

CHAPTER 9

Redemption of Debenture

Meaning : Redemption of debentures means repayment of the due amount of debentures to the debenture holders. It may be at par or at premium.

Time of redemption : **(a) At maturity :** when repayment is made at the date of maturity of debentures which is determined at the time of issue of debentures.

(b) Before maturity : If articles of association and terms of issue mentioned in prospectus allows, then a company can redeem its debentures before maturity date.

Redemption methods : **(1) Redemption is Lump-sum :-** When redemption is made at the expiry of a specific period, as per the terms of issue.

(2) Redemption by draw of lots :- In this method a certain proportion of debentures are redeemed each year, the debenture for which repayment is to be made is selected by draw.

(3) Redemption by purchase in open market :- if articles of association of a company authorize, it may purchase its own debentures from open market i.e. stock exchange.

Advantage of this method : 1. When market price of own debentures is low than the redeemable value.

2. Decrease the amount of interest payable to outsiders.

3. if term of issue is provided that debentures are to be redeemed at premium then such premium can be decrease.

Sometimes company can purchase the debentures at more than the redeemable value due to the following reasons :

1. To maintain the solvency ratio.

2. To utilize the surplus money or funds which are lying idle with the company.

3. When rate of interest on debentures is more than the current market rate of interest on debentures in the industry.

4. Redemption by conversion : As per the terms of issue, convertible debentures may be convert into shares or new debentures at the option of debenture holders. This option of conversion is given to the debentureholder within specific period. In this case no need to transfer profit to Debenture Redemption Reserve Account.

Sources of Redemption of debentures.

1. Proceeds from fresh issue of share capital or debenture holders.

2. From accumulated profits.

3. Proceeds from sale of fixed assets.

4. A company may purchases its own debentures out of its surplus funds.

Two terms which are used in the redemption of debentures :

1. Redemption out of capital : when a company not used its reserve or accumulated profit for redemption of its debentures. It is called redemption out of capital. So company using this method are not transfer it profit to DRR A/c. But as per SEBI guidelines it is necessary for a company to transfer 50% amount of nominal value of debentures to be redeemed in DRR A/c before redemption of debentures commence.

March,31	10% Debentures A/c To Debentureholders A/c (Being the amount due to debenture holders)	Dr. 	1,00,000	1,00,000
March,31	Debenture holders A/c To Bank A/c (Being the amount paid to the debenture holder)	Dr. 	1,00,000	1,00,000
March,31	Debenture Redemption Reserve A/c To General Reserve A/c (Being Deb. Red. Reserve A/c closed by transfer to General Reserve)	Dr. 	50,000	50,000

(B) Redemption At Premium : Illustration 2. Z Ltd. Redeemed its 1,00,000 10% Debentures of Rs.10 each at 5% premium on 31st March, 2011.

Z Ltd.

Date	Particulars		Debit ₹	Credit ₹
2011 March, 31	Profit & Loss Appropriation A/c To Debenture Redemption Reserve A/c (Being Profit transfer to DRR A/c)	Dr. 	5,00,000	5,00,000
March,31	10% Debentures A/c Premium on Redemption of Debentures A/c To Debentureholders A/c (Being the amount due to debenture holders)	Dr. Dr. 	1,00,000 50,000	10,50,000
March,31	Debentureholders A/c To Bank A/c (Being the amount to the debenture holders)	Dr. 	10,50,000	10,50,000
March,31	Debenture Redemption Reserve A/c To General Reserve A/c (Being Deb. Red Reserve A/c closed by transfer to General Reserve A/c)	Dr. 	5,00,000	5,00,000

Illust. 3 : Rajesh Export Ltd. has 2,000, 9% Debentures of Rs.100 each due on redemption on 31st March 2011. Debentures redemption reserve has a balance of Rs.30,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.				
Date	Particulars		Debit ₹	Credit ₹
2011 March, 31	Profit & Loss Appropriation A/c To Debenture Redemption Reserve A/c (Being the profit transfer to DRR A/c)	Dr. 	70,000	70,000
March, 31	10% Debentures A/c To Debentureholder a/c (Being the amount due to debenture holders)	Dr. 	2,00,000	2,00,000

March, 31	Debentureholders A/c To Bank A/c (Being the amount paid to the debenture holders)	Dr.	2,00,000	2,00,000
March, 31	Debenture Redemption Reserve A/c To General Reserve A/c (Being Deb. Red Resource A/c closed by transfer General Reserve a/c)	Dr.	1,00,000	1,00,000

Illust. 4 : Rahul Ltd. has 50,000, 9% Debentures of Rs.50 each due on redemption on 31st March 2011. Debentures redemption reserve has a balance of Rs.15,00,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.

Date	Particulars		Debit ₹	Credit ₹
2011 March, 31	Profit & Loss Appropriation A/c To Debenture Redemption Reserve A/c (Being the Profit transfer DR A/c)	Dr.	10,00,000	10,00,000
March, 31	10% Debentures A/c To Debentureholder a/c (Being the amount due to debanture holders)	Dr.	25,00,000	25,00,000
March, 31	Debentureholder A/c To Bank A/c (Being the amount paid to the debenture holders)	Dr.	25,00,000	25,00,000
March, 31	Debenture Redemption Reserve A/c To General Reserve A/c (Being Debenture Redemption Reserve A/c transferred to Gen. Reserved A/c)	Dr.	25,00,000	25,00,000

Note : In this case DRR is Already more than 50% of nominal value of debentures, then it is created upto the 100% of the nominal value of debenture

Illust.5 : Saket Ltd.(an infrastructure co.) has outstanding 10,000, 9% Debentues of Rs.50 each due on redemption on 31st March, 2011. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.

Date	Particulars		Debit ₹	Credit ₹
2011 31st March,	Profit & Loss Appropriation A/c To Debenture Redemption Reserve A/c (Being the profit transferred to DRR A/c)	Dr.	2,50,000	2,50,000
31st March	10% Debentures A/c To Debentureholders A/c	Dr.	5,00,000	5,00,000

31st March	(Being the amount due to debenture holders)	5,00,000	5,00,000
	Debentureholders A/c Dr. To Bank A/c		
31st	(Being the amount paid to the debenture holders)	2,50,000	2,50,000
	Debenture Redemption Reserve A/c Dr, To General Reserve A/c (Being Deb. Red. Res. A/c transferred to Gen. Reserve A/c)		

(Note : The infrastructure Companies are exempted from creating DRR as per SEBI guidelines. However these companies may create DRR at its option.)

Redemption Method : 2 Draw of lots

Illustration 6 : S Ltd. redeemed its Rs.10,000, 8% Debentures out of capital by drawing a Lot on 30 Nov.2011 Journalise.

S Ltd.

Date	Particulars	Debit ₹	Credit ₹
2011 30th Nov.	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the Profit transfered to DRR A/c)	5,000	5,000
30th Nov.	10% Debenture A/c Dr. To Debenture holders A/c (Being the amount due to debenture holders)	10,000	10,000
30th Nov.	Debenture holders A/c Dr. To Bank A/c (Being the amount due to debenture holders)	10,000	10,000

(Note : the DRR Balance will be transferred to General Reserve after all the debentures are redeemed)

Illustration 7 : Y Ltd. redeemed its Rs.20,000, 9% debentures out of profit by drawing of lot on 30th Nov. 2011. Journalise.

Y Ltd.

Date	Particulars	Debit ₹	Credit ₹
2011 30th Nov.	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the Profit transferred to DRR A/c)	20,000	20,000
30th Nov.	10% Debentures A/c Dr. To Debentureholders A/c (Being the Profit transferred to DRR A/c)	20,000	20,000
30th Nov.	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to Debentured)	20,000	20,000

(Note : the DRR Balance will be transferred to General Reserve after all the debentures are redeemed.)

Redemption method 3 : Redemption of Debentures by Conversion : A Company may offer to the debentureholder to convert their debenture into a new class of securities like Equity shares or preference share or new debentures. The debentureholder may accept the offer or not. If debentures are converted.

Calculation of Number of new securities to be issued

= Amount due to debentureholders/Issue Price

Issue Price = Nominal Price + Securities Premium on Issue of New Securities

Or Issue Price = Nominal Price- Discount on Issue of New Securities.

Illustration 8 : 2000, 8% Debenture Rs.100 each issued at par redeemable at 5% premium were converted into equity share of Rs.10 each at par, Journalise.

Solution :

JOURNAL

Date	Particulars	Debit ₹	Credit ₹
	8% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debenturholder A/c (Being the amount due debentureholder)	2,00,000 10,000	2,10,000
	Debentureholders A/c Dr. To Equity Share Capital A/c (Being the conversion of 2,000, 8% Debentures in 21,000 equity share of ₹ 10 issued at par)	2,10,000	2,10,000

Number of Equity shares to be issued : ₹ 2,10,000/10=21,000

Illustration 9 : L Ltd. redeemed 4,000 9% Debentures of ₹ 100 each which were issued at par by converting them into 10% Preference Share of ₹ 10 each issued at a premium of 25% Journalise.

Solution :

L Ltd.

Date	Particulars	Debit ₹	Credit ₹
	8% Debentures A/c Dr. To Debentureholder A/c (Being the amount due debentureholder)	4,00,000	4,00,000
	Debentureholders A/c Dr. 10% Preference Share Capital A/c	4,00,000	3,20,000

	To Equity Share Capital A/c (Being the conversion of 4,000, 9% Debentures in 32,000 equity share of ₹ 10 issued at ₹ 12.50)			80,000
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Number of Preference shares to be issued : ₹ 4,00,000/12.50 = 32,000

Illustration 10. : Jai Ltd. redeemed ₹ 1,80,000, 12% Debentures of ₹ 100 each at 110% by converting them into equity shares of ₹ 100 each, ₹ 90 paid-up Journalise.

Solution

Jai Ltd.

Date	Particulars	Debit ₹	Credit ₹
	8% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholder a/c (Being the amount due debentureholder)	1,80,000 18,000	1,98,000
	Debentureholders A/c Dr. To Equity Share Capital A/c (Being the conversion of 1,800, 12% Debentures in 2200 Equity share of ₹ 10, ₹ 90 paid-up)	1,98,000	1,98,000

Number of Equity shares to be issued : ₹ 1,98,000/90= 2,200 Equity Shares

Illustration 11. : Rashi Ltd. redeemed 5,280, 12% Debentures of ₹ 100 each, at 110% by converting them into equity shares of ₹ 100 each, at 4% discount. Journalise.

Solution

Rashi Ltd.

Date	Particulars	Debit ₹	Credit ₹
	12% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholder A/c (Being the amount due debentureholder)	5,28,000 52,800	5,80,800
	Debentureholders A/c Dr. Discount on issue of shares A/c Dr. To Equity Share Capital A/c (Being the conversion of 5,280, 12% Debentures in 6,050 Equity share of ₹ 100 at ₹ 96.00 each)	5,80,800 24,200	6,05,000

Number of Equity shares to be issued : ₹ 5,80,800/96.00 = 6050 Equity Shares

Illustration : 12 Pass the necessary journal entries for the issue and redemption of

Debentures in the following cases :

(i) 10,000 10% Debentures of ₹ 120 each issued at 5% premium repayable at par.

(ii) 20,000 9% Debentures of ₹ 200 each issued at 20% premium repayable at 30% premium

Date	Particulars	L.F.	Debit ₹	Credit ₹
(i)	Bank A/c Dr. To Debenture Application and Allotment A/c (Being receipt of Application money)		12,60,000	12,60,000
	Debenture Application and Allotment A/c Dr. To 10% Debenture A/c To Securities Premium A/c (Being Issue of 10% Debenture at premium redeemable at par)		12,60,000	12,00,000 60,000
At the time of redem	10% Debenture A/c Dr. To Debentureholder A/c (Being amount due to debentureholder)		12,00,000	12,00,000
	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to debentureholders)		12,00,000	12,00,000
(ii)	Bank A/c Dr. To Debenture Application and Allotment A/c (Being receipt of Application money)		48,00,000	48,00,000
	Debenture Application and Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 9% Debenture A/c To Securities Premium A/c To Premium on Redemption of Debentures A/c (Being Issue of 9% Debenture at premium redeemable at premium)		48,00,000 12,00,000	40,00,000 8,00,000 12,00,000
At the time of redeem	9% Debenture A/c Dr. Premium on Redemption of Debenture A/c Dr. To Debentureholder A/c (Being amount due to debentureholder)		40,00,000 12,00,000	52,00,000
	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to debenture holders)		52,00,000	52,00,000

Conversion of Debentures into shares which are originally issued at a Discount :

When debentures are originally issued at discount, discount on issue of debenture account is debited with the amount of discount, Discount on issue of debenture account is written off during the time period of debenture as as issue date to redemption date.

Note : By the maturity date the discount on issue of debenture account is fully written off from the Profit & Loss A/c.

(a) When conversion done after the maturity of debenture :- The conversion is done with the full amount of debenture the discount on issue of debenture account is fully written off, so discount account is not credited on the date of conversion in maturity of debentures : e.g.

1st April, 2005 X Ltd. issued 20,000, 9% debentures of Rs.10 each at a discount of 10% redeemable at par after 5 years by converting them into equity shares of Rs.10 each issued at a premium of 25% pass journal entries for the redemption of debentures.

Sol :

Date	Particulars	L.F.	Debit ₹	Credit ₹
1.4. 2010	9% Debentures A/c Dr. To Debentures holders A/c (Being amount due to debenture holders on conversion at maturity date)		2,00,000	2,00,000
1.4. 2010	Debenture holders A/c Dr. To Equity Share Capital To Securities Premium A/c (Being amount due on conversion discharge by issue of 16,000 equity shares) 2,00,000/12.5=16,000		2,00,000	1,60,000 40,000

(1) Discount A/c already written off. conversion is done with the full amount of Debentures.

(B) Conversion before Maturity date of redemption of debentures : In this situation the discount on issue of debentures account is not fully written off because conversion is before the due date of the redemption. So the actual amount received on issue of debenture at the time of issue is to be determined and it should be taken as amount due to debenture holders and new equity shares are to be issued for the amount actually received at the time of issue of debentures. If this rule is not applied, the provisional conditions of section 79 of the companies Act 1956 would be violated.

If a company, convert it debentures into equity share before the maturity, then Discount in issue of debentures Account should be credited with the amount if discount which has not yet been written off and Profit & Loss Account should be credited with the amount of discount which has already written off e.g.

On 1st April 2010, X Ltd. issued 50,000, 10% Debentures of Rs.10 each at 4% discount and redeemable at par after 5 year. It offered the debentureholders option to convert their debentures in equity share of Rs.10 each after 31st March, 2012. On 1st April, 2012, 25% of debentureholders accepted & exercised their option. Give necessary journal entries at the time of conversion of debentures.

Date	Particulars	Debit ₹	Credit ₹
1.4. 2010	10% Debentures A/c Dr. To Discount on issue of Deb. A/c To Profit & Loss A/c To Debenture holder's A/c	1,25,000	3,000 2,000 1,20,000

	(Being the amount due to debenture holder's on conversion of debentures)		
1.4. 2012	Debentureholder's A/c Dr. To Equity Share Capital A/c (Being the issue of 12,000 Equity Shares of Rs.10 each at par on conversion of 12,500 10% Debentures)	1,20,000	1,20,000

Note : In the above Illustration discount on issue of debentures account is credited with the amount of discount not written off on the conversion date i.e. total Debenture.

Total No. of Debentures issue = ₹ 50,000

Debentures to be converted 25% of 50,000 = 12,500 debentures of ₹ 10/- each

Total Discount at the time of issue on 12,500 10% Debentures =

$12500 \times 10 = 125000 \times 4/100 = ₹ 5000$, term of Deb.5 years.

Discount written off per year = $5000/5 = ₹ 1,000$

Discount written off of between issue date (1/4/2010) to conversion date (1/4/2012) is two year = $1000 \times 2 = ₹ 2,000$.

Discount not written off $₹ 5,000 - 2,000 = ₹ 3,000$

Discount in issue of Debenture Account should be credited with ₹.3000

Discount in issue of debenture has the debit balance ₹ 3000 on the date of conversion of debentures. so the discount on issue of debenture Account should be credited with ₹ 3000.

Discount on issue of debentures ₹.2000 has been written off by debited the profit and loss account till on conversion of debenture date so Profit & Loss a/c should be credited with ₹.2,000.

Note If there is no information about the date of conversion, it will be assumed that conversion took place before the date of maturity. In this case it is not possible to calculate the amount of discount which has been written off upto date of conversion and which has not written off. It is assumed in this case that no discount has been written off and discount on issue of debenture account should be credited with whole amount of discount e.g.

X Ltd. redeemed its 1,000; 10% Debentures of Rs.100 each which were issued at a discount of 5% by converting them into equity shares of Rs.10 each issued at a Premium of 25% Journalise.

Date	Particulars	Debit ₹	Credit ₹
	10% Debentures A/c Dr. To Discount on issue of debentures A/c To Debentureholders A/c (Being the amount due to debenture holders)	1,00,000	5,000 95,000
	Debenture holders A/c Dr. To Equity Share Capital a/c (7600x10) To Securities Premium A/c (7600x2.5) (Being the issue of 7600 equity shares of Rs.10 each at 12.50 = $95000/12.5 = 7600$)	95,000	76,000 19,000

Note : The provision of Sec 79 of companies Act, 1956 applies only on the issue of shares only. The amount of discount on issue of debentures should be considered for when redemption is made on conversion into share only. If redemption is made on conversion into new class of debenture, then the provision of Sec 79 not violated. The discount on issue of debenture account should not be credited e.g. 2,500, 10% Debentures of ₹ 100 each issued at a discount of 5% and redeemable at par after each 4 years were converted into 14% Debentures of ₹ 10 each issued at par before maturity. Give the necessary journal entries for redemption of debentures

Sol. :

Date	Particulars	Debit ₹	Credit ₹
	10% Debentures A/c Dr. To Debenture holder's A/c (Being the amount due to debenture holders)	2,50,000	2,50,000
	Debentureholder's A/c Dr. To 14% Debentures A/c (Being issue of 25,000; 14% Debentures of ₹ 10 each at par on conversion = 2,50,000/10=25,000 debenturs)	2,50,000	2,50,000

Illustration 13 :- Journalise the following transactions :

- A Ltd. redeemed 5,000, 12% debentures of ₹ 100 each which were issued at a discount of 8% by converted them into equity shares of ₹ 10 each issued at par.
- B Ltd. redeemed 600, 14% debentures of ₹ 10 each which were issued at a discount of 5% by converting them 12% preference shares of ₹ 100 each at a premium of ₹ 25 per share.
- C Ltd. redeemed 1000, 10% Debentures of ₹ 100 each which were issued at a discount of 10% by converting them equity shares of ₹ 50 each, ₹ 45 paid-up.
- D Ltd. redeemed 4000, 12% Debentures of ₹ 100 each which were issued at a discount of 35% by converting them into 8% Debentures ₹100 each issued at par, before the maturity date of debentures.

Sol. :

Date	Particulars	Debit ₹	Credit ₹
(i)	12% Debentures A/c Dr. To Discount on issue of Debentures A/c To Debenture holders A/c (Being the amount due to debentureholders)	5,00,000	40,000 4,60,000
	Debentureholders A/c Dr. To Equity Share Capital A/c (Being amount due to debentureholders on conversion discharged issue of 4,60,000/10 = 46,000 equity shares of ₹ 10 each)	4,60,000	4,60,000
(ii)	14% Debentures A/c Dr.	60,000	

	To Discount on issue of Debentures A/c		3,000
	To Debenture holders A/c		57,000
	(Being the amount due to debentureholders)		
	Debentureholders A/c Dr.	57,000	
	To 12% performance share capital a/c		45,600
	To Securities Premium A/c		11,400
	(Being amount due to debentureholders on conversion discharged by issue of $57000/125=456$ 12% preference shares at a premium of Rs.25 each)		
(iii)	10% Debentures A/c Dr.	1,00,000	
	To Discount on issue of Debentures A/c		10,000
	To Debenture holders A/c		90,000
	(Being the amount due to debentureholders)		
	Debentureholders A/c Dr.	90,000	
	To Equity share capital A/c		90,000
	(Being amount due to debentureholders on conversion discharged by issue of $90,000/45=2000$ Equity shares of ₹ 50 each, ₹ 45 paid-up)		
(iv)	12% Debentures A/c Dr.	4,00,000	
	To Debentureholders A/c		4,00,000
	(Being amount due to debenture holders)		
	Debentureholders A/c Dr.	4,00,000	
	To 8% Debentures		4,00,000
	(Being the amount due to debenture holders on conversion discharged by issue of $4,00,000/10$ 4000,8) Debenture of Rs.100 each at par)		

Note : In the above first three cases nothing is mentioned about the date of issue & date of maturity of debentures. It is assumed that debentures were redeemed before maturity date & discount on issue of debentures A/c credited with the amount of discount allowed at the time of issue. The new shares under Sec. 79 would be issued amount equal to Net amount received from debentureholders at the time of issue of original from debentureholders. Case 4. Sector-79 does not apply on issue of debentures discount A/c not credited in the solution.