Insurance Test Practice

Colorado Insurance Practice Test

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1. The mandatory 'Time of Payment of Claims' provision requires the insurer to pay claims:

A) Within 30 days of receiving notice of claim
✔ B) Immediately upon receiving proper proof of loss
C) Within 60 days of receiving proof of loss
D) Within 90 days of the date of loss

Explanation: The insurer must pay benefits immediately upon receipt of due written proof of loss. For disability income benefits, periodic payments must be made at least monthly, if the period of disability is sufficiently long.

2. Under the ACA dependent coverage provision up to what age must health plans allow adult children to remain on a parent's plan?

✔ A) Age 26
B) Age 25
C) Age 21
D) Age 23

Explanation: The ACA requires all health plans that offer dependent coverage to allow children to remain on their parent's plan until they turn 26, regardless of the child's marital status, financial dependency, student status, or availability of employer-sponsored coverage.

3. What is a common benefit trigger for a Long-Term Care policy besides being unable to perform ADLs?

A) Reaching age 65
B) Being unemployed for over a year
✔ C) Having a severe cognitive impairment
D) A physician's diagnosis of a chronic illness

Explanation: LTC benefits are typically triggered if the insured is either (1) unable to perform a specified number of ADLs, or (2) requires substantial supervision to protect their health and safety due to a severe cognitive impairment, such as Alzheimer's or dementia.

4. 'Separate account' assets in variable life insurance are:

✔ A) Legally segregated from the insurer's general account and protected from the insurer's creditors
B) Blended with the insurer's general account for unified investment management
C) Accessible only after the insurer's general account obligations are satisfied
D) Managed by a federally regulated bank on behalf of the insurer

Explanation: The separate account in a variable life or variable annuity product is legally segregated from the insurer's general account assets. This segregation protects policyholders' subaccount investments from the insurer's creditors in the event of insolvency. Separate account assets are NOT available to the insurer's general creditors.

5. In a deferred annuity, what is the 'surrender charge'?

A) A fee for annuitizing the contract.
B) A fee for taking out a loan.
✔ C) A penalty for withdrawing money from the annuity during a specified period after purchase.
D) The tax on the annuity's earnings.

Explanation: A surrender charge is a type of back-end sales charge. It is a penalty assessed if the owner withdraws funds from the annuity during the surrender charge period, which typically lasts for the first 5 to 10 years of the contract. The charge is usually a percentage of the amount withdrawn and declines over time.

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6. In a fixed-indexed annuity, the 'annual reset' (ratchet) feature means:

A) The owner must reconfirm their investment selections each year
✔ B) Each year's interest is locked in and the new starting index value is reset at the year-end level, protecting gains from future market declines
C) The index value resets to zero each year and starts fresh
D) The insurer resets the cap rate and participation rate annually based on market conditions

Explanation: The annual reset (ratchet) feature locks in index-linked interest credits at the end of each year. The new starting value for the next crediting period is then set at the year-end index level. This means prior year gains are protected from future index declines — a key consumer benefit of indexed annuities over direct index investing.

7. The 'level' in level term insurance refers to:

A) Only the premium remaining constant while the death benefit increases
B) A level risk that never changes over the term
C) The policy being available at multiple coverage levels
✔ D) Both the premium and the death benefit remaining constant throughout the entire term

Explanation: Level term insurance provides a constant (level) death benefit and a constant (level) premium for the entire specified term period. This is the most common and simplest form of term life insurance. It provides predictable, stable costs and protection.

8. Group underwriting differs from individual underwriting primarily because the underwriter evaluates which of the following?

A) Each individual member's health history in detail
B) The financial status of each member's beneficiary
✔ C) The characteristics of the group as a whole rather than individual members
D) Only the youngest members of the group

Explanation: Group underwriting focuses on the characteristics of the group itself, such as size, type of industry, turnover rate, and age distribution, rather than the health of each individual member. This is a fundamental principle of group insurance.

9. Under what circumstances are life insurance premiums paid by a business deductible as a business expense?

A) When the business is the beneficiary of the policy.
B) Premiums are never deductible.
C) When the policy is a term life policy.
✔ D) When the employee's family is the beneficiary and the premium is treated as a bonus.

Explanation: If a business pays the premium for an employee's life insurance policy where the employee's family is the beneficiary (e.g., in an executive bonus plan), the premium is considered compensation to the employee. It is deductible for the business and taxable income for the employee.

10. An individual health insurance policy that the insurer cannot cancel and cannot increase the premium on is classified as:

A) Optionally renewable
✔ B) Non-cancellable
C) Conditionally renewable
D) Guaranteed renewable

Explanation: A non-cancellable policy provides the strongest protection for the insured. The insurer cannot cancel the policy, raise the premium, or reduce benefits, as long as premiums are paid on time. This is the most expensive type of renewability provision.

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11. What is the purpose of the Automatic Premium Loan (APL) provision?

✔ A) To automatically pay a premium from the policy's cash value to prevent a lapse.
B) To allow the insurer to increase the premium automatically.
C) To provide a loan to the policyowner for any purpose.
D) To provide a loan to pay for a different insurance policy.

Explanation: The Automatic Premium Loan (APL) provision is an optional feature that authorizes the insurer to use the policy's cash value to pay a premium that is past due. It is essentially a loan against the cash value to prevent an unintentional policy lapse.

12. Variable Universal Life (VUL) insurance combines features of:

A) Annuities and term life insurance
B) Group life and individual life insurance
✔ C) Universal life (flexible premiums) and variable life (subaccount investing)
D) Whole life and term life insurance

Explanation: Variable Universal Life (VUL) combines the flexible premiums and adjustable death benefit of universal life with the investment component (separate account subaccounts) of variable life. The policyowner can vary premiums and allocate cash values among investment subaccounts, bearing all investment risk.

13. A foreign insurer is found to have committed a series of intentional violations of rate regulations in Colorado. What is the maximum civil penalty the Commissioner can impose for each intentional violation?

A) Up to $1,000 per violation
✔ B) Up to $5,000 per violation
C) Up to $10,000 per violation
D) Up to $50,000 per violation

Explanation: Under Colorado law, the Colorado Division of Insurance (CDOI) may impose a civil penalty of up to $5,000 per intentional violation.

14. How much can an employer charge a former employee for COBRA continuation coverage?

✔ A) 102% of the premium
B) 110% of the premium
C) 150% of the premium
D) 100% of the premium

Explanation: The employer can charge the former employee up to 102% of the total premium (the employee's share plus the employer's share). The extra 2% is to cover administrative costs.

15. A policyholder has an insolvent life insurance policy. What is the maximum coverage provided by the Colorado Guaranty Association for cash surrender value?

A) $50,000
✔ B) $100,000
C) $250,000
D) $300,000

Explanation: The Association covers up to $100,000 in life insurance cash surrender or withdrawal values.

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16. How many categories of Essential Health Benefits (EHBs) are required under the Affordable Care Act?

A) 8
B) 5
C) 12
✔ D) 10

Explanation: The ACA mandates that all individual and small group health insurance plans cover 10 categories of Essential Health Benefits, including ambulatory services, emergency services, hospitalization, maternity and newborn care, mental health and substance use disorder services, prescription drugs, rehabilitative services, laboratory services, preventive and wellness services, and pediatric services including dental and vision.

17. An insurer refuses to issue a health policy to a person solely because they possess the sickle-cell trait. Under Colorado law, what is this action classified as?

- ✔ A) Unfair discrimination
- B) Acceptable underwriting practice
- C) Redlining
- D) Boycott

Explanation: Refusing to issue a policy or charging higher premiums solely because an individual has genetic traits like sickle-cell is illegal unfair discrimination.

18. What is a Business Overhead Expense (BOE) disability policy designed to cover?

- ✔ A) The fixed business expenses, such as rent and utilities, when the owner is disabled.
- B) The cost of buying out a disabled partner.
- C) The cost of hiring a permanent replacement for the disabled owner.
- D) The business owner's lost income.

Explanation: A BOE policy is owned and paid for by the business. If the business owner becomes disabled, the policy pays a benefit to the business to cover ongoing overhead expenses (rent, salaries, utilities, etc.). The owner's salary is not covered.

19. A fraternal benefit society differs from a stock or mutual insurer because it:

- A) Only provides group life insurance to employers
- B) Is regulated by the federal government, not state agencies
- ✔ C) Is nonprofit and sells insurance only to its own members through a lodge system
- D) Sells coverage to the general public without any membership requirement

Explanation: A fraternal benefit society is a nonprofit organization with a lodge or ritualistic structure that provides insurance and social benefits only to its members. Membership is usually based on a common bond such as religion, ethnicity, or profession.

20. In a group health insurance plan, the contract is between the:

- A) Employee and the employer
- B) Employer and the state
- C) Employee and the insurer
- ✔ D) Employer and the insurer

Explanation: In a group plan, the master policy is held by the sponsoring organization (the employer). The contract exists between the employer and the insurance company.

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21. The 'spread' in a fixed-indexed annuity is:

- ✔ A) A percentage that is deducted from the index return before crediting interest to the annuity
- B) The difference between the cap rate and the floor rate
- C) The difference between the credited rate and the guaranteed minimum rate
- D) The insurer's profit margin disclosed in the prospectus

Explanation: A spread (or 'asset fee') is a type of index crediting method in which the insurer deducts a fixed percentage from the index return before crediting the annuity. For example, if the index gains 8% and the spread is 2%, the annuity is credited 6%. Spreads, caps, and participation rates all limit the annuity owner's upside in exchange for downside protection.

22. The Fair Credit Reporting Act (FCRA) gives consumers the right to:

A) Correct any errors in their MIB report.
B) Prevent insurers from accessing their credit history.
✓ C) Receive a copy of any consumer report an insurer uses.
D) Demand insurance coverage regardless of their credit score.

Explanation: The FCRA protects consumers' privacy regarding information collected by credit reporting agencies. It requires that consumers be notified if a negative decision is made based on a credit report and gives them the right to review and dispute the information.

23. An agent distributes a pamphlet that describes a competitor as 'financially unstable and on the verge of bankruptcy,' knowing this statement is false. What trade practice has the agent violated?

✓ A) Defamation
B) Rebating
C) Churning
D) Misrepresentation

Explanation: Making or circulating false or maliciously critical statements designed to injure any person in the insurance business is defamation.

24. 'Aggregation rules' for annuity taxation mean:

✓ A) All annuities from the same insurer owned by the same person are treated as one contract for tax purposes
B) Multiple annuities can be aggregated for a tax-free 1035 exchange
C) Tax is calculated on the aggregate value of all qualified plans
D) All annuities owned by a person's family are taxed together

Explanation: IRS aggregation rules (IRC Section 72(e)(12)) treat multiple annuity contracts issued after October 21, 1988 by the same insurer to the same owner in the same calendar year as a single contract for tax purposes. This prevents owners from using multiple contracts to avoid paying gains first on withdrawals.

25. A 'cost of living adjustment' (COLA) rider on a life insurance or disability income policy:

A) Pays an additional benefit only if the cost of the funeral exceeds a set amount
B) Adjusts the premium if the cost of living in the insured's area increases
✓ C) Automatically increases the benefit over time to keep pace with inflation (often tied to the CPI)
D) Reduces the benefit if inflation causes costs to rise

Explanation: The COLA rider automatically increases the death benefit or disability income benefit periodically — often tied to changes in the Consumer Price Index (CPI) — to help the coverage keep pace with inflation. This rider is especially important for long-term disability income policies where benefits are paid for years and could lose purchasing power.

26. A 'guaranteed level premium' term policy guarantees that:

- ✔ A) Both the death benefit and premium remain unchanged throughout the guaranteed level term period
- B) Premiums will never increase under any circumstances for the insured's lifetime
- C) The policy will automatically renew at the same rate after the term ends
- D) The death benefit will remain level for the guaranteed period

Explanation: A guaranteed level premium term policy locks in both the death benefit and the premium at a fixed amount for the entire guaranteed level period (e.g., 10, 20, or 30 years). After the level period expires, premiums typically increase significantly (annual renewable term rates) and many policyholders choose not to renew.

27. Once a variable annuity is annuitized, the number of annuity units:

- A) Increases each year.
- ✔ B) Remains fixed.
- C) Fluctuates daily.
- D) Decreases each year.

Explanation: At the time of annuitization, the accumulation units are converted into a fixed number of annuity units. This number does not change for the rest of the payout period. However, the value of each annuity unit changes, causing the income payment amount to fluctuate.

28. What is a single premium deferred annuity (SPDA)?

- ✔ A) An annuity funded with one lump sum, with payments starting at a future date.
- B) An annuity funded with one lump sum, with payments starting immediately.
- C) An annuity funded with flexible premiums over time, with payments starting in the future.
- D) An annuity that only pays out a single lump sum.

Explanation: An SPDA is purchased with a single, lump-sum premium. The funds are then left to accumulate on a tax-deferred basis, and income payments are deferred until a later date chosen by the owner.

29. Which of the following describes the role of a surplus lines broker?

- A) Placing coverage with admitted insurers at preferred rates
- ✔ B) Placing coverage with non-admitted insurers when admitted coverage is unavailable
- C) Managing an insurer's investment portfolio
- D) Representing the insured exclusively as a fiduciary

Explanation: Surplus lines brokers are licensed to place coverage with non-admitted (unlicensed in the state) insurers when the risk cannot be placed with admitted companies. The broker must diligently search the admitted market first. Surplus lines policies are not protected by state guaranty funds.

30. When does the 7-pay test apply?

- A) When calculating the taxable portion of a policy loan.
- ✔ B) When determining if a life insurance policy is a Modified Endowment Contract (MEC).
- C) When a policy is transferred to a new owner.
- D) When a policy is surrendered for cash.

Explanation: The 7-pay test is the mechanism used by the IRS to determine if the total premiums paid into a life insurance policy within its first seven years are in excess of the amount needed to have the contract be paid-up in seven years. If it fails this test, it becomes a MEC.

31. Which type of insurance organization is characterized by members mutually insuring each other and being managed by an Attorney-in-Fact?

A) Mutual company
✔ B) Reciprocal insurer
C) Stock company
D) Risk retention group

Explanation: A reciprocal insurer (or reciprocal exchange) is an unincorporated organization where subscribers (policyholders) mutually insure each other. Each subscriber assumes a portion of the other subscribers' risk. The exchange is managed by an Attorney-in-Fact on behalf of all subscribers.

32. In a Health Maintenance Organization (HMO), the 'primary care physician' (PCP) serves as:

A) An administrative role with no patient care responsibilities
B) An independent contractor with no obligation to refer within the HMO network
C) The physician who performs all medical procedures within the HMO network
✔ D) The gatekeeper who coordinates care and provides referrals to specialists within the HMO network

Explanation: In traditional HMO models, the primary care physician (PCP) serves as the gatekeeper for the member's healthcare. Members must select a PCP and must obtain a referral from their PCP before seeing a specialist (except for emergencies). The PCP coordinates all of the member's care within the HMO network. This gatekeeper model is designed to control costs and ensure coordinated, appropriate care. Some newer HMO models (open-access HMOs) allow self-referrals to specialists.

33. If an insured and primary beneficiary die in a common disaster and the policy has a common disaster provision, what is the assumption?

A) The contingent beneficiary is disqualified.
✔ B) The insured survived the beneficiary.
C) The beneficiary survived the insured.
D) They died at the same time.

Explanation: The common disaster provision, or the Uniform Simultaneous Death Law, creates a presumption that the primary beneficiary died first. This prevents the death benefit from passing through the primary beneficiary's estate and ensures it goes directly to the contingent beneficiary.

34. What is another name for Medicare Part C?

A) Prescription Drug Plan
B) Medicare Supplement (Medigap)
C) Original Medicare
✔ D) Medicare Advantage

Explanation: Medicare Part C is the Medicare Advantage program. These are private health plans (like HMOs or PPOs) that are approved by Medicare and must provide at least the same level of coverage as Original Medicare (Parts A and B), but can offer additional benefits.

35. A shared care rider on an LTC policy for a couple allows:

A) The couple to share one premium payment.
B) The premium to be waived if one spouse enters a nursing home.
✔ C) One spouse to use the benefits from the other spouse's policy if their own benefits are exhausted.
D) The policy to pay for care for both spouses simultaneously.

Explanation: A shared care or shared benefit rider is a feature on two separate LTC policies for a couple. It allows them to pool their benefits. If one spouse uses up all of their policy's benefits, they can then start drawing from the benefits available under their spouse's policy.

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36. What legal principle prevents a party from re-asserting a right they have previously waived?

A) Subrogation
B) Adhesion
C) Waiver
✔ D) Estoppel

Explanation: Estoppel is the legal principle that prevents someone from arguing something or asserting a right that contradicts what they previously said or did. For example, if an insurer consistently accepts late premiums, they may be estopped from canceling the policy for a late payment.

37. An annuity is designed primarily to provide:

A) A death benefit
B) Coverage for medical expenses
✔ C) Protection against outliving one's income
D) Short-term savings

Explanation: Annuities are financial contracts issued by life insurance companies that are designed to protect against the risk of 'superannuation' or outliving your money. They provide a stream of income, typically during retirement.

38. The 'annuitization' of a deferred annuity is the process of:

A) Transferring the annuity to a new owner
B) Rolling the annuity into a qualified retirement plan
✔ C) Irrevocably converting the accumulated value into a guaranteed income stream
D) Converting cash value to a paid-up policy

Explanation: Annuitization is the irrevocable conversion of a deferred annuity's accumulated value into a series of periodic income payments based on the selected payout option. Once annuitized, the owner typically cannot access a lump sum and the arrangement is generally irreversible. Most modern annuities also offer guaranteed withdrawal benefits that provide income without full annuitization.

39. John has a dispute with his insurer over an ambiguous clause in his health insurance contract. Since the contract was written solely by the insurer with no negotiation, how will a court typically resolve the ambiguity?

A) In favor of the insurer because they wrote it
✓ B) In favor of John because the contract is a contract of adhesion
C) By declaring the contract void due to lack of mutual agreement
D) By split decision dividing the benefit 50/50

Explanation: Because insurance contracts are contracts of adhesion (offered on a 'take-it-or-leave-it' basis by the insurer), any ambiguities are legally resolved in favor of the adhering party (the insured).

40. A policyowner, David, has an individual life insurance policy in Colorado. His premium was due on May 1, but he forgot to pay. If David dies on May 20, how will the insurer handle the claim?

A) The claim will be denied because the policy lapsed on May 1.
B) The claim will be paid in full, and the premium is waived.
✓ C) The claim will be paid, but the overdue premium will be deducted from the death benefit.
D) The claim is pended for 90 days.

Explanation: Under the grace period for individual life insurance in Colorado, the policy remains in force. If the insured dies during this time, the death benefit is paid minus the overdue premium.

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41. Which of the following describes a single premium whole life policy?

A) A policy with a single beneficiary.
B) A policy that is paid up after one year.
✓ C) A policy that requires only one premium payment for the life of the contract.
D) A policy where the premium can be paid at any time.

Explanation: A single premium whole life (SPWL) policy is funded with one large, lump-sum premium at the time of purchase. The policy is instantly paid-up and provides a death benefit and tax-deferred cash value growth for the insured's entire life.

42. A 'guaranteed minimum withdrawal benefit' (GMWB) rider on a variable annuity:

A) Guarantees the owner will never lose principal in the subaccounts
B) Converts the variable annuity to a fixed annuity if subaccounts decline below a threshold
C) Guarantees a minimum death benefit equal to the original premium
✓ D) Guarantees the owner can withdraw a specified percentage of the benefit base annually regardless of subaccount performance

Explanation: A GMWB rider guarantees the owner can withdraw a specified percentage (e.g., 5-7%) of the benefit base (often the original premium or a 'high-water mark') annually without triggering the annuity's surrender charges and without depleting the guaranteed withdrawal amount — even if the actual account value falls to zero due to market losses. This provides income security in variable annuities.

43. What is the purpose of a Health Reimbursement Arrangement (HRA)?

A) It is a savings account funded by the employee.
B) It is a portable account that the employee takes with them when they leave a job.
C) It is a government program for low-income individuals.
✔ D) It is an employer-funded account that reimburses employees for qualified medical expenses.

Explanation: An HRA is funded solely by the employer; employees cannot contribute. The employer sets the terms, and the funds can be used to reimburse employees tax-free for medical expenses. Unused funds may roll over, but the account is owned by the employer and is not portable.

44. Annuity suitability regulations require the producer to make a record of:

A) The client's family medical history.
B) The producer's commission rate.
C) The client's political views.
✔ D) The recommendation made to the client and the basis for it.

Explanation: Producers must document their recommendations and the reasons why a particular product was deemed suitable. This record-keeping is a key part of complying with suitability rules and protects both the consumer and the producer.

45. When interest rates rise after an annuity is purchased, an annuity with an MVA provision may:

A) Terminate the contract and return all premiums
B) Increase the surrender value by applying a positive market value adjustment
C) Automatically increase the credited rate to match market rates
✔ D) Reduce the surrender value by applying a negative market value adjustment if the contract is surrendered

Explanation: If interest rates rise after a fixed annuity with an MVA is purchased and the owner surrenders early, a negative MVA may be applied — reducing the surrender value below the accumulation value. This reflects the insurer's loss from having to sell bonds at lower prices in a rising rate environment. Conversely, falling rates may produce a positive MVA.

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46. A replacing insurer in Colorado receives an application that involves replacing a policy from another insurer. Within how many days must the replacing insurer notify the existing insurer of the proposed replacement?

✔ A) Within 3 working days of receiving the application
B) Within 5 working days
C) Within 10 working days
D) Within 15 working days

Explanation: The replacing insurer must notify the existing insurer in writing within 5 working days (or 3 working days depending on state regulations) of receiving the application.

47. A decreasing term life policy is often used to cover:

A) Group employee benefit plans
B) Income replacement for working-age adults
C) Estate taxes for high-net-worth individuals
✔ D) A mortgage balance that decreases over time as payments are made

Explanation: Decreasing term insurance provides a death benefit that decreases over time, typically in proportion to a declining financial obligation such as a mortgage balance. The premium stays level while the coverage amount decreases. It is also used for business loans or other declining debts.

48. Under the ACA, how long can a young adult remain on their parent's health insurance plan?

A) Until age 18
B) Until they are married
C) Until age 21
✔ D) Until age 26

Explanation: The Affordable Care Act allows young adults to stay on a parent's health insurance plan until they turn 26. They can remain on the plan even if they are married, not living with their parents, attending school, or financially independent.

49. An agent, Melissa, is auditing her CE records. She realizes she has completed 28 hours of CE for her qualification, which is more than required. What happens to these extra hours?

A) A limited number of excess CE hours can be carried over to the next renewal period.
✔ B) Colorado does not allow carryover of excess CE credits.
C) She receives a cash refund.
D) She can use them to waive her ethics requirement.

Explanation: Colorado CE regulations govern the carryover of excess credits.

50. The 'residual disability' provision is important for:

A) Paying benefits after the maximum benefit period ends
B) Covering pre-existing conditions that result in partial disability
✔ C) Providing proportional benefits to insureds who return to work at reduced capacity and earn less than before their disability
D) Covering total disability only

Explanation: Residual (partial) disability benefits are essential for encouraging return to work. If an insured can work but earns less due to their disability, the residual provision pays a benefit proportional to the earnings loss. Without this provision, an insured who returns to work but earns less might have an incentive to remain totally disabled to maintain full benefits.