strategies that conflict with the stated preference. Option C introduces substantial unsystematic risk because five mining stocks do not represent the Canadian equity market. Option D preserves capital but does not provide equity-market exposure. The planner should still perform suitability work: risk tolerance, time horizon, liquidity needs, tax location, and concentration in the client's existing assets must be reviewed. The product answer is not "ETF because ETFs are always best"; it is ETF because the investment philosophy and desired exposure point to passive, diversified market replication. References/topics: efficient market theory, passive investing, ETFs, diversification.

**NO.8** In order to increase the assets in Rebecca's retirement savings, her financial planner is considering making a number of recommendations. Prior to obtaining her current employment, she withdrew funds from her RRSP under the Lifelong Learning Plan to upgrade her skills. She has four annual installments remaining on her Lifelong Learning Plan withdrawal and a small amount of savings in a TFSA. Rebecca now works as a sales associate in a small clothing store that has a group RRSP program for all employees which matches employee contributions. Which recommendation provides the best long-term impact to grow her retirement savings?

- A. Transfer her existing TFSA savings to her RRSP and start a monthly contribution plan.
- B. While keeping within her risk tolerance, maximize the equity component of her RRSP and TFSA plans in order to achieve significantly better returns over time.
- C. Repay the final four annual installments remaining on her Lifelong Learning Plan and start a

monthly contribution plan to her RRSP.

**D.** Enroll in her company's group RRSP program and start a monthly contribution.

**Answer:** D

Explanation:

The company group RRSP match is the strongest long-term retirement recommendation because it provides immediate additional savings from the employer. A matching contribution is effectively a guaranteed enhancement to Rebecca's retirement funding that she cannot replicate by simply transferring her TFSA or changing her asset mix. Repaying the Lifelong Learning Plan installments is required, but it does not create new employer-funded retirement capital. Maximizing equity exposure may improve expected return, but it must remain within risk tolerance and does not replace the value of free matching contributions. Transferring TFSA savings to an RRSP may produce a deduction, yet it sacrifices TFSA flexibility and does not address the employer match. The AFP planning priority is to capture available employer contributions first, then coordinate LLP repayments, TFSA use, and ongoing RRSP savings. Study Guide focus: group RRSPs, employer matching, LLP repayment, retirement accumulation, and savings prioritization. Missing the match would leave employer money unclaimed, which is rarely defensible when the employee can afford the contribution.

**NO.9** A client wants to increase net worth by identifying spending reductions and increasing monthly surplus.

Which document is most useful for this purpose?

**A.** Net worth statement only.

**B.** Current cash flow statement and budget.

**C.** Beneficiary designation form.

**D.** Investment policy statement only.

**Answer:** B

Explanation:

Expense control is a cash flow problem. A net worth statement shows assets, liabilities, and net worth at a point in time, but it does not explain where monthly income is going. A current cash flow statement identifies inflows and outflows, while a budget converts that information into a forward-looking spending and savings plan. Option A is incomplete because the balance sheet can show that debt exists but not which behaviours are creating or reducing surplus. Option C relates to estate transfer, not spending control. Option D governs investment objectives and constraints; it does not normally capture household expense categories. To increase net worth, the planner must connect the income statement and balance sheet: reduce unnecessary outflows, direct surplus to debt repayment or savings, and measure progress through updated net worth statements. The practical planning sequence is diagnose cash flow, set a budget, automate surplus allocation, and review outcomes. References/topics: cash flow statement, budgeting, net worth improvement, expense management.

**NO.10** Mina has \$20,000 in a savings account earning 3% before tax. She also has a \$9,000 credit card balance at

22%, a \$7,000 unsecured line of credit at 10%, and a \$14,000 car loan at 4%. Her marginal tax rate is 35%.

Which liability should she target first?

- A. Car loan.
- B. Credit card balance.
- C. Unsecured line of credit.
- D. No debt; keep all funds in savings.

**Answer:** B

Explanation:

The credit card is the highest-cost non-deductible liability and should be the first repayment target, subject to retaining an adequate emergency reserve. Mina's savings account produces only 3% before tax, or 1.95% after tax at a 35% marginal rate. That return is overwhelmed by a 22% credit card rate. Paying the card produces a risk-free improvement equal to avoided interest; no conservative investment can justify carrying that balance. Option A is lower priority because the car loan rate is modest. Option C is important but still secondary to the credit card. Option D ignores the after-tax spread between savings income and debt cost. The planning principle is not simply "pay debt"; it is to compare after-tax investment returns with after-tax borrowing costs, prioritizing expensive consumer debt while preserving liquidity. The planner should then structure a repayment plan and address the spending pattern that created the balance. References/topics: debt prioritization, cash flow, after-tax return, asset and liability management.

**NO.11** A client wants a policy that pays a lump sum if she is diagnosed with a covered serious illness and survives the required waiting period. Which product matches this need?

- A. Long-term care insurance.
- B. Disability insurance.
- C. Accidental death insurance.
- D. Critical illness insurance.

**Answer:** D

Explanation:

Critical illness insurance is structured around diagnosis, survival period, and a lump-sum benefit. It is not designed primarily to replace monthly employment income; it provides capital that the insured can use for treatment costs, debt reduction, time away from work, travel, home modifications, private care, or family support. Option A is different: long-term care insurance responds to loss of independence, inability to perform activities of daily living, or cognitive impairment requiring care. Option B replaces income when a disability prevents work, usually through periodic benefits. Option C pays on accidental death and does not assist a living insured who survives a serious illness. In a planning file, the product should be tested against existing disability coverage, emergency reserves, debt obligations, family support needs, and affordability. Policy wording matters: covered conditions, exclusions, definitions, survival period, recurrence provisions, and return-of-premium options should be reviewed. References/topics: critical illness insurance, health risk, lump-sum benefit, insurance needs analysis.

**NO.12** If a deceased person was entitled to rights or things at death, what strategy should the estate representative use to enhance the net estate value after tax?

- A. Transfer ownership of the rights or things to the beneficiaries of the estate.
- B. Include the rights or things in a second personal tax return for the deceased.
- C. Include the rights or things in the deceased's final personal tax return.
- D. File for annual tax reassessments on the terminal tax return until all rights or things are paid.

**Answer: B**

Explanation:

Rights or things are amounts the deceased was entitled to receive at death but had not yet received, such as unpaid employment income, declared dividends, or certain other receivables. The estate representative can often file a separate optional return for rights or things. This can enhance the net estate value because graduated tax rates and separate credits may reduce the total tax compared with including everything on the terminal return. Transferring ownership directly to beneficiaries does not address the tax-reporting opportunity. Including the amounts only on the final return may be administratively simpler but may produce more tax. Filing annual reassessments until payment is received is not the planning strategy. The AFP point is that optional returns can be used after death to minimize tax where the deceased had qualifying income categories. The executor should coordinate with a tax professional to identify eligible rights or things and filing deadlines. Study Guide focus: terminal returns, optional returns, rights or things, estate taxation, and post-mortem tax planning.