

VIDYA BHAWAN BALIKA VIDYA PITH

शक्तिउत्थानआश्रमलखीसरायबिहार

Class 12 commerce Sub. ACT Date 04.01.2021

Teacher name – Ajay Kumar Sharma

Issue and Redemption of Debentures (H.W)

Question 9:

Can a company purchase its own debentures in the open market? Explain.

ANSWER:

Yes, a company can purchase its own debentures provided it is authorised by its Article of Association. As per the Company Act, if a company is authorised by its Article of Association, only then it may purchase its own debentures from the open market. The main purposes of such purchase are as follows:

1. For immediate cancellation of debenture liability, if the interest rate on its debenture is higher than the market rate of interest.
2. A company may also purchase its own debentures with the motive of investment and sell them at higher price in future and thereby earn profit.

A company may purchase its own debentures at discount or at premium for cancellation.

1. If Debentures are purchased at Discount for Cancellation

When the company purchases its own debentures at discount for cancellation, then the following Journal entries are recorded.

Own Debentures A/c

Dr.

To Bank A/c

(Own debentures purchased)

Debentures A/c	Dr. (with the face value)
To Own Debentures A/c	(with the amount paid)
To Profit on Cancellation of Own Debentures A/c	(with the difference between the face value and amount paid)

(Own debentures cancelled)

Profit on Cancellation of Own Debentures A/c	Dr.
To Capital Reserve A/c	

(Profit on Cancellation of Own Debentures transferred to Capital Reserve)

2. If Debentures are Purchased at Premium for Cancellation

Own Debentures A/c	Dr.
To Bank A/c	

(Own debentures purchased)

Debentures A/c	Dr. (with the face value)
Loss on Redemption of Debentures A/c	(with the difference between Amount paid and face value)
To Own Debentures A/c	

(Own Debentures cancelled)

Question 10:

What is meant by conversion of debentures? Describe the method of such a conversion.

ANSWER:

When a debenture holder can convert his/her debentures into shares or new debentures after the expiry of a specified period of time, then it is known as redemption of debentures by conversion. As the company does not need to pay any funds for the redemption, so there is no need to maintain Debenture Redemption Reserve (DRR). The new shares or debentures may be issued at par, premium or at discount.

If a debenture holder exercises the conversion option, then the issue price of shares must be equal to or less than the amount actually received from debentures.

Accounting Treatment

1. For amount due to debenture holders

Debenture A/c	Dr.
To Debenture holders A/c	
(Debentures redeemed)	

2. For discharging liability to the debenture holders

Debenture holders A/c	Dr.
To Shares/Debentures (New) A/c	
(Debenture holder amount discharged)	
