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PRM Certification - Exam IV: Case Studies; Standards: Governance, Best Practices and Ethics

PRMIA 8004

Version Demo

Total Demo Questions: 14

Total Premium Questions: 141

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Topic Break Down

Topic	No. of Questions
Topic 1, Case Studies	76
Topic 2, Standards and Best Practices	20
Topic 3, Governance and Ethics	44
Topic 4, Mix Questions	1
Total	141

QUESTION NO: 1

For the sentence

"The organization shall encourage all employees to keep abreast of the latest developments in their particular areas of expertise, through ____________, _____________, and _____________ and shall make adequate resources available to enable this to occur,"

Choose the correct combinations of words from the following options:

A. courses, conferences, journals

B. conferences, discussion groups, blog sites

C. courses, educational certification, journals

D. journals, courses, compliance mandates

ANSWER: A

Explanation:

The correct completion is **"courses, conferences, journals."** This language reflects the professional-development expectation in PRMIA's standards and ethics framework: organizations should support employees in maintaining current, relevant expertise through structured learning, professional engagement, and ongoing access to technical and industry knowledge. Courses provide formal training and skills development; conferences enable exposure to current market practice, research, regulation, and professional dialogue; and journals provide continuing access to published analysis, standards, and developments relevant to a practitioner's specialist area.

The requirement that adequate resources be made available is important because maintaining competence is not merely an individual aspiration. Effective governance treats continuing professional development as an organizational responsibility, with sufficient time, funding, learning access, and management support for personnel to remain capable of performing their risk-management responsibilities appropriately. This supports sound professional judgment, informed challenge, and the ability to respond to evolving methodologies, products, markets, and regulatory expectations.

PRMIA's professional standards and certification materials emphasize competence, ethical conduct, and continued development as core features of professional risk management. See PRMIA's Standards publications and its certification and professional-development resources.

QUESTION NO: 2

What was the most important loss for Bankers Trust?

A. Money due to unfavourable market moves

B. Loss of its' reputation due to actions seen as detrimental to their clients

C. Loss of market share due to their licenses being revoked

D. Time spent on legal proceedings in courts

ANSWER: B

Explanation:

Loss of its' reputation due to actions seen as detrimental to their clients was Bankers Trust's most consequential loss. The Bankers Trust derivatives controversies of the mid-1990s, notably disputes with corporate clients over complex interest-rate and currency products, created a perception that the firm had not communicated product risks, valuation implications, and potential losses with the degree of candour expected in a client relationship. In financial services, reputation is a core risk asset: clients must be able to rely on the institution's integrity, fair dealing, suitability processes, and transparency when entering products whose risks may be difficult to assess independently.

Reputational damage can extend far beyond the immediate financial effect of an individual transaction or lawsuit. It can reduce client willingness to trade, impair the firm's ability to win mandates, invite increased supervisory attention, weaken employee confidence, and raise the cost of restoring controls and trust. The episode is therefore a classic conduct-risk and governance lesson: sales incentives and product sophistication must be balanced by clear disclosure, appropriate client treatment, effective oversight, and a culture that protects the firm's long-term standing. The Federal Reserve's historical enforcement materials provide context on supervisory expectations for banking organizations: Federal Reserve enforcement actions. PRMIA also identifies professional conduct and ethics as essential foundations of sound risk practice: PRMIA Professional Standards.

QUESTION NO: 3

The Fortress Re accounting risk transfer procedures

A. made it straightforward for TFMI to determine whether risk had actually been transferred and they decided not to take out more catastrophe insurance cover

B. made it difficult for TFMI to determine whether risk had actually been transferred so they had to take out additional catastrophe insurance cover

C. made it straightforward for TFMI to determine when the risk had been transferred and to take out additional catastrophe insurance cover

D. made it difficult for TFMI to determine whether risk had actually been transferred and whether it had sufficient catastrophe insurance cover

ANSWER: D

Explanation:

"made it difficult for TFMI to determine whether risk had actually been transferred and whether it had sufficient catastrophe insurance cover" is correct because the case highlights the governance and risk-management problem created when accounting treatment, contract structure, and the underlying economic transfer of catastrophe exposure are not sufficiently transparent. A cedant cannot rely solely on the existence of a reinsurance arrangement or its accounting presentation; it must be able to evidence that material underwriting and timing risk have genuinely passed to the reinsurer. Where procedures and documentation do not provide that clarity, management cannot reliably measure the remaining net catastrophe exposure, determine the adequacy of protection, or make informed capital and insurance-purchasing decisions. Sound practice therefore requires independent assessment of risk transfer, complete and timely exposure aggregation, clear contractual terms, and reporting that enables senior management and the board to understand residual risk. This is consistent with PRMIA's emphasis on effective risk governance, independent challenge, and reliable risk information, described in its Standards of Best Practice. It also aligns with the supervisory focus on robust reinsurance risk management and documentation reflected in the NAIC Risk Management and Own Risk and Solvency Assessment Model Act.

QUESTION NO: 4

Mary Jones wants the Bylaws of PRMIA to be changed so that people can't join PRMIA unless they meet a set of criteria she has devised with her colleagues. She can do this by getting which of the following approvals:

A. The Board of Directors, but only if the Blue Ribbon Panel affirms the change

B. The Board of Directors and a majority of the Members

C. The Board of Directors alone

D. 34 of all Members

ANSWER: B

Explanation:

The Board of Directors and a majority of the Members is correct because imposing new eligibility conditions for joining PRMIA changes the Association's membership rules and therefore requires a formal amendment to the Bylaws. Bylaws are the governing rules of the organization; they cannot be changed merely through an informal proposal or an operational decision. PRMIA's amendment process requires both governance-level approval by the Board of Directors and approval by the membership by the required majority. This dual-approval structure ensures that the Board can assess whether a proposed amendment is consistent with PRMIA's mission, legal obligations, and governance framework, while Members retain the authority to approve a change affecting the fundamental rules of their professional association. A membership restriction is especially significant because it affects who may participate in PRMIA and access its professional community, programs, and member rights. Accordingly, Mary's proposed criteria can become part of the Bylaws only after approval by the Board of Directors and a majority of the Members, following the procedures set out in the governing documents. See PRMIA's Bylaws and its governance information.

QUESTION NO: 5

The collapse of Enron illustrates that a principal weakness of relying on reported earnings and share-price performance as indicators of financial health is that

A. complex related-party arrangements can conceal leverage, losses, and conflicts of interest

B. share-price performance provides independent assurance of accounting accuracy

C. special-purpose entities cannot affect an issuer's risk profile

D. mark-to-market accounting always prevents manipulation of reported earnings

ANSWER: A

Explanation:

complex related-party arrangements can conceal leverage, losses, and conflicts of interest is correct. Enron used special-purpose entities and related-party transactions in ways that obscured debt, transferred poorly performing assets, and distorted reported financial results. The case demonstrates that boards, auditors, investors, and risk functions must look beyond headline earnings to the substance of transactions, the independence of counterparties, off-balance-sheet commitments, valuation assumptions, and conflicts involving senior executives.

The SEC's Enron enforcement release describes allegations concerning misleading financial reporting. The SEC's Sarbanes-Oxley Act resources provide further context on governance and reporting reforms.

QUESTION NO: 6

The Fortress Re finite reinsurance model

A. allowed Fortress to claim re-insurance claims payments from the finite reinsurers and paid premiums to cover these deals over a 5 year period, and as the risks were spread out over time the annual premiums were accounted for as current liabilities on the books of the pool members, giving a true impression of profitability

B. allowed Fortress to claim re-insurance claims payments from the finite reinsurers and paid annual premiums to cover these policies, and as the risks were spread out over the year the annual premiums were accounted for as current liabilities on the books of the pool members, giving a true impression of profitability

C. allowed Fortress to claim re-insurance claims payments from the finite reinsurers and paid premiums to cover these deals over a 5 year period, and as the risks were spread out over time the future premiums were accounted for as current liabilities on the books of the pool members, giving a true impression of profitability

D. allowed Fortress to claim re-insurance claims payments from the finite reinsurers and paid premiums to cover these deals over a 5 year period, but as the risks were spread out over time the future premiums were not accounted for as current liabilities on the books of the pool members, thus giving a false impression of profitability

ANSWER: D

Explanation:

The correct description is: “allowed Fortress to claim re-insurance claims payments from the finite reinsurers and paid premiums to cover these deals over a 5 year period, but as the risks were spread out over time the future premiums were not accounted for as current liabilities on the books of the pool members, thus giving a false impression of profitability.” The essential feature of the Fortress Re structure was the timing mismatch it created. Pool members could recognise a reinsurance recovery for current claims, improving reported results in the near term, while the economic cost of the arrangement included substantial premium commitments extending into future periods. Where those future obligations are not appropriately recognised or transparently reflected, current financial statements can overstate profitability and understate the obligations associated with obtaining the reinsurance benefit. The issue is therefore not simply that the contract extended for five years; it is that reporting did not faithfully convey the present economic burden of future premium payments in relation to current claim recoveries. Sound insurance accounting and governance require recognition, measurement, and disclosure that reflect the substance of reinsurance arrangements, including risk transfer and related obligations. This aligns with the IAIS supervisory material on the evaluation of reinsurance and with IFRS requirements for presenting relevant obligations faithfully. See the IAIS Insurance Core Principles and IFRS 17 overview.

QUESTION NO: 7

A bank reports a large reduction in its credit valuation adjustment exposure after entering into a hedge with a single financial counterparty. Which additional risk requires particular attention?

A. wrong-way risk arising if the hedge counterparty becomes weaker when the underlying exposure increases

B. the elimination of counterparty risk through a bilateral derivative contract

C. the certainty that collateral can never decline in value

D. the removal of all concentration risk once a hedge is executed

ANSWER: A

Explanation:

wrong-way risk arising if the hedge counterparty becomes weaker when the underlying exposure increases is correct. A hedge reduces risk only to the extent that it performs when needed. If the hedge provider is likely to suffer financial stress in the same market conditions that increase the bank’s original exposure, the apparent mitigation may fail precisely during stress. The bank must assess counterparty credit quality, collateral, concentration, legal enforceability, and correlations between exposure and counterparty default risk.

The Basel Committee’s framework for counterparty credit risk discusses wrong-way risk and the need to identify adverse dependence between exposure and counterparty creditworthiness.

QUESTION NO: 8

A risk assessment report generated by a PRMIA member creates an apparent conflict of interest between the PRMIA standards and those of the client organization.

Of the following, which is the correct hierarchy to follow to resolve the conflict?

I. The decision of a superior within the organization

II. PRMIA Standards

III. Guidelines from the regulators in which the organization operates

IV. The laws of the country

A. I, II, III, and IV

B. IV, III, II, and I

C. II, I, IV, and III

D. III, II, IV, and I

E. The decision of a superior within the organization
II. PRMIA Standards
III. Guidelines from the regulators in which the organization operates
IV. The laws of the country

ANSWER: B

Explanation:

IV, III, II, and I is the appropriate hierarchy because a PRMIA member's professional conduct must first comply with the binding law of the jurisdiction in which the work is performed. Law is the highest authority because it establishes mandatory legal duties and prohibitions. Regulatory guidance is next: regulators oversee the organization's activities and may impose enforceable rules, supervisory expectations, reporting requirements, and conduct standards within their remit. PRMIA Standards then provide the applicable professional and ethical framework for members, including expectations of integrity, objectivity, and responsible risk-management practice. Finally, a superior's instruction is relevant within the employment relationship, but it must be applied consistently with all higher-ranking legal, regulatory, and professional obligations. This sequence gives the member a practical escalation framework when organizational expectations appear to conflict with independent professional responsibilities. It also supports the central PRMIA ethical principle that members act with integrity and observe applicable laws, rules, and professional standards while carrying out risk-management work. See PRMIA's professional standards and membership resources at PRMIA and the organization's governance materials at PRMIA Governance.

QUESTION NO: 9

While doing a work assignment, a PRMIA member notices behaviour that is outside the ethical standards of their client organization and reports the matter to their immediate supervisor in the organization (if he or she wasn't the one engaging in such behaviour). The matter is neither progressed nor actioned.

The PRMIA member should:

A. stay silent on the basis that they have reported it

B. report the matter to their PRMIA chapter

C. contact the Whistle-Blowing Hotline of the organization or, if none exits, to the PRMIA Ethics Committee for guidance and assistance

D. report the matter to the organization's Compliance Dept.

ANSWER: C

Explanation:

"Contact the Whistle-Blowing Hotline of the organization or, if none exists, the PRMIA Ethics Committee for guidance and assistance" is correct because a member who has raised a good-faith ethical concern through the normal management channel should pursue an appropriate escalation route when the issue is not addressed. An organizational whistle-blowing hotline is specifically designed to receive allegations confidentially and independently, helping ensure that misconduct concerns can be reviewed even where local management has failed to act. Where the client organization has no such mechanism, seeking guidance from PRMIA's Ethics Committee is the appropriate professional step. It allows the member to obtain support on how to uphold PRMIA's ethical obligations while handling the concern responsibly, confidentially, and in accordance with applicable legal and organizational requirements. This approach reflects the principle that ethical duties do not end merely because an initial report has been ignored; members should take reasonable further action through proper channels. PRMIA's Code of Professional Conduct establishes members' obligations to act with integrity and to support ethical professional conduct. See PRMIA Standards of Best Practice, Conduct and Ethics and PRMIA Ethics Committee.

QUESTION NO: 10

The main governance lesson from the UBS rogue-trading loss in 2011 was that

A. profitable trading activity should be exempt from independent operations review

B. reconciliation breaks and control exceptions require independent and persistent escalation

C. market-risk limits should be set only by front-office management

D. exchange-traded derivatives eliminate operational risk

ANSWER: B

Explanation:

reconciliation breaks and control exceptions require independent and persistent escalation is correct. The loss arose after unauthorized trading activity was concealed through fictitious hedging transactions. Control systems generated warnings and reconciliation exceptions, but those signals were not effectively resolved, challenged, or escalated. A control framework cannot rely merely on producing exception reports; it must assign ownership, require evidence-based closure, and ensure that unresolved or recurring exceptions are visible to risk management and senior management.

The Basel Committee's operational-risk principles describe the need for effective internal controls, independent assurance, and escalation of material control weaknesses.

QUESTION NO: 11

Which of the following best distinguishes liquidity risk from solvency risk?

A. Liquidity risk concerns the ability to meet obligations when due, whereas solvency risk concerns whether asset values are sufficient to cover liabilities

B. Liquidity risk and solvency risk are identical because both concern accounting profit

C. Solvency risk concerns only the timing of daily cash payments

D. Liquidity risk can arise only when a firm has negative equity capital

ANSWER: A

Explanation:

Liquidity risk concerns the ability to meet obligations when due, whereas solvency risk concerns whether asset values are sufficient to cover liabilities is correct. A firm may be solvent on a balance-sheet basis but still fail if it cannot obtain cash or sell assets quickly enough to meet withdrawals, margin calls, or maturing funding obligations. Conversely, access to short-term liquidity does not remedy a position in which losses have reduced asset values below liabilities.

The two risks are closely linked because a liquidity crisis can force asset sales at distressed prices, thereby crystallising losses and impairing capital. Risk governance should therefore assess liquidity, collateral, funding concentration, and market-value stress alongside capital adequacy rather than treating them as wholly independent issues. The Basel Committee's Principles for Sound Liquidity Risk Management and Supervision discuss this relationship.

QUESTION NO: 12

Boards, including Audit and Risk Committees must:

I. Clearly articulate the corporate risk appetite to senior management

II. Thoroughly review compensation plans of potentially "highly compensated positions" for consistency with corporate risk appetite, competitive market conditions and fiduciary responsibility to shareholders

III. Have a single member formally given responsibility for understanding and reporting the effectiveness of the corporation's risk management infrastructure

IV. Be fully accountable to shareholders and work to the benefit of public good and financial stability

A. I and II only

B. I, II and IV only

C. I, II and III only

D. All of these are responsibilities of Board and Audit Committees

E. Clearly articulate the corporate risk appetite to senior management
II. Thoroughly review compensation plans of potentially "highly compensated positions" for consistency with corporate risk appetite, competitive market conditions and fiduciary responsibility to shareholders
III. Have a single member formally given responsibility for understanding and reporting the effectiveness of the corporation's risk management infrastructure
IV. Be fully accountable to shareholders and work to the benefit of public good and financial stability

ANSWER: D

Explanation:

All of these are responsibilities of Board and Audit Committees is correct because sound risk governance requires the board and its committees to provide clear direction, effective oversight, and identifiable accountability for the firm's risk-management framework. Establishing and communicating risk appetite gives senior management an approved boundary for business decisions, risk taking, capital deployment, and escalation. Board-level review of remuneration—particularly for roles capable of taking material risk—is integral to ensuring compensation does not create incentives that are inconsistent with the firm's approved risk appetite or its long-term interests.

Governance also requires clear ownership of oversight activities. Formally assigning a member to understand and report on the effectiveness of the risk-management infrastructure supports informed committee deliberation, regular challenge of management, and timely escalation of weaknesses, while not displacing the collective accountability of the board. Ultimately, directors' fiduciary responsibilities and the systemic importance of financial institutions require governance to promote sustainable shareholder value while considering the public interest and financial stability. The Basel Committee's corporate-governance principles emphasize board responsibility for approving risk appetite and overseeing the risk-management framework; its compensation guidance similarly connects remuneration governance to prudent risk taking. See the Basel Committee's Corporate Governance Principles for Banks and Principles for Sound Compensation Practices.

QUESTION NO: 13

Boards of Directors, including Audit and Risk Committees must review thoroughly compensation plans of potentially "highly compensated positions" for:

I. competitive market conditions

II. ensuring compliance with their corporate risk appetite and fiduciary responsibility to shareholders

III. ensuring any discretionary bonus plans are geared towards keeping high income / revenue generators

IV. reporting all such personnel to the local regulator

A. II, III and IV only

B. I, II and IV only

C. All of the above

D. I and II only

E. competitive market conditions
II. ensuring compliance with their corporate risk appetite and fiduciary responsibility to shareholders
III. ensuring any discretionary bonus plans are geared towards keeping high income / revenue generators
IV. reporting all such personnel to the local regulator

ANSWER: D

Explanation:

I and II only is correct because board and committee oversight of compensation must address both whether remuneration is appropriate in the relevant talent market and whether its design is aligned with the institution's risk governance obligations. Competitive-market review helps the board establish that remuneration arrangements are reasonable, sustainable, and capable of attracting and retaining suitably qualified personnel without creating an unjustified cost or risk burden for the firm.

More importantly, compensation governance is a core risk-management responsibility. The board must ensure that incentives, including variable compensation, are consistent with the organization's risk appetite, long-term financial soundness, and duties to shareholders. This requires an effective process for identifying and controlling incentives that could encourage excessive risk-taking, short-termism, or conduct inconsistent with the firm's strategy and control framework. Audit and risk committees provide challenge and independent oversight of these arrangements as part of their broader governance responsibilities.

The Financial Stability Board's Principles for Sound Compensation Practices emphasize alignment of compensation with prudent risk-taking. The Basel Committee's Corporate governance principles for banks likewise assigns the board responsibility for ensuring remuneration policies are consistent with the bank's risk culture and risk appetite.

QUESTION NO: 14

Which of the following best characterizes the problems that developed at Bankgesellschaft Berlin?

A. Volume growth at the expense of margin.

B. Excessive reliance on volatile trading income.

C. Banking is a "for-profit" business, not a means of fulfilling political goals.

D. A company culture where profits may justify "excesses."

ANSWER: C

Explanation:

Banking is a "for-profit" business, not a means of fulfilling political goals. This best captures the central governance failure at Bankgesellschaft Berlin. The bank was controlled by the State of Berlin and became deeply involved in property-related investments and fund structures whose risks were amplified by public-policy considerations, political influence, and a weak separation between the owner's political role and the institution's commercial risk-management responsibilities. The resulting losses required a major public rescue and restructuring. The key lesson is that a bank's board and management must make lending, investment, pricing, and capital-allocation decisions according to prudent commercial standards, independently assessed risk, and the interests of the institution—not as instruments for political objectives. Public ownership does not remove the need for clear accountability, independent oversight, transparent limits, and disciplined risk governance. The European Commission's review of the restructuring and state support illustrates the scale of the intervention required after the crisis: European Commission press release on Bankgesellschaft Berlin. This conclusion also aligns with the OECD principle that state-owned enterprises should operate with clear mandates and professional, accountable governance: OECD Guidelines on Corporate Governance of State-Owned Enterprises.