

Investments

- as line of business
- idle cash
- purpose
- financial instruments
 - stocks
 - bonds
 - derivatives

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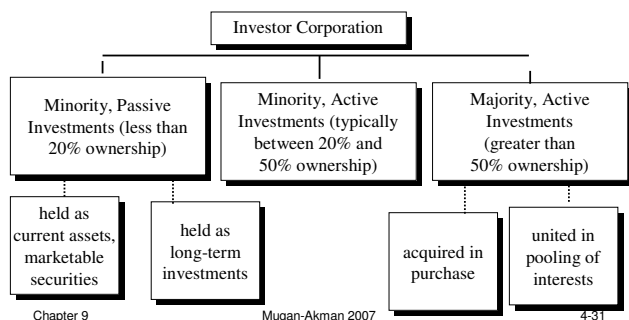
Accounting for Debt and Equity Investments

Debt				
Valuation Method	Short term <i>(trading securities)</i>	Long term		
	Fair Value (Market Value)	Held for resale*	Held to maturity	
		Fair market value	Amortized Cost	
Stocks				
Valuation Method	Short term <i>(trading securities)</i>	Long term		
		Ownership percentage		
	Fair Value (Market Value)	0 –20% of the investee shares*	20-50% of the investee shares	Greater than 50% of the investee shares
	Fair Value (Market Value)	Fair Value (Market Value)	Equity Method	Consolidation

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 * usually classified as available for sale investments

Types of Investments-Stocks

The accounting for investments depends on the purpose of the investment and the percentage of voting stock held.



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Classification of Financial Instruments

- *Financial assets at fair value through profit or loss*: has two subcategories:
 - *Trading securities*: Marketable securities – both equity and debt securities – that are held for short-term profit purposes; and
 - *Derivatives*: financial instruments that do not have a value by themselves but derive their value from the underlying security or asset such as shares, foreign exchange, commodities etc.- except for cash flow hedges that are accounted for similar to trading securities;
- *Held to Maturity*: Debt securities for which a firm has both the positive intent and ability to hold to maturity
- *Available for Sale Securities*: Neither trading securities nor securities held to maturity- usually classified as long term investments.

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Short-Term Investments-Trading Securities

- usually consist of :
 - marketable equity securities (stocks of other companies)
 - savings accounts (time deposits)
 - investment funds
 - precious metals like gold
 - government bonds
 - treasury bills
 - asset securitized bonds
 - private bonds
- Characterized by frequent and active buying and selling with the object of generating profit
- Typically only financial institutions hold trading securities
- Since trading securities are acquired for short-term profit, unrealized gains or losses that result from adjustments to market value pass through the income statement and increase or reduce net income before there is a sale of the securities.

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Accounting for Trading Securities

- Accounting for trading securities has the following key points:
- Recording of purchase,
- Dividends or interest received,
- Valuation at the end of the accounting period, and
- Sale of securities.

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Accounting for Marketable Equity Securities

- record them at the acquisition cost that includes the price of the security plus any brokerage commissions and applicable taxes, and other costs incurred
- record dividend revenue when dividends declared and later when cash is received
- adjust to fair market value at the end of the accounting period-adjusting entry

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Accounting for Marketable Equity Securities

Bizim Bank acquires 1.000 shares of Is Bankasi (C) for TL 150 plus TL 2.000 for taxes and commissions

Date	Account Title and Description	Debit	Credit
13-Jan-07	Trading Securities	152.000	
	Cash		152.000
	Purchase of securities.		

IS Bankasi declares dividends of TL 15.000 on 15 April 2007 to Bizim Bank

Date	Account Title and Description	Debit	Credit
15-Apr-07	Dividends Receivable	15.000	
	Dividend Revenue		15.000
	Recording dividend revenue.		

receives cash for the dividends declared

Date	Account Title and Description	Debit	Credit
15-May-07	Cash	15.000	
	Dividends Receivable		15.000
	Recording cash dividend received.		

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End of the period-example

Assume that no securities are purchased or sold during the second quarter of 2007. At the end of June:

Gross Unrealized Holding Gain	TL 80	ISC TL 10 and VS TL 70
Gross Unrealized Holding Loss	(50)	DG
Net Unrealized Holding Gain (Loss)	TL 30	

Date	Account Title and Description	Debit	Credit
30-Jun-07	Unrealized Holding Loss- DG	50	
	Trading Securities	30	
	Unrealized Holding Gain- VS		70
	Unrealized Holding Gain- ISC		10
	Recording of unrealized holding loss and gain		

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Sale of Trading Securities

Sonsan A.S. sold all DG shares for TL 320 in August 2007

Date	Account Title and Description	Debit	Credit
Aug-07	Cash	320	
	Trading Securities		220
	Gain on Sale of Trading Securities		100
	Realized gain on sale of DG shares.		

Trading Securities			
15-Jan-07	500	31-Mar-07	40
1-Feb-07	300	15-Aug-07	220
15-Feb-07	200	30-Sep-07	10
30-Jun-07	30		
Balance	760		

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Accounting for Marketable Debt Securities

- same as the accounting for marketable equity securities –both are trading securities
- carrying value of these securities will be compared to the market or fair value at the reporting dates
- carrying value = the market value or fair value at the latest reporting date
- unrealized holding gains or losses will be reflected in the income statement

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Available for Sale Securities

- neither as trading securities or held to maturity securities
- held by non-financial companies usually
- both equity and debt securities
- non-derivative financial assets that are initially designated by the management as available for sale (AFS)
- typically tied to a specific cash need
- usually classified as long-term assets
- measured at fair value in the balance sheet
- unlike trading securities; any unrealized holding gains or losses - shown under the owners' equity section with the name "**Unrealized Holding Gains or Losses**"
- realized gain or loss when these securities are sold
- interest or dividend revenues received from AFS securities are reflected in the income statement

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AFS - example

Bala A.S. acquires of shares of Alda A.S. on 17 November 2007 for the purpose of generating funds for its new manufacturing facility. Bala pays TL 400.000 including brokerage fees, taxes and other applicable duties

Date	Account Title and Description	Debit	Credit
17-Nov-07	Available for Sale Securities-Alda	400.000	
	Cash		400.000
	Recording the purchase of share of Alda		

31 December 2007- end of the accounting period-Alda's market value TL 435.000

Date	Account Title and Description	Debit	Credit
31-Dec-07	Available for Sale Securities-Alda	35.000	
	Unrealized Holding Gain or Loss		35.000
	Recording unrealized holding gain		

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AFS- example

3 January 2008, Bala sells the shares of Alda and receives TL 480.000

Date	Account Title and Description	Debit	Credit
3-Jan-08	Cash	480.000	
	Available for Sale Securities-Alda		400.000
	Gain on Sale of securities		80.000
	Recording the realized holding gain		

Date	Account Title and Description	Debit	Credit
3-Jan-08	Unrealized Holding Gain or Loss	35.000	
	Available for Sale Securities-Alda		35.000
	Recording the realized holding gain		

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Comparison - trading and available for sale securities

- both are recorded at acquisition cost
- both are written up or down to market with adjusting entries at the reporting date.
- both give rise to an unrealized holding gain or loss account upon adjustment.
- unrealized holding gain or loss for *trading securities* is charged to revenues –when sold, realized gain or loss is determined by taking the difference between the carrying value and proceeds from the sale
- unrealized holding gain or loss for *available for sale securities* remains on the balance sheet until such assets are sold-when sold, this account must then be closed and the realized gain or loss is computed by comparing the historical cost and proceeds from the sale

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Derivatives as Trading Securities

- financial instruments that derive their value from the underlying security or asset
- value of a derivative changes in response to the change in an underlying variable
- requires a minimal amount of initial investment or no initial investment
- *Options*
- *Futures*
- When derivatives are used as financial instruments they are accounted for similar to trading securities

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Long-term Investments

- investments in
 - stocks
 - bonds
 - long-term receivables and loans

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Long-term Equity Securities Investments

- to receive income in addition to the regular income of the business
- to secure trade ties with the invested companies
- less than 20% ownership
- between 20% and 50%

Equity Method of Accounting for Investments

- 20% and 50% of the voting power - **associate** or an **affiliate**
- significant control - use the **equity method**
- accounts for the failure and success of the investee
- investment increases by the share of net income (or decreases by the share of net loss) of the investee
- dividends received from the associate causes a decrease in the carrying value of the investment

Equity Method - example

Edin AS purchases 30 % of the shares of Burg AS for TL 4.000 in January 2007

Date	Account Title and Description	Debit	Credit
3-Jan-07	Long-term Equity Investments	4.000	
	Cash		4.000
	Purchase of equity investment.		

Burg AS reports net income of TL 2.500

Date	Account Title and Description	Debit	Credit
31-Dec-07	Long-term Equity Investments	750	
	Revenues from Equity Investments		750
	Recording revenue from equity investment.		

30% x 2.500= TL 750