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International Financial Reporting Standards for Compensation Professionals Exam

WorldatWork T7

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QUESTION NO: 1

What are the usual and customary costs that a company incurs to support its main business called?

A. Operating expenses

B. Current liabilities

C. Current debt

D. Total expenses

ANSWER: A

Explanation:

Operating expenses are the usual and customary costs incurred in running and supporting a company's principal business activities. They include recurring costs needed to operate the business, such as employee compensation, rent, utilities, marketing, insurance, professional services, and administrative costs. In financial reporting, these expenses are recognized in profit or loss in the periods in which the related goods or services are consumed. Their purpose is to support the entity's ongoing revenue-generating operations rather than to acquire or construct a long-term asset. For compensation professionals reviewing financial statements, employee pay, benefits, payroll taxes, and many human-resources-related costs will commonly be included within operating expenses or within a functional expense category such as selling, general, and administrative expenses. IAS 1 requires entities to present an analysis of expenses recognized in profit or loss using either their nature or function, helping users understand the costs of operating the business. See IFRS Foundation's IAS 1 overview and the SEC EDGAR company-filings database for examples of how operating expenses are reported in practice.

QUESTION NO: 2

Which of the following should be used when discounting a benefit in order to determine the present value of the defined benefit obligation and the current service cost?

A. Fair value

B. Time value of money

C. Net present value

D. The corporate vision

E. A discount rate based on market yields on high-quality corporate bonds

ANSWER: E

Explanation:

A discount rate based on market yields on high-quality corporate bonds should be used to measure the present value of a defined benefit obligation and the related current service cost under IAS 19. The rate reflects the time value of money applicable at the reporting date; it is not a rate based on the plan's expected asset returns or the employer's particular funding position. IAS 19 requires the corporate-bond yields to be denominated in the same currency as the benefits and to have terms consistent with the estimated timing of benefit payments. Where there is no deep market in high-quality corporate bonds in the relevant currency, market yields on government bonds must be used instead. Applying this rate to projected benefit cash flows produces the present-value measurement used in the defined benefit accounting model, including the current service cost recognized for employee service in the period. IAS 19 also emphasizes that the discount rate reflects the time value of money, but the technically required input is the specified market-yield-based discount rate. See IFRS Foundation: IAS 19 Employee Benefits and Deloitte IAS Plus: IAS 19 summary.

QUESTION NO: 3

What is a constructive obligation?

A. When a company recognizes the expected cost of profit-sharing and bonus payments

B. When a company has no realistic alternative but to make payments

C. When a change in the company’s informal practices would cause unacceptable damage to its relationship with employees

D. The required accounting entry for liabilities or accrued expenses or cash paid

ANSWER: C

Explanation:

When a change in the company’s informal practices would cause unacceptable damage to its relationship with employees is correct because a constructive obligation can arise from an entity’s established conduct even when no contractual or legal requirement exists. In the context of profit-sharing and bonus plans, IAS 19 recognizes that an employer’s consistent informal practice may create a valid expectation among employees that payments will be made. If discontinuing or changing that practice would unacceptably harm the employer-employee relationship, the entity is treated as having a constructive obligation to make the payment. The obligation is therefore based on the practical effect of the entity’s past actions and the expectations those actions have created, rather than solely on a written plan, contract, or statute. Once that constructive obligation exists, the expected cost is recognized as an employee-benefit expense and liability when the applicable IAS 19 recognition conditions are met. This treatment ensures that financial statements faithfully reflect obligations created through an employer’s customary compensation practices. See the IAS 19 overview published by the IFRS Foundation at IAS 19 Employee Benefits and the standard text’s discussion of profit-sharing and bonus plans at IAS 19—Employee Benefits.

QUESTION NO: 4

Which fundamental qualitative characteristics make accounting information useful for decision-making?

A. Relevance and faithful representation

B. Cost and materiality

C. Assets and liability

D. Income and expenses

ANSWER: A

Explanation:

Relevance and faithful representation are the two fundamental qualitative characteristics in the IFRS Conceptual Framework. Information is relevant when it is capable of making a difference to users’ economic decisions, including by having predictive value, confirmatory value, or both. In a compensation context, relevant financial information can help users evaluate performance measures, assess the financial effects of awards, and make informed decisions based on the entity’s reported results.

Faithful representation means that financial information depicts the economic substance of the underlying phenomenon as completely, neutrally, and free from error as possible. It does not require absolute perfection; rather, it requires an appropriate, unbiased and sufficiently complete portrayal supported by sound estimates and disclosures where measurement uncertainty exists. Together, these characteristics ensure information is both decision-useful and a credible depiction of the transactions or events it reports. The IFRS Foundation’s Conceptual Framework identifies these as the fundamental characteristics, while comparability, verifiability, timeliness and understandability enhance useful information. See the IFRS Conceptual Framework for Financial Reporting and the IFRS Foundation Conceptual Framework project page.

QUESTION NO: 5

Recognition of revenue when earned and the matching of expenses when incurred describes which of the following practices?

A. Business accounting

B. Cash basis accounting

C. IASB accounting

D. Accrual accounting

ANSWER: D

Explanation:

Accrual accounting is the practice of recognizing the effects of transactions when the underlying economic events occur, rather than waiting until cash is received or paid. Revenue is therefore recorded when it is earned—when the entity has satisfied the relevant performance obligation or otherwise obtained the right to consideration under the applicable requirements. Expenses are recognized in the period in which resources are consumed or obligations are incurred, so that reported profit reflects the economic activity of that reporting period.

This approach provides a more faithful and useful picture of an organization's financial performance and financial position because it links income and related costs to the periods in which they arise. The IFRS Conceptual Framework identifies accrual accounting as depicting the effects of transactions and other events in the periods in which those effects occur, even if cash flows happen in a different period. This distinction is especially important for compensation professionals evaluating financial statements, since items such as bonus accruals, share-based-payment expense, and unpaid payroll costs may be recognized before payment occurs. See the IFRS Conceptual Framework and the IFRS 15 revenue standard overview.

QUESTION NO: 6

Employee benefits provided in exchange for the end of an employee's employment are considered what kind of benefits?

A. Short-term benefits

B. Post-employment benefits

C. Termination benefits

D. Long-term benefits

ANSWER: C

Explanation:

Termination benefits is correct because IAS 19 defines termination benefits as employee benefits provided in exchange for the termination of an employee's employment. This classification applies when an entity can no longer withdraw an offer of those benefits, or when it recognizes costs for a restructuring that is within the scope of IAS 37 and includes payment of termination benefits. The defining feature is that the benefit is provided because the employment relationship ends, rather than being compensation for services an employee will provide in the future. Examples can include payments made when an employer decides to end employment before the normal retirement date, or benefits offered to encourage an employee to accept voluntary redundancy. IAS 19 requires entities to recognize the associated liability and expense at the earlier of the point when the offer can no longer be withdrawn and the point when relevant restructuring costs are recognized. This distinct treatment helps ensure that the financial statements reflect the obligation created by ending employment. See IAS 19's definition and recognition requirements in the IFRS Foundation's IAS 19 overview and the standard text available through IAS 19 Employee Benefits.

QUESTION NO: 7

Level 2 of the conceptual framework of International Accounting Standards Board (IASB) identifies qualitative characteristics of accounting information. These characteristics distinguish more useful information from less useful information.

To what end is this distinction useful?

A. For reporting purposes

B. For business strategy

C. For decision-making purposes

D. For organizational vision

ANSWER: C

Explanation:

For decision-making purposes is correct because the IASB Conceptual Framework defines the objective of general-purpose financial reporting as providing financial information that is useful to existing and potential investors, lenders, and other creditors when they make decisions about providing resources to an entity. Those decisions include buying, selling, or holding equity and debt instruments, as well as providing or settling loans and other forms of credit.

The qualitative characteristics at this level of the framework identify what makes reported financial information useful in serving that objective. Relevance and faithful representation are the fundamental qualitative characteristics: information is relevant when it can make a difference to a resource-provider's decision, including through predictive or confirmatory value, and it faithfully represents the economic phenomena it purports to depict. Comparability, verifiability, timeliness, and understandability enhance the usefulness of information when applicable. Thus, the distinction between more useful and less useful accounting information is directly tied to improving informed economic decision-making by users of financial statements. This connection is set out in the IASB's Conceptual Framework for Financial Reporting and summarized in the IFRS Foundation's Conceptual Framework publication.

QUESTION NO: 8

The profit-sharing plan of Company ABC requires the company pay a specified proportion of its profit for the year to employees who serve throughout the year. If no employees leave during the year, the total profit-sharing payments for the year will be 3% of profit. The company estimates that staff turnover will reduce the payments to 2.5% of profit. What does Company ABC recognize as a liability and an expense?

A. 0.5% of profit

B. 2.5% of profit

C. 3% of profit

D. 5.5% of profit

ANSWER: B

Explanation:

2.5% of profit is the amount Company ABC recognizes as both a liability and an expense. IAS 19 treats profit-sharing and bonus arrangements as short-term employee benefits when they are expected to be settled wholly before 12 months after the end of the reporting period in which employees provide the related service. The entity recognizes the expected cost of those payments when it has a present legal or constructive obligation resulting from past service and the obligation can be estimated reliably.

Here, eligibility depends on employees serving throughout the year. Although the contractual maximum is 3% of profit if every employee remains employed, ABC expects turnover to reduce the amount ultimately payable. Consequently, the best estimate of the obligation at the reporting date is the expected payment of 2.5% of profit. The expense reflects employee service received during the year, while the corresponding liability represents the amount expected to be paid under the plan. This application of an expected-payment estimate ensures the recognized amount reflects the plan's service condition and management's current, supportable turnover estimate. See the IFRS Foundation's IAS 19 overview and Deloitte's IAS 19 summary.

QUESTION NO: 9

What are the main equity categories in a statement of stockholders' equity?

A. Retained earnings and treasury stock

B. Investing activities and financing activities

C. Operating revenues and noncurrent assets

D. Revenue items and owners' equity

ANSWER: A

Explanation:

Retained earnings and treasury stock is correct. A statement of stockholders' equity reconciles changes in the equity interests attributable to owners during the reporting period. Retained earnings represents the cumulative profits and losses that have been retained in the business rather than distributed to shareholders as dividends. It is therefore a central measure of the portion of equity generated through the entity's operating performance over time.

Treasury stock represents the company's own shares that it has repurchased and continues to hold. These shares are presented as a deduction from total equity, rather than as an asset, because an entity cannot hold an ownership interest in itself that creates an economic resource. Movements in retained earnings and treasury stock are consequently important disclosures in explaining how shareholders' equity changes from one reporting date to the next. Under IAS 1, an entity presents a reconciliation for each component of equity, including profit or loss, other comprehensive income, owner contributions, and distributions. See IAS 1—Presentation of Financial Statements and the IAS 1 standard text.

QUESTION NO: 10

Company XYZ grants equity-settled share options with a three-year service condition. At the end of the first year, the company determines that several employees are no longer expected to complete the required service period. What is the appropriate accounting treatment?

A. Continue recognizing expense for all options originally granted

B. Revise the cumulative expense to reflect the number of options expected to vest

C. Remeasure the options at current fair value and recognize the increase in equity

D. Recognize the entire remaining expense immediately

ANSWER: B

Explanation:

Revise the cumulative expense to reflect the number of options expected to vest is correct. A service condition is not included in the grant-date fair value of an equity-settled award. Instead, IFRS 2 requires the entity to recognize expense for awards expected to vest and to update that estimate at each reporting date. If fewer employees are expected to complete the required service period, Company XYZ reduces the cumulative compensation expense recognized to reflect the revised estimate. At the vesting date, the cumulative expense is based on the number of awards that actually vested, except where a market condition is involved. See the IFRS Foundation's IFRS 2 Share-based Payment overview.

QUESTION NO: 11

IAS 19 classifies employee benefits into four main categories. Which of the following best represent those categories?

A. Wages, short-term benefits, long-term benefits, termination benefits

B. Wages, profit-sharing, bonuses, non-monetary bonuses

C. Short-term benefits, post-employment benefits, long-term benefits, termination benefits

D. Wages, short-term benefits, bonuses, termination benefits

ANSWER: C

Explanation:

The correct classification is **Short-term benefits, post-employment benefits, long-term benefits, termination benefits**. IAS 19, *Employee Benefits*, groups benefits according to their nature and the timing or circumstances in which the employer's obligation is settled. Short-term employee benefits are expected to be settled wholly within 12 months after the end of the annual reporting period in which employees provide the related service; examples include salaries, wages, paid annual leave, and short-term bonuses. Post-employment benefits are payable after employment ends and include retirement and other post-employment arrangements. Other long-term employee benefits encompass benefits that do not fall into the preceding categories and are not expected to be settled wholly within that 12-month period, such as long-service leave. Termination benefits arise when an entity ends employment before the normal retirement date or when an employee accepts an offer in exchange for terminating employment. These four categories provide the IAS 19 framework for determining the relevant recognition, measurement, and disclosure requirements for employee-benefit obligations. See the IFRS Foundation's IAS 19 Employee Benefits standard page and the IAS Plus IAS 19 summary.