Questions

Question 1

Which statement is true in the definition of a financial liability?

a) The key component to the definition is that it is based on a written contract.
b) It includes a contractual obligation to deliver cash or other financial asset.
c) It includes instruments that economically obligate one entity to deliver cash or other financial asset to another entity.
d) It does not include instruments that can be settled only using the entity's own equity shares.

Question 2

Which of the following would preclude the classification of an instrument as equity?

a) The entity's ability to make distributions
b) The entity's history of making distributions in prior years
c) Cash payments are not at the discretion of the entity
d) The liquidation ranking (for example, preferred share versus ordinary share)

Question 3

Which instrument would be classified as equity under IFRS?

a) A preferred share that is redeemable only if there is a change in control of the entity
b) A warrant where the issuer can decide to settle either in cash or by delivering own shares
c) A warrant giving the counterparty a right to acquire a fixed number of the entity's shares for a fixed amount of cash
d) A contract where the amount of cash that will be delivered is based on changes in the market price of the entity's own equity

Question 4

A company has issued non-cumulative, non-redeemable, 5% preference shares where the payment of the dividend is solely at the discretion of the board of directors. How should the instrument be classified?

a) As equity, because the shares are non-redeemable and dividends are solely at the issuer's discretion
b) It depends on the legal form of the instrument.
c) As a liability, because of the stated dividend percentage and the intention of the company to pay
d) As mezzanine or temporary equity, because the preference shares have characteristics of both a liability and equity

Question 5

Which of the following is the best example of a “compound” instrument (that is, has both a liability component and an equity component) based on the facts provided?

a) A non-redeemable preference share that converts into a fixed number of equity shares anytime at the option of the holder
b) A preference share that is redeemable for cash in ten years and pays discretionary dividends
c) A convertible bond that may be converted into a variable number of equity shares in three years and has cumulative mandatory coupons
d) Not applicable − instruments should not be split into different components.

Question 6

A puttable instrument is one that requires the issuer to repurchase or redeem the instrument for cash or other financial asset on exercise of the put. The “puttables amendment” was issued in 2008. Which of the following statements is true about the amendment?

a) It is an exception, whereby all puttable instruments may be classified as equity.
b) It requires the put to be accounted for as a derivative and the rest of the instrument (that is, the share) to be classified as equity.
c) The puttable instrument can be classified in equity if the issuer is only required to redeem the instrument based on a contingent event that is very remote.
d) One of the criteria for a puttable instrument to be classified in equity is that it is the most subordinate instrument.

Question 7

When evaluating a bond that is convertible into equity shares, which of the following features would result in the conversion option’s being classified as equity?

a) The convertible bond is denominated in a foreign currency.
b) An adjustment is made to the number of shares converted that entitles the instrument holder to additional benefits over that of the shareholder.
c) Cash settlement alternatives at the discretion of either the issuer or the holder
d) Gross physical settlement for a fixed amount of cash in exchange for a fixed amount of shares (that is, considered to be fixed for fixed)

Question 8

On December 1, 2011, an entity enters into a contract to purchase 10 million shares of its common stock after one year at C2 per share. The contract can only be settled “gross” in shares (physical delivery) in exchange for a fixed amount of cash (C2 per share). Which statement describes the most appropriate accounting?

a) Liability for the present value of the redemption amount (that is, the proceeds to be paid on settlement), with the offsetting entry to equity
b) Derivative based on the fair value of the forward contract
c) Equity only
d) Liability only

Question 9

Other than financial liabilities measured at fair value through profit or loss, how are financial liabilities subsequently measured under IFRS?

a) The amount of undiscounted cash that would be required to settle the obligation at the reporting date
b) Amortized cost using the effective interest rate method
c) Amortized cost using the stated interest rate of the debt
d) Either fair value or amortized cost at the choice of the issuer

Question 10

Where should interest payments on a financial liability be recognized?

a) Equity
b) Profit or loss
c) It is management's policy choice.
d) It depends on the facts and circumstances (for example, whether the instrument is subsequently convertible).