Insurance Test Practice

Massachusetts Insurance Practice Test

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1. **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.

2. **Credit life insurance is designed to do which of the following?**

   A) Insure the lender against investment losses
   ✓ B) Pay off the remaining balance of a debtor's loan if the debtor dies
   C) Replace the borrower's income for their family
   D) Provide retirement income to the borrower

   Explanation: Credit life insurance is a type of group life insurance that pays off the remaining balance of a borrower's debt if the borrower dies before the loan is fully repaid. The creditor is the policyholder and beneficiary, and the amount of coverage decreases as the loan balance decreases.

3. **A client is considering replacing their current annuity with a new one. The agent must ensure that the replacement is not a 'churning' transaction, which means:**

   A) The client is over age 65.
   B) The new annuity has a higher interest rate.
   ✓ C) The replacement is done without considering the client's best interest, often just to generate a new commission.
   D) The replacement involves a 1035 exchange.

   Explanation: Churning is the unethical practice of repeatedly replacing insurance or annuity policies for the same client primarily to generate new commissions for the agent, often without any demonstrable benefit to the client and potentially causing harm through new surrender charge periods.

4. **The National Association of Insurance Commissioners (NAIC) is best described as:**

   A) A trade association that lobbies for insurance companies
   ✓ B) A voluntary organization of state insurance regulators that develops model laws and promotes uniformity
   C) A consumer protection agency funded by the federal government
   D) A federal agency that regulates all insurance companies

   Explanation: The NAIC is a voluntary organization composed of the chief insurance regulators from all 50 states, the District of Columbia, and U.S. territories. It develops model laws and regulations that states can adopt to promote consistency in insurance regulation across the country.

5. Under the ACA for plan years beginning on or after January 1, 2014, annual and lifetime dollar limits on:

A) All benefits are prohibited
B) All limits were grandfathered and remain in effect
C) Only inpatient hospital benefits are prohibited
✔ D) Essential health benefits are prohibited; lifetime limits on non-essential benefits may still apply

Explanation: The ACA prohibits annual and lifetime dollar limits on essential health benefits (EHBs) in non-grandfathered plans. Insurers cannot cap the annual or lifetime amount they will pay for EHBs. However, annual and lifetime limits may still be applied to benefits that are not EHBs.

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6. An agent, Jessica, suggests that a prospect drop their existing disability policy and buy a new one because the old company is 'going bankrupt,' though she has no evidence of this. What violation has she committed?

✔ A) Defamation and twisting
B) Rebating
C) Churning
D) Unfair discrimination

Explanation: Making unsubstantiated derogatory claims about a competitor's financial state to convince a client to replace a policy is defamation and twisting.

7. Under the doctrine of respondeat superior, when an authorized agent commits an error while acting within the scope of their authority, who is held liable?

A) Only the agent
B) Only the insured
C) The state Department of Insurance
✔ D) The principal (insurer) is held vicariously liable

Explanation: Under respondeat superior (let the master answer), the principal (insurer) is held vicariously liable for the acts and omissions of its agents performed within the scope of their actual or apparent authority. This is a key concept in insurance law.

8. Life insurance is considered a personal contract, which means:

A) The policy must be delivered in person
B) The contract terms are personalized for each insured
C) Only individuals can purchase it
✔ D) The policy insures the person rather than property and cannot be freely transferred to another party

Explanation: Because life insurance is a personal contract, it follows the person rather than insuring a specific piece of property. The policyowner cannot transfer (assign) ownership of the policy to another party without the insurer's consent.

9. When a non-qualified annuity is inherited by a non-spouse beneficiary, the inherited value is:

A) Eligible for a step-up in basis to the date-of-death value
B) Completely income-tax-free because the decedent already paid taxes
C) Subject to capital gains tax at the beneficiary's capital gains rate
✔ D) Subject to income tax on the gain (above cost basis) as the beneficiary takes distributions

Explanation: When a non-qualified annuity passes to a non-spouse beneficiary, the beneficiary is subject to income tax on the gain (earnings above the decedent's cost basis) as they take distributions. Unlike inherited stocks and real estate, annuities do NOT receive a step-up in basis at death. The beneficiary inherits the original owner's cost basis.

10. What document does an individual member of a group life insurance plan receive as proof of coverage?

A) A master policy
✔ B) A certificate of insurance
C) A declaration page
D) A binder of coverage

Explanation: Individual group members do not receive the actual policy. Instead, they receive a certificate of insurance that summarizes their coverage, benefits, and conversion rights.

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11. The 'common disaster' clause in a life insurance policy is designed to address the situation where:

✔ A) The insured and the primary beneficiary die in the same accident.
B) The policyowner and the insured are different people.
C) The insured dies in a natural disaster.
D) The beneficiary dies before the insured.

Explanation: The Uniform Simultaneous Death Act (or a common disaster clause) addresses the issue of determining who died first when the insured and primary beneficiary die in the same accident. It typically stipulates that the primary beneficiary is presumed to have died first, allowing the death benefit to pass to the contingent beneficiary.

12. Under the ACA, 'grandfathered' health plans are:

A) Plans that qualify for grandfather-level premium tax credits
✔ B) Plans issued before 2010 that can maintain certain pre-ACA features if they do not make significant changes
C) Plans sponsored by grandfather-owned family businesses
D) Plans provided to grandparents and other senior citizens over age 65

Explanation: Grandfathered plans are health insurance plans that existed as of March 23, 2010 (when the ACA was signed). They are exempt from many ACA requirements as long as they do not make significant changes. However, they must cover dependents to age 26 and cannot impose lifetime dollar limits. They do not need to cover essential health benefits or provide preventive care at no cost-sharing.

13. 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.

14. Before a variable life insurance or variable annuity product can be sold, the prospective buyer must receive a:

A) Policy summary
B) Certificate of insurance
C) Buyer's guide
✔ D) Prospectus

Explanation: Because variable products are classified as securities, federal law requires that a prospectus be provided to the prospective buyer before or at the time of solicitation. The prospectus contains detailed information about the product's investment objectives, risks, fees, and expenses.

15. The 'extended term' nonforfeiture option uses a lapsed policy's cash value to:

A) Continue the policy in force for 5 more years automatically
B) Provide a cash distribution to the policyowner
C) Purchase a reduced face amount of whole life insurance with no further premiums
✔ D) Purchase term insurance for the full original face amount for a limited term period

Explanation: The Extended Term nonforfeiture option uses the policy's cash value as a single premium to purchase term insurance for the full original face amount for as long as the cash value can support. A larger cash value extends the term for a longer period. This differs from Reduced Paid-Up, which lowers the face amount but provides permanent (whole life) coverage.

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16. Medicare Part C (Medicare Advantage) differs from Original Medicare because:

A) It requires no premiums or cost-sharing
B) It provides only prescription drug coverage
C) It only covers beneficiaries over age 75
✔ D) It is offered by private insurers approved by Medicare and must cover at least the same benefits as Original Medicare

Explanation: Medicare Advantage (Part C) plans are offered by private insurers approved by Medicare. They must cover all Original Medicare services (Parts A and B) and often include additional benefits (vision, dental, hearing). MA plans have their own networks, cost-sharing structures, and rules that differ from Original Medicare.

17. Medicare Part B has a monthly premium that:

A) Is paid by the Social Security Administration on behalf of all beneficiaries
B) Is the same for all beneficiaries
C) Is waived for all beneficiaries over age 75
✓ D) Is standard but higher-income beneficiaries pay more through IRMAA (Income-Related Monthly Adjustment Amount)

Explanation: Medicare Part B has a standard monthly premium, but higher-income beneficiaries pay more through the Income-Related Monthly Adjustment Amount (IRMAA). IRMAA adds a surcharge to the standard premium for individuals and couples above income thresholds. The Part B premium is typically deducted automatically from Social Security benefits for most enrolled beneficiaries.

18. The 'death benefit' provision in most deferred variable annuities:

A) Is not included because variable annuities are pure investment products
B) Only pays the current account value at the time of death
✓ C) Guarantees the beneficiary will receive at least the greater of the account value or the total premiums paid if the owner dies during accumulation
D) Pays twice the original premium if death occurs before age 65

Explanation: Most variable deferred annuities include a death benefit that guarantees the beneficiary receives at least the greater of: (a) the current account value or (b) the total premiums paid (minus prior withdrawals). This 'return of premium' death benefit guarantees heirs won't receive less than was invested, even if the market has declined.

19. The period during which an annuity makes payments to the annuitant is the:

A) Accumulation period
B) Growth period
C) Contribution period
✓ D) Liquidation period

Explanation: The liquidation period, also known as the annuitization or payout period, is the phase when the contract begins to make regular income payments to the annuitant. Once this phase begins, it generally cannot be altered.

20. In group insurance, who is responsible for paying the policy premiums to the insurer?

A) The Third-Party Administrator
✓ B) The employer
C) The agent of record
D) The employee

Explanation: The employer, as the master policyholder, is responsible for collecting the employee's share of the premium (if any) and remitting the total premium to the insurance company on a regular basis.

21. Susan has a life insurance policy with an Accidental Death Benefit (Double Indemnity) rider for $100,000. Her base policy face amount is $100,000. If Susan dies from a heart attack, how much will her beneficiary receive?

A) $200,000
✓ B) $100,000
C) $0
D) $50,000

Explanation: The Accidental Death Benefit rider only pays the additional benefit if death results from an accident. Because a heart attack is an illness (natural cause), only the base policy face amount of $100,000 is paid.

22. Medicare beneficiaries are generally eligible at age:

A) 67
B) 62
C) 60
✓ D) 65

Explanation: Medicare eligibility generally begins at age 65 for U.S. citizens or permanent residents. Younger individuals under 65 may also qualify if they have received Social Security disability benefits for 24 months or have end-stage renal disease (ESRD) or ALS (Lou Gehrig's disease).

23. An agent is assisting a client with a claim. Massachusetts Division of Insurance (DOI) requests information from the agent about the transaction. What is the agent's primary obligation?

A) Respond within 15 working days.
✓ B) Cooperate fully and provide all requested documentation.
C) Keep files confidential from Massachusetts Division of Insurance (DOI).
D) Referral to the insurer.

Explanation: All licensees must cooperate fully with investigations by Massachusetts Division of Insurance (DOI) and provide requested books and records.

24. Which rider allows the policyowner to purchase additional amounts of insurance at future dates without evidence of insurability?

A) Cost of Living Rider
✓ B) Guaranteed Insurability Rider
C) Accidental Death Benefit Rider
D) Payor Benefit Rider

Explanation: The Guaranteed Insurability Rider (GIR) gives the policyowner the right to buy specified amounts of additional life insurance on the insured at stated intervals (e.g., every three years or at marriage/childbirth) without having to prove insurability.

25. A lender requires a homebuyer, Paul, to purchase life insurance as collateral for a mortgage. The lender insists that Paul buy the policy from a specific agency associated with the bank. What is this practice known as?

- ✔ A) Coercion
- B) Rebating
- C) Twisting
- D) Churning

Explanation: Coercion involves entering into agreements that restrict trade or create a monopoly, such as forcing a borrower to buy insurance from a specific source as a condition of a loan.

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26. 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.

27. Under group term life insurance, if an employee converts their coverage to an individual whole life policy upon termination:

- ✔ A) The premium is based on the insured's attained age at the time of conversion with no evidence of insurability required
- B) The converted policy will have the same premium as the group plan for 2 years
- C) The premium is based on the group rate they were paying before termination
- D) The converted policy has a 2-year contestability period beginning from the original group enrollment date

Explanation: Upon conversion of group term to individual whole life, the insured pays the standard premium for their current age (attained age) for the type of individual policy issued. No evidence of insurability is required. The premium will be significantly higher than the group rate because individual policies are more expensive per unit of coverage than group rates.

28. The role of an insurance underwriter is to:

- A) Process and pay insurance claims on behalf of the insurer
- B) Regulate insurance companies on behalf of the state
- C) Sell insurance products directly to consumers
- ✔ D) Evaluate and select risks to be insured based on company guidelines and actuarial data

Explanation: An underwriter is responsible for evaluating insurance applications, assessing risk, determining whether to accept or reject the risk, and setting appropriate premiums and conditions. Underwriters use actuarial data, company guidelines, and individual risk characteristics to make these decisions.

29. An Attending Physician Statement (APS) is:

A) A government form required for all insurance applications
✔ B) A report from the applicant's personal doctor providing their medical history
C) A statement from the insurer's medical director
D) A summary of the agent's observations about the applicant

Explanation: An APS is a detailed report obtained from the applicant's personal physician. It provides the underwriter with the applicant's medical history, diagnoses, treatments, and prognosis. It is one of the most thorough and reliable sources of medical underwriting information.

30. Dividends from a participating whole life policy left to 'accumulate at interest' result in:

A) All accumulated amounts being tax-free until the policy matures
B) Tax-free accumulation of both dividends and interest
✔ C) Dividends remaining tax-free but the interest earned on accumulated dividends being taxable annually
D) Conversion of the accumulation into paid-up additions

Explanation: When dividends are left to accumulate at interest with the insurer, the dividends themselves (as returns of premium) are not taxable. However, the interest credited by the insurer ON the accumulated dividends IS taxable as ordinary income each year as it is credited — it must be reported by the policyowner annually.

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31. A 'contributory' group health plan means:

A) Employees contribute through payroll taxes
B) The employer pays 100% of the premium
C) The government contributes to the premium
✔ D) Both the employer and employees contribute to the premium

Explanation: In a contributory group plan, both the employer and employees share the premium cost. Employees' contributions are typically deducted from their paycheck. Most group health plans in the U.S. are contributory. Contributory plans typically require at least 75% employee participation to prevent adverse selection.

32. Long-Term Disability (LTD) insurance typically has a benefit period of:

A) For the lifetime of the insured
B) Exactly 5 years
✔ C) At least 2 years, and often to age 65 or longer
D) Less than one year

Explanation: Long-Term Disability is designed to cover serious, long-lasting disabilities. Benefit periods are usually a minimum of 2 years and can extend to 5 years, 10 years, or most commonly, to the insured's Social Security retirement age (e.g., 65 or 67).

33. The purpose of the conditional receipt in life insurance is to:

- ✔ A) Provide coverage from the application date if the applicant is approved as applied for
- B) Allow the insurer to deny coverage without explanation
- C) Prove that the agent collected the first premium
- D) Replace the need for a medical examination

Explanation: The conditional receipt provides temporary coverage from the date of application (or medical exam if required), conditional on the applicant being found insurable as applied for at the standard rate. If the applicant is approved, coverage is retroactive to the application date. If not approved, no coverage existed and premiums are returned.

34. The separate account of a variable life insurance policy is similar to a:

- A) Savings account
- ✔ B) Mutual fund
- C) Certificate of deposit
- D) Money market account

Explanation: The separate account functions similarly to a mutual fund. It pools the premiums of multiple policyowners and invests them in a diversified portfolio of stocks, bonds, or other securities. Like mutual funds, the value of the account fluctuates with the performance of the underlying investments.

35. If an insured commits suicide within the period specified by the suicide clause, what will the insurer pay?

- A) The policy's cash value
- B) Nothing
- ✔ C) A refund of the premiums paid, without interest
- D) The full death benefit

Explanation: The suicide clause, typically in effect for the first two years of the policy, stipulates that if the insured commits suicide during this period, the insurer's liability is limited to a refund of the premiums paid. If suicide occurs after this period, the full death benefit is paid.

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36. A 1035 exchange allows a policyowner to:

- ✔ A) Exchange a life insurance policy for an annuity contract without triggering taxes.
- B) Transfer policy ownership to a family member without gift tax.
- C) Exchange a life insurance policy for stocks and bonds tax-free.
- D) Receive the cash value of a policy tax-free.

Explanation: Section 1035 of the tax code permits the tax-free exchange of certain insurance products. A life insurance policy can be exchanged for another life insurance policy, an endowment policy, or an annuity contract without any immediate tax consequences on the accumulated gain.

37. The Spendthrift Clause in a life insurance policy is designed to:

- ✔ A) Protect the death benefit proceeds from the beneficiary's creditors.
- B) Prevent the beneficiary from changing the settlement option.
- C) Allow the insurer to hold and manage the death benefit proceeds for the beneficiary.
- D) Protect the policyowner from creditors.

Explanation: The Spendthrift Clause protects the policy proceeds from being claimed by the beneficiary's creditors or being recklessly spent by the beneficiary. When this clause is active, the insurer retains the proceeds and pays them out to the beneficiary in installments according to a settlement option.

38. Under health insurance, an 'in-network' provider is one that:

- A) Is located within a specified geographic radius of the insured's home
- B) Is a specialist who provides only inpatient care
- ✔ C) Has contracted with the health plan to provide services at negotiated rates
- D) Provides only emergency care services

Explanation: An in-network provider has signed a contract with the health insurance plan agreeing to accept negotiated rates for covered services. Using in-network providers results in lower cost-sharing for the insured. Out-of-network providers have not signed such contracts and may charge higher amounts, resulting in higher cost-sharing for the insured.

39. Because the insurer writes the policy and the insured has no say in its wording, an insurance policy is considered a(n):

- A) Unilateral contract
- B) Contract of indemnity
- ✔ C) Contract of adhesion
- D) Aleatory contract

Explanation: A contract of adhesion is a contract offered on a 'take-it-or-leave-it' basis by one party (the insurer) to the other (the insured). Any ambiguities in the contract are therefore interpreted in favor of the insured.

40. Social insurance offset riders in disability income policies:

- ✔ A) Reduce the disability benefit by the amount received from Social Security or workers' compensation
- B) Increase the benefit when Social Security disability is also paid
- C) Allow benefits to be collected before Social Security eligibility
- D) Provide additional coverage for federal employees only

Explanation: A Social Insurance Offset (or Social Security offset) rider reduces the disability income benefit by the amount the insured receives from Social Security disability or similar government programs. This coordination prevents over-indemnification and allows the insurer to lower premiums while still providing adequate total income replacement.

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41. What does a 'guaranteed renewable' provision ensure?

- A) The insured can renew the policy at any time without underwriting.
- B) The insurer cannot cancel the policy or increase premiums.
- C) The policy benefits are guaranteed to increase with inflation.
- ✔ D) The insurer cannot cancel the policy, but can increase premiums by class.

Explanation: A guaranteed renewable policy requires the insurer to renew the policy as long as premiums are paid. However, the insurer can raise the premium rates for an entire class of insureds, but not on an individual basis.

42. Under the ACA, the 'actuarial value' of a Silver plan is approximately:

- ✔ A) 70%
- B) 80%
- C) 60%
- D) 90%

Explanation: ACA metal tiers reflect the plan's actuarial value (the percentage of covered costs paid by the plan on average): Bronze = ~60%, Silver = ~70%, Gold = ~80%, Platinum = ~90%. Silver plans also offer cost-sharing reduction subsidies (CSRs) to qualifying lower-income enrollees, which increase the effective actuarial value.

43. What is the tax status of a transfer-for-value?

- A) It has no impact on the taxability of the death benefit.
- B) It makes the death benefit fully taxable.
- C) It makes the death benefit subject to capital gains tax.
- ✔ D) It makes the death benefit partially taxable as ordinary income.

Explanation: The transfer-for-value rule states that if a life insurance policy is sold or transferred for valuable consideration, a portion of the death benefit becomes subject to income tax. The taxable portion is the death benefit minus the new owner's cost basis.

44. A life insurance policy is delivered to a client in Massachusetts. The policy does not contain a free-look provision. What is the status of the policy?

- ✔ A) It is void and violates Massachusetts insurance laws.
- B) It is valid if the client signs a waiver.
- C) It is valid for 1 year only.
- D) It is allowed if the insurer is a mutual company.

Explanation: The free-look provision is a mandatory provision for individual life insurance policies in Massachusetts.

45. The 'cash value accumulation test' (CVAT) is one method used to determine if a life insurance policy qualifies as:

- A) A variable annuity product
- B) A modified endowment contract
- C) A qualified retirement plan
- ✔ D) A life insurance contract under IRC Section 7702

Explanation: IRC Section 7702 establishes two tests to determine whether a contract qualifies as life insurance for tax purposes: the Cash Value Accumulation Test (CVAT) and the Guideline Premium and Corridor Test (GPT). Under the CVAT, the policy's cash value cannot exceed the net single premium needed to fund the death benefit. Policies must satisfy one of these tests to receive favorable life insurance tax treatment (tax-deferred growth, income-tax-free death benefit).

46. An insurance company formed under the laws of Indiana is selling policies in Boston. How is this insurer classified in Massachusetts?

A) Domestic insurer
✓ B) Foreign insurer
C) Alien insurer
D) Reciprocal insurer

Explanation: A foreign insurer is an insurance company formed under the laws of another state of the United States.

47. The 'personal' nature of an insurance contract means:

A) Insurance contracts can be inherited by the insured's heirs automatically
B) Personal information disclosed on the application is kept strictly confidential
C) Only individuals, not businesses, can purchase insurance
✓ D) The insurance contract is a personal agreement with the insured and generally cannot be assigned to another without insurer consent

Explanation: Insurance contracts are personal in nature — they are agreements between the insurer and the specific individual or entity based on the unique characteristics of that person or entity. Most insurance contracts (especially life and health) cannot be transferred to another party without the insurer's consent because the insurer accepted the original insured's specific risk profile.

48. What is the payment model where an HMO pays a physician a set amount per member per month, regardless of the services provided?

A) Fee-for-service
B) Per-diem
✓ C) Capitation
D) Cost-plus

Explanation: Capitation is the primary way HMOs pay their network physicians. The provider receives a fixed monthly payment for each enrolled member assigned to them, creating an incentive to focus on preventative care and cost containment.

49. Which of the following describes 'reentry term' life insurance?

A) Term insurance that can be reentered after a lapse with no waiting period
B) Term insurance that requires a new medical exam at each renewal
✓ C) Term insurance that allows the insured to reenter at lower rates if they pass a medical exam at certain intervals
D) Term insurance where coverage reenters after the contestability period

Explanation: Reentry Term allows the insured to qualify for lower ('select') rates at specified reentry dates by providing evidence of continued good health. If the insured cannot meet health requirements at reentry, they continue at higher 'ultimate' rates. This structure rewards healthy insureds with significant premium savings.

50. The Long-Term Care (LTC) rider on a life insurance policy allows the policyowner to:

A) Double the death benefit if death occurs in a long-term care facility.

B) Waive the policy premium if they enter a nursing home.

C) Receive a monthly income for life after age 65.

✔ D) Access a portion of the policy's death benefit to pay for long-term care expenses.

Explanation: An LTC rider is a type of accelerated benefit rider. It allows the policyowner to use some or all of the policy's death benefit to cover qualifying long-term care costs if they are unable to perform activities of daily living (ADLs) or have a cognitive impairment.