FINAL EXAMINATION

December 2025

P–20B(RMBI)
Syllabus 2022

RISK MANAGEMENT IN BANKING AND INSURANCE

Time Allowed: 3 Hours | Full Marks: 100

The figures in the margin on the right side indicate full marks.
All workings should from part of the answer.
Answer Question No. 1 *and* any five *from* Question No. 2, 3, 4, 5, 6, 7 *and* 8.

Section-A

Answer Question No. 1 which is compulsory.

1. (a) **Choose the correct answer from the given four alternatives:** 2×10=20

(i) What is a fundamental principle for sound liquidity risk management as per the Basel Committee?

(A) Banks are responsible for managing liquidity risk and maintaining sufficient liquid assets.

(B) Supervisors like RBI is solely responsible for assessing a Bank's Liquidity.

(C) A Bank should only rely on unsecured funding sources to meet obligations.

(D) Liquidity risk is not a concern, if the bank has profitable assets.

(ii) Which type of off-balance sheet risk is directly related to the possibility of a borrower failing to meet their obligations?

(A) Operational Risk

(B) Market Risk

(C) Reputational Risk

(D) Credit Risk

(iii) The principle of indemnity is generally not applicable to _________.

(A) Property Insurance

(B) Marine Insurance

(C) Life Insurance

(D) Fire Insurance

(iv) What is the primary goal of underwriting in health insurance?

(A) To guarantee high investment returns

(B) To assess and price the risk of potential policyholders

(C) To provide Micro Insurance Products

(D) To manage Company administration

(v) What is the primary process by which insurance companies evaluate and select individual risks to be insured, deciding whether to accept them and at what premium?
(A) Risk Transfer
(B) Underwriting
(C) Diversification
(D) Risk Avoidance

(vi) Risk and Return have _________ relation.
(A) Indirect
(B) Direct
(C) Neutral
(D) Negative

(vii) Which of the following risks are addressed by Asset Liability Management?
(A) Market Risk
(B) Liquidity Risk
(C) Interest Rate Risk
(D) All of the above

(viii) The price of a forward or futures contract_________.
(A) is Zero at the initiation of a Contract
(B) is equal to Spot Price at expiration
(C) remains same throughout the contract period
(D) differs from each other

(ix) What is the primary role of an insurance intermediary?
(A) To assess customer risk and set premium rates of different policies
(B) To advise customers, act as an agent in buying and selling insurance contracts
(C) To manage the investments of collected insurance premiums
(D) To process and settle claims directly with the insured

(x) Which of the following principles is generally NOT applicable to life insurance?
(A) Principle of Utmost Good Faith
(B) Principle of Insurable Interest
(C) Principle of Indemnity
(D) Principle of Subrogation

(b) **Based on the following case study, you are required to answer the question nos. (xi) to (xv):** 2x5=10

Banks fail due to liquidity risk, when they can't meet their short-term financial obligations because they lack readily available cash or assets convertible to cash. This often stems from funding long-term assets with short-term liabilities, leading to an asset-liability mismatch. Reasons for failure include sudden deposit withdrawals (a "bank run"), poor risk management, reliance on unstable funding sources, or a loss of market confidence.

Liquidity is a bank's capacity to fund increase in assets and meet both expected and unexpected cash and collateral obligations at reasonable cost and without incurring unacceptable losses. Liquidity Risk for banks mainly manifests on account of the following:

(i) Funding Liquidity Risk
(ii) Market Liquidity Risk

The Basel Committee on Banking Supervision (BCBS) published "Principles for Sound Liquidity Risk Management and Supervision" in September, 2008. The broad principles for sound liquidity risk management by banks cover the following areas:

I. Fundamental principles for the management and supervision of liquidity risk
II. Governance of liquidity risk management
III. Measurement and management of liquidity risk
IV. Public disclosure

The organisational set up for liquidity risk management should be as under:

- The Board of Directors (BoD)
- The Risk Management Committee
- The Asset-Liability Management Committee (ALCO)
- The Asset Liability Management (ALM) Support Group

In this situation, choose the correct option from the four alternatives given:

(xi) The BoD should have the overall responsibility for management of __________.
(A) Credit Risk
(B) Interest Risk
(C) Liquidity Risk
(D) Market Risk

(xii) The Risk Management Committee reports to the __________.
(A) Managing Director
(B) Board of Directors
(C) Chief Executive Officer
(D) Chairman

(xiii) The Asset Liability Management Committee consists of ________.

(A) Top Management of the Bank

(B) Treasury Management of the Bank

(C) Operations Management of the Bank

(D) All Committees of the Bank

(xiv) The ALM process rests on ________ pillars.

(A) Two

(B) Three

(C) Four

(D) Difficult to say

(xv) How many time buckets in ALM Statement to be submitted by the banks to RBI?

(A) Five

(B) Six

(C) Seven

(D) Eight

Section-B

Answer *any five* Questions from Question No. 2 to Question No. 8.

Each question carries 14 marks. 14×5=70

2. (a) Describe how Risk Assessment and Measurement differ from Risk Control and Monitoring in Risk Management Process. 7

(b) Explain how to measure the Interest Rate Risk in the Banking Sector. 7

3. (a) Alpha Bank Ltd. is grappling with a rising portfolio of stressed assets. The board of directors has decided to implement a policy for the sale of these assets in compliance with RBI guidelines to enhance transparency and maximize value.

Explain the key RBI directives regarding the identification of assets for sale and the process for inviting bids that Alpha Bank Ltd. must incorporate into its policy to ensure transparency and better price discovery. 7

(b) Explain any four common warning signs which indicate that a company may be approaching insolvency or is at risk of going bankrupt. Also explain three distinct strategic actions that a company's management can undertake to reduce its insolvency risk, when facing financial distress. 7

4. (a) For the purpose of operational risk management, banks are required to map their business lines activities as per the New Capital Adequacy Framework. Explain seven key principles to be followed by the banks for business line mapping. 7

(b) Sound Bank provided following information about its NPA account as on 31st March 2025.

Total loans ₹40,000 Crores.

Standard Accounts ₹38,000 Crores including Direct Agriculture and SME loans of ₹10,000 Crores.

Sub-standard ₹800 Crores out of which unsecured Sub-standard ₹200 Crores.

Doubtful up to 1 Year ₹800 Crores, Doubtful above 1 year up to 3 years ₹200 Crores, Doubtful above 3 Years ₹120 Crores and Loss Accounts ₹80 Crores.

All doubtful loans are fully secured.

Based on the above information, calculate the following: 7

(i) Provision on standard accounts

(ii) The amount of provision on sub-standard loan accounts

(iii) The amount of provision on doubtful loan accounts

(iv) The amount of total provision on NPA loan

5. (a) The Modern Bank has furnished the following data as on 31st March, 2025:

	(₹)
<u>The Risk Weighted Assets (RWAs) for</u>:	
Credit and Operational Risks	10,000 crore
Market Risk	4,000 crore
<u>Tier –I Capital</u>:	
Paid up Capital	100 crore
Free Reserves	300 crore
Perpetual Non-cumulative Preference Shares	400 crore
<u>Tier-II Capital</u>:	
Provisions and Contingencies Reserves	200 crore
Revaluation Reserve	300 crore
Subordinated Debt	300 crore

Based on the above information, compute the following: 7

(i) Total capital

(ii) Capital Adequacy Ratio (CAR)

(iii) Minimum capital required to support credit, operational and market risks.

(b) The Insurance Regulatory and Development Authority of India (IRDAI) is the apex body responsible for regulating and developing the insurance sector in India. One of its primary objectives is to protect the interest of the policyholders. In this context, explain any seven key functions performed by IRDAI. 7

6. (a) Corporate agents, acting as insurance intermediaries, are subject to specific IRDAI regulations regarding their remuneration and record-keeping obligations to ensure operational transparency and compliance.

(i) Explain the regulations that govern the payment of remuneration by an insurer to a corporate agent for soliciting insurance business.

(ii) List any four key records which are required to be maintained by a corporate agent and state the minimum period for which these records must be preserved. 7

(b) The Central Government Employees and Pensioners Health Insurance Scheme provide unique advantages as compared to many other standard health insurance plans available in the market. Explain any seven significant benefits provided to the members under this plan. 7

7. (a) Section 64V of the Insurance Act, 1938, prescribes the methodology for valuing the assets and liabilities of an insurer to ascertain compliance with solvency margin requirements. State the general principles for the valuation of an insurer's assets and liabilities. 7

(b) Captive insurance is a risk financing tool used by corporations to manage their own risks. In this context, answer the following: 7

(i) Define a 'Captive Insurer'.

(ii) Explain three primary objectives or reasons why a parent company might choose to establish a captive.

(iii) Distinguish between a captive insurer and a mutual insurance company, focusing on the nature of ownership, control, and capital investment by the insureds.

8. (a) M/s XYZ Bank's Branch is having "7 NPA" Accounts as mentioned below. The outstanding and security available to each account is as on 31.03.2025.

(₹ in Lakhs)

Account No.	**Outstandings in the A/c**	**Security Available**	**NPA Date**
A1	120	40	30.09.2024
A2	100	60	30.07.2022
A3	160	80	30.06.2023
A4	120	100	31.08.2024
A5	150	150	31.07.2022
A6	160	0	31.10.2023
A7	200	120	30.08.2022

Based on the above information, answer the following questions: 7

(i) What is the provision required against account A1?

(ii) What is the provision required against account A2?

(iii) What is the provision required against account A3?

(iv) What is the provision required against account A4?

(v) What is the provision required against account A5?

(vi) What is the provision required against account A6?

(vii) What is the provision required against account A7?

(b) Rampant malpractices are bleeding public sector insurance companies, and they need to restructure their activities to bring about a change in the sector. Claims ratio is as high as 150 percent and there are too many malpractices in the health sector.

The structural inefficiencies are hampering the development of the sector. Insurers need to develop a framework for collecting statistics and databases, develop comprehensive products which are transparent and user-friendly. Health insurance should be made mandatory for all jobs and employees should be encouraged to go in for the Central Government Health Schemes (CGHS) as well as policies provided by Insurance Companies.

The health care sector is estimated at ₹ 80,000 crores and is expected to grow by ₹ 10,000 crores every year. Expenditure on health insurance is expected to touch six per cent of household income, up from the current two per cent. Government spending accounts for less than 25 per cent of expenditure on health, while in developed countries the figure is in the range of 40 to 60 per cent. Although the insurable population is placed at two million, the potential market is placed at 315 million people. Insurance companies are keen to resolve the stalemate, as they do not make money from health insurance. Another key area where business is impacted is in mergers and acquisitions.

A survey on health insurance was carried out and nearly 38 per cent of respondents opined that corruption could impact the valuation of a company thereby denying shareholders of a fair price. Moreover, this could also make it difficult for them to find a suitable business partner, thereby seriously impacting the growth prospects of the business.

Based on the above information, answer the following questions: 7

a) What are the ethical aspects of claims management, particularly in the case of health insurance?

b) What is the procedure followed by the insurance companies in cases of close proximity claims?
