



ATHENA FINANCIAL
& INSURANCE ASSOCIATES



Life & Health Pre-Licensing **PREP REVIEW**

*based on XCEL's study materials to support
licensing exam preparation.*

ANNUITIES

BUSINESS INCOME

1. Which of these is NOT considered to be a purpose of an annuity?

Correct Answer: *"Annuities are intended to create an estate". All of these are purposes of an annuity except "Annuities are intended to create an estate"*

2. Which type of annuity guarantees a stated number of income payments, whether or not the annuitant is still alive to receive them?

Correct Answer: *"Life annuity certain". A life annuity certain provides a guaranteed minimum number of benefit payments, whether the annuitant live or dies.*

3. What is the primary reason for buying an annuity?

Correct Answer: *"Provide future economic security ". The main reason for purchasing an annuity is to provide future economic security.*

4. Which type of annuity stops all payments upon the death of the annuitant?

Correct Answer: *"Life annuity". The type of annuity in which all payments cease upon the death of an annuitant is referred to as a life annuity.*

5. Which of these statements regarding the annuitant is CORRECT?

Correct Answer: *Annuity payments are based on the annuitant's life expectancy.*

6. An annuitant dies during the distribution period. What kind of annuity will return to a beneficiary the difference between the annuity value and the income payments already made?

Correct Answer: *"Refund annuity". An annuity that returns the difference between the annuity value and the income payments made to a beneficiary when the annuitant dies during the distribution period is a refund annuity.*

ANNUITIES

7. Which settlement option pays a stated amount to an annuitant, but no residual value to a beneficiary?

Correct Answer: "Life income". The settlement option that pays a specified amount to an annuitant, but pays no residual value to a beneficiary is known as life income.

8. An annuitant is guaranteed to NOT outlive their benefits with a(n)

Correct Answer: A guaranteed lifetime withdrawal benefit (GLWB) is a rider on a variable annuity that allows minimum withdrawals from the invested amount without having to annuitize the investment. This rider guarantees that a certain percentage (often based on age) of the amount invested can be withdrawn each year for as long as the contract holder lives.

9. How do interest earnings accumulate in a deferred annuity?

Correct Answer: "On a tax-deferred basis". Deferred annuities accumulate interest earnings on a tax-deferred basis.

10. Kathy's annuity is currently experiencing tax-deferred growth until she retires. Which phase is this annuity in?

Correct Answer: "Accumulation period". Kathy's annuity is in the accumulation period.

11. Phil is shopping for an annuity that guarantees he CANNOT outlive the benefits. Which of these benefit options would he choose?

Correct Answer: The guaranteed lifetime withdrawal benefit normally requires a fee, but it ensures that the income benefit will be paid for life without actually annuitizing the contract.

12. When does an immediate annuity begin making payments?

Correct Answer: "After the first premium has been paid". An immediate annuity begins making payments after the first premium has been paid.

ANNUITIES

BUSINESS INCOME

13. Which of the following is an annuity that is linked to a market-related index?

Correct Answer: "Equity-indexed annuity". An equity-indexed annuity is linked to a market-related index.

14. Which of these annuities require premium payments that vary from year to year?

Correct Answer: "Flexible premium deferred annuity". Flexible premium deferred annuities require premium payments that vary from year to year.

15. Fixed annuities provide each of the following EXCEPT

Correct Answer: "Hedge against inflation." Fixed annuities do NOT provide for a hedge against inflation.

16. Fixed period settlement options are considered to be a form of a(n)

Correct Answer: "annuity". A fixed period settlement option is actually a form of an annuity.

17. How are annuities given favorable tax treatment?

Correct Answer: "Gains are taxed at distribution". Annuity gains are typically tax deferred until distribution.

18. Lisa has recently bought a fixed annuity. Which of these is considered to be a disadvantage of owning this type of annuity?

Correct Answer: "During periods of inflation, annuitants will experience a decrease in purchasing power of their payments". The disadvantage of fixed annuities is annuitants could experience a decrease in the purchasing power of their payments over a period of years due to inflation.

ANNUITIES

BUSINESS INCOME

19. Which market index is normally associated with an indexed annuity's rate of return?

Correct Answer: "S & P 500". An indexed annuity rate of return is linked to a market index, like the S & P 500.

20. Which of these will have the highest monthly payout upon annuitization?

Correct Answer: "Straight life". A straight life annuity will have the highest monthly payout.

21. Who assumes the investment risk with a fixed annuity contract?

Correct Answer: It is the insurance company that bears the investment risk of a fixed annuity. The insurance company guarantees the annuitant's principal as well as a guaranteed minimum rate of return, even if the underlying assets underperform the guaranteed rate.

22. An annuity is primarily used to provide

Correct Answer: "retirement income". The principal use of an annuity is to provide income for retirement.

23. An immediate annuity has been purchased with a single premium. When does the annuitant typically begin receiving benefit payments?

Correct Answer: "1 month". When an immediate annuity is funded with a single premium, the annuitant may begin receiving payments after 1 month.

24. The taxable portion of each annuity payment is calculated using which method?

Correct Answer: The Exclusion Ratio is used to determine the taxable portion of each annuity payment.

ANNUITIES

BUSINESS INCOME

25. What happens to interest earned if the annuitant dies before the payout start date?

Correct Answer: *"It is taxable". If the annuitant dies before the payout start date, the interest earned is taxable.*

26. Andy the annuitant dies before the annuity start date. Which of the following is a TRUE statement?

Correct Answer: *"Premiums paid plus interest earned is returned to the beneficiary". If an annuitant dies before the annuity start date, the beneficiary receives the premiums paid plus interest earned.*

27. During the accumulation period, who can surrender an annuity?

Correct Answer: *"Policyowner". The policyowner is the only one who can surrender an annuity during the accumulation period.*

28. What will the beneficiary receive if an annuitant dies during the accumulation period?

Correct Answer: *"The greater of the accumulated cash value or the total premium paid". If an annuitant dies during the accumulation period, his or her beneficiary will receive the greater of the accumulated cash value or the total premium paid.*

29. How soon can the benefit payments begin with a deferred annuity?

Correct Answer: *"A minimum of 12 months after date of purchase". A deferred annuity is an annuity contract in which periodic income payments are not scheduled to begin for at least 12 months.*

30. Which annuity payout option allows the policyowner to choose a pre-determined number of benefit payments?

Correct Answer: *"Period certain". An annuity where the policyowner chooses a pre-determined number of benefit payments is called period certain.*

ANNUITIES

BUSINESS INCOME

31. If the annuitant dies before the annuity start date,

Correct Answer: *"the premiums paid plus interest earned will be given to the beneficiary". If the annuitant dies before the annuity start date, the beneficiary receives the premiums paid plus interest earned.*

32. Kristi purchases an annuity that will pay her husband an income for 15 years. If he dies, this income will become payable to their children for the remainder of the period. Kristi has what kind of annuity?

Correct Answer: *"Temporary annuity certain". Under a temporary annuity certain, the company guarantees that payments will be made for a specified number of years. Since this income is guaranteed, if the annuitant dies before receiving payments for the full specified period of time, the annuitant's beneficiary will receive the payments for the remaining number of years.*

33. Which of the following annuity payout options makes no additional payments regardless of when the annuitant dies?

Correct Answer: *"Life only". The life only annuity payout option has no additional payouts regardless of when the annuitant dies.*

34. Maria would like an annuity that provides a guaranteed accumulation or payout. The type of annuity she is seeking is called

Correct Answer: *"annuity certain". A type of annuity that provides a guaranteed accumulation or payout is called annuity certain.*

35. Simon has purchased a fixed immediate annuity. His payment amount will be dependent upon principal, interest, and the contract's

Correct Answer: *"income period". The amount of a fixed immediate annuity payment is dependent upon starting principal, interest, and the annuity's income period.*

ANNUITIES

36. Which of the following is considered to be the period when the accumulated value in an annuity is paid out?

Correct Answer: "Annuitization phase". The period when the annuitant starts to receive payments from the annuity is the annuitization phase.

37. Under the terms of a non-qualified annuity, annuity income payments are taxable

Correct Answer: "according to the exclusion ratio that has been calculated". The taxable and non-taxable portions of annuity payments are determined by the exclusion ratio, which characterizes a portion of each payment as interest income and the remainder as the return of one's after-tax premiums, which are excluded from taxation. If withdrawals are taken from the annuity's accumulation account without annuitizing the contract, then those withdrawals would be considered interest until all the interest was paid out. The key here is that the payments are considered "annuity income," which on a state insurance exam indicates an annuitized contract.

38. What is the nonforfeiture value of an annuity before annuitization?

Correct Answer: The nonforfeiture value of an annuity prior to annuitization is all premiums paid, plus interest, minus any withdrawals and surrender charges.

39. Within how many days must a Traditional IRA be rolled over to another IRA in order to avoid tax consequences?

Correct Answer: "60". To avoid tax consequences, a rollover from a Traditional IRA to another IRA must be done within 60 days.

40. All of the following are exempt from the 10% tax penalty for early qualified plan withdrawals EXCEPT

Correct Answer: Withdrawing funds from a qualified plan for the purpose of purchasing stocks or other securities would trigger a 10% tax penalty.

ANNUITIES

41. Mike has inherited his father's traditional IRA. As beneficiary, he will pay ____ taxes on any money withdrawn.

Correct Answer: "income". When a beneficiary inherits a traditional IRA, an income tax is paid when money is withdrawn.

42. When a qualified plan starts making payments to its recipient, which of the following choices BEST describes the portion of each distribution that is taxable?

Correct Answer: The choice "Gains" is BEST answer out of the choices. While the entire distribution would be taxed assuming the contributions were made pre-tax, the IRS would characterize all distributions as taxable gains. Not all qualified plans have employer contributions. Neither do all plans include employee contributions. In certain circumstances, even some traditional IRA contributions might not qualify as deductible and therefore would not be taxed when withdrawn. Gains are ALWAYS taxable. The IRS characterizes all previously untaxed distributions as gains. Therefore, "Gains" is the BEST answer among the choices given. TIP: When answering a question on a state insurance exam, watch out for words like BEST and MAXIMUM. You will also find imperfect choices, such as were presented here. When in doubt, "Pick the one that stinks the least."

43. Which of the following would disqualify a company's retirement plan from receiving favorable tax treatment?

Correct Answer: A retirement plan will not qualify for favorable tax treatment if it is temporary.

44. Which of these retirement plans do NOT qualify for a federal income tax deduction?

Correct Answer: All of these retirement plans qualify for a federal income tax deduction EXCEPT a Roth IRA.

ANNUITIES

45. Dana is an employee who deposits a percentage of her income into her individual annuity. Her company also contributes a percentage into a separate company pension plan. What kind of annuity is this considered?

Correct Answer: *In this situation, her annuity is considered a qualified retirement annuity.*

46. A Roth IRA owner must be at least what age in order to make tax-free withdrawals?

Correct Answer: *"59 1/2 and owned account for a minimum of 5 years". To be able to make tax-free withdrawals from a Roth IRA, an account owner should be AT LEAST age 59 1/2 and have held the account for at least 5 years.*

47. An example of a tax-qualified retirement plan would be a(n)

Correct Answer: *A defined contribution plan is considered a tax-qualified plan.*

48. Erica is 35 years old and owns an IRA. At what age can she begin to receive distributions without a tax penalty?

Correct Answer: *"59 1/2". An individual can begin to receive distributions from an IRA at age 59 1/2 without a tax penalty.*

49. How are contributions made to a Roth IRA handled for tax purposes?

Correct Answer: *"Not tax deductible". Contributions made to a Roth IRA are not tax deductible.*

50. Which of the following is NOT a federal requirement of a qualified plan?

Correct Answer: *"Employee must be able to make unlimited contributions". A qualified plan does not allow the employee to make unlimited contributions.*

ANNUITIES

51. Which of these statements concerning Traditional IRAs is CORRECT?

Correct Answer: *"Earnings are taxable when withdrawn". Traditional IRA earnings are taxable when withdrawn.*

52. Within how many days must a rollover be completed in order to avoid being taxed as current income?

Correct Answer: *After you receive funds from your IRA, you have 60 days to complete the rollover to another IRA.*

53. A rollover from a Traditional IRA to another IRA MUST be done within ___ days to avoid tax consequences.

Correct Answer: *"60". A distribution received from a Traditional IRA is eligible for a tax-free rollover if it is reinvested in another IRA within 60 days following receipt of the distribution and if the plan participant does not actually take physical receipt of the distribution.*

54. Rob has a benefit at work which enables him to defer his current receipt of income and have it paid at a later date, when he will probably be in a lower tax bracket. Which benefit fits this description?

Correct Answer: *Deferred compensation option". A deferred compensation option enables an employee to defer current receipt of income and have it paid at a later date, when presumably the employee will be in a lower income tax bracket.*

55. Under a Traditional IRA, interest earned is taxed

Correct Answer: *"upon distribution". Interest earned on a Traditional IRA is taxed upon distribution at ordinary income tax rates.*

56. Which of the following employers is required to follow ERISA regulations?

Correct Answer: *A local electrical supply company with 12 employees would be subject to ERISA.*

ANNUITIES

57. Who were Keogh plans designed to provide pension benefits for?

Correct Answer: "The self-employed". Keogh plans were designed to provide pension benefits for self-employed individuals.



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