Insurance Test Practice

Minnesota Insurance Practice Test

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1. Which of the following best describes the role of a Managing General Agent (MGA)?

A) A government official who oversees insurance markets
✔ B) An agent with broad authority from the insurer, including underwriting, binding, and claims functions
C) An agent who manages a producer's agency on their behalf
D) An agent who exclusively manages claims for the insurer

Explanation: A Managing General Agent (MGA) is an agent with expanded authority granted by the insurer, including the power to underwrite risks, bind coverage, issue policies, and sometimes handle claims and appointing sub-agents, all on behalf of the insurer.

2. A family policy typically provides what kind of insurance on the children?

A) Universal life insurance
B) Whole life insurance
C) Variable life insurance
✔ D) Term life insurance

Explanation: A family policy is a package policy that usually provides whole life coverage for the primary breadwinner and a smaller amount of convertible term life insurance for the spouse and children.

3. Which of the following is covered as a preventive service at no cost-sharing under the ACA?

✔ A) Vaccines recommended by the Advisory Committee on Immunization Practices (ACIP)
B) All prescription medications regardless of purpose
C) Elective cosmetic procedures
D) Dental fillings for adults

Explanation: ACA requires non-grandfathered health plans to cover ACIP-recommended vaccines at no cost-sharing. Other no-cost preventive services include USPSTF 'A' and 'B' rated screenings (mammograms, colonoscopies, blood pressure checks) and HRSA guidelines for preventive care for women. Cosmetic procedures, prescription drugs generally, and adult dental are NOT required preventive services.

4. A 'trustee beneficiary' designation means:

A) The proceeds are paid to the deceased insured's estate attorney
B) The beneficiary must be a licensed fiduciary to receive proceeds
C) A bank is automatically appointed to manage the proceeds
✔ D) The proceeds are paid to a named trustee to be managed according to the terms of a trust for the benefit of the trust's beneficiaries

Explanation: Naming a trustee as beneficiary directs the life insurance proceeds to be paid to the trustee of a named trust (rather than directly to individuals). The trustee then manages and distributes the funds according to the trust's terms. This arrangement is commonly used in estate planning for large estates or to manage funds for minor children.

5. A Social Security Rider (or Social Insurance Supplement) on a private disability policy will:

A) Pay a benefit in addition to Social Security benefits.
✔ B) Pay a benefit during the Social Security waiting period and if Social Security denies the claim.
C) Pay a benefit only if the insured is not eligible for Social Security.
D) Replace Social Security benefits entirely.

Explanation: This rider pays an additional monthly benefit to the insured during the 5-month Social Security waiting period or if their claim for Social Security benefits is denied. If Social Security benefits are approved, the rider benefit usually stops or is reduced.

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6. What is a flexible premium deferred annuity (FPDA)?

A) An annuity with a flexible interest rate.
B) An annuity funded with a single premium for a flexible payout.
C) An annuity that can be converted from fixed to variable.
✔ D) An annuity that allows the owner to make multiple premium payments over time, with payouts deferred to the future.

Explanation: An FPDA allows the owner to pay premiums over a period of time, offering flexibility in the amount and frequency of contributions. Payouts are deferred to a future date.

7. An employer wants to insure a key executive under the company's group life plan with a benefit amount significantly higher than other employees. Which group insurance principle could this potentially violate?

A) The doctrine of adhesion
B) The law of large numbers
✔ C) The requirement that benefit amounts be determined by a formula that precludes individual selection
D) The principle of indemnity

Explanation: A fundamental principle of group underwriting is that benefit amounts must be determined by a formula related to factors such as salary, position, or length of service. This prevents individual selection (adverse selection) by not allowing specific individuals to choose disproportionately high coverage.

8. Vision insurance typically covers all of the following EXCEPT:

✔ A) Treatment for eye diseases like glaucoma
B) Contact lenses
C) Eyeglasses
D) Eye exams

Explanation: Routine vision insurance covers eye exams, frames, and lenses. Medical treatment for eye diseases, injuries, or conditions like glaucoma or cataracts would be covered under the insured's major medical health insurance policy, not their vision plan.

9. 'Blending' or 'loading' in a participating whole life policy refers to:

A) Blending both fixed and variable components in the same policy
B) Loading higher premiums onto smoker-rated policies
✔ C) Mixing whole life with paid-up additions to increase cash value and reduce net premium cost
D) Adding term insurance rider to increase coverage at a lower cost

Explanation: In participating whole life, 'blending' (or 'overfunding') refers to combining base whole life with paid-up additions (PUAs) to maximize the ratio of cash value to death benefit. This strategy is used in Infinite Banking and Bank On Yourself concepts where the policy is designed primarily for its cash value accumulation efficiency.

10. When money is withdrawn from a non-qualified annuity, how is the distribution taxed?

A) First-In, First-Out (FIFO) - cost basis is withdrawn first.
✔ B) Last-In, First-Out (LIFO) - taxable earnings are withdrawn first.
C) The entire withdrawal is taxed as ordinary income.
D) The entire withdrawal is tax-free.

Explanation: Annuity withdrawals are taxed on a LIFO basis. This means the taxable earnings are considered to be taken out before the non-taxable return of principal (cost basis). This is less favorable than the FIFO treatment for life insurance cash values.

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11. In a group life insurance plan, who is the policyowner and who receives the certificate of insurance?

✔ A) The employer is the policyowner; the employee receives the certificate.
B) The insurer is the policyowner; the employee receives the certificate.
C) Both the employer and employee are policyowners.
D) The employee is the policyowner; the employer receives the certificate.

Explanation: In a group life plan, the sponsoring organization (e.g., the employer) is the master policyowner. The individual members of the group (e.g., the employees) are not parties to the contract but receive a certificate of insurance as evidence of their coverage.

12. In a Point of Service (POS) plan, what happens when a member chooses to receive care from an out-of-network provider without a referral?

A) The claim is denied entirely
B) The provider is automatically added to the network
✔ C) The member pays significantly higher out-of-pocket costs
D) The member receives the same level of benefits as in-network care

Explanation: A POS plan is a hybrid of HMO and PPO features. When members use their PCP and obtain referrals, they receive HMO-level benefits. When they go out-of-network without a referral, they pay substantially higher deductibles and coinsurance, similar to an indemnity plan.

13. Variable insurance products must be registered with the:

A) State Department of Insurance only
B) Federal Reserve Board
✓ C) Securities and Exchange Commission (SEC)
D) National Association of Insurance Commissioners (NAIC)

Explanation: Because variable products are both insurance contracts and securities, they must be registered with the SEC under the Securities Act of 1933 and the Investment Company Act of 1940. Additionally, the agent selling them must be registered with FINRA and licensed by the state Department of Insurance.

14. The primary reason a young healthy individual might choose term over whole life insurance is:

✓ A) Term insurance provides more death benefit per premium dollar for the same coverage amount during the years when coverage need is highest
B) Term insurance has a guaranteed conversion feature that whole life does not
C) Term insurance builds more cash value than whole life during the first 20 years
D) Term insurance is automatically renewable for life at no additional cost

Explanation: For young individuals with significant insurance needs (mortgage, family income replacement, business obligations) and limited budgets, term insurance provides the most death benefit per premium dollar. The savings on premiums compared to whole life can be invested separately. This is the basis of the 'buy term and invest the difference' philosophy.

15. In a whole life policy, the relationship between cash value and death benefit is:

A) Directly proportional — both increase together at the same rate
B) Inverse — as cash value grows, the death benefit decreases by the same amount
C) There is no relationship between cash value and death benefit
✓ D) The total death benefit is level; as cash value grows within the total, the net amount at risk decreases

Explanation: In a whole life policy with a level death benefit (most common structure), the policy's total value stays constant at the face amount. As the cash value component grows, the 'net amount at risk' (pure insurance) shrinks proportionally, since: face amount = cash value + net amount at risk.

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16. A business owner buys a life insurance policy on her own life and names the business as the beneficiary. What is the business purpose of this policy?

A) Split-dollar arrangement
✓ B) Business continuation
C) Key person insurance
D) Executive bonus plan

Explanation: This arrangement is often used for business continuation, specifically to provide liquidity to a sole proprietorship. Upon the owner's death, the death benefit provides cash for the owner's heirs to pay off business debts and facilitate the orderly transfer or liquidation of the business.

17. 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.

18. In insurance, what is the term for the cause of a loss?

A) Indemnity
✔ B) Peril
C) Risk
D) Hazard

Explanation: A peril is the direct cause of a loss. For example, in a fire insurance policy, fire is the peril.

19. A disability buy-sell agreement funded by a disability policy is designed to:

✔ A) Provide funds for the able partners to buy out the business interest of a disabled partner.
B) Provide income to a disabled partner.
C) Pay for a disabled partner's medical bills.
D) Cover the overhead expenses of the business.

Explanation: Similar to a life insurance-funded buy-sell, a disability buy-out policy provides the funds needed for the business or remaining partners to execute the buy-sell agreement and purchase the disabled partner's share of the business.

20. Under the Medical Loss Ratio (MLR) requirement, what percentage of premium revenue must individual and small group health insurers spend on medical claims and quality improvement?

A) 75%
B) 70%
C) 85%
✔ D) 80%

Explanation: The ACA requires individual and small group health insurers to spend at least 80% of premium revenue on medical claims and quality improvement activities. This is known as the 80/20 rule. If insurers fail to meet this threshold, they must issue rebates to policyholders.

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21. Medicare Advantage (Part C) plans must cover all of the following EXCEPT:

A) Medicare Part A and Part B services
B) Skilled nursing facility care after a qualifying hospital stay
C) Emergency care services nationwide
✔ D) Long-term custodial care in a nursing home indefinitely

Explanation: Medicare Advantage plans are required to cover all services covered by Original Medicare (Parts A and B). They are NOT required to cover long-term custodial (non-skilled) nursing home care beyond what Medicare covers. Long-term care (custodial care) is not a Medicare benefit — it must be covered by private LTC insurance or Medicaid.

22. Dividends received from a participating life insurance policy are:

A) Taxable as ordinary income.
B) Tax-deductible for the policyowner.
C) Taxable as capital gains.
✔ D) Generally considered a tax-free return of premium.

Explanation: Policy dividends are not guaranteed and are considered a return of an overpayment of premium. As such, they are not taxable income to the policyowner. However, if dividends are left to accumulate at interest, the interest earned is taxable.

23. 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.

24. How is the death benefit from an annuity treated for tax purposes if the owner dies during the accumulation phase?

A) It is received entirely tax-free by the beneficiary.
B) The entire benefit is taxed as a capital gain.
C) The death benefit is subject to a 10% penalty regardless of the beneficiary's age.
✔ D) The earnings portion of the benefit is taxable as ordinary income to the beneficiary.

Explanation: If the annuity owner dies before annuitization, the beneficiary receives the death benefit. The portion of the benefit that represents earnings (the amount exceeding the owner's cost basis) is taxable as ordinary income to the beneficiary.

25. The 'nondiscrimination rules' under ACA Section 1557 prohibit:

✔ A) Discrimination in health programs or activities receiving federal financial assistance based on race, color, national origin, sex, age, or disability
B) Charging different premiums to employees based on their claims history
C) Offering wellness program incentives that vary by health status
D) Employers from offering different benefit tiers to different employee groups

Explanation: ACA Section 1557 prohibits discrimination in health programs or activities receiving federal financial assistance on the basis of race, color, national origin, sex, age, or disability. This includes Medicaid, Medicare, and plans offered through the ACA marketplace. Insurance companies and providers receiving federal funding must comply.

26. What is the difference between Universal Life Option A and Option B?

A) Option A is term insurance, while Option B is permanent insurance.
B) Option A has a flexible premium, while Option B has a fixed premium.
✓ C) Option A provides a level death benefit, while Option B provides an increasing death benefit.
D) Option A's cash value is invested in the general account, while Option B's is in separate accounts.

Explanation: Under Universal Life, Option A (or Option 1) provides a level death benefit where the cash value is included within the face amount. Option B (or Option 2) provides an increasing death benefit, which is the face amount plus the accumulated cash value.

27. Under federal COBRA, how long can a spouse and dependent children continue coverage if the covered employee dies or gets divorced?

✓ A) 36 months
B) 29 months
C) Coverage terminates immediately.
D) 18 months

Explanation: For dependents, qualifying events like the death of the employee, divorce or legal separation, or the employee becoming eligible for Medicare allow for a continuation period of up to 36 months.

28. Under the ACA, a Bronze plan has an actuarial value of approximately 60%. This means that on average the enrollee is expected to pay what percentage of covered medical costs through cost-sharing?

✓ A) 40%
B) 20%
C) 30%
D) 10%

Explanation: A Bronze plan's 60% actuarial value means the plan covers approximately 60% of the average total cost of covered services, leaving the enrollee responsible for about 40% through cost-sharing mechanisms such as deductibles, copayments, and coinsurance. Bronze plans have the lowest premiums but highest out-of-pocket costs.

29. How long does an individual have to elect COBRA coverage after receiving the election notice?

✓ A) 60 days
B) 14 days
C) 45 days
D) 30 days

Explanation: After a qualifying event, the employer must notify the plan administrator, who then provides an election notice to the qualified beneficiary. The beneficiary has 60 days from the date the notice is sent or the date coverage ended (whichever is later) to elect to continue coverage.

30. An insured has a medical bill of $5,000. Their PPO plan has a $500 deductible and 90/10 coinsurance for in-network care. How much will the insured pay?

- ✔ A) $950.00
- B) $5,000.00
- C) $1,000.00
- D) $500.00

Explanation: The insured first pays the $500 deductible. This leaves a balance of $4,500. The insured's coinsurance portion is 10% of this balance, which is $450. The insured's total out-of-pocket cost is the deductible ($500) + coinsurance ($450) = $950.

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31. A policy that allows the policyowner to convert their term coverage to permanent coverage without evidence of insurability is called a:

- A) Renewable Term policy
- B) Decreasing Term policy
- C) Level Term policy
- ✔ D) Convertible Term policy

Explanation: A convertible term policy includes a provision that allows the policyowner to convert the term policy into a whole life or other permanent policy at a later date without having to prove their insurability. Premiums for the new policy will be based on the insured's attained age at the time of conversion.

32. The mandatory 'Physical Examination and Autopsy' provision gives the insurer the right to:

- ✔ A) Require a physical exam of the insured at any time during a claim, at the insurer's expense
- B) Require the insured to pay for a medical exam before benefits are paid
- C) Require an annual physical as a condition of coverage
- D) Deny any claim without a physical exam

Explanation: The insurer has the right to have the insured examined by a physician of its choice, as often as reasonably required during the pendency of a claim. The insurer also has the right to request an autopsy in the event of death, where not prohibited by law. All costs are borne by the insurer.

33. 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.

34. A Modified Endowment Contract (MEC) occurs when:

A) An annuity's interest rate is modified by the insurer
B) A variable annuity includes a guaranteed minimum death benefit rider
C) An annuity's cash value exceeds its death benefit
✔ D) A life insurance policy is over-funded beyond IRS limits based on a 7-pay test

Explanation: A Modified Endowment Contract (MEC) is a life insurance policy that has been funded with cumulative premiums exceeding the IRS 7-pay test limit. MECs lose certain tax advantages of life insurance — withdrawals and loans are taxed on LIFO basis (gains first), and pre-59½ withdrawals face a 10% penalty. MECs are not annuities but share similar tax treatment.

35. Which type of policy pays a fixed, per-day benefit for each day the insured is hospitalized, regardless of the actual costs?

A) Surgical Expense Insurance
B) Major Medical Insurance
✔ C) Hospital Indemnity Insurance
D) Comprehensive Health Insurance

Explanation: Hospital Indemnity (or Hospital Confinement) insurance pays a specified daily, weekly, or monthly cash benefit directly to the insured during a hospital stay. This money can be used for any purpose, not just medical bills.

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36. The part of the policy that outlines the duties and responsibilities of both the insurer and the insured is the:

A) Exclusions
B) Insuring Clause
✔ C) Conditions
D) Declarations

Explanation: The Conditions section sets forth the rules of conduct, duties, and obligations for both the policyholder and the insurer. Examples include the requirement to provide proof of loss and the insurer's obligation to pay claims in a timely manner.

37. Annuities are unique among insurance products in that they are primarily designed to:

✔ A) Liquidate accumulated assets into a guaranteed income stream over time
B) Insure against property losses
C) Accumulate tax-deferred savings with no distribution requirement
D) Provide a death benefit to protect survivors

Explanation: The primary unique purpose of an annuity — what sets it apart from other financial and insurance products — is its function as a mechanism for systematically distributing (liquidating) accumulated savings into periodic income payments, particularly providing income that cannot be outlived in a life annuity structure.

38. A disability policy that covers accidents but not sickness is known as:

A) A limited risk policy
B) An accidental death and dismemberment (AD&D) policy
✔ C) An accident-only disability income policy
D) A comprehensive disability policy

Explanation: An accident-only policy provides coverage for disability resulting from an accident and does not cover disability due to illness or sickness. It has a lower premium than a comprehensive policy.

39. What is apparent authority?

- ✔ A) Authority the public reasonably believes an agent has, based on the insurer's actions
- B) Authority written in the agent's contract
- C) Authority granted by the state's Department of Insurance
- D) Authority required to transact business that is not written down

Explanation: Apparent authority is the perception by a third party that an agent has authority to act on behalf of the insurer, even if that authority has not been granted. This perception is created by the actions of the insurer (e.g., providing logos and application forms).

40. How are distributions (withdrawals or loans) from a Modified Endowment Contract (MEC) taxed?

- A) As capital gains.
- ✔ B) Last-In, First-Out (LIFO) - earnings are taxed first.
- C) First-In, First-Out (FIFO) - return of premium first.
- D) Tax-free.

Explanation: MECs are subject to less favorable tax rules. All distributions are taxed on a Last-In, First-Out (LIFO) basis, meaning the taxable earnings are withdrawn first. Additionally, a 10% penalty may apply to distributions taken before age 59 1/2.

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41. A policyowner who stops paying premiums on a whole life policy and chooses the Cash Surrender option will receive:

- A) A paid-up term policy.
- B) The total premiums paid back.
- ✔ C) The accumulated cash value, less any outstanding loans.
- D) A reduced paid-up whole life policy.

Explanation: The Cash Surrender Value nonforfeiture option allows the policyowner to terminate the policy and receive the net cash value (cash value minus any surrender charges and outstanding loans).

42. A policyowner takes a withdrawal from a universal life policy. Which of the following is true regarding taxation?

- A) The withdrawal is taxed on a LIFO basis.
- B) The entire withdrawal is taxed.
- C) The withdrawal is treated as a loan and is never taxed.
- ✔ D) The withdrawal is treated as a return of premium up to the policy's cost basis and is not taxed.

Explanation: For non-MEC policies, withdrawals are treated on a FIFO (First-In, First-Out) basis. This means the policyowner can withdraw up to their cost basis (total premiums paid) without incurring any taxes. Withdrawals exceeding the cost basis are taxable as ordinary income.

43. The provision that allows a policyowner to restore a lapsed policy to its original status is the:

A) Grace Period Provision
✔ B) Reinstatement Provision
C) Incontestability Clause
D) Free Look Provision

Explanation: The Reinstatement Provision allows the owner of a lapsed policy to put it back in force, provided certain conditions are met, such as paying back premiums with interest and proving continued insurability. This is usually allowed within 3 to 5 years of lapse.

44. A 'group captive' is best described as:

A) A type of surplus lines carrier for high-risk groups
B) An insurer that was seized by a state regulator
✔ C) A captive insurer formed by a group of unrelated businesses with similar risk profiles to insure their own risks
D) An employer health plan covering a captive group of employees

Explanation: A group captive (or association captive) is a jointly owned captive insurer formed by multiple unrelated businesses that share similar risk profiles (often in the same industry). Each member contributes capital and premiums. Group captives allow smaller businesses to access the benefits of captive insurance — greater control, potential savings, and customized coverage.

45. A policyowner wants to ensure that her spouse receives a monthly income from the life insurance proceeds, but also wants to ensure their children receive the principal after the spouse dies. Which settlement option should be chosen?

A) Life Income
B) Fixed Period
C) Fixed Amount
✔ D) Interest Only

Explanation: The 'Interest Only' option is ideal for this scenario. The insurer holds the principal and pays out the interest earned to the spouse. Upon the spouse's death, the principal is then paid to the contingent beneficiaries (the children).

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46. The 'face amount' in a universal life policy under Option B (Increasing Death Benefit) refers to:

A) The level insurance component excluding any cash value
B) The guaranteed minimum cash value
✔ C) The specified amount (also called corridor amount) to which the cash value is added to determine the total death benefit
D) The total death benefit including cash value

Explanation: Under Universal Life Option B, the death benefit = specified (face) amount + cash value. The 'specified amount' (or corridor amount) is the pure insurance component. As cash value grows, the total death benefit grows accordingly. This option provides an increasing death benefit that keeps pace with cash value growth.

47. A quarter of coverage under Social Security is earned by:

A) Paying a flat quarterly fee to the Social Security Administration
✔ B) Earning a specified minimum amount of wages or self-employment income in a calendar quarter
C) Working for any employer for three consecutive months
D) Being employed full-time for at least one quarter of the year

Explanation: A quarter of coverage (also called a credit) is earned by receiving a minimum amount of earnings subject to Social Security tax in a calendar quarter. The amount required is adjusted annually for inflation. A maximum of 4 credits can be earned per year.

48. The optional 'Overinsurance' provision protects against:

A) A provider overbilling for medical services
B) An insurer charging excessive premiums
C) An agent overselling coverage to a client
✔ D) An insured having too much coverage from multiple policies and profiting from a loss

Explanation: The overinsurance (or relation of earnings to insurance) provision prevents an insured from collecting more in disability benefits than their actual income. If total benefits from all policies exceed a specified percentage of the insured's earnings, the insurer can reduce its benefit proportionally.

49. A traditional fee-for-service health plan is also known as a(n):

✔ A) Indemnity Plan
B) Capitation Plan
C) HMO Plan
D) Managed Care Plan

Explanation: An indemnity plan is a traditional plan that pays a set percentage of charges for services, allowing the insured to see any medical provider they choose. The insurer reimburses the insured or pays the provider directly after a claim is filed.

50. The section of an insurance policy that identifies the specific risks being covered is the:

A) Exclusions
✔ B) Insuring Clause
C) Conditions
D) Declarations

Explanation: The Insuring Clause (or Insuring Agreement) is the core of the policy. It contains the insurer's fundamental promise to pay for covered losses and specifies the perils covered.