# Investment in Debt and Equity Securities

## Types of securities

| Characteristics | Debt securities | | Equity securities | |
|---|---|---|---|---|
| **Instruments** | Bonds | | Share capital | |
| **Relationship** | Creditor | | Owner | |
| **Returns** | Interest revenue<br>Capital gain | | Dividend revenue<br>Capital gain | |
| **Classification** | (1) Trading [ST]<br>(2) Available-for-sale [ST or LT]<br>(3) Held-to-maturity [ST or LT] | No influence \| passive investment | (1) Trading [ST]<br>(2) Available-for-sale [ST or LT] | No influence \| passive investment |
| | | | (3) Joint venture [LT] | Joint control |
| | | | (4) Associate [LT] | Significant influence 20%-50% ownership |
| | | | (5) Subsidiary [LT] | Control >50% ownership |

## CLASSIFICATION #1: Held-to-maturity securities

Held-to-maturity securities are ***debt securities*** a company intends and is able to hold until maturity

--> Intent and Ability

Classification: Current VS Noncurrent

- They are reported in current assets if their maturity dates are within one year or the operating cycle, whichever is longer.
- HTM securities are reported in long-term assets when the maturity dates extend beyond one year or the operating cycle, whichever is longer.

All HTM securities are recorded **at cost when purchased**, and **interest revenue is recorded when earned**.

The interest revenue is determined under the "***effective interest amortization***" method

The portfolio of HTM securities is reported at ***amortized cost*** on the **statement of financial position** as part of the assets.

Example:

| | | | | | |
|---|---|---|---|---|---|
| Par | 1,000,000 | | Issue date | Jan. 1, 20X1 | |
| Stated i | 5% | per year | Due date | Dec. 31, 20X2 | |
| Period | Quarterly | | Life | 2 | years |
| Market i | 4% | per year | | | |

Investment in Bond -- Price Calculation

[N=8, I=1%, PV=?, PMT=12,500,FV=1,000,000] ฿1,019,129

**Effective Interest Amortization Method**

| Interest Receipt Period | Book Value of Investment in Bonds at the Beginning of the period | Effective Interest Revenue = BV x MKTi x Time | Cash Interest Receipt = Par x STATEDi x Time | Discount/ Premium Amortization | Unamortized Discount/ Premium | Book Value of Investment in Bonds at the End of the period AMORTIZED COST |
|---|---|---|---|---|---|---|
| 0 | | | | | 19,129 | 1,019,129 |
| 1 | 1,019,129 | **10,191** | 12,500 | 2,309 | 16,820 | 1,016,820 |
| 2 | 1,016,820 | **10,168** | 12,500 | 2,332 | 14,489 | 1,014,489 |
| 3 | 1,014,489 | **10,145** | 12,500 | 2,355 | 12,134 | 1,012,134 |
| 4 | 1,012,134 | **10,121** | 12,500 | 2,379 | 9,755 | **1,009,755** |
| 5 | 1,009,755 | 10,098 | 12,500 | 2,402 | 7,352 | 1,007,352 |
| 6 | 1,007,352 | 10,074 | 12,500 | 2,426 | 4,926 | 1,004,926 |
| 7 | 1,004,926 | 10,049 | 12,500 | 2,451 | 2,475 | 1,002,475 |
| 8 | 1,002,475 | 10,025 | 12,500 | 2,475 | 0 | 1,000,000 |

Prepare journal entries related to investment in held-to-maturity securities.

| Date | General Journal | Debit | Credit |
|---|---|---|---|
| Jan. 1, 20X1 | Dr. Investment in HTM (A+) | 1,019,129 | |
| | Cr. Cash (A-) | | 1,019,129 |
| | Acquired investment in bonds at a price of ฿1,019,129. | | |
| Mar. 31, 20X1 | Dr. Cash (A+) | 12,500 | |
| | Cr. Interest revenue (REV+, E+) | | 10,191 |
| | Investment in HTM (A-) | | 2,309 |
| | Recorded the interest revenue under effective interest method. | | |
| | ...... n = 8 | | |
| Dec. 31, 20X2 | Dr. Cash (A+) | 1,000,000 | |
| | Cr. Investment in HTM (A-) | | 1,000,000 |
| | Recorded the maturity of bonds. | | |

Prepare partial statement of financial position and statement of comprehensive income for the year 20X1.

**COMPANY A**
**STATEMENT OF FINANCIAL POSITION (PARTIAL)**
**AS AT DECEMBER 31, 20X1**
**(IN BAHT)**

| | |
|---|---|
| ASSETS | |
| CURRENT ASSETS | |
| **Investment in HTM, at amortized cost** | **1,009,755** |
| NONCURRENT ASSETS | |
| **Investment in HTM, at amortized cost** | **xxx** |
| LIABILITIES | |
| EQUITY | |

**COMPANY A**
**STATEMENT OF COMPREHENSIVE INCOME (PARTIAL)**
**FOR THE YEAR ENDED DECEMBER 31, 20X1**
**(IN BAHT)**

| | |
|---|---|
| REVENUE | |
| **Interest revenue** | **40,626** |
| EXPENSES | |
| GAINS/LOSSES | |
| PROFIT FOR THE YEAR | |
| OTHER COMPREHENSIVE INCOME | |
| TOTAL COMPREHENSIVE INCOME | |

**CLASSIFICATION #2: Trading securities**

Trading securities are **<u>debt and equity securities</u>** that the company intends to **<u>actively manage and trade for profit.</u>**

Frequent purchases and sales are expected and are made to earn profits on short-term price changes.

The entire portfolio of trading securities is reported at its ***market value (fair value)*** ; this requires a market adjustment from the cost of the portfolio.

>> The term portfolio refers to a group of securities.

Any unrealized gain (or loss) from a change in the market value of the portfolio of trading securities is reported on the Statement of Comprehensive Income. It will affect the ***<u>profit for the year</u>*** (net income).

<u>Example:</u>

On Nov. 1, 20X1, Company A purchased a portfolio of trading securities at a total cost of 11,500 Baht.

| Date | General Journal | Debit | Credit |
|---|---|---|---|
| Nov. 1, 20X1 | **Dr. Investment in TRD (A+)** | **11,500** | |
| | **Cr. Cash (A-)** | | **11,500** |
| | Acquired investment in trading securities at a price of ฿11,500. | | |

Company A's portfolio of trading securities had a total cost of 11,500 Baht and **<u>a market value of 13,000 Baht on Dec. 31, 20X1</u>**, the first year it held trading securities.

The difference between the 11,500 Baht cost and the 13,000 Baht market value reflects a 1,500 Baht gain.

It is an unrealized gain because it is not yet confirmed by actual sales.

The market adjustment for trading securities is recorded with an adjusting entry at the end of each period to equal the difference between the portfolio's cost and its market value.

| Date | General Journal | Debit | Credit |
|---|---|---|---|
| Dec. 31, 20X1 | **Dr. Allowance to adjust investment to market value -- TRD (AdjunctA+, A+)** | **1,500** | |
| | **Cr. Unrealized holding gain -- TRD (REV+, PL+, RE+, E+)** | | **1,500** |
| | To reflect the changes in the market value of trading securities. | | |

Prepare partial statement of financial position and statement of comprehensive income for the year 20X1.

**COMPANY A**
**STATEMENT OF FINANCIAL POSITION (PARTIAL)**
**AS AT DECEMBER 31, 20X1**
**(IN BAHT)**

| | | | |
|---|---|---|---|
| ASSETS | | | |
| CURRENT ASSETS | | | |
| **Investment in trading securities, at market value** | [11,500+1,500] | **13,000** | |
| NONCURRENT ASSETS | | | |
| LIABILITIES | | | |
| EQUITY | | | |

**COMPANY A**
**STATEMENT OF COMPREHENSIVE INCOME (PARTIAL)**
**FOR THE YEAR ENDED DECEMBER 31, 20X1**
**(IN BAHT)**

| | | |
|---|---|---|
| REVENUE | | |
| **Interest\|Dividend revenue** | **xxx** | |
| EXPENSES | | |
| GAINS/LOSSES | | |
| **Unrealized holding gain -- Trading** | **1,500** | |
| **PROFIT FOR THE YEAR** | **PL** | |
| OTHER COMPREHENSIVE INCOME | | |
| TOTAL COMPREHENSIVE INCOME | | |

## CLASSIFICATION #3: Available-for-sale securities

Available-for-sale securities are **debt and equity securities** not classified as trading or held-to-maturity securities.
AFS securities are purchased to yield interest, dividends, or increases in market value (called capital gain).
If the intent is to sell AFS securities within the longer of one year or operating cycle, they are classified as **short-term investments.**
Otherwise, they are classified as **long-term investments.**

As with trading securities, companies adjust the cost of the portfolio of AFS securities to reflect changes in ***market value***. The investment in AFS securities must be presented at its market value on the statement of financial position as part of assets.
Any unrealized gain (or loss) for the portfolio of AFS securities is reported in
(1) **OTHER COMPREHENSIVE INCOME** section of Statement of Comprehensive Income and
(2) **EQUITY** section of the Statement of Financial Position.
--> UNREALIZED HOLDING GAIN|LOSS FROM AFS SECURITIES WILL ***NOT*** AFFECT **PROFIT FOR THE YEAR** (NET INCOME).

**Example:**
The company must record year-end adjusting entry to record the market value of these investments.
Cost and market value of the investments in bonds and shares on Dec. 31, 20X1 are as follows:

| | Cost | Market Value | Unrealized Gain (Loss) |
|---|---|---|---|
| Improv bonds | 30,000 | 29,050 | -950 |
| Intex common stock, 500 shares | 43,000 | 45,500 | 2,500 |
| Total | 73,000 | 74,550 | 1,550 |

| Date | General Journal | Debit | Credit |
|---|---|---|---|
| Nov. 1, 20X1 | **Dr. Investment in AFS (A+)** | **73,000** | |
| | **Cr. Cash (A-)** | | **73,000** |
| | Acquired investment in AFS securities at a price of ฿73,000. | | |
| Dec. 31, 20X1 | **Dr. Allowance to adjust investment to market value -- AFS (AdjunctA+, A+)** | **1,550** | |
| | **Cr. Unrealized holding gain -- AFS (OCI+, E+)** | | **1,550** |
| | To reflect the changes in the market value of AFS securities. | | |

Prepare partial statement of financial position and statement of comprehensive income for the year 20X1.

**COMPANY A**
**STATEMENT OF FINANCIAL POSITION (PARTIAL)**
**AS AT DECEMBER 31, 20X1**
**(IN BAHT)**

| | | |
|---|---|---|
| ASSETS | | |
| CURRENT ASSETS | | |
| **Investment in available-for-sale securities, at market valu** | [73,000 + 1,550] | **74,550** |
| NONCURRENT ASSETS | | |
| **Investment in available-for-sale securities, at market value** | | **xxx** |
| LIABILITIES | | |
| EQUITY | | |
| OCI -- Unrealized holding gain -- AFS securities | | 1,550 |

**COMPANY A**
**STATEMENT OF COMPREHENSIVE INCOME (PARTIAL)**
**FOR THE YEAR ENDED DECEMBER 31, 20X1**
**(IN BAHT)**

| | |
|---|---|
| REVENUE | |
| **Interest|Dividend revenue** | **xxx** |
| EXPENSES | |
| GAINS/LOSSES | |
| **PROFIT FOR THE YEAR = Net income** | **PL** |
| OTHER COMPREHENSIVE INCOME (OCI) | |
| **Net unrealized holding gain|loss -- AFS securities** | **1,550** |
| TOTAL COMPREHENSIVE INCOME | |