

## UNIT-II

### **Issue of preference shares and debentures — Redemption of preference shares and debentures (Balance Sheet as per Revised Schedule VI)**

#### **PREFERENCE SHARES**

A preference share is one, which enjoys certain preferential rights. First, on preference shares a fixed dividend is guaranteed before any payment of dividend is made in respect of equity shares. The second preference enjoyed by the preference shares is in respect of return of capital in the event of winding up of the company. Preference shareholders are paid back their capital before any other classes of shareholders

#### **TYPES/CLASSES OF PREFERENCE SHARES**

##### **(a) On basis of Dividend:**

**(i) Cumulative Preference Shares:** Cumulative preference shares are the preference shares whose holders are entitled to receive arrears of dividend before any dividend is paid on equity shares.

**(ii) Non-cumulative Preference Shares:** Non-cumulative preference shares are the preference shares whose holders do not have the right to receive arrears of dividend. If no dividend is declared in any year due to any reason, they get nothing, nor can they claim unpaid dividend in any subsequent years.

##### **(b) On basis of Participation**

**(i) Participating Preference Shares:** In addition to the fixed preference dividend, such shares carry a right to participate in the surplus profit, if any, after providing dividend at a stipulated rate to equity shareholders.

**(ii) Non-Participating Preference Shares:** Such shares get only a fixed rate of dividend every year and do not have a right to participate in the surplus profit, if any.

##### **(c) On basis of Convertibility**

**(i) Convertible Preference Shares:** They are preference shares with a right/option to be converted into equity shares

**(ii) Non-Convertible Preference Shares:** These are preference shares, which do not have the right/ option to be converted into equity shares.

**Sum No:1** K Ltd issued 75000 equity shares of Rs 10 each and 5000 12% preference shares of Rs 100 each payable as under:

	<b>On equity shares</b>	<b>On preference shares</b>
with application	2	20
on allotment	2	30
on first call	3	50
on second call	3	-

The company received applications for 1,35,000 equity shares and 4,500 preference shares Applications totalling for 10,000 equity shares were rejected, allotment on other applications for equity shares was made on pro-rata basis. All the applications for preference shares were accepted in full. Calls were made on due dates all money were duly received. Show journal entries for the above transactions

## Redemption of preference shares

The preference shares can be redeemed only when they are fully paid up

- Out of the profits of the company, which would otherwise be available for dividend, or
- Out of the proceeds of a fresh issue of shares made for the purposes of such redemption.

**Case 1:** Redemption of preference shares out of the profits of the company, which would otherwise be available for dividend.

In case redeemable preference shares are redeemed out of company profits, which are otherwise available for dividend, the “Capital Redemption Reserve Account” is to be created that will represent the redeemable preference shares in the balance sheet after redemption. This capital redemption reserve should be equivalent to the amount of Preference Shares, which are to be redeemed. The profits available for dividend have to be transferred to Capital Redemption Reserve Account.

### 1. Transfer profits available for dividend to Capital Redemption Reserve Account:

General Reserve Account Dr.

Profit and Loss Appropriation A/c Dr.

Dividend Equalization Account Dr.

To Capital Redemption Reserve A/c (with the nominal value of the shares to be redeemed)

### 2. If current assets are realized to provide cash for redemption of preference shares:

Bank A/c Dr.

To Respective Assets Account with the realized value of assets

### 3. On transfer of redeemable preference share-capital to be redeemed to Preference Shareholders Account:

Redeemable Preference Share-Capital A/c Dr. with the nominal value of the shares to be redeemed

To Preference Shareholders A/c

### 4. If preference shares are redeemed at a premium:

Redeemable Preference Share-Capital A/c Dr.

Premium on Redemption of Preference Shares A/c Dr. with the amount of premium payable

To Preference Shareholders A/c

### 5. For providing premium on redemption of preference shares:

Securities Premium Account Dr. with amount of premium paid on redemption

or Profit and Loss Appropriation A/c Dr.

To Premium on Redemption of Preference Shares Account

### 6. On redemption of preference shares:

Preference Shareholders Account Dr. with the amount paid

To Bank A/c

**Case 2:** If the redeemable preference shares are redeemed out of the proceeds of a fresh issue of shares made for the purpose of redemption:

In a case where redeemable preference shares are redeemed out of proceeds received from fresh issue of shares, the Share Capital Account raised by fresh issue shall take the place of Redeemable Preference Share Capital Account after redemption. Thus, in such a case, new Share Capital Account (Equity or Preference) must be equal to the redeemable preference shares redeemed. First of all, entries for fresh issue of shares will be passed. Then entries for redemption passed as has been given in the previous case.

**Case 3:** If the redeemable preference shares are redeemed partly out of the profits of the company which would otherwise be available for dividend and partly out of the proceeds of a fresh issue of shares made for the purpose of redemption: In such a case, the Capital Redemption Reserve Account and the new Share Capital Account taken together will replace

the Redeemable Preference Share Capital redeemed. Thus, Redeemable Preference Share Capital redeemed = Capital Redemption Reserve Account + New Share Capital Account (Equity or Preference). Here, all the entries shown under Case (i) and Case (ii) have to be passed. But there are certain common entries which can be combined together.

**Sum No:2 (Redemption without fresh issue of shares (or) Redemption out of revenue reserves)**

Sympcox Ltd., issued 75,000 equity shares of Rs.10 each and 50,000 redeemable preference shares of Rs.100 each all shares being fully called and paid up on 31-03-1992. Profit & Loss account showed undistributed profit of Rs.3,00,000 and general reserve stood at Rs.2,50,000. On 1-4-1992, the directors decided to redeem the existing preference shares at Rs.105 utilising as much profit as required for the purpose. You are required to pass journal entries in the books of the company.

**Sum No:3**

Redemption of 20,000 preference shares of Rs.100 each was carried out by utilisation of reserves and by issue of 8,000 equity shares of Rs.100 each at Rs.125. How much should be credited to capital redemption reserve a/c?

**Sum No:4**

Redemption of 10,000 preference shares of Rs.100 each was carried out of reserves and out of the issue of 4,000 shares of Rs.100 each @ Rs.95. What is the amount of capital redemption reserve account that is received?

**Sum No:5**

The following extract from the balance sheet of Vijay Ltd. as on 31st December 1997 is given to you.

Share capital	Rs.
2,00,000 equity shares of Rs.10 each	20,00,000
2,00,000 6% redeemable preference shares of Rs.10 each	20,00,000
Capital reserve	10,00,000
General reserve	6,00,000
Profit & Loss account	17,00,000

The company exercises its option to redeem the preference shares on 1st Jan. 2010

**Sum No:6**

The following balances appear in the ledger of a company as on 30.06.2004:

Share capital	Rs.
Equity shares(fully paid up)	6,00,000
Redeemable preference shares(fully paid up)	3,00,000
General reserve	2,00,000
Profit and loss A/c(Cr.balance)	1,25,000
Securities premium A/c	50,000

The company decided to redeem the preference shares at a premium of 10% out of its general reserve and undistributed profits. Give journal relating to redemption of the preference shares.

**Sum No:7** The following is the balance sheet of Raman company Ltd. as on 31.12.96.

Liabilities	Rs.	Assets	Rs.
Share capital:			
1000 6% Redeemable preference		Fixed assets	3,10,000

shares of Rs.100 each fully paid	1,00,000	Cash at bank	1,40,000
20,000 equity shares of Rs.10 each	2,00,000		
Profit & Loss A/c	1,20,000		
Sundry creditors	30,000		
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	4,50,000		4,50,000
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The company resolved to redeem its preference shares at a premium of 2% out of profits. Give necessary journal entries.

### Redemption at par out of profits

**Sum No:8** The following extract from the balance sheet of Gayathri Co. Ltd., as on 31st Dec. 2008, is given to you:

Share capital :	Rs.
2,00,000 equity shares of Rs.10 each	20,00,000
3,00,000 6% redeemable preference shares of Rs.10 each	30,00,000
Capital reserve	15,00,000
General reserve	9,00,000
Profit and loss a/c	25,50,000

The company exercises its option to redeem the preference shares on 1st Jan. 2009. The company has sufficient cash. Give journal entries to record the redemptions.

**Sum No:9** The balance sheet of Wallace Ltd. as on 31st Dec. 2009 was as under:

Liabilities	Rs.	Assets	Rs.
Share capital			
1,000 redeemable preference shares of Rs,100 each	1,00,000	Sundry assets	3,65,000
2,000 equity shares of Rs.100		Bank balance	
1,40,000			
each fully paid	2,00,000		
General reserve	80,000		
Profit and Loss A/c	50,000		
Sundry creditors	75,000		
	5,05,000		
5,05,000			

On this date, the preference shares were redeemed at par. Journalise and prepare balance sheet after redemption.

### Redemption at a premium out of profits

**Sum No:10** The balance sheet of Exchange Ltd., as on 31-3-2009 was as follows:

Liabilities	Rs.	Assets	Rs.
Share capital:			
50,000 equity shares of Rs.10 each, fully paid	5,00,000	Sundry assets	9,20,000
4,000 redeemable preference Shares of Rs.100 each fully paid	4,00,000	Bank balance	6,00,000
Profit and loss a/c	5,20,000		

Creditors	1,00,000	
	15,20,000	15,20,000

On the above date, the preference shares were redeemed at a premium of 10%. You are required to pass journal entries and give the amended balance sheet.

**Sum No:11** The following balance sheet of Raj Ltd. as on 31st Dec. 2009.

Liabilities	Rs.	Assets	Rs.
Share capital:			
50,000 equity shares of Rs.10 each	5,00,000	Sundry assets	6,00,000
2,000 8% redeemable preference			
Shares of Rs.100 each	2,00,000	Cash at bank	4,40,000
Profit and loss a/c	2,40,000		
Sundry creditors	1,00,000		
	10,40,000		10,40,000

The company resolved to redeem its preference shares at a premium of 20% out of profits.

Pass necessary journal entries and show the important ledger accounts and the company's balance sheet after completion of redemption

#### **Redemption at par out of fresh issue**

**Sum No:12** Modern Fibres Ltd., has part of its share capital as 5,000 redeemable preference shares of Rs.100 each. When the shares became due for redemption, the company decided that the whole amount will be redeemed out of a fresh issue of equal amount of equity shares of Rs.10 each. Show the journal entries in the books of the company.

#### **Redemption at a premium, partly out of profits and partly out of fresh issue**

**Sum No:13** Streling Ltd., have part of their share capital in 2,500 6% redeemable preference shares of RS.100 each. The company decided to redeem the preference shares at premium of 10%. The general reserve of the company shows the credit balance of Rs.3,00,000. The directors decided to utilise 60% of the reserve in redeeming the preference shares and the balance is to be met from the proceeds of fresh issue of sufficient number of shares of Rs.10 each. The premium is to be met from the year's profit and loss appropriation a/c.

Give journal entries to record the above transactions.

#### **Redemption at a premium and fresh issue at premium**

**Sum No:14** A company has 10,000 9% redeemable preference shares of Rs.100 each fully paid. The company decides to redeem the shares on 31 Dec. 2004 at a premium of 10%.

The company makes the following issues:

a)6,000 equity shares of Rs.100 each at a premium of 10%

b)4,000 8% debentures of Rs.100 each

The issue was fully subscribed and allotments were made. The redemption was duly carried out. The company has sufficient profits. You are required to give the necessary entries.

#### **Redemption at par and fresh issue at premium**

**Sum No:15** On 30th June 1998, the balance sheet of Sandhya Ltd., stood as follows:

Liabilities	Rs.	Assets
Rs.		
Equity share capital	10,00,000	sundry assets
14,00,000		

Redeemable preference share capital	4,00,000	Bank
5,00,000		
P& L a/c	3,00,000	
Sundry creditors	2,00,000	
	19,00,000	
19,00,000		

On the above date, the preference shares have to be redeemed. For this purpose 2,000 equity shares of Rs.100 each were issued at Rs.110. the company also issued 8% debentures totalling Rs.3,00,000. The shares and debentures were immediately subscribed and paid for. The preference shares were duly redeemed. Give the journal entries and balance sheet after redemption.

**DEBENTURES: Debentures** are part of loan capital and the company is liable to pay interest thereon whether it earns profit or not. Debentures include debenture stock, bonds or any other instrument of a company evidencing a debt whether constituting a charge on the assets of the company or not.

**ISSUE OF DEBENTURES: Subject** to the restrictions imposed by Section 71 of the Companies Act, 2013, a company can issue debentures. Applications for debentures are invited from the public through a prospectus and the applicants are asked to pay the application money along with the applications. The company may ask for payment of the whole of the amount along with the application or by instalments.

**Difference between debentures and shares**

Points	Debentures	Shares
Capital	Debenture is a part of loan capital or borrowing	Share capital is an ownership capital.
Status	Debenture holder is creditor of company	Shareholder is the owner of the company
Income	Interest is the income on the investment in debentures	Dividend is the income on investment in shares
Charges or Appropriation	Payment of interest is charge against and is payable even if there is no profit	Payment of dividend is an appropriation of profit and not payable if there is no profit.
Voting rights	Debenture holders do not have any voting rights.	Shareholders generally enjoy the voting rights
Issue at discount	No restriction is imposed on the issue of debentures at discount	Section 53 prohibits the issue of shares at discount
Rate	Rate of interest is fixed	Rate of dividend may vary from year to year for equity shares
Convertibility	Debentures can be convertible	Equity shares can never be convertible

**Issue of debentures for cash**

Debentures may be issued for cash on a par, a premium or discount. When the debentures are issued for cash, the entire issue price may be received on application itself or the amount may be payable in instalments, such as on application, on allotment and balance in calls

Any premium or discount on the issue of debentures is generally recorded at the time of making allotment.

**Accounting treatment when the debentures are at a par:**

(a) When the full issue price is payable in lump sum along with application

(1) On receipt of application money:

Bank A/c Dr. (with the money received on application)  
To Debentures Application and Allotment A/c

(2) On allotment:

Debenture Application and Allotment A/c Dr. ( money received on debentures allotted)  
To Debentures A/c

(b) When the amount is payable in instalments

1. On receipt of application money:

Bank A/c Dr. (with the money received on application)  
To Debentures Application A/c

2. On Allotment of debentures:

Debenture Application A/c Dr. (with the application money o debentures allotted)  
To Debentures A/c

3. On allotment money due

Debenture allotment A/c Dr (with the allotment money due)  
To Debenture A/c

4. On receipt of allotment money:

Bank A/c Dr. (with the money received on allotment)  
To Debenture Allotment A/c

5. On making calls:

Debenture Calls A/c Dr. (with the money due on respective calls)  
To Debenture A/c

6. On receipt of call money:

Bank A/c Dr. (with the money received on respective calls)  
To Debenture Calls A/c

**Over subscription:** The excess application money may be retained for adjustment towards allotment and particular calls similar to share application money. However, money received from applicants to whom no debenture has been allotted will be refunded to them.

The following journal entry is made in this regard:

Debenture Application A/c Dr  
To Bank A/c

### **Issue of debentures at premium**

When the debentures are issued for cash at premium, the amount of premium is recorded at the time of making entries for allotment money. The entries for receipt of application money and transfer of application money to debenture account are same as issue at par.

The entries for allotment are

(i) When allotment money becomes due

Debenture Allotment A/c Dr  
To Debenture A/c

To Securities Premium A/c

(ii) When allotment money is received

Bank A/c Dr  
To Debenture Allotment A/c

And for calls the entries are same as for issue at par

**Issue of debentures at discount** If the debentures are issued at a price lower than the nominal value of the debentures, the debentures are said to be issued at a discount. The difference between the nominal value and the issue price is regarded as the discount. Such a discount on the issue of debentures may be written off either against revenue profit or capital profits of the company. When debentures are issued at a discount the Debentures Account

should be credited with the nominal value of the debentures and the discount allowed on issue of debentures. It being a capital loss should be debited to "Discount on Issue of Debentures Account". Thus, the accounting entry will be as follows:

Debentures Allotment A/c Dr (with the amount due on allotment)

Discount on issue of Debentures A/c Dr (with the amount of discount)

To Debentures A/c (with the total)

### **ISSUE OF DEBENTURES FOR CONSIDERATION OTHER THAN CASH**

Sometimes a company may allot debentures (on a par, premium or discount) to vendors as a payment for the purchase price of the assets. The issue of debentures is then for consideration other than cash. In such a case,

#### **(1) For acquisition of assets:**

Sundry Assets (Individually) A/c Dr. (with the value of assets)

To Vendors A/c (with the purchase price)

Notes: (i) If the value of debentures allotted is more than the agreed purchase price, the difference is debited to Goodwill Account.

(ii) Similarly, if the value of debentures allotted is less than the agreed purchase price, it is credited to Capital Reserve Account.

#### **(2) (a) On allotment of debentures (at par)**

Vendors A/c Dr. (with the value of debentures)

To Debentures A/c

#### **(b) On allotment of debentures (at premium)**

Vendors A/c Dr. (with the purchase price)

To Debentures A/c (with the nominal value)

To Securities Premium A/c (with the amount of premium)

#### **(c) On allotment of debentures (at a discount)**

Vendors A/c Dr. (with the amount of purchase)

Discount on Issue of Debentures A/c Dr. (with the amount of discount)

To Debentures A/c (with the nominal value)

### **ISSUE OF DEBENTURES**

**SumNo:16** Timex Lld., issued 1000 , 8%debentures of Rs.100 each. Give appropriate journal entries in the books of the company, if the debenture were issued as follows:

Issued at par, redeemable at par,

- Issued at a discount of 5%, repayable at par.
- Issued at a premium of 10%, repayable at par.
- Issued at par, redeemable at a premium of 10%.
- Issued at a discount of 5%, repayable at a premium of 10%

You are also required to show how the items concerned appear in the balance sheet in each of the above cases.

**Sum No:17** Exel Ltd. Made the following issues of debentures on 1.4.97

1) 200 10% debentures of Rs. 100 each to settle a creditor who supplied a machine on credit some time ago at a price of Rs. 18000.

2) 300 10% debentures of Rs. 100 each for cash at a discount of 5%.

3) 1000 10% debentures of Rs. 100 each to the bankers as collateral security for a loan of Rs. 80000. All the above issues are redeemable at par. Pass journal entries to record the above in the books of the company and show how these items are to be shown when the company's balance sheet is prepared.

**Sum No:18** Moon Rays Ltd. Issued 50000 8% debentures of Rs. 10 each to the public at par, to be paid Rs. 4 on application and the balance on allotment. Applications were received for

48000 debentures. Allotment was made to all the applicants and the amount due was received promptly Give journal entries to record the transaction and show how they appear in the balance sheet of the company.

**Sum No:19** Earth Movers Ltd. Issued 15000 14% debentures of Rs. 100 each for public subscription, at a premium of 10% payable as to Rs. 30 on application, Rs. 50 (including premium) on allotment and the balance in one call. 25000 applications were received. 4000 applications were rejected and debentures were allotted to the remaining applicants pro-rata. Allotment amount was received from all the allotted one of whom paid then call amount due on his 1000 debentures along with allotment money. The call amount was also collected on then due date. You are required to pass necessary journal entries in the company's books.

**Sum No:20** Goutham Ltd. Issued 15000 8% debentures of Rs. 100 each at a discount of 5% payable after 5 years at a premium of 5% . You are required to show : (1) journal entries at the time of issue and redemption of debentures; (2) show the "Loss on Issue of debentures A/c " over the period. journalise the following issues:

- a) A company issued 1000 ,6% debentures of Rs. 100 each at a par.
- b) A company issued 1000,6% debentures of Rs. 100 each at 10% premium .
- c) A company issued 1000,6% debentures of Rs. 100 each at 10% discount.
- d) A company issued 1000 ,6% debentures of Rs. 100 each at a par.
- e) A company issued 1000,6% debentures of Rs. 100 each at 10% premium .
- f) A company issued 1000,6% debentures of Rs. 100 each at 10% discount

## **REDEMPTION OF DEBENTURES**

### **MEANING**

Redemption of debentures means repayment of loan due on debentures to the debenture holders. The terms and conditions of redemption are generally given in the prospectus. But irredeemable debentures are perpetual in nature and are redeemable on the happening of a contingency and not otherwise.

### **METHODS OF REDEMPTION**

Redeemable debentures are redeemed either at par or at a premium and following methods of redemption are available to the company to discharge its liability

#### **(1) Lumpsum**

The redemption is made in one lumpsum at the expiry of a specified period promised as the redemption date when the debentures were issued.

**(2) Annual Instalments or Draw by Lots** Under this method, a certain amount of debentures is redeemed at regular intervals, say yearly, during the life of debentures. The amount of annual drawings may or may not be equal.

#### **(3) Conversion into Shares**

A company may issue convertible debentures, giving options to the debenture holders to exchange their debentures for equity shares or preference shares in the company.

**(4) Purchase of Its Own Debentures In Open Market** A company is entitled to purchase its own debentures in open market, i.e., through the stock exchange. When the company purchases its own debentures for immediate cancellation, it leads to automatic redemption. Own debentures may also be purchased by the company for its own investment and same may be reissued in future too.

### **Sources of Redemption**

A company can arrange funds from the following sources

- (a) Out of capital
- (b) Out of profit
- (c) Through conversion

## **REDEMPTION OUT OF CAPITAL**

When debentures are redeemed out of capital, no debenture redemption reserve is created out of profit of the company. Thus, the profit would not be reduced and the same can be utilized in future for the payment of dividend.

### **A. When debentures are redeemed at par**

#### **(i) On debentures becoming due for payment**

Debentures A/c Dr (with the nominal value of debentures)

To Debenture holders A/c

#### **(ii) On redemption**

Debenture holders A/c Dr

To Bank A/c

### **B. When debentures are redeemed at premium**

#### **(i) On debentures becoming due for payment**

Debentures A/c Dr (with the nominal value of debentures)

Premium on redemption of Debentures A/c Dr (with the amount of premium)

To Debenture holders A/c

#### **(ii) On redemption**

Debenture holders A/c Dr

To Bank A/c

#### **(iii) On writing off premium on redemption since it was not recorded at the time of issue of debentures**

Securities Premium A/c Dr

Free reserves A/c Dr

To Premium on redemption of debentures A/c

### **C. When debentures are redeemed at discount**

Although it's a very rare possibility, the accounting treatment would be

#### **(i) On debentures becoming due for payment**

Debentures A/c Dr (with the nominal value of debentures)

To Debenture holders A/c (with the amount payable)

To Capital Reserve A/c (with the amount of discount)

#### **(ii) On redemption**

Debenture holders A/c Dr

To Bank A/c

### **For appropriation of surplus or withholding of profits in the form of DRR**

Surplus A/c Dr (with the amount appropriated)

To DRR A/c

DRR would be shown or disclosed as Shareholder's Funds on the Balance Sheet under the heading: Reserves and Surplus.

### **On transferring the balance of DRR when the debentures are redeemed**

DRR A/c Dr

To General Reserve A/c

### **Sinking Fund Method (Debenture Redemption Fund Method)**

A sinking fund may be defined as a fund created by an appropriation of certain profits and investments of the same for the redemption of debentures. The investment may be in the form of Government Bonds or other quickly saleable securities so that the same can be sold without much difficulty.

### **Types of Sinking Funds**

- (i) Cumulative Sinking Fund
- (ii) Non- Cumulative Sinking Fund

### **Cumulative Sinking Fund**

A cumulative sinking fund is maintained based on annual appropriation of the profits and the interest earned on the sinking fund investments.

**The accounting entries for maintaining a cumulative sinking fund are as follows:**

#### **A. At the end of First year**

##### **(i) For appropriation of required amount for Sinking Fund**

Surplus A/c Dr

To Sinking Fund A/c

##### **(ii) For investing the surplus appropriated**

Sinking fund investment A/c Dr

To Bank A/c

#### **B. At the end of second and subsequent years**

##### **(i) For receiving interest on Sinking Fund Investment**

Bank A/c Dr

To interest on Sinking Fund Investment A/c

##### **(ii) For transferring interest to Sinking Fund Account**

Interest on sinking fund investment A/c Dr

To Sinking Fund A/c

##### **(iii) For annual appropriation**

Surplus A/c Dr

To Sinking Fund A/c

##### **(iv) For investing the surplus appropriated and the interest received**

Sinking Fund Investment A/c Dr

To Bank A/c

#### **C. At the end of Last Year**

##### **(i) For receiving interest on Sinking Fund Investment**

Bank A/c Dr

To Sinking Fund A/c

##### **(ii) For annual appropriation**

Surplus A/c Dr

To Sinking Fund A/c

##### **(iii) For sale of Sinking Fund Investment**

###### **(a) In case of profit**

Bank A/c Dr

To Sinking Fund Investment A/c

To Sinking Fund A/c (with the amount of profit)

###### **(b) In case of loss**

Bank A/c Dr

Sinking Fund A/c Dr (with the amount of loss)

To Sinking Fund Investment A/c

##### **(iv) For redemption of debentures (a) At par**

Debentures A/c Dr

To Bank A/c

###### **(b) At premium**

Debentures A/c Dr

Premium on Redemption of Debentures A/c Dr

To Bank A/c

##### **(v) For closing the Sinking Fund Account**

Sinking Fund A/c Dr

To General Reserve A/c

**Sum No:21** Prakash Ltd. issued Rs. 10,00,000, 10% debentures on January 1, 2017. These were to be redeemed on 31st December, 2019. For this purpose the company established Sinking Fund. Investments were expected to earn 5% interest p.a. Sinking Fund table shows that 0.317208 invested annually at 5% amount to Rs. 1 in 3 years. On 31st December, 2019 the investment was sold for Rs. 6,56,000. Interest received and investments are made in multiples of Rs. 100. Journalize and ignore narration and debenture interest.

### **Insurance Policy Method**

Under this method also, annual sum is appropriated out of surplus and credited to Debenture Redemption Fund A/c in the same manner as it is done in Sinking Fund method. However, the appropriate profit is not invested in marketable securities, instead an insurance policy is taken for the required amount and an amount equal to profit set aside is paid as premium to insurance company. At the end of policy period, the insurance company returns the total accumulated amount which is sufficient to pay the debenture holders.

### **Accounting Treatment**

#### **A. From year to year**

##### **(i) On payment of premium**

Debenture Redemption Fund Policy A/c Dr. (with the annual premium amount)

To Bank A/c

(ii) For appropriation of profit equivalent to amount of premium paid during the year  
Surplus A/c Dr

To Debenture Redemption Fund A/c

#### **B. At the time of maturity and redemption**

##### **(i) On realization of policy**

Bank A/c Dr (with the amount of policy)

To Debenture Redemption Fund Policy A/c

##### **(ii) On transfer of interest earned on premium**

Debenture Redemption Fund Policy A/c Dr (with the difference between the amount of  
policy realized and the total premium paid)

To Debenture Redemption Fund A/c

##### **(iii) On transfer of premium on redemption of debentures**

Debenture Redemption Fund A/c Dr

To Premium on redemption

##### **(iv) For closing the Debenture Redemption Fund Account**

Debenture Redemption Fund A/c Dr

To General Reserve A/c

**Sum No:22** Go Ltd. issued 500, 12% Debentures of Rs. 100 each at par on 1st April, 2015, repayable at par after 3 years on 31st March, 2018. The directors decided to take out an insurance policy to provide necessary cash for the redemption of the debentures. The annual premium for the policy payable on 1st April every year was Rs. 15,705.

You are required to show the journal entries in the books of the company

### **REDEMPTION BY CONVERSION**

A company can issue convertible debentures. It means that the debentures would be converted into new class of debentures or shares.

#### **(a) When shares are issued at par**

Debentures A/c Dr

To Share capital A/c

#### **(b) When shares are issued at a premium**

Debentures A/c Dr

To Share Capital A/c (with the nominal value of shares issued)

To Securities Premium A/c (with the amount of premium)

**Sum No:23** Bima Ltd. had issued 11% 5,00,000 debentures of Rs. 100 each redeemable on 31st March 2019 at a premium of 5%.

The company offered three options to debenture holders as under:

(i) 13% Preference shares of Rs.10 each at Rs.10.50

(ii) 14% debentures of Rs. 100 at par.

(iii) Redemption in cash.

The options were accepted as under :

Option (i) by holders of 1,00,000 debentures.

Option (ii) by holders of 1,00,000 debentures.

Option (iii) by holders of 3,00,000 debentures.

The company carried out the redemption. Pass the necessary journal entries.

**Sum No:24.** Z ltd . redeemed Rs.10000 12% debentures, out of capital by drawing a lot and it has also redeemed Rs. 20,000 10% debentures out of profit by drawing a lot journalise.

**SumNo:25** MK Ltd. Issued 4000 6% debentures of Rs. 100 each in 2000 interest payable being on 30th june and 31st December every year. On 30.9.2002, the company purchased 400 debentures at Rs. 97 ex-interest and cancelled immediately. Show journal entry for cancellation of debentures.

**Sum No:26** RK Ltd. Has Rs. 50000 10% debentures on 1st January 2001. On 1.3.2002, the company purchased Rs. 10000 debentures at Rs. 98 Cum-interest. The debentures interest is payable half yearly on 30th june and 31st Dec. every year. Show journal entry for purchase and cancellation of debentures.

**Sum No:27** Goodwill Ltd. Issues 1000 6% debentures Rs. 100 each. Give journal entries in each of the following cases:

a) The debentures are issued and redeemable at par.

b) They are issued at a discount of 6% , but redeemed at par.

c) They are issued at a premium of 5%, but redeemed at par.

d) They issued at a discount of 4% but are redeemable at a premium of 5%.

**SumNo:28.** Zed Ltd. Issued 1000 9% debentures of Rs. 100 each payable , Rs. 20 on application and the balance on allotment. Applications were received for 1500 debentures out of which applications for 900 were allotted fully. Applicants for 400 debentures were allotted 100 debentures and the remaining were rejected. All sums due were received.

Give journal entries and show how these transaction will be reflected in the balance sheet of the company.

**Sum No:29.**Narayanan & Co. Ltd., purchased assets worth Rs. 28,80,000. It issued debentures in satisfaction of the purchase price. Calculate how many debentures will be issued:

a) In case the debentures are of Rs. 100 each and are issued at a discount of 4% and

b) In case the debentures are of Rs. 80 each and are issued at a premium of Rs. 10 per debenture.

Also, pass the journal entries required for the issue of debentures.

REDEMPTION OF DEBENTURES

**Sum No:30** Journalise the following transaction at the time of issue of debentures and redemption of debenture:

- a) Debenture issue at Rs. 95, repayable at Rs. 100
- b) Debenture issue at Rs. 95, repayable at Rs. 105
- c) Debenture issue at Rs. 100, repayable at Rs. 105
- d) Debenture issue at Rs. 95, repayable at Rs. 100

The face value of each debenture Rs.100.

**Sum No:31.**X Ltd. Issued 5000 8% debentures of Rs. 10 each at par on 1.4.2000 which are repayable at 10% premium at the end of 4 years. Give journal entries for issue and redemption if a) The redemption is out of profits. b) The redemption is out of capital.

#### REDEMPTION BY CONVERSION

**Sum No:32** On 1.4.1997, Rama Ltd. Issued 2500 8% debentures of Rs. 100 each at 5% discount. Holders of the debentures have option to convert their holding into equity shares of Rs. 100 each at a premium of Rs. 25 per share at any time within 3 years. On 31.3.98, holders of 500 debentures notified their intention to exercise the option. Show the necessary journal entries in the company's books relating to issue and conversion of the debentures. Also show how the items affected would appear in the company's balance sheet.

**Sum No: 33** S Ltd. Issued Rs. 500000 10% debentures of Rs.100 each at a discount of 10%. The debentureholders have an option to convert them into equity shares of Rs. 10 each at par after the expiry of 2 years. The due date for redemption of the debentures at par is at the end of the 10th year. You are required to find out the No. of shares a debenture holder gets and also give the necessary journal entries.

- a) If he converts his 200 debentures at the end of the second year from the date of issue;
- b) If he converts his 200 debentures at the end of Tenth year, on the agreed date of the redemption.

**Sum No: 34** Estern plastics Ltd. Issued fully convertible 10% debentures of Rs. 100 each for Rs. 10,00,000. The following were the terms of issue:

- a) Date of issue January 1, 1993.
- b) 60% of the debentures issued will be converted into equity shares of Rs. 10 each at a premium of 20% on 31.12.95.
- c) Balance of 40% of the debentures will be converted into equity shares of Rs. 10 each at a premium of Rs. 6 per share on 31.12.96.

pass journal entries in the books of the company for conversion of the debentures.

**Sum No: 35** Balaji Ltd. Issued 5000 12% debentures of Rs.100 each at a discount of 10% holders being given the right to exercise the option of converting the debentures into 15% preference shares of Rs. 100 each at a premium of 10% before the redemption date.

Holders of 1650 debentures expressed their willingness to exercise the option to convert their debentures into preference shares. Ascertain the number and amount of preference shares to be issued and give necessary journal entries for the issue and conversion of the debentures.

**Sum No: 36** On 1.1. 92, 'A' Ltd. , issued 200 5% debentures of Rs. 1000 at Rs. 950 each. Debenture holders had an option to convert their holdings into 6% preference shares of Rs. 100 each at a premium of Rs. 25 per share. On 31.12.92, one year's interest had accrued on these debentures which was not paid. A holder of 20 debentures notified his intention to

convert his holding into 6% preference shares. Journalise the above transaction and draw the company's balance sheet as at 31.12.92, assuming no other transaction took place.

**Sum No: 37** On 1.7.91, Solvents Ltd. issued, 400 7% debentures of Rs. 1000 each at Rs.950. The debenture holders were given option to convert their holdings into 8% preference shares of Rs. 100 each at a premium of Rs.20 per share any time after 2 years. On 1.7.93, holders of 60 debentures exercised their option of conversion. Show the journal entries for issue and conversion of the debentures, ignoring interest. Also give relevant extracts from the company's balance sheet, after the conversion.

### **REDEMPTION IN INSTALMENTS**

**Sum No: 38** Rashid Ltd. has Rs. 10,00,000 8% debentures outstanding on 1.1.96. The company has been redeeming every year on January 1st Rs. 1,00,000 debentures by drawings by lot, at par. Give necessary journal entries:

- a) if the redemption is out of profits
- b) If the redemption is out of capital.

### **OPEN MARKET BUYING METHOD**

**Sum No: 39** Krishna Ltd. which had Rs. 50,00,000 10% debentures outstanding, made the following purchases in the open market for immediate cancellation:

1.4.1997 1000 debentures of Rs. 100 each at Rs. 99

1.9.1997 2000 debentures of Rs. 100 each at Rs. 97

You are required to give the journal entries for purchase and cancellation of the debentures.

If the above purchase rates are 'Ex-interest'

If the above purchase rates are 'Cum-interest' . Assume that interest is payable every year on 30th June and 31st December.

**Sum No: 40** Mohith Ltd. which has Rs. 10,00,000 8% debentures of Rs. 100 each outstanding on 1.1.96 on which interest is payable on 30th June and 31st December each year is permitted to purchase its own debentures in the open market and cancel them or retain them or resell them at its option. The company made the following purchase in the open market on 1.4.96 500 debentures at Rs. 97 ex-interest.

Give appropriate journal entries, if

The debentures were cancelled on the same day;

The debentures were retained till 1.7.96 on which date they were cancelled.