Insurance Test Practice

Iowa Insurance Practice Test

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1. A variable annuity and variable life insurance are alike in that both:

A) Provide a guaranteed minimum cash value regardless of investment performance
B) Must be sold with a prospectus that is updated every year
✔ C) Require a state insurance license and FINRA registration to sell
D) Are suitable for all clients regardless of risk tolerance

Explanation: Both variable life insurance and variable annuities are classified as both insurance products and securities. Producers must hold a state insurance license AND be FINRA-registered (typically with Series 6 or Series 7 plus Series 63) to sell either type of product. Both also require the distribution of a prospectus to prospective purchasers.

2. Under the ACA employer mandate, coverage is considered 'affordable' if the employee's required contribution for self-only coverage does not exceed approximately what percentage of their household income?

✔ A) 9.5% (adjusted annually for inflation)
B) 8%
C) 15%
D) 5%

Explanation: The ACA's affordability threshold is approximately 9.5% of household income (adjusted annually). If an applicable large employer offers coverage that costs the employee more than this threshold for self-only coverage, the coverage is not considered affordable, and the employee may qualify for marketplace subsidies.

3. The incontestability clause in a life insurance policy means:

A) The insured cannot contest premium increases
B) Claims can never be contested
✔ C) The policy cannot be contested by the insurer based on misrepresentation after the policy has been in force for 2 years
D) The beneficiary cannot contest the face amount

Explanation: The incontestability clause provides that after a life insurance policy has been in force for 2 years (during the contestability period), the insurer generally cannot void the policy or deny a claim due to misrepresentation or concealment on the application. Fraud may still be an exception in some jurisdictions.

4. Which of the following life insurance products is classified as a 'vanishing premium' arrangement?

A) A group term life policy with employer-paid premiums
B) A universal life policy with minimum premium payments
C) Level term with return of premium rider
✔ D) A whole life policy structured so that dividends are expected to offset the premium at a certain point (though not guaranteed)

Explanation: A 'vanishing premium' arrangement involves a participating whole life policy in which the projected dividends are expected to be sufficient to pay the premiums at a certain point, effectively making the policy self-sustaining. This is a non-guaranteed projection — if dividends are lower than projected, premiums may continue. Vanishing premium illustrations have been the subject of regulatory scrutiny for unrealistic projections.

5. What is the 'option B' death benefit in a Universal Life policy?

A) A decreasing death benefit.
✔ B) An increasing death benefit equal to the face amount plus the cash value.
C) A level death benefit equal to the policy's face amount.
D) A death benefit linked to a stock market index.

Explanation: Universal Life Option B provides an increasing death benefit. The beneficiary receives the policy's specified face amount plus the accumulated cash value. This results in a higher death benefit but also higher monthly cost of insurance deductions.

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6. What is insurable interest?

✔ A) A financial interest in the life or property being insured
B) An interest in making a profit from insurance
C) A general interest in being safe
D) The insurance company's interest in collecting premiums

Explanation: Insurable interest means that the policyowner must face a demonstrable financial loss if the insured event occurs. It must exist at the time of application for life insurance and at the time of loss for property insurance.

7. The advantage of life insurance proceeds being paid to a named beneficiary rather than the estate is:

A) Named beneficiaries receive a higher death benefit than the estate
B) Proceeds paid to a named beneficiary are completely exempt from federal estate taxes
C) The insurer waives administrative fees when paying a named beneficiary
✔ D) Proceeds bypass probate and are available more quickly and privately to the beneficiary

Explanation: Naming a specific beneficiary (rather than the estate) means life insurance proceeds avoid the probate process — they pass directly to the beneficiary quickly and privately, without court involvement or public record. Note: proceeds are still subject to estate taxes in the insured's estate if they own the policy, even when paid to a named beneficiary.

8. Under the ACA's modified community rating rules, the maximum age rating ratio that insurers may apply between the oldest and youngest adult policyholders is:

✔ A) 3:1
B) 5:1
C) 2:1
D) 4:1

Explanation: The ACA limits the age rating ratio to 3:1, meaning that the highest premium charged to the oldest adults in the individual and small group markets cannot exceed three times the premium charged to the youngest adults. This restriction prevents insurers from imposing excessively high premiums on older individuals.

9. 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.

10. A 'health reimbursement arrangement' (HRA) is characterized by:

A) A health insurance policy that reimburses providers directly
B) An employee-funded account that reimburses medical expenses
C) A retirement account that can only be used for healthcare costs after age 65
✔ D) An employer-funded account used to reimburse employees for qualifying medical expenses and premiums tax-free

Explanation: An HRA is a tax-advantaged arrangement funded ENTIRELY by the employer (no employee contributions). Employers reimburse employees for qualifying medical expenses and health insurance premiums on a tax-free basis. Unused HRA funds may roll over (at the employer's discretion). HRAs are employer-controlled and not portable.

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11. The 'employer mandate' under the ACA applies to applicable large employers (ALEs). An ALE is a business with:

A) Any employer that offers health benefits voluntarily
✔ B) 50 or more full-time equivalent employees
C) 25 or more full-time equivalent employees
D) 100 or more full-time equivalent employees

Explanation: Under the ACA, an Applicable Large Employer (ALE) is a business with 50 or more full-time equivalent employees (FTEs) in the prior calendar year. ALEs must offer minimum essential coverage to full-time employees and their dependents, or potentially owe an employer shared responsibility payment (employer penalty).

12. 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.

13. In an insurance contract, the insured's consideration is the:

A) Issuance of the policy
B) Promise to pay claims
✔ C) Application and initial premium payment
D) Agent's commission

Explanation: Consideration is the value exchanged by the parties to a contract. The insured's consideration consists of the statements made in the application and the payment of the first premium.

14. Life insurance premiums are primarily based on which of the following?

✔ A) The insured's age, health, sex, and the type and amount of coverage
B) The insured's current financial status and net worth
C) The premium the policyowner wishes to pay
D) The beneficiary's age and financial need

Explanation: Life insurance premiums are primarily determined by actuarial factors including: the insured's age (mortality risk increases with age), health status (medical underwriting), sex (females have longer life expectancy so typically lower rates), the type of policy (term vs. permanent), and the face amount. The beneficiary's characteristics do not affect the premium.

15. The 'paid-up at 65' whole life policy is one in which:

A) Cash value equals face amount at age 65
✔ B) Premium payments end at age 65 but the policy remains in force for life
C) Coverage terminates when the insured reaches age 65
D) The policy automatically converts to term at age 65

Explanation: A Paid-Up at 65 (or Paid-Up at 70) policy requires premiums to be paid until the specified age, after which the policy is fully paid-up and no further premiums are required — but coverage continues for the insured's entire lifetime. Higher premiums during the working years fund the policy completely by the target age.

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16. A policyowner, David, has an individual life insurance policy in Iowa. 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 Iowa, the policy remains in force. If the insured dies during this time, the death benefit is paid minus the overdue premium.

17. '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.

18. Qualified annuities held within a Traditional IRA are subject to Required Minimum Distributions (RMDs). Under current law, RMDs must generally begin by April 1 following the year the owner turns:

- A) Age 75
- ✔ B) Age 73
- C) Age 59 1/2
- D) Age 65

Explanation: Under the SECURE 2.0 Act, the required beginning date for RMDs from qualified retirement accounts (including qualified annuities in IRAs) is age 73 for individuals born between 1951 and 1959, increasing to age 75 for those born in 1960 or later. Failure to take the RMD results in a penalty tax on the amount not distributed.

19. John named his two children, Amy and Ben, as his primary beneficiaries on a per capita basis. Ben dies before John. When John dies, who receives the death benefit?

- A) Amy receives 50% and Ben's children receive 50%.
- ✔ B) Amy receives the entire death benefit.
- C) Amy receives 50% and Ben's 50% goes to John's estate.
- D) The entire death benefit is paid to John's estate.

Explanation: Under a 'per capita' (by the head) distribution, the proceeds are divided equally only among the surviving members of the named class. Since Ben is deceased, his share is redistributed to the other surviving beneficiary, Amy. Ben's children receive nothing.

20. A licensed producer, Jennifer, moves her residence to Des Moines. Under Iowa regulations, within how many days must Jennifer notify Iowa Insurance Division (IID) of her change of address?

- A) 10 calendar days
- B) 15 calendar days
- ✔ C) 30 calendar days
- D) 60 calendar days

Explanation: Iowa producers must notify Iowa Insurance Division (IID) in writing within 30 days of any change of address.

21. Which of the following would NOT be considered a rebate in Iowa?

- ✔ A) Offering a client a promotional pen valued at $5 with the agency logo during a sales presentation
- B) Offering to pay the client's first monthly premium
- C) Sharing half of the commission with the client
- D) Offering a $100 cash back promotion to new policyholders

Explanation: Iowa law allows agents to distribute advertising novelties of nominal value (typically under $25) without it being considered rebating.

22. An agent fails to appear at a scheduled Iowa Insurance Division (IID) hearing regarding a client complaint. What action can the Commissioner take?

- ✔ A) Suspend or revoke the license in the agent's absence.
- B) Dismiss the complaint.
- C) Sentence the agent to jail immediately.
- D) Fine the customer who complained.

Explanation: If a licensee fails to appear at a scheduled hearing, the Commissioner can proceed in their absence and suspend or revoke their license.

23. How are earnings in a non-qualified deferred annuity taxed during the accumulation phase?

- A) They are taxed at capital gains rates.
- ✔ B) They grow tax-deferred.
- C) They are tax-free.
- D) They are taxed annually as ordinary income.

Explanation: A key feature of non-qualified annuities is that the interest and investment gains accumulate on a tax-deferred basis. No taxes are due on the growth until money is withdrawn from the contract.

24. An employee who does not enroll in a group life insurance plan during the initial eligibility period and later wishes to join is considered a:

- A) Preferred risk
- B) Substandard risk
- ✔ C) Late enrollee
- D) Non-eligible employee

Explanation: A late enrollee is an employee who does not sign up for group coverage during their initial eligibility period. Because late enrollment raises adverse selection concerns, the insurer typically requires the late enrollee to provide evidence of insurability (proof of good health) before coverage is granted.

25. An annuity that credits interest based on the performance of a stock market index, but guarantees the principal, is a(n):

- A) Fixed Annuity
- B) Immediate Annuity
- ✔ C) Equity-Indexed Annuity
- D) Variable Annuity

Explanation: An Equity-Indexed Annuity (EIA), also known as a Fixed-Indexed Annuity (FIA), is a type of fixed annuity. It offers the potential for higher returns by linking its interest crediting to an external index (like the S&P 500), while also protecting the principal from market losses with a guaranteed minimum interest rate.

26. Which type of life insurance offers pure death benefit protection with no cash value?

A) Universal Life
B) Endowment
✔ C) Term Life
D) Whole Life

Explanation: Term Life insurance provides coverage for a specific period (term). It pays a death benefit only if the insured dies during that term. It is the purest form of life insurance and does not build any cash value.

27. In group health insurance, the employer's role is generally to:

A) Underwrite each employee individually
B) Pay all medical claims directly to providers
✔ C) Select the plan, contribute to premiums, and serve as the policyholder
D) Provide insurance without any employee contribution

Explanation: In group health insurance, the employer serves as the policyholder and typically selects the plan(s), negotiates with the insurer, and contributes a portion (or all) of the premium. Employees receive certificates of coverage and may contribute to premiums through payroll deductions. The employer does not personally pay claims.

28. A Medicare beneficiary who wants to enroll in a Medicare Advantage (Part C) plan must have:

✔ A) Medicare Parts A and B
B) Medicare Part B only
C) Medicare Part A only
D) A Medigap policy

Explanation: To be eligible to enroll in a Medicare Advantage plan, an individual must be enrolled in both Medicare Part A and Medicare Part B. They must also live in the plan's service area.

29. A client, age 55, takes a $10,000 withdrawal from his non-qualified annuity. His cost basis is $50,000 and the current value is $70,000. How much of the withdrawal is taxable, and what is the penalty?

✔ A) $10,000 is taxable, plus a $1,000 penalty.
B) The taxable amount is zero, but there is a $1,000 penalty.
C) The taxable amount is $2,857, plus a $285 penalty.
D) The entire $10,000 is a tax-free return of basis.

Explanation: Under LIFO rules, the withdrawal comes from the $20,000 of earnings first. So, the entire $10,000 withdrawal is taxable as ordinary income. Because the client is under age 59 1/2, a 10% penalty applies to the taxable amount, which is 10% of $10,000 = $1,000.

30. The 'Welcome to Medicare' preventive visit is a one-time benefit available:

A) Only for those enrolled in a Medicare Advantage plan.
B) To all seniors, regardless of Medicare enrollment.
✔ C) Anytime during the first year of Medicare Part B enrollment.
D) Within the first 6 months of having Medicare Part A.

Explanation: The 'Welcome to Medicare' visit is a one-time, comprehensive preventive visit offered to new Medicare beneficiaries within the first 12 months of their Part B enrollment. It helps to establish a baseline for future care.

31. To sell variable annuities, a producer must hold which licenses?

A) A life insurance license only.
✔ B) Both a life insurance license and a securities license (e.g., FINRA Series 6 or 7).
C) A securities license only.
D) A property and casualty license.

Explanation: Because variable annuities involve investments in securities (the separate account), they are regulated by both state insurance departments and the SEC/FINRA. A producer must hold a state life insurance license and a federal securities registration to sell them.

32. The doctrine of 'reasonable expectations' most commonly applies to:

A) Set reasonable premium standards for actuarial pricing
✔ B) Resolve coverage ambiguities in favor of the insured when policy language is unclear
C) Require insurers to pay benefits beyond the stated policy limits
D) Hold agents personally liable for misrepresentations

Explanation: The reasonable expectations doctrine is applied by courts when insurance policy language is ambiguous. Courts look at what a reasonable insured would expect the coverage to be, and resolve ambiguities in favor of the insured's reasonable interpretation rather than the insurer's narrower reading.

33. What is the primary purpose of life insurance?

A) To fund the insured's retirement income needs
B) To pay medical expenses for the insured's family
C) To provide investment returns to the policyowner
✔ D) To replace the financial loss caused by the premature death of the insured

Explanation: The primary purpose of life insurance is to replace the income and financial support lost when the insured dies prematurely, protecting dependents and family from financial hardship. Retirement income and investment are secondary or ancillary purposes.

34. Which element is NOT required for a valid insurance contract?

A) Competent parties
B) Legal purpose
✔ C) A licensed agent
D) Consideration

Explanation: The four essential elements of a valid contract are: offer and acceptance, consideration, competent parties, and legal purpose. A licensed agent is not a legal requirement for contract validity, though agents are required for soliciting insurance.

35. An insurer fails to adopt and implement reasonable standards for the prompt investigation of claims. What violation is this under Iowa Code?

✔ A) Unfair Claims Settlement Practice
B) Twisting
C) Churning
D) Boycott

Explanation: Failing to adopt and implement reasonable standards for the prompt investigation of claims is defined as an unfair claims settlement practice.

36. An insurer needs to deny a claim but does so verbally without sending any written confirmation. Under Iowa law, what is the status of this action?

A) It is a standard industry practice.
✓ B) It is an unfair claims settlement practice; all denials must be in writing.
C) It is allowed if the claim is under $100.
D) Only for auto insurance.

Explanation: All claim denials must be provided in writing to the claimant, stating the specific reasons and policy provisions on which they are based.

37. The 'payout rate' in an immediate annuity refers to:

✓ A) The ratio of annual income payments to the lump-sum premium — used to compare annuity income efficiency
B) The maximum allowable interest rate on the annuity contract
C) The percentage of the premium returned each year as income
D) The rate of return earned by the insurer on the annuity premium

Explanation: The payout rate (or payment rate) is the annual income per $1,000 of premium, used to compare immediate annuity quotes. A higher payout rate means more income for the same premium. Payout rates depend on the annuitant's age, sex (where applicable), interest rates, and the chosen payout option.

38. How are premiums for an individual life insurance policy generally treated for tax purposes?

✓ A) They are not tax-deductible.
B) They are tax-credits.
C) They are tax-deductible.
D) They are partially tax-deductible.

Explanation: Premiums paid for individual life insurance policies are considered a personal expense and are therefore not tax-deductible.

39. The 10% early withdrawal penalty on annuity distributions taken before age 59 1/2 does NOT apply in which of the following situations?

A) The owner takes a withdrawal to pay off credit card debt
B) The owner takes a withdrawal to buy a new car
✓ C) The owner takes substantially equal periodic payments (SEPPs) based on life expectancy under IRS Section 72(t)
D) The owner withdraws funds to invest in the stock market

Explanation: Section 72(t) of the Internal Revenue Code allows annuity owners to avoid the 10% early withdrawal penalty if they take distributions as a series of substantially equal periodic payments (SEPPs) based on their life expectancy. Once started, the payments must continue for at least 5 years or until age 59 1/2, whichever is longer. Other exceptions include death, disability, and certain immediate annuity payments.

40. Can a minor be named as a beneficiary of a life insurance policy?

A) No - beneficiaries must be of legal age.
B) Yes - and the minor can directly receive the funds.
✓ C) Yes - but a guardian or trustee must be appointed to receive and manage the funds.
D) Yes - but the funds will be held by the insurer until the minor reaches age 18.

Explanation: A minor can be named as a beneficiary, but they cannot legally receive the death benefit proceeds directly. The funds would be paid to a court-appointed guardian or a trustee named in the policy (e.g., through a UTMA/UGMA designation), which can be a complex and costly process if not planned for.

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41. Short-Term Disability (STD) insurance typically provides benefits for a period of:

A) Up to 5 years
B) To age 65
C) Up to 2 years
✓ D) Up to 6 months

Explanation: Short-Term Disability policies have short elimination periods (e.g., 7-14 days) and short benefit periods, usually ranging from 3 to 6 months, and never more than 2 years.

42. The McCarran-Ferguson Act of 1945 established that:

A) State regulation of insurance is prohibited
B) All insurance companies must be federally chartered
✓ C) Insurance is regulated by the states, unless federal law specifically relates to insurance
D) The federal government has exclusive authority to regulate insurance

Explanation: The McCarran-Ferguson Act declared that the continued regulation and taxation of the insurance industry by the states is in the public interest. Federal law does not preempt state insurance regulation unless the federal law specifically relates to the business of insurance.

43. An HSA account holder turns 65 and enrolls in Medicare. They withdraw HSA funds to pay for a new television. Which of the following describes the tax treatment of this withdrawal?

A) It is subject to income tax plus a 20% penalty
B) It is tax-free because the account holder is over 65
✓ C) It is subject to income tax only with no additional penalty
D) It is not permitted under HSA rules

Explanation: Once an HSA account holder reaches age 65, the 20% penalty for non-qualified withdrawals no longer applies. However, non-qualified withdrawals are still subject to regular income tax, similar to a traditional IRA distribution.

44. An agent fails to renew their license on time. Under Iowa law, what is the late renewal penalty fee Gary must pay in addition to the standard renewal fee?

A) $50
B) $100
✓ C) A 100% surcharge (double the renewal fee)
D) $250

Explanation: Under Iowa regulations, a late renewal incurs a penalty equal to double the standard licensing fee if renewed within the reinstatement window.

45. Coinsurance in health insurance means:

A) The insured pays a fixed dollar amount per service
B) The insurer pays 100% of all expenses after a certain date
C) Two insurers share coverage on the same risk
✓ D) After the deductible, the insured pays a percentage of covered expenses while the insurer pays the remainder

Explanation: Coinsurance requires the insured to pay a percentage of covered expenses after the deductible is satisfied. A common arrangement is 80/20 (the insurer pays 80%, the insured pays 20%) until the out-of-pocket maximum is reached, after which the insurer pays 100%.

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46. In a fixed-indexed annuity, 'downside protection' means:

✓ A) The annuity will never lose value due to index declines; the floor rate (typically 0%) protects against negative crediting
B) The insurer will never let the annuity value fall below the original premium
C) The insurer guarantees returns will match market performance even when markets decline
D) The annuity owner receives compensation for any year the index falls

Explanation: Downside protection in FIAs means the annuity owner's account value is protected from loss when the index performs negatively. The floor rate (typically 0%) means the credited rate is never negative — a declining index results in zero credit for that period, not a loss of principal. This principal protection distinguishes FIAs from direct index investing.

47. 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.

48. Under Iowa law, an agent must complete how many hours of approved Annuity Suitability training before selling annuities?

A) 1 hour
✓ B) 4 hours
C) 8 hours
D) 12 hours

Explanation: Iowa requires a one-time 4-hour Annuity Suitability training course for any producer selling annuity products.

49. Which of the following is the CORRECT definition of the 'face amount' of a life insurance policy?

A) The maximum loan value available against the policy
✔ B) The stated death benefit payable upon the insured's death
C) The total amount of premiums paid over the policy's lifetime
D) The cash value at the time of surrender

Explanation: The face amount (also called the death benefit or face value) is the stated amount the insurer will pay to the beneficiary upon the insured's death. It is shown on the declarations page of the policy. Riders or policy changes may increase or decrease the actual death benefit paid.

50. The difference between 'copayment' and 'coinsurance' in health insurance is:

✔ A) A copay is a fixed dollar amount per service; coinsurance is a percentage of costs after the deductible
B) Copays apply only to HMOs; coinsurance applies only to PPOs
C) Coinsurance applies only to hospital care; copays apply to outpatient care
D) Both terms mean the same thing — a percentage of covered costs

Explanation: A copayment (copay) is a fixed dollar amount paid per service (e.g., $30 per doctor visit). Coinsurance is a percentage the insured pays after the deductible is met (e.g., 20% of all covered expenses). Both are forms of cost-sharing designed to reduce premium costs and encourage appropriate utilization of healthcare services.