Insurance Test Practice

Pennsylvania Insurance Practice Test

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1. 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.

2. In which type of annuity does the owner bear the investment risk?

- A) Immediate Annuity
- ✔ B) Variable Annuity
- C) Deferred Annuity
- D) Fixed Annuity

Explanation: In a variable annuity, the contract owner directs their premium payments into various investment subaccounts (similar to mutual funds). The contract's value and the future income payments depend on the performance of these investments, so the owner assumes all investment risk.

3. The primary risk that annuities are designed to mitigate is:

- A) Catastrophic medical expenses in old age
- B) Market losses in a retirement investment portfolio
- ✔ C) Living longer than expected and outliving one's financial resources
- D) Dying prematurely before accumulating enough savings

Explanation: Annuities are specifically designed to address longevity risk — the risk of outliving one's savings. Life insurance addresses mortality risk (dying too soon). An annuity that pays income for life ensures the retiree will have income no matter how long they live, transferring the longevity risk to the insurance company.

4. A life insurance beneficiary designation of 'children of the insured equally' means:

- ✔ A) All legally recognized children (biological, adopted, and potentially stepchildren if legally adopted) share equally
- B) Only biological children of the insured share the proceeds
- C) Adult children receive double the share of minor children
- D) Children must be named individually to receive proceeds

Explanation: A designation of 'children of the insured equally' (or 'children equally') distributes proceeds equally among all legally recognized children — including biological and legally adopted children. Stepchildren who have not been legally adopted may or may not be included depending on jurisdiction and the specific policy language.

5. A health insurance claimant, Lisa, requests claim forms from her insurer. Within how many days of receiving the request must the insurer provide the forms to Lisa?

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

Explanation: Insurers must provide claim forms to claimants within 10 working days of receiving a request.

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6. An independent insurance agent represents:

- ✔ A) Multiple insurers and owns their own book of business
- B) The state insurance department in regulatory proceedings
- C) Only one insurer exclusively
- D) The insured exclusively as a fiduciary

Explanation: An independent agent represents multiple insurance companies and owns the expirations (renewals) on the policies they write. They can place business with any insurer they are appointed with and typically work on a commission basis.

7. A producer, Robert, is preparing to renew his resident license. Pennsylvania licenses are renewed every two years. How is the renewal deadline determined?

- A) On the producer's birthday in odd-numbered years
- ✔ B) On the producer's birthdate every two years
- C) Exactly two years from the date of license issuance
- D) On June 30 of every second year

Explanation: Pennsylvania licenses are renewed biennially on the producer's birthdate.

8. What is the term for the process of determining if a medical service is covered under a patient's health plan?

- A) Appeals process
- ✔ B) Prior authorization
- C) Underwriting
- D) Claims submission

Explanation: Prior authorization (or pre-authorization/pre-certification) is a requirement from the health insurer that a provider must obtain approval from the plan before delivering a specific service, such as a non-emergency hospital admission or a complex diagnostic image, to qualify for payment.

9. The 'critical illness rider' (or living benefit rider) in a life insurance policy:

- ✔ A) Provides accelerated access to the death benefit upon diagnosis of a specified serious illness
- B) Pays an additional benefit equal to twice the death benefit if death results from a critical illness
- C) Replaces the need for health insurance coverage for critical illnesses
- D) Provides coverage only for illnesses lasting more than 90 days

Explanation: A critical illness (or living benefit) rider allows the insured to accelerate (access early) a portion of the life insurance death benefit upon diagnosis of a qualifying critical illness such as cancer, heart attack, or stroke. The acceleration reduces the remaining death benefit. This provides financial resources to cover treatment costs or lost income.

10. If a corporation owns a non-qualified annuity, how is the growth taxed?

- A) It is tax-free.
- ✔ B) It is taxed annually as ordinary income.
- C) It grows tax-deferred.
- D) It is taxed at corporate capital gains rates.

Explanation: The tax-deferral benefit of annuities generally does not apply when the contract is owned by a non-natural person, such as a corporation. In this case, the annual growth in the contract is treated as taxable ordinary income to the corporation each year.

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11. 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.

12. An annuity premium paid in one lump sum is called a:

- A) Level premium
- ✔ B) Single premium
- C) Flexible premium
- D) Scheduled premium

Explanation: A single premium is a one-time lump-sum payment that fully funds the annuity contract. Single Premium Deferred Annuities (SPDAs) and immediate annuities are typically funded with a single premium. Flexible premium annuities allow additional contributions at varying amounts and timing.

13. Modified premium whole life insurance is characterized by:

A) A death benefit that decreases over time
B) Premiums that decrease after the first year
✓ C) Lower premiums in the early years that increase after a specified period
D) A policy that becomes paid-up after 10 years automatically

Explanation: Modified premium whole life (or Modified Whole Life) charges lower premiums during an initial period (usually the first 3-5 years) that then increase to a higher level premium for the remainder of the policy. This appeals to buyers who expect their income to increase over time but want permanent coverage now.

14. Which of the following is an example of risk avoidance?

✓ A) Deciding not to skydive to avoid the risk of injury
B) Setting aside funds to cover potential losses
C) Installing a sprinkler system to reduce fire damage
D) Purchasing fire insurance on your home

Explanation: Risk avoidance involves eliminating the risk entirely by avoiding the activity that creates it. Deciding not to skydive eliminates the risk of skydiving-related injury. This differs from risk reduction (installing sprinklers), risk transfer (insurance), or risk retention (self-funding).

15. An annuity purchased with after-tax dollars and not held in a qualified retirement plan is called a:

✓ A) Non-qualified annuity
B) Roth annuity
C) Qualified annuity
D) Tax-sheltered annuity

Explanation: A non-qualified annuity is purchased with after-tax (already taxed) dollars outside of a qualified retirement plan. Only the earnings (gains) are subject to income tax upon distribution, not the return of the original after-tax investment (cost basis). This differs from a qualified annuity where all distributions are taxable.

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16. A client age 35 wants to save for retirement, has a high risk tolerance, and wants the potential for high growth. Which annuity would be most suitable?

✓ A) Variable annuity
B) Fixed annuity
C) Annuity certain
D) Immediate annuity

Explanation: A variable annuity would be the most suitable for this client. It allows them to invest directly in the market through subaccounts, offering the potential for higher returns that align with their high risk tolerance and long time horizon.

17. ACA-compliant health plans must cover the following preventive services at no cost-sharing:

A) All preventive services recommended by the insured's physician
✔ B) Preventive services with an 'A' or 'B' rating from the USPSTF, ACIP immunizations, and preventive care for women
C) Preventive services only for children and pregnant women
D) Only services provided by in-network providers at a hospital

Explanation: Under the ACA, non-grandfathered health plans must cover preventive services rated 'A' or 'B' by the U.S. Preventive Services Task Force (USPSTF), ACIP-recommended immunizations, and preventive care guidelines from HRSA — without any cost-sharing. Examples include mammograms, colonoscopies, and flu shots.

18. 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.

19. An insurer regularly offers claimants substantially less than the amounts ultimately recovered in actions brought by those claimants. What is this practice classified as?

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

Explanation: Compelling insureds to institute litigation to recover amounts due under an insurance policy by offering substantially less than the amounts ultimately recovered is an unfair claims practice.

20. The Health Insurance Portability and Accountability Act (HIPAA) provides portability for group health plans. This means it:

A) Makes all group health plans portable across state lines.
B) Allows employees to take their health plan with them when they change jobs.
C) Requires employers to offer a portable savings account.
✔ D) Limits the ability of a new group plan to exclude coverage for pre-existing conditions.

Explanation: A key feature of HIPAA was to improve the portability of health insurance. It limited the extent to which a new group health plan could impose pre-existing condition exclusions on a new employee who had creditable coverage from a previous plan. This role is now largely handled by the ACA.

21. How is the death benefit of a life insurance policy paid to a beneficiary generally treated for tax purposes?

A) It is subject to capital gains tax.
✔ B) It is received income tax-free.
C) It is subject to estate tax for the beneficiary.
D) It is taxed as ordinary income.

Explanation: Death benefits from a life insurance policy are generally paid to the beneficiary free of any federal or state income tax.

22. A retiree, Helen, wants to invest $100,000 in an immediate annuity. She wants to receive the absolute maximum monthly income possible for the rest of her life and does not care about leaving any remaining funds to beneficiaries. Which payout option should she choose?

A) Life with Period Certain
B) Cash Refund
✔ C) Life Only (Straight Life)
D) Joint and Survivor

Explanation: The Life Only (Straight Life) option provides the highest monthly income because it stops immediately upon the annuitant's death, with no refund or survivor guarantees. The insurer assumes less risk, resulting in a higher payout rate.

23. An insurer decides to terminate the appointment of producer Michael. Within how many days must the insurer notify PID of the termination?

A) 10 days
B) 15 days
✔ C) 30 days
D) 45 days

Explanation: The insurer must notify PID within 30 calendar days of terminating a producer's appointment.

24. John has a Whole Life policy with a Waiver of Premium rider. He is totally disabled in a car accident and remains disabled for 8 months before recovering. What happens to the premiums paid during his disability?

A) Under no condition are any premiums refunded
✔ B) The premiums are waived during his disability, and any premiums paid during the initial 6-month waiting period are refunded
C) The insurer pays the premiums but deducts them from the cash value
D) The rider only applies if he remains disabled for life

Explanation: The Waiver of Premium rider waives premiums after a specified waiting period (typically 6 months) during total disability. Once met, the waiver is retroactive to the start of the disability, and any premiums paid during the waiting period are refunded.

25. 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.

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26. Under group life insurance, the 'master policyholder' is the:

A) State insurance department that approves the group policy
B) ERISA-appointed trustee who holds the policy in trust
C) Insured employee with the highest death benefit
✓ D) Employer or organization that enters into the contract with the insurer

Explanation: The master policyholder (or policy sponsor) in group life insurance is the employer or organization that contracts with the insurer and receives the master policy. Individual employees are not parties to the insurance contract — they are certificates holders who receive evidence of their coverage under the group plan.

27. The 'gift tax annual exclusion' and life insurance gifting strategies are relevant because:

A) Life insurance death benefits are always subject to gift taxes
B) Death benefits paid to non-family beneficiaries are treated as taxable gifts
C) Annuity premium payments are subject to gift tax in all cases
✓ D) Transferring ownership of an existing life insurance policy may trigger gift tax if the policy's value exceeds the annual exclusion amount

Explanation: When a policyowner transfers ownership of an existing life insurance policy to another person (e.g., an irrevocable life insurance trust), the transfer may be subject to gift tax based on the policy's value (interpolated terminal reserve plus any unearned premium). This is a key estate planning consideration for using life insurance to reduce taxable estates.

28. The period of time an insured must be disabled before disability income benefits begin to be paid is the:

✓ A) Elimination period
B) Grace period
C) Probationary period
D) Benefit period

Explanation: The elimination period (or waiting period) is a deductible measured in time rather than dollars. It is the length of time from the onset of a disability that the insured must wait before benefits are payable. Common elimination periods are 30, 60, or 90 days.

29. An indexed annuity's 'floor' rate means:

A) The lowest surrender charge in the schedule
✔ B) The minimum interest rate that will be credited, ensuring the owner cannot receive negative interest crediting
C) The minimum annuity payment the owner will receive in the payout phase
D) The minimum premium the owner must pay

Explanation: The floor in a fixed-indexed annuity is the minimum interest that will be credited in any given period — typically 0% (meaning the owner will never receive a negative credit and will never lose principal due to index performance). The combination of a 0% floor and a cap rate gives indexed annuity owners participation in index gains with principal protection.

30. Which of the following is considered a qualified medical expense for HSA withdrawals?

A) Cosmetic surgery for aesthetic purposes
B) Health insurance premiums paid outside of COBRA or Medicare
✔ C) Prescription medications
D) Gym membership fees

Explanation: Prescription medications are qualified medical expenses under IRS Section 213(d). Cosmetic surgery for purely aesthetic reasons, gym memberships, and most health insurance premiums (with exceptions like COBRA and Medicare) are not qualified expenses.

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31. A claimant submits a claim to their health insurer. The insurer requests a medical record that is completely unrelated to the condition being claimed. Is this permitted under Pennsylvania claims rules?

✔ A) No, requesting unrelated records is an unfair practice.
B) Yes, insurers have unlimited rights to medical records.
C) Yes, if the claim is over $1,000.
D) Only for group plans.

Explanation: Insurers are prohibited from requesting unrelated medical records, as it is considered an unfair attempt to delay claims processing.

32. Which managed care model involves physicians and other providers being employed directly by the HMO?

A) Point-of-Service HMO
B) Independent Practice Association (IPA) model HMO
✔ C) Staff model HMO
D) Network or group model HMO

Explanation: A Staff Model HMO employs physicians and other providers directly as salaried staff. The HMO owns the facilities and controls service delivery. This is the most tightly controlled HMO model. Members can only use HMO-employed providers. This model is less common today than network or IPA models.

33. A hazard that increases the probability of loss due to a person's dishonest character is called a:

A) Physical hazard
B) Morale hazard
✔ C) Moral hazard
D) Speculative hazard

Explanation: A moral hazard is dishonesty or character defects that increase the frequency or severity of loss. It differs from a morale hazard, which is carelessness due to indifference because insurance exists.

34. When a non-qualified annuity owner dies and names a non-spouse beneficiary:

A) The annuity is automatically annuitized at the beneficiary's age
B) The beneficiary must take a full lump sum distribution immediately
C) The non-spouse beneficiary inherits the annuity with no required distributions
✔ D) The non-spouse beneficiary must distribute the full contract value within 5 years or begin distributions within 1 year

Explanation: When a non-qualified annuity owner dies, non-spouse beneficiaries must generally: (1) take a lump sum distribution, or (2) annuitize the contract within 1 year of the owner's death and receive payments over the beneficiary's life expectancy, or (3) take the full distribution within 5 years. Spouse beneficiaries have more flexibility and can continue the contract.

35. What is the primary purpose of reinsurance?

A) To replace a primary insurance policy
B) To sell insurance directly to consumers
C) To provide insurance in foreign countries
✔ D) For an insurer to protect itself against catastrophic losses

Explanation: Reinsurance is a process where an insurance company (the ceding insurer) transfers a portion of its risk to another insurer (the reinsurer). This is done to limit the primary insurer's exposure to very large or catastrophic losses.

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36. The waiver of a known legal right or advantage by one party to an insurance contract is called:

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

Explanation: Waiver is the voluntary relinquishment of a known legal right or advantage. If an insurer waives a policy condition (e.g., late premium payment), it cannot later enforce that condition.

37. Which element is NOT required for a risk to be considered insurable?

A) The loss must be definite and measurable.
✔ B) The loss must pose a minimal financial hardship.
C) The loss must not be catastrophic.
D) The loss must be due to chance.

Explanation: For a risk to be insurable, the potential loss must be significant enough to cause financial hardship. Trivial or minimal risks are generally not insurable because the cost of the policy would outweigh the benefit.

38. The suicide clause in most life insurance policies states:

A) The insurer can deny any claim without an investigation if suicide is suspected
✔ B) If the insured dies by suicide within the first 1-2 years of the policy, the insurer will only return the premiums paid
C) Suicide doubles the death benefit due to the accidental nature
D) Suicide is always excluded from coverage

Explanation: The standard suicide clause provides that if the insured dies by suicide within a specified period (usually 1-2 years from the policy date), the insurer will refund the premiums paid but will not pay the death benefit. After the suicide clause period expires, suicide is covered like any other cause of death.

39. What is a Modified Endowment Contract (MEC)?

A) A life insurance policy with a flexible premium.
B) A type of annuity contract.
✔ C) A life insurance policy that has been overfunded according to IRS rules.
D) A policy designed for estate planning.

Explanation: A Modified Endowment Contract (MEC) is a life insurance policy where the cumulative premiums paid during the first seven years exceed a federally set limit (the 7-pay test). This changes the tax treatment of the policy to be less favorable.

40. 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.

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41. 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.

42. A policyholder, Donald, submits a claim to his health insurer. Under Pennsylvania regulations, what is the insurer's duty regarding the acknowledgement of this claim notice?

- ✔ A) Acknowledge receipt of the claim within 10 working days.
- B) Acknowledge receipt within 15 working days.
- C) No acknowledgement is needed until the claim is approved.
- D) Pay the claim immediately.

Explanation: Under Pennsylvania claims regulations, insurers must acknowledge receipt of a claim notice within 10 working days.

43. A 'calendar-year deductible' in health insurance means:

- ✔ A) The deductible amount resets to zero each calendar year on January 1
- B) The deductible is paid in a specific calendar month only
- C) The insured pays a deductible for each separate calendar-year claim
- D) The deductible is the same each year for 5 years and then resets

Explanation: Most individual and group health insurance plans use a calendar-year deductible that resets to zero on January 1 of each year. Once the deductible is met in a given year, coinsurance or copayments apply for the rest of that year. Starting January 1, the insured must meet the deductible again before the insurer begins sharing costs.

44. An annuity that begins making payments to the annuitant one payment interval after it is purchased is a(n):

- A) Deferred Annuity
- B) Flexible Premium Annuity
- ✔ C) Immediate Annuity
- D) Single Premium Annuity

Explanation: An immediate annuity is funded with a single, lump-sum premium and is designed to start paying out income almost immediately (within one year, but typically within one month).

45. Which of the following is typically considered a 'major' service under a dental plan?

- A) Routine cleanings
- B) X-rays
- ✔ C) Crowns and bridges
- D) Fillings

Explanation: Dental plans often categorize services. Preventive (cleanings), Basic (fillings), and Major (crowns, bridges, dentures, orthodontia). Major services usually have the highest level of cost-sharing (e.g., 50% coinsurance) and may have a waiting period.

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46. 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.

47. In a contributory group health plan, what is the typical minimum participation requirement?

A) 90% of eligible employees
✔ B) 75% of eligible employees
C) 100% of eligible employees
D) 50% of eligible employees

Explanation: In a contributory plan, where employees share the cost of the premium, insurers typically require that at least 75% of eligible employees enroll. This helps to prevent adverse selection.

48. Which method of handling risk involves accepting financial responsibility for potential losses without purchasing insurance?

A) Risk sharing
B) Risk transfer
✔ C) Risk retention
D) Risk avoidance

Explanation: Risk retention (self-insurance) means accepting the financial consequences of a potential loss rather than transferring the risk to an insurer. This can be intentional or unintentional.

49. Which of the following best describes group term life insurance?

A) It requires individual medical underwriting for each member
✔ B) It provides temporary protection that typically renews annually and does not accumulate cash value
C) It guarantees coverage until age 100 for all members
D) It builds cash value over the life of the policy

Explanation: Group term life insurance provides temporary death benefit protection, usually on a yearly renewable term basis. It does not build cash value. Group permanent life insurance, by contrast, would include a savings or cash value component.

50. An insurance company, Penn Mutual, is declared insolvent by a Pennsylvania court. Which entity is responsible for protecting policyholders and paying covered claims?

A) The Pennsylvania State Treasury
✔ B) The Pennsylvania Life and Health Insurance Guaranty Association (PLHIGA)
C) The Federal Deposit Insurance Corporation (FDIC)
D) The NAIC Insolvency Fund

Explanation: The Pennsylvania Life and Health Insurance Guaranty Association (PLHIGA) protects policyowners and beneficiaries against financial loss caused by insurer insolvency.