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GARP Financial Risk and Regulation (FRR) Series Sample Questions (Q341-Q346):

NEW QUESTION # 341

Which of the following statements regarding CDO-squared is correct?

- I. CDO-squared use other CDOs and CMOs as collateral.
- II. Risk assessment of CDO-squared is almost impossible due to their complexity.
- III. CDO-squared have lower credit risk than CMOs but higher than CDOs.

- A. I only
- **B. I and II**
- C. I, II, and III
- D. II and III

Answer: B

NEW QUESTION # 342

A trader for EtaBank wants to take a leveraged position in Collateralized Debt Obligations. If these CDOs can be used in a repo transaction at a 20% haircut, what is the maximum leverage factor for a transaction with the CDOs?

- A. 1.5
- B. 0.8
- **C. 0**
- D. 1

Answer: C

NEW QUESTION # 343

According to the principles of the Basel II Accord, the implementation and relative weights of the elements of the operational risk framework depend on:

- I. The culture of the financial institution
- II. Regulatory drivers
- III. Business drivers
- IV. The bank's reporting currency

- A. I, IV
- **B. I, II, III**
- C. II, III
- D. II, IV

Answer: B

Explanation:

According to the principles of the Basel II Accord, the implementation and relative weights of the elements of the operational risk framework depend on the culture of the financial institution (I), regulatory drivers (II), and business drivers (III). The bank's reporting currency (IV) is not relevant to the implementation of the operational risk framework under Basel II. References: Basel II Accord principles on operational risk.

NEW QUESTION # 344

A trader inadvertently booked a trade with incorrect information. A subsequent market move resulted in a gain to the bank. Should the bank include this amount of gain into its operational loss event data program?

- I. The bank should include this gain in its operational loss event data program as a gain realized due to operational risk events.

II. The bank should include this gain in its operational loss event data program as it indicates that a control failed or a process is flawed.

III. The bank should include this event in its operational loss event data program and record the gain as a loss resulting from operational risk. The bank should not include this event in its operational loss event data program as it is not a loss event, but a market risk event.

- A. I, II and III
- **B. II and III**
- C. I and II
- D. I and III

Answer: B

Explanation:

When a trader inadvertently books a trade with incorrect information and a subsequent market move results in a gain for the bank, the event should be included in the operational loss event data program because:

* Indication of Control Failure (II): The gain indicates that a control failed or a process is flawed. Even if the outcome was a gain, the underlying issue was a mistake, pointing to a weakness in the bank's operational controls that needs to be addressed.

* Recording the Event as a Loss (III): Although the event resulted in a gain, it should be included in the operational loss event data program and recorded as a loss. The principle behind this is to ensure that all operational risk events are tracked, irrespective of their financial outcome, to provide a complete picture of operational risk exposures and to improve risk management practices.

Including such events helps in identifying and correcting process flaws to prevent future incidents that could result in actual losses.

References

* How Finance Works.pdf, Index section

NEW QUESTION # 345

A trader for EtaBank wants to take a leveraged position in Collateralized Debt Obligations. These CDOs can be used in a repurchase transaction at a 20% haircut. Starting with \$100 worth of CDOs, which one of the following four positions would completely utilize the available leverage?

- A. The trader can buy \$100 in CDO's, and repo the CDO's to get back \$20, plus interest.
- **B. The trader can buy \$100 in CDO's, and repo the CDO's to get back \$80, less interest.**
- C. The trader can buy \$100 in CDO's, and repo the CDO's to get back \$100, less interest.
- D. The trader can buy \$100 in CDO's, and repo the CDO's to get back \$60, plus interest.

Answer: B

Explanation:

* Identify the transaction details:

* Initial value of CDOs = \$100

* Haircut = 20%

* Repo transaction:

* With a 20% haircut, the trader can use the CDOs to obtain 80% of their value in cash:

Cash obtained = $100 \times (10.20) = 80$

* Explanation:

* The trader buys \$100 worth of CDOs and then uses these CDOs in a repo transaction to get back \$80 (less interest). This fully utilizes the leverage provided by the repo transaction under the specified conditions.

References:

* This explanation aligns with standard financial practices for repo transactions and the leverage principles outlined in the document .

NEW QUESTION # 346

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