

CHAPTER – 10

COMPANY ACCOUNTS-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 in 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 of lots.

Sometimes company purchase's 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.

Sources of Redemption of Debentures

1. Proceeds from fresh issue of Share Capital or Debentures.
2. From accumulated profit.
3. Proceeds from sale of fixed assets.
4. A company may purchase 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 has not used its reserve or accumulated profit for redemption of its debentures, it is called redemption out of capital, So company using this method have not transferred its profit to DRR A/c. But as per Companies Act, 2013 it is necessary for a company to transfer 25% amount of nominal value of debentures to be redeemed in DRR A/c before redemption of debentures commences.
 2. **Redemption out of profit:** Redemption out of profit means that adequate amount of profits are transferred to DRR A/c from Balance in Statement of Profit & Loss A/c before the redemption of debenture commences. This reduces the amount available for dividends to shareholders.

Debenture Redemption Reserve (DRR): Section 71 (4) of the Companies Act, 2013 requires the company to create DRR out of the profits available for dividend and the amount credited in DRR shall not be utilized for any purpose except redemption.

Rule 18(7) of Companies (Share Capital and Debentures) Rules, 2014 requires every Company to create DRR of an amount equal to 25% of the value of outstanding debentures.

Exemption to Create DRR

- a) NBfc registered with RBI
- b) All India financial institutions (AIFs) regulated by RBI and Banking companies (for both public as well as privately placed debentures)
- c) Financial institutions other than All India finance Companies registered with RBI
- d) Housing finance Companies registered with National Housing Bank.
DRR is required for publicly issued debentures by the above three classes of companies, not for privately placed.
- e) Any other Company (Whether listed or unlisted), DRR to be created for Public and Private placed debentures.

As per Rule 18(7)(c), every company required to create/maintain DRR shall invest or deposit before 30th April in specified securities a sum which shall not be less than 15% of the amount of debentures maturing for payment during the year ending 31st March of the next year.

Specified securities for Debenture Redemption Investment

1. In deposits with any scheduled bank, free from any charge or lien.
2. In unencumbered securities of central or any state Government.
3. In unencumbered securities mentioned in clause (a) to (d) and (ee) of section 20 of Indian Trusts Act, 1882.
4. In unencumbered bonds issued by a company which is notified under sec 20 (f) of Indian Trust Act, 1882.

(A) Redemption at Par

Illustration 1: X Ltd. Redeemed its 10,000 10% Debentures of ₹10 each at par on 31st March 2015.

X Ltd.

Date	Particulars	L.F	Debit (₹)	Credit (₹)
2014 March 31 st	Balance in Statement of Profit & Loss A/c Dr To Debenture Redemption Reserve A/c. (Being transfer of profit to Debenture Red. Reserve)		25,000	25,000
2014 April 30 th	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment made in specified securities)		15,000	15,000
2015 31 st March	Bank A/c Dr. To Debenture Redemption Investment A/c (Investment being enclosed)		15,000	15,000
31 st March	10% Debenture A/c Dr. To Debenture holder A/c (Being the amount due to Debenture holders)		1,00,000	1,00,000
31 st March	Debenture holder A/c Dr. To Bank A/c (Being the amount paid to Debenture holder)		1,00,000	1,00,000
31 st March	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being DRR A/c closed by transfer to General Reserve A/c after redemption of all Debentures)		25,000	25,000

(B) Redemption at Premium

Illustration 2: Z Ltd. Redeemed its 1, 00,000 10% Debentures of ₹10 each at 5% premium on 31 March 2015.

Z Ltd.

Date	Particulars	LF.	Debit (₹)	Credit (₹)
2014 31st March	Balance in Statement of Profit & Loss A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of profit to Debenture Redemption Reserve)		2,50,000	2,50,000
2014 April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment made in specified securities)		1,50,000	1,50,000
2015 March 31 31st March	Bank A/c Dr. To Debenture Redemption Investment A/c (Being Investment enclosed)		1,50,000	1,50,000
31st March	10% Debenture A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debenture holders A/c (Being the amount due to Debentures holders)		10,00,000 50,000	10,50,000
31st March	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to Debenture holders)		10,50,000	10,50,000
31st March	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being DRR A/c closed by transfer to General Reserve A/c after redemption of all Debentures)		2,50,000	2,50,000

Illustration 3: Rajesh Export Ltd. has 2,000, 9% Debentures of ₹ 100 each due for redemption on 31st march 2015. Debentures redemption reserve has a balance of ₹ 30,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.

Date	Particulars	LF.	Debit (₹)	Credit (₹)
2014 31st March	Balance in Statement of Profit & Loss A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of profit to Debenture Redemption Reserve)		20,000	20,000
2014 April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Being investment in specified securities made)		30,000	30,000
2015 31st March	Bank A/c Dr. To Debenture Redemption Investment A/c (Being Investment enclosed)		30,000	30,000
31st March	10% Debentures A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holders)		2,00,000	2,00,000
31st March	Debentures holders A/c Dr. To Bank A/c (Being the amount paid to Debentures holders)		2,00,000	2,00,000
31st March	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being DRR A/c closed by transfer to General Reserve A/c after redemption of all Debentures)		50,000	50,000

Illustration 4: Rahul Ltd. has 50,000; 9% Debentures of ₹ 50 each due for redemption on 31st March 2015. Debentures redemption reserve has a balance of ₹ 5,00,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Journal

Date	Particulars	LF.	Debit (₹)	Credit (₹)
2014 31st March	Balance in Statement of Profit & Loss A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of profit to Debenture Redemption Reserve)		1,25,000	1,25,000
2014 April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment in specified securities made)		3,75,000	3,75,000
31st March	Bank A/c Dr. To Debenture Redemption Investment A/c (Being investment are closed)		3,75,000	3,75,000
2015 31st March	10% Debentures A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holders)		25,00,000	25,00,000
31st March	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to Debenture holder)		25,00,000	25,00,000
2015 31st March	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being DRR A/c Closed by transfer to General Reserve A/c after redemption of all debentures)		6,25,000	6,25,000

Illustration 5: HDFC Bank Ltd has outstanding 10,000; 9% Debentures of ₹ 50 each due for redemption on 31st March 2015. Record the necessary journal entries at the time of redemption of debentures

Journal of HDFC Bank Ltd.

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2015 31st March	10% Debenture A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holder)		5,00,000	5,00,000
31st March	Debenture holder A/c Dr. To Bank A/c (Being the amount paid to Debenture holders)		5,00,000	5,00,000

Note: The Banking Companies are exempted from creating DRR as per Rule 18(7) of Companies (Share Capital and Debentures) Rules, 2014.

Illustration 6: ICICI Bank Ltd., a banking company has outstanding 10 lac, 9% Debentures of ₹ 5 each due for redemption on 30th Sept. 2015. Record the necessary entries at the time of redemption of Debentures.

Journal of ICICI Bank Ltd.

Date	Particulars	L.F.	Debit (₹ in lakh)	Credit (₹)
2015 30 th Sept.	9% Debenture A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holder on Redemption)		50	50
30 th Sept.	Debenture holders A/c Dr. To Bank A/c (Being the amount due to Debenture holders paid)		50	50

Note: As per Companies Rules, 2014 Banking companies are exempted from creating Debenture Redemption Reserve.

Illustration 7: Abha Ltd. has 5,000; 10% Debentures of ₹ 20 each due for redemption on 30th Sept. 2015. Debenture Redemption Reserve has a balance of ₹ 20,000 on that date. Record the necessary entries at the time of redemption of debentures.

Journal in the Books of Abha Ltd.

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2015 March 30	Balance in Statement of Profit and Loss A/c Dr. To Debenture Redemption Reserve A/c (Being the require amount transferred to DRR)		5,000	5,000
April 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Being investment made)		15,000	15,000
30 th Sept	Bank A/c Dr. To Debenture Redemption Investment A/c (Being investment are closed)		15,000	15,000
30 th Sept.	10% Debenture A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holder on redemption)		1,00,000	1,00,000
30 th Sept	Debenture holders A/c Dr. To Bank A/c (Being the amount due to Debenture holder paid)		1,00,000	1,00,000
30 th Sept.	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the DRR transferred to General Reserve)		25,000	25,000

Illustration 8: Vivek Transport Ltd. has 5,000; 10% Debentures of ₹ 20 each due for redemption on 30th Sept. 2015. Debenture Redemption Reserve has a Balance of ₹ 80,000 on that date. Record the necessary entries at the time of redemption of debentures.

Solution :

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2015 31 st March	Balance in Statement of Profit and Loss A/c Dr. To Debenture Redemption Reserve A/c (Being debenture Red. Reserve created upto 100% of amount of debentures)		20,000	2,000
30April	Debenture Redemption Investment A/c Dr. To Bank A/c (Being investment made for debentures redemption)		15,000	15,000
30 th Sept	Bank A/c Dr. To Debenture Redemption Investment A/c (Being investment encashed)		15,000	15,000
30 th Sept.	10% Debenture A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holder on redemption)		1,00,000	1,00,000
30 th Sept	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to Debenture holder)		1,00,000	1,00,000
30 th Sept.	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the Debenture Redemption Reserve Amount transferred to General Reserve)		1,00,000	1,00,000

Note: DRR exist in the books more than 25% of the debentures face value, so it assumed that redemption is out profit. In this case DRR is to be created up to 100% face value of Debentures. So DRR A/c is credited with the difference amount i.e. ₹ 1,00,000- ₹ 80,000 = ₹ 20,000.

Illustration 9: Rahul Ltd. redeemed ₹ 25, 00,000; 12% Debentures at a premium of 5% out of Profit on 30th Sept. 2015. Pass the necessary journal entries for the redemption of debentures.

Solution:

Date	Particulars	LF.	Debit (₹)	Credit (₹)
2015 31st Apr.	Balance in Statement of Profit and Loss A/c Dr. To Debenture Redemption Reserve A/c (Being the required amount transferred to DRR)		25,00,000	25,00,000
30 th April	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment made equal to 15% of the debenture to be redeemed in current financial year)		3,75,000	3,75,000
30 th Sep.	10% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debenture holder's A/c (Being the amount due to Debenture holders)		25,00,000 1,25,000	26,25,000
30 th Sep.	Bank A/c Dr. To Debenture Redemption Investment A/c (Being Debenture Redemption Investment encashed)		3,75,000	3,75,000
30 th Sep.	Debenture holder's A/c Dr. To Bank A/c (Being the amount due to Debenture holders paid)		26,25,000	26,25,000
30 th Sep.	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the DRR transferred to General Reserve)		25,00,000	25,00,000

Note: (1) If in any question it is mentioned that redemption of debenture is out of profit, then the Debenture Redemption Reserve A/c should be created with the full face value (100%) of debentures. If DRR is created only with 25% of the total amount of debentures, it would mean that remaining 75% of the debentures have been redeemed out of capital.

(2) So, it would be clear if in a question it is mentioned that the redemption is out of profit, then an amount equal to total amount of debentures (100% of face value of debentures) is to be transferred to DRR A/c. in all other cases (except Companies exempted by the SEBI) DRR would be created with the 25% of the face value of the total debentures.

The rule **[Rule 18(7)(b) of the Companies (Share Capital and Debentures) Rules, 2014]** It means that a company shall have DRR of at least 25% of the value of outstanding debentures that are to be redeemed.

Please note that DRR is not created on Debentures that are fully convertible or on the convertible part of the partially convertible debenture. Besides, some classes of companies like AIFI, Banking Companies etc., are exempt from creating DRR.

Therefore, where the debentures are redeemed in parts, proportionate amount of DRR to the debentures redeemed shall be transferred to General Reserve after the redemption.

Illustration 10. Max Ltd. had issued 10,000, 7% Debentures of ₹ 100 each on 1st April, 2013, which were to be redeemed as follows:

- (a) 2,000 Debentures on 30th June, 2016;
- (b) 3,000 Debentures on 31st December, 2016; and
- (c) Balance on 30th June, 2017.

Max Ltd. shall create DRR of ₹ 2,50,000 being 25% of ₹ 10, 00,000, i.e., value of outstanding debentures out of profits available for distribution as dividend to shareholders on 31st March, 2016 or in earlier years.

- (a) On 30th June, 2016, after redeeming 2,000; 7% Debenture, it shall transfer ₹ 50,000 out of DRR being the amount proportionate to 2,000; 7% Debentures. The Journal entry will be:

Debenture Redemption Reserve A/c	...Dr.	₹ 50,000
To General Reserve A/c		₹ 50,000

(Being the proportionate amount of 2,000;
7% Debentures redeemed transferred from
DRR to General Reserve)

After the transfer of ₹ 50,000 from DRR Account to General Reserve Account, balance left in DRR Account is ₹ 2,00,000 which is 25% of the value of outstanding debentures, i.e., ₹ 8,00,000 (₹ 10,00,000 less ₹ 2,00,000, being the amount of debenture redeemed).

- (b) On 31st December, 2016 again the company will follow the same process. After redeeming 3,000; 7% Debentures it shall transfer ₹ 75,000 from DRR Account to General Reserve Account being the amount proportionate to 3,000 Debentures. The Journal entry will be:

Debenture Redemption Reserve A/c	...Dr.	₹ 70,000
To General Reserve A/c		₹ 70,000

(Being the proportionate amount of 3,000;
7% Debentures redeemed transferred from
DRR to General Reserve)

After the transfer of ₹ 75,000 from DRR Account to General Reserve Account, balance left in DRR Account is ₹ 1,25,000 which is 25% of the value of outstanding debentures, i.e., ₹ 5,00,000 (₹ 8,00,000 less ₹ 3,00,000, being the amount of debentures redeemed).

- (c) On 30th June, 2017 again the company will follow the same process. After redeeming the balance 5,000; 7% Debentures it shall transfer the balance amount in DRR Account, i.e., ₹ 1,25,000 to General Reserve Account. The Journal entry will be:

Debenture Redemption Reserve A/c	...Dr.	₹ 1,25,000
To General Reserve A/c		₹ 1,25,000

(Being the balance amount transferred from
DRR to General Reserve)

After the transfer of ₹ 1,25,000 from DRR Account balance left in DRR Account will be Nil.

Redemption method: 2 Draw of lots

Illustration 11: S Ltd. redeemed its ₹ 10,000, 8% Debentures out of capital by drawing a lot on 30 Nov. 2015. Journalise.

Solution

Journal of S. Ltd.

Date	Particulars	LF.	Debit(₹)	Credit(₹)
2015 March 31	Balance in Statement of Profit & Loss A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of profit to Debenture Redemption Reserve)		2,500	2,500
2015 30 th April	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment in specified securities made)		1,500	1,500
30 th Nov.	Bank A/c Dr. To Debenture Redemption Investment A/c (Being investment Encashed)		1,500	1,500
30 th Nov.	10% Debentures A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holders)		10,000	10,000
30 th Nov.	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to Debenture holders)		10,000	10,000
30 th Nov.	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the proportionate amount of DRR transferred to General Reserve)		2,500	2,500

Illustration 12: Y Ltd redeemed its ₹ 20,000, 9% debentures out of profit by drawing of lot on 30th Nov. 2015 Journalise.

Y Ltd.

Date	Particulars	LF.	Debit (₹)	Credit (₹)
20 Apr. 2015	Balance in Statement of Profit & Loss A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of profit to Debenture Redemption Reserve)		20,000	20,000
2015 30 th Nov.	Debenture Redemption Investment A/c Dr. To Bank A/c (Being Investment made)		3,000	3,000
2015 30 th Nov.	Bank A/c Dr. To Debenture Redemption Investment A/c (Being investment encashed)		3,000	3,000
30 th Nov.	10% Debentures A/c Dr. To Debenture holders A/c (Being the amount due to Debenture holders)		20,000	20,000
30 th Nov.	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to Debenture holders)		20,000	20,000
30 th Nov.	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the proportionate amount of DRR transferred to General Reserve A/c)		20,000	20,000

Illustration 13: Pass the necessary journal entries for this 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.

Journal

Date	Particulars	LF.	Debit (₹)	Credit (₹)
(i) At the time of redemption	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 Reserve A/c (Being amount due to debenture holder)		12,60,000	12,00,000 60,000
	10% Debenture A/c Dr. To Debenture holder A/c (Being amount due to debenture holder)		12,00,000	12,00,000
	Debenture holder A/c Dr. To Bank A/c (Being the amount paid to debenture holders)		12,00,000	12,00,000
(ii) At the time of redemption	Bank A/c Dr. To Debenture Application and Allotment A/c (Being receipt application money)		48,00,000	48,00,000
	Debenture Application and Allotment A/c Dr. Loss on Issue of Debenture A/c Dr. To 9% Debenture A/c To Securities Premium Reserve A/c To Premium on Redemption of Debenture A/c (Being issue 9% debenture at premium redeemable at premium)		48,00,000 12,00,000	40,00,000 8,00,000 12,00,000
	9% Debenture A/c Dr. Premium on Redemption of Debenture A/c Dr. To Debenture holder A/c (Being amount due to debenture holder)		40,00,000 12,00,000	52,00,000
	Debenture holder A/c Dr. To Bank A/c (Being the amount paid to debenture holder)		52,00,000	52,00,000

Note- 1. It is assumed that Company has investment 15% of the redeemable amount on April 30 and encashed it as per Companies Act, 2013.

2. It is assumed that Company has created Debenture Redemption Reserve @ 25% of the redeemable debenture and transferred it to General Reserve after redemption of all the debentures.

Practice Questions

Ruchi Ltd. issued 42,000 7% debenture of Rs. 100 each on 1st April 2011, redeemable at a premium of 8% on 31st March 2015. The company decided to create required debenture redemption reserve on 31st March 2014. The company invested the funds as required by law in a fixed deposit with state Bank of India on 1st April 2014 earning @ 10% per annum. Tax was deducted at source by the bank on interest @10% per annum pass necessary journal entries regarding issue and redemption of debenture.

Practice Questions

Issue of Debenture

1. Rai Ltd. company purchased assets of the book value of Rs. 99,000 from another firm. It was agreed that purchase consideration be paid by issuing 11 % debentures of Rs. 100 each.

Assume debentures have been issued

1. At par
2. At discount of 10 % and
3. At a premium journal entries

Record necessary journal entries

2. Raj Printers, Ltd; purchased building worth Rs, 1,50,000, machinery worth rs. 1,40,000 and furniture worth rs. 10,000 from XYZ co. took over its liabilities of Rs. 20,000 for a purchase consideration of Rs. 3,15,000. Raj Printers Ltd. paid the purchase consideration by issuing 12 % debentures of Rs. 100 each at a premium of 5 % Record necessary Journal entries

3. Sanyo Ltd. purchased machinery worth Rs. 1,98,000 from Aryan Ltd. The payment was made by issue of 12 % debentures of Rs. 100 each. Pass the necessary journal entries for the purchase of machinery and issue of debentures when: (i) Debentures are issued at par; (ii) Debentures are issued at 10% discount; and (iii) Debentures are issued at 10% premium

4. Pass the journal entries relating to the issue of the debentures in the books of Axe Ltd;