

VIDYA BHAWAN BALIKA VIDYA PITH

शक्तिउत्थानआश्रमलखीसरायबिहार

Class 12 commerce Sub. ACT Date 29.12.2020

Teacher name – Ajay Kumar Sharma

Issue and Redemption of Debentures (H.W)

Question 15:

Can the company purchase its own debentures?

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.

Question 16:

What is meant by redemption of debentures by 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 do not need to pay any funds for the redemption, so there is no need to maintain the Debenture Redemption Reserve (DRR). The new shares or debentures may be issued at par, premium or at discount.

Question 17:

How would you deal with 'Premium on Redemption of Debentures'?

ANSWER:

When the debentures are redeemed at a price more than its face value or the par value, then it is said that the debentures are redeemed at premium. The difference between the redeemed price and the par value is regarded as a capital loss and this loss is written off till the redemption of the debentures. The Premium on Redemption of Debenture is shown in the Notes to Accounts under the sub-head of 'Other Long-term Liabilities'. The final balance is shown under the main head of 'Non-Current Liabilities' on the Equity and Liabilities side of the Company's Balance Sheet.

Accounting Treatment for Premium on Redemption on Debentures:

1. At the time of the Issue of Debenture:

Bank/Debenture Allotment A/c	Dr.
Loss on issue of Debenture A/c	Dr.
To Debenture A/c	
To Premium on Redemption	

(Debenture issued with the term of redemption at premium)

2. At the time of Redemption of Debentures:

Debenture A/c	Dr.
Premium on Redemption A/c	Dr.
To Debenture Holder A/c	

(Amount of debentures due to debenture holders)

Question 18:

What is meant by 'Redemption out of Capital?'

ANSWER:

When debentures are redeemed out of capital and no profits are utilised for redemption, then such redemption is termed as redemption out of capital. In such a situation, no profits are transferred to the Debenture Redemption Reserve.

As per the guideline laid down by Securities and Exchange Board of India (SEBI) and the Section 117C of Company Act of 1956, the creation of Debenture Redemption Reserve is mandatory (DRR). Therefore, it is not possible to redeem debentures purely out of capital, as it reduces the value of assets. The following companies are exempted from the creation of DRR.

1. Infrastructure companies (i.e. those companies that are engaged in the business of developing, maintaining and operating infrastructure facilities)
2. A Company that issues debentures with a maturity up to 18 months

The following are the necessary Journal entries that need to be passed, in case the debentures are redeemed out of capital.

a. If debentures are redeemed out of capital at Par

Debenture A/c Dr.
 To Debenture holder A/c
(Amount of debentures due to debenture holders)

Debenture holder A/c Dr.
 To Bank A/c
(Amount of debentures paid to debenture holders)

b. If debentures are redeemed out of capital at Premium

Debenture A/c Dr.
Premium on Redemption A/c Dr.
 To Debenture holder A/c
(Amount of debentures due to debenture holders)

Debenture holder A/c Dr.
 To Bank A/c
(Amount of debentures paid to debenture holders)

Question 19:

What is meant by redemption of debentures by 'Purchase in the Open Market'?

ANSWER:

According to 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 purpose of such purchase is 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.
-

Question 20:

Under which head is the 'Debenture Redemption Reserve' shown in the Balance Sheet?

ANSWER:

As per the Revised Schedule VI, Debenture Redemption Reserve (DRR) is shown in the Notes to Accounts of Reserve and Surplus. The final balance after adding DRR, is shown as the sub-head 'Reserves and Surplus' under the main head of Shareholders' Funds on the Equity and Liabilities side of the Company's Balance Sheet.
