# Unit – III (Investment Account)

**Investment :** An investment is the purchase of goods that are not consumed today but are used in the future to create wealth. In finance, an investment is a monetary asset purchased with the idea that the asset will provide income in the future or will later be sold at a higher price for a profit.

Investment is an asset which generates an income. Individuals, organizations, firms invest money in different types of assets like real estate, bank deposits, securities such as Govt. securities, debentures, bonds, shares etc. to earn some amount of income. Income from investment may be in the form of interest or dividend.

**Types of investment :** From the view point of nature of income, investment may be classified as under ……

1. Fixed income bearing securities : Fixed income bearing securities are those in which the rate of return is fixed. For example: 12% debenture, 11% bond, 8% preference share etc.
2. Variable income bearing securities : Variable income bearing securities are those in which the rate of return is not fixed. It may be vary from year to year depending on the profits of the company.

**Investment Accounting :** Investment accounting means the process of recording transactions relating to each type of security in a separate account in order to make available full information about that type of security.

**Features of investment account :**

1. **Columnar form :** An investment account contains three amount columns on either side Nominal, Capital and Income columns.
2. **Simultaneous recording in three columns :** When investment are purchased or sold, not only the cost price or sale price is recorded in the capital column but also nominal value of investment and accrued interest are also recorded.
3. **Determination of profit or loss on sale :** Profit or loss on sale of investment is ascertained by balancing the capital column. Profit/loss on sale of investment is transferred to Profit and Loss account.
4. **Closing balance :** Closing balance of investment account at the end of the accounting period shows the nominal value, capital value and accrued interest on nominal value in respective columns.
5. **Valuation of current assets :** At the time of annual closing, securities in hand are valued them as current assets and are valued at cost or market price whichever is lower.

**Objectives of Investment account :**

1. **Recording of detailed information :** Primary objective of preparing investment account is to get detailed information of the transactions relating to each type of security.
2. **Determination of value of securities :** Another objective of preparing investment account is to determine the value of each security at the end of the accounting period.
3. **Profit or loss in dealings :** Determination of the profit or loss made on the sale of each security is another objective of preparing investment account.

**Cum-interest :** **Cum interest** is the amount of **interest** accrued in the duration between the last coupon date and the settlement date or transaction date. In this regard, it is to be understood that the closing register date of the coupon is due.

**Ex-interest :** **Ex-interest** is the amount of coupon **interest** between transaction date or settlement date and the next coupon date. In this regard, it is to be understood that the closing register date of the coupon is due.

**Difference between cum-interest and ex-interest :**

1. In case of cum interest quoted price includes the interest accrued up to the date of purchase whereas this is not included in case of ex interest.
2. In case of cum interest nothing is payable for interest accrued in addition to the quoted price whereas it is payable in case of ex interest.
3. In case of cum interest quoted price is more than the actual price of the security whereas in case of ex interest quoted price is the actual price.

**Right share :** Right shares are the shares that are issued by a company for its existing shareholders. A rights issue is a way by which a listed company can raise additional capital. However, instead of going to the public, the company gives its existing shareholders the right to subscribe to newly issued shares in proportion to their existing holdings. The existing shareholders have their right to subscribe to these shares unless some special rights reserve them for some other persons.

**Advantages of the Rights Issue of Shares :**

- The shares are offered to the shareholders at the discounted price to encourage them to purchase the rights issue.
- The company saves a significant amount of money, such as underwriting fees, advertisement cost and so on.
- The control of the company remains in the hands of the existing shareholders. This is because the shares are only issued to those shareholders who on the date of rights issue are the holders of the shares.
- There is an equitable distribution of the shares and the same proportion of the voting rights.

**Disadvantages of the Rights Issue of Shares :**

- The company may not be able to raise more funds and fail to achieve their target. This may happen if the existing shareholders of the company are not too keen to invest more.
- The value of each share may get diluted if there are an increased number of shares issued.
- If a well-established company is going for the rights issue of the shares, then it goes on to create a negative market sentiment. It is assumed that the company is struggling to run its business operations smoothly.

**Bonus share :** Bonus shares are additional shares given to the current shareholders without any additional cost, based upon the number of shares that a shareholder owns. Bonus shares are issued to the shareholders without any additional cost.

**Advantages of bonus share :**

1. There is no need for investors to pay any tax on receiving bonus shares.
2. Issuing bonus shares helps to increase the issued share capital of the company.
3. It takes more money from the cash reserve than issuing dividends does.
4. It is beneficial for the long-term shareholders of the company who want to increase their investment.
5. Bonus shares give positive sign to the market that the company is committed towards long term growth story.
6. Bonus shares increase the outstanding shares which in turn enhances the liquidity of the stock.

**Disadvantages of bonus issues :**

1. Dividends should be paid according to the number of shares increased.
2. Over capitalization may appear due to the issues.
3. It encourages to speculate the stock.

**Inter company investment :** Inter company **investment** occurs when a **company** makes an **investment** in another **company**. It could be through the purchase of shares of a publicly-traded **company** on a public exchange or a privately negotiated deal for a share of a **company** that is not publicly traded.

**Important topics for exam :**

1. Procedure of accounting for investment in Fixed Income bearing securities.(page 3.4)
2. Procedure of accounting for investment in Variable Income bearing securities.(page 3.31)