

4. ISSUE OF DEBENTURES

4.1 Debenture – Definition and its important features

1. **Definition:**

- (a) Debenture includes Debenture Stock, Bonds and any other instrument of a Company evidencing a debt, whether constituting a charge on the assets of the Company or not. [Sec. 2(30)]
- (b) It is a document issued by a Company indicating its **indebtedness**.

2. **Features:**

- (a) **Debt:** Debenture is a document which evidences a loan made to a Company. The term Debenture refers to an acknowledgement of a debt, and obligation to repay, which is accompanied by some charge or security.

- (b) **Under Common Seal:** Though not mandatory, a Debenture is issued under the Company's Seal.
- (c) **Interest:** The Company pays a fixed rate of interest on Debentures, due on specific dates. Such interest is payable, irrespective of whether the Company has earned profit or not.
- (d) **Date of maturity / redemption:** Generally Debentures are issued for a specified period of time, after which they mature or have to be redeemed by the Company by paying the money. Sometimes, they may be converted into Equity Shares, after the maturity period.
- (e) **Creation of Charge:** Most Debentures are secured by way of a charge on the assets / part of the assets of the Company. However, there may also be unsecured Debentures.
- (f) **Movable Property [Sec.44]:** Like Shares, Debentures are also movable property, capable of being transferred in the manner provided in the AOA of the Company.
- (g) **Trading:** Debentures may be bought or sold through the Stock Exchange, at a price above or below the face value. Hence, Debentures may be traded, in the same manner as Shares.
- (h) **No Voting Rights [Sec. 71(2)]:** Debenture Holders are mere lenders to the Company, who are generally secured for payment. Hence they **do not have any right as to voting** in meetings. The Company shall not issue any Debentures carrying voting rights.
- (i) **Specific performance [Sec.71(12)]:** A contract with a company to take up and pay for any debentures of the company may be enforced by a decree of Specific Performance.

4.2 Shares vs Debentures

Basis	Share	Debenture
1. Meaning	A Share is the Share in the Share Capital of the Company.	A Debenture is the acknowledgment of Debt .
2. Nature	Share Capital is the part of the Capital of the Company.	Debentures constitute the Loan of the Company.
3. Holders	Shareholders are the Owners of the Company.	Debentureholders are the Creditors .
4. Kinds	There are only two basic kinds of Shares – (a) Equity, and (b) Preference Shares.	Debentures can be classified in different ways. [Refer next question.]
5. Voting	Shareholders generally enjoy voting rights .	Debentures do not have any voting rights.
6. Return	Dividend is paid only out of the profits of the Company.	Interest on Debentures is paid even if there are no profits .
7. Variation in return	Dividend on Equity Shares may vary from year to year. [However, Dividend on Preference Shares is paid at a fixed rate.]	Rate of Interest on Debentures is fixed .
8. Nature of Payment	Dividend is an appropriation of Profits of the Company. Hence, it is not deductible as an "expense" for tax purposes.	Interest on Debentures is a " charge " on the profits of the Company. Interest payment gives tax savings to the Company.
9. Disclosure	Shares are shown under " Share Capital " on the Liabilities Side of the Balance Sheet.	Debentures are shown under " Secured Loans " on the Liabilities Side of the Balance Sheet.
10. Conversion	Shares cannot be converted into Debentures under any circumstances.	Debentures may be converted into Shares (partly or fully) as per the terms of issue.
11. Forfeiture	Shares can be forfeited for non-payment of Allotment or Call Moneys, as per AOA.	Debentures cannot be forfeited for non-payment of Call Money.
12. Charge on Assets	Shares do not carry any charge on Assets.	Debentures generally have a charge on the Assets of the Company.
13. Priority of repayment	Upon winding-up, they are paid after Debentureholders are settled.	They are paid before Shareholders, since they are the Creditors of the Company.
14. Risk	Higher Risk than Debentureholders.	Lower Risk than Equity Shareholders.
15. Control	Higher degree of control over the Company.	Minimum / No control.

4.3 Different kinds of Debentures

Kinds of Debentures – Based on

Priority	Negotiability	Redeemability	Security	Convertibility
(a) First Mortgage Debentures	(a) Bearer or Unregistered Debentures	(a) Redeemable Debentures	(a) Secured Debentures	(a) Convertible Debentures
(b) Second Mortgage Debentures	(b) Registered Debentures	(b) Irredeemable or Perpetual Debentures	(b) Unsecured or Naked Debentures	(b) Non-Convertible Debentures

1. Based on Priority

	First Mortgage Debentures	Second Mortgage Debentures
(a)	They are ranked first and are to be paid first in priority to other Debentures which may be issued later or subsequently by the Company.	They are issued subsequent to First Debentures and rank next in matters of repayment, i.e. they can be repaid or redeemed only after first Debentures are repaid / redeemed.
(b)	These constitute first priority in repayment.	These constitute second priority in repayment.

2. Based on Negotiability

	Bearer or Unregistered Debentures	Registered Debentures
(a)	These are payable to Bearer . Interest is paid through coupons attached to Certificate. On maturity, principal is paid to the Bearer.	These are payable to Registered Holders, i.e. whose names appear on the Certificate and are entered as a Holder in the Register of Debenture Holders of the Company.
(b)	These are similar to Negotiable Instruments, and are freely transferable, by mere delivery, ensure good title.	They are transferable only as per conditions endorsed in it, i.e. by way of execution of transfer deed and registration with the Company.
(c)	Stamp duty is not paid on transfer.	Stamp duty is paid on transfer.

3. Based on Permanence / Redeemability

	Redeemable Debentures	Irredeemable / Perpetual Debentures
(a)	They are issued for a specified period of time upon whose expiry, Company has the right to pay back the Holders and have its properties released from charge.	It is a Debenture which contains no clause as to payment , or which contains a clause that it shall not be paid back .
(b)	Payment / Redemption is made at the end of the specified period.	Payment / Redemption is only upon winding-up or a very long period of time, or happening of such other event as specified in the terms of issue.

4. Based on Security

	Secured Debentures	Unsecured / Naked Debentures
(a)	These are secured by a charge on the assets / part of the assets of the Company.	These are issued without any security. They do not create any charge on the Company's Assets.
(b)	The Charge may either be Fixed or Floating. (See Note below.)	Holders are like ordinary Unsecured Creditors and may sue the Company for recovery .
(c)	Holders of such Debentures have lower risk.	These type of Debentures are very risky from the viewpoint of Investors.

Note: A **Fixed Charge** is a mortgage on specific assets, e.g. Machinery, Land and Building, etc. These assets cannot be sold without the consent of the Debentureholders. The sale proceeds of these assets are utilized first for repaying Debentureholders. A **Floating Charge** generally covers all assets of the Company, including future assets, e.g. Stock, Receivables, Debtors, etc.

5. Based on Convertibility

	Convertible Debentures	Non Convertible Debentures
(a)	They are issued with an option that they can be converted into Equity or Preference Shares (at par or premium or discount), after a certain period.	They do not have any option as to convertibility.
(b)	They can be fully convertible or partly convertible. It shall be approved by a special resolution passed at a general meeting [Sec.71(1)]	They become fully payable on maturity, as specified in the terms of issue. Special resolution not required.

4.4 Journal Entries for Issue of Debentures

	Transaction	Journal Entry	
1.	Receipt of Money from Debenture Applicants	Bank	Dr. To Debenture Application A/c
2.	Transfer of Application Money to Debentures A/c		
(a)	Issued at Par, and redeemable at par	Debenture Application A/c	Dr. To% Debentures A/c
(b)	Issued at Premium, and redeemable – (i) at par, or (ii) at discount	Debenture Application A/c	Dr. To% Debentures A/c To Securities Premium A/c
(c)	Issued at Discount, and redeemable – (i) at par, or (ii) at Discount	Debenture Application A/c Discount on Issue of Debentures A/c	Dr. Dr. To% Debentures A/c
(d)	Issued at Par, and redeemable at premium [Note: Here, Loss on Issue of Debentures = Premium payable on Redemption only.]	Debenture Application A/c Loss on Issue of Debentures A/c	Dr. Dr. To% Debentures A/c To Premium on Redemption of Debentures
(e)	Issued at Premium, and redeemable at premium [Note: Here, Loss on Issue of Debentures = Premium payable on Redemption only.]	Debenture Application A/c Loss on Issue of Debentures A/c	Dr. Dr. To% Debentures A/c To Securities Premium A/c To Premium on Redemption of Debentures
(f)	Issued at Discount, and redeemable at premium [Note: Here, Loss on Issue of Debentures = Discount on Issue + Premium payable on Redemption only]	Debenture Application A/c Disc./ Loss on Issue of Debentures A/c	Dr. Dr. To% Debentures A/c To Premium on Redemption of Debentures
3.	Debentures issued for non-cash consideration		
(a)	Assets purchased from Vendor / business taken over, etc.	Sundry Assets A/c To Sundry Liabilities A/c, if any To Vendor A/c	Dr.
(b)	Allotment of Debentures to Vendor, at par / premium / discount	Vendor A/c Discount on Issue of Deb. A/c (if any) To% Debentures A/c To Securities Premium A/c (if any)	Dr. Dr. Dr.

Note: In the above scheme, it is assumed that the entire money is collected at the time of application itself. If the moneys are collected in instalments, e.g. Application, Allotment, Calls, etc. the Journal Entries are similar to that of Issue of Shares. In such case, Premium / Discount is adjusted at the time of allotment.

4.5 Issue of Debentures as Collateral Security

1. Meaning:

- (a) Collateral Security means **secondary or supporting security** for a loan, which can be realized by the Lender, when the original loan is not paid on due date.
- (b) Companies may issue their Own Debentures as Collateral Security for a Loan or Overdraft facility taken from Bank / other Lenders.

2. Effect:

- (a) If the Company repays the loan on the due dates, the Debentures will be released, along with the main security.
- (b) If the Company is not able to repay the loan or the interest thereon, the Lender will become the Debentureholders of the Company. However, such Debentureholders will receive interest only to the extent of Loan Amount, and not on the amount of debentures.

Note: The Holder of Debentures are entitled to interest only on amount of loan but not on value of Debentures.

- 3. Accounting Treatment:** There are two methods of showing Debentures issued as Collateral Security –

Situation	Method I	Method II
Journal Entry for issue of Debentures as Collateral Security	No Entry. It is only a Memorandum Method.	Debenture Suspense A/c Dr. To% Debentures A/c
Disclosure in the Balance Sheet till Loan is settled	The issue of Debentures and Loan Outstanding is shown as a Note under "Secured Loans".	<ul style="list-style-type: none"> • Debenture Suspense A/c will appear on the Assets Side. • Debentures A/c will appear on the Liabilities Side under Secured Loans.
Treatment after settlement of Loan	The Note given as above will be discontinued.	The Journal Entry given above will be reversed in order to cancel Debentures.

4.6 Treatment for Discount / Loss on Issue of Debentures

1. **Treatment:** Discount / Loss on Issue of Debentures is **written-off** or **amortized** over the period between the date of issue and date of redemption.

2. Determination of write-off amount:

Situation	Amount written off is computed as under –
(a) Debentures redeemed at lumpsum at the end of a given period	Total Amount of Discount / Loss should be written off equally over the life of debentures, i.e. Straight Line Method is used.
(b) Debentures redeemed in different / unequal instalments	Total Amount of Discount / Loss should be written off in the ratio of benefit derived from Debenture Loan in any particular year, i.e. Sum of Digits Method is used in this case.
(c) Debentures are irredeemable	Total Amount of Discount / Loss should be written off gradually over a long period .

3. Journal Entry:

Profit and Loss Account

Dr.

To Discount / Loss on Issue of Debentures A/c

Note: The unamortized amount is shown on the Assets Side of the Balance Sheet, under the heading Miscellaneous Expenditure (to the extent not written off or adjusted)

4.7 Accounting Treatment for Payment of Interest on Debentures

- Interest:** Interest on Debentures is a charge against the profits of the Company. Interest is paid at specified dates, (e.g. on half-yearly or annual basis) on the **Nominal Value** of Debenture.
 - Tax Deducted at Source:** The Company will pay interest to the Debentureholders after deducting the amount of tax, as specified in the Income Tax Rules. The Company is under an obligation to deduct tax at source and deposit the deducted tax amount with the Income Tax Authorities.

3. Journal Entries:

	Transaction	Journal Entry	
(a)	Interest due on Debentures	Interest on Debentures A/c To Debentureholders A/c	Dr.
(b)	Payment of Interest after deduction of tax at source (TDS)	Debentureholders A/c To TDS Payable A/c To Bank A/c	Dr.
(c)	Remittance Tax Deducted at Source with Government	TDS Payable A/c To Bank A/c	Dr.
(d)	Transfer of Interest on Debentures to P&L A/c	Profit and Loss A/c To Interest on Debentures A/c	Dr.

Illustration 1: Debentures issued at par – amount collected in full on application

Aswini Limited issued 10,000, 10% Debentures of ₹ 100 each at par payable in full on application by 1st January. Application was received for 12,000 Debentures. Debentures were allotted on 5th January. Excess application money was refunded on the same date. Pass the necessary Journal Entries in the books of the Company.

Solution:**Journal Entries**

	Date	Particulars	Dr.	Cr.
1.	2008 Jan 1	Bank A/c To 10% Debenture Application A/c (Being application money recd on 12,000 Debentures at ₹ 100 each)	12,00,000	12,00,000
2.	Jan 5	10% Debenture Application A/c To 10% Debenture A/c (Being the allotment of 10,000, 10% debentures of ₹ 100 each at par)	10,00,000	10,00,000
3.	Jan 5	10% Debenture Application A/c To Bank A/c (Being excess appln money on 2,000 Debentures at ₹ 100 refunded)	2,00,000	2,00,000

Illustration 2: Debentures Issue at a Premium – amount collected in instalments

Bharani Limited issued 10,000 9% Debentures of ₹ 100 each at a premium of 10% payable ₹ 25 on application, ₹ 35 on allotment (including Premium) and the balance on first and final call. Applications were received for 15,000 Debentures. All allotment was made proportionately, over-subscription being applied to the amount due on allotment. All sums due were received by the Company on due dates. Journalise the above transactions.

Solution:**1. Journal Entries**

	Particulars	Dr.	Cr.
1.	Bank A/c To Debenture Application A/c (Being the application money received on 15,000 Debentures at ₹ 25)	3,75,000	3,75,000
2.	Debenture Application A/c To 9% Debenture A/c (Being the transfer of application money on allotment of 10,000 Debentures)	2,50,000	2,50,000
3.	Debenture Allotment A/c To 9% Debenture A/c To Securities Premium A/c (Being allotment money of ₹ 35 per Debenture including ₹ 10 for premium due on 10,000 Debentures)	3,50,000 2,50,000 1,00,000	
4.	Debenture Application A/c To Debenture Allotment A/c (Being adjustment of surplus application money on 5,000 Debentures towards amount due on allotment)	1,25,000	1,25,000
5.	Bank A/c To Debenture Allotment A/c (Being balance of allotment money received on 10,000 Debentures)	2,25,000	2,25,000
6.	Debenture First and Final Call A/c To 9% Debenture A/c (Being Call Money of ₹ 50 per Debenture due on 10,000 Debentures)	5,00,000	5,00,000
7.	Bank A/c To Debenture First and Final Call A/c (Being first and final call money received on 10,000 Debentures of ₹ 50)	5,00,000	5,00,000

Illustration 3: Issue of Debentures at Discount

Krithika Limited issued 2,000 9% Debentures of ₹ 100 each at a discount of 4% payable ₹ 30 on application and the balance on allotment. Give the necessary Journal entries.

Solution:

1. Journal Entries

	Particulars	Dr.	Cr.
1.	Bank A/c To Debenture Application A/c (Being amount received on application on 2,000 Debentures at ₹ 30 each)	60,000	60,000
2.	Debenture Application A/c To 9% Debenture A/c (Being Debenture Application money transferred to Debentures Account)	60,000	60,000
3.	Debenture Allotment A/c Discount on issue of Debentures A/c To 9% Debenture A/c (Being Allotment money due on 1,000 Debentures)	1,32,000 8,000	1,40,000
4.	Bank A/c To Debenture Allotment A/c (Being Amount received on allotment)	1,32,000	1,32,000

Illustration 4: Issue of Debentures to Vendors for non-cash consideration

Rohini Ltd purchased assets of the Book Value of ₹ 99,000 from another Firm. It was agreed that the purchase consideration be paid by issuing 11% Debentures of ₹ 100 each. Pass Journal Entries assuming Debentures have been issued – (a) at par, (b) at discount of 10%, and (c) at a premium of 10%.

Solution:

1. Journal Entries

	Particulars	Dr.	Cr.
1.	Assets A/c To Vendor A/c (Being assets purchased from Vendor for ₹ 99,000)	99,000	99,000
2.	Issued at Par: Vendor A/c To 11% Debentures A/c (Being the amount of 990, 11% Debenture of ₹ 100 at par to the Vendor)	99,000	99,000
3.	Issued at Discount: Vendor A/c Discount on Issue of Debenture A/c To 11% Debentures A/c (Being 1,100 (₹ 99,000 ÷ ₹ 90) debentures of ₹ 100 each issued at discount of 10% to Vendor)	99,000 11,000	1,10,000
4.	Issued at Premium: Vendor A/c To 11% Debentures A/c To Securities Premium A/c Being 900 (₹ 99,000 ÷ ₹ 110) debentures of ₹ 100 each issued at premium of 10%)	99,000	90,000 9,000

Illustration 5: Issue of Debentures – various scenarios

Journalise the following issues of Debentures in the books of the Issuing Company (each situation is independent)

- 25,000 nos. of 8% Debentures of ₹ 100 each, issued at a premium of ₹ 15 per Debenture, the total amount is collected at the time of application itself.
- Machinery worth ₹ 38 lakhs was purchased. The amount due to the Vendor was settled by way of issue of 6% Debentures of ₹ 400 each, issued at a discount of 5%.
- 50,000 nos. 9% Fully Convertible Debentures issued at face value of ₹ 50 each, the entire amount being collected at the time of application.

Solution:**Situation (a)**

Particulars		Dr.	Cr.
1. Bank Account	Dr. To Debentures Application and Allotment Account (Being amt received on issue of 25,000 8% Debentures of ₹ 100 each, at a premium of ₹ 15 per debenture = 25,000 × ₹ 115)	28,75,000	28,75,000
2. Debentures Application and Allotment Account	Dr. To 8% Debentures Account (₹ 100 each) To Securities Premium (Being allotment of 25,000 8% Debentures of ₹ 100 each, at a premium of ₹ 15 per debenture)	28,75,000 25,00,000 3,75,000	

Situation (b)

1. Machinery Account	Dr. To Asset Vendor Account (Being the purchase of machinery, amount due to the Vendor)	38,00,000	38,00,000
2. Asset Vendor Account	Dr. Discount on Issue of Debentures To 6% Debentures Being the allotment of 10,000 6% Debentures of ₹ 400 each, at a discount of ₹ 20 per debenture) (Face Value is ₹ 400, issued at 5% disc. Hence Issue Price = ₹ 380. No. of Debentures issued = 38,00,000 ÷ 380 = 10,000)	38,00,000 2,00,000	40,00,000

Note: Discount on Issue of Debentures ₹ 2,00,000 will be written off to the Profit and Loss Account, during the period of the Debentures, in the proportion of the amount lying outstanding every year.

Situation (c)

1. Bank Account	Dr. To Debentures Application and Allotment Account (Being the issue of 50,000 9% Debentures of ₹ 50 each at par)	25,00,000	25,00,000
2. Debentures Application and Allotment Account	Dr. To 9% Fully Convertible Debentures (₹ 50 each) (Being the allotment of 50,000 9% FCD of ₹ 50 each)	25,00,000	25,00,000

Illustration 6: Issue of Debentures under various scenarios

Give Journal Entries in respect of the following independent situations –

1. 50,000, 8% Debenture of ₹ 100 each were issued and redeemable at par any time after 6 years.
2. 10,000, 9% Debentures of ₹ 50 each were issued at a discount of 8%, redeemable at par after 9 years.
3. ₹ 80,000, 9% Debentures were issued at a premium of 5%, redeemable at par.
4. ₹ 80,000 9% Debentures were issued at par and redeemable at 10% Premium.
5. 5,000, 9% Debentures of ₹ 1000 each issued at a discount of 6%, and redeemable at a premium of 8%.

Solution:**Journal Entries**

Particulars		Dr.	Cr.
1. Bank A/c	To Debenture Application A/c (Being application money received at ₹ 100 on 50,000 Debentures)	50,00,000	50,00,000
	Debenture Application A/c To 8% Debentures A/c (Being application money transferred to 8% Debenture Account)	50,00,000	50,00,000
2. Bank A/c	To Debenture Application A/c (Being application money received on 10,000 Debentures)	4,60,000	4,60,000

	Particulars	Dr.	Cr.
	Debenture Application A/c Discount on Issue of Debentures A/c To 9% Debentures A/c (Being application money transfer to Debentures Account, and recorded along with Discount on Issue of Debentures)	Dr. 4,60,000 40,000	5,00,000
3.	Bank A/c To Debenture Application A/c (Being application money received)	Dr. 84,000	84,000
	Debenture Application A/c To 9% Debentures A/c To Securities Premium A/c (Being debenture issued at 5% Premium and redeemable at par)	Dr. 84,000	80,000 4,000
4.	Bank A/c To Debenture Application A/c (Being application money received)	Dr. 80,000	80,000
	Debenture Application A/c Loss on Issue of Debentures A/c To 9% Debentures A/c To Premium on Redemption of Debentures A/c (Being debenture issued at par and redeemable at 10% premium) [Note: Premium on Redemption of Debentures A/c is a Personal A/c]	Dr. 80,000 8,000	80,000 8,000
5.	Bank A/c To Debenture Application A/c (Being application money received at ₹ 940 on 5,000 Debentures)	Dr. 47,00,000	47,00,000
6.	Debenture Application A/c Loss on Issue of Debentures A/c To 9% Debentures A/c To Premium on Redemption of Debentures A/c (Being debenture issued at 6% disc. and redeemable at 8% premium)	Dr. 47,00,000 7,00,000	50,00,000 4,00,000

Illustration 7: Discount on Issue of Debentures written off in Equal Instalments

A Company issues ₹ 20 Lakhs Debentures at a discount of 5%, repayable at the end of five years. What amount of discount will be written off every year?

Solution: Discount on Issue of Debentures = ₹ 20 Lakhs at 5% = ₹ 1,00,000. Since the amount is to be repaid after 5 years, Discount written off every year to P&L A/c = ₹ 10,00,000 ÷ 5 yrs = ₹ 20,000.

Illustration 8: Discount on Issue of Debentures – written off in proportionate amounts

Vayu Ltd issued 5,000 5% Debentures of ₹ 100 each, at a discount of 8%. The debentures were redeemable at par, in five equal annual instalments, commencing from the date of issue. Show for each year, (a) the amount of interest paid to Debentureholders, and (b) the amount of discount on issue of debentures written off to P&L Account. Assume that the issue was made on 1st July of Year 1 and the Company closes its accounts on 31st December every year. Interest is payable half-yearly on 30th June and 31st December every year.

Solution:

Total amount of Debentures = 5,000 × ₹ 100 = ₹ 5,00,000. Since Discount is 8%, Total Discount = ₹ 40,000. Also, amount redeemable on 30th June every year = ₹ 1,00,000 (5 instalments).

Year	Avg amount of deb. outstanding	Debenture Disc. w/off	Interest for the year
1	5,00,000 × 6/12 = 2,50,000	40,000 × 25/150 = 6,667	2,50,000 × 5% = 12,500
2	(5,00,000 × 6/12) + (4,00,000 × 6/12) = 4,50,000	40,000 × 45/150 = 12,000	4,50,000 × 5% = 22,500

Year	Avg amount of deb. outstanding	Debenture Disc. w/off	Interest for the year
3	$(4,00,000 \times 6/12) + (3,00,000 \times 6/12) = 3,50,000$	$40,000 \times 35/150 = 9,333$	$3,50,000 \times 5\% = 17,500$
4	$(3,00,000 \times 6/12) + (2,00,000 \times 6/12) = 2,50,000$	$40,000 \times 25/150 = 6,667$	$2,50,000 \times 5\% = 12,500$
5	$(2,00,000 \times 6/12) + (1,00,000 \times 6/12) = 1,50,000$	$40,000 \times 15/150 = 4,000$	$1,50,000 \times 5\% = 7,500$
6	$(1,00,000 \times 6/12) = 50,000$	$40,000 \times 5/150 = 1,333$	$50,000 \times 5\% = 2,500$
Total	15,00,000	(See Note 1) 40,000	(See Note 2) 75,000

Note:

1. Total Debenture Discount is written off to P&L Account in the ratio of the Debentures outstanding during that year, i.e. as per Column 2 above.
2. Interest for the year = Average Amount of Debentures outstanding × Interest Rate i.e. 5%.

Illustration 9: Company Accounts – Accounting for Forfeiture of Debentures

N 18

Pure Ltd issues 1,00,000 12% Debentures of ₹ 10 each at ₹ 9.40 on 1st January 2018. Under the terms of issue, the Debentures are redeemable at the end of 5 Years from the date of issue. Calculate the amount of Discount to be written-off in each of the 5 Years.

Solution:

Particulars	₹
1. Discount on Issue of 12% Debentures (per Debenture)	₹ 10.00 – ₹ 9.40
2. Total Discount on Issue of 12% Debentures	$1,00,000 \times ₹ 0.60$
4. Term of the 12% Debentures	5 Years
5. Amortisation of Discount on Issue of 12% Debentures	$₹ 60,000 \div 5 \text{ Years}$

Illustration 10: Debentures issued as a Collateral Security

Indra Company obtained a Cash Credit Limit of ₹ 250 Lakhs from Heavens Bank Ltd. In addition to the primary security of stocks and book debts of the Company, the loan agreement provided for the issue of 1,00,000 7.5% Debentures of a face value of ₹ 300 per bond, as Collateral Security. How will this issue of Debentures be treated in the books of Indra Company?

Solution: When Debentures are issued as Collateral Security, no interest is actually payable on the same. They can be treated in any of the following methods –

Method 1: Memorandum Method: No Journal Entry is recorded in the Books of Account. In the Balance Sheet –

Liabilities	₹ Lakhs	Assets	₹ Lakhs
Secured Loans: Cash Credit from Heavens Bank Ltd (secured against Stock and Book Debts) (Further Secured by 7.5% Debentures – 100000 nos. of ₹ 300 each as Collateral Security ₹ 300 Lakhs)	250.00		

Note: The amount of Debentures ₹ 300 Lakhs will not be shown in the outer column for totalling purposes. It is only a memorandum entry for information of the readers.

Method 2: Debenture Suspense Method: The following Journal Entry is recorded in the Books of Account.

Debentures Suspense Account	Dr.	₹ 300 Lakhs	₹ 300 Lakhs
To 7.5% Debentures Account			

(Being the issue of 1,00,000 7.5% Debentures of ₹ 300 each, issued as Collateral Security towards Cash Credit Limit of ₹ 250 Lakhs)

Illustration 11: Treatment of Interest on Debentures

Aakash Ltd issued 5,00, 10% Debentures of ₹ 100 each 6% on 1st January at a discount of 10% redeemable at a premium of 10%. Give Journal Entries, assuming that the interest was payable half-yearly on 30th June and 31st December and tax deducted at source is 10%. The Company follows calendar year as its accounting year.

Solution:**Journal Entries**

	Date	Particulars	Dr.	Cr.
1.	Jan 1	Bank A/c To Debenture Application A/c (Being the amount received on application)	Dr. 45,000	45,000
2.	Jan 1	Debenture Application A/c Loss on Issue of Debentures A/c To 10% Debenture A/c To Premium on Redemption of Debentures A/c (Being Debentures issued @ discount of 10% and redeemable @ 10% premium)	Dr. 45,000 10,000	50,000 5,000
3.	June 30	Debenture Interest A/c ($\text{₹ } 50,000 \times 10\%$ interest for 6 months) To TDS Payable A/c ($\text{₹ } 2,500 \times 10\%$ TDS Rate) To Debentureholders A/c (Being interest due for first 6 months and TDS thereon at 10%)	Dr. 2,500	250 2,250
4.	June 30	Debentureholders A/c To Bank A/c (Being the payment of interest for first half-year)	Dr. 2,250	2,250
5.	June 30	TDS Payable A/c To Bank A/c (Being Income Tax TDS from Debenture Interest paid to Govt.)	Dr. 250	250
6.	Dec 31	Debenture Interest A/c To TDS Payable A/c To Debentureholders A/c (Being interest due for next 6 months and TDS thereon at 10%)	Dr. 2,500	250 2,250
7.	Dec 31	Debentureholders A/c To Bank A/c (Being the payment of interest for second half-year)	Dr. 2,250	2,250
8.	Dec 31	TDS Payable A/c To Bank A/c (Being Income Tax TDS from Debenture Interest paid to Govt.)	Dr. 250	250
9.	Dec 31	Profit and Loss A/c To Debenture Interest A/c ($\text{₹ } 2,500 + \text{₹ } 2,500$) (Being the transfer of Debenture Interest to Profit and Loss Account)	Dr. 5,000	5,000

Illustration 12: Accounting for Companies - Debentures**M 19**

On 1st January 2018, Ankit Ltd. issued 10% debentures of the face value of ₹ 20,00,000 at 10% discount. Debenture interest after deducting tax at source @ 10% was payable on 30th June and 31st December every year. All the debentures were to be redeemed after the expiry of five year period at 5% premium

Pass necessary journal entries for the accounting year 2018.

Solution:**Journal Entries**

	Date	Particulars	Dr.	Cr.
1.	Year 2018	Bank A/c To Debenture Application A/c (Being the amount received on application)	Dr. 18,00,000	18,00,000

	Date	Particulars	Dr.	Cr.
2.	Jan 1	Debenture Application A/c Loss on Issue of Debentures A/c To 10% Debenture A/c To Premium on Redemption of Debentures A/c (Being Debentures issued @ discount of 10% and redeemable @ 5% premium)	Dr. 18,00,000 Dr. 3,00,000	20,00,000 1,00,000
3.	June 30	Debenture Interest A/c ($\text{₹ } 20,00,000 \times 10\%$ interest for 6 months) To TDS Payable A/c ($\text{₹ } 1,00,000 \times 10\%$ TDS Rate) To Debentureholders A/c (Being interest due for first 6 months and TDS thereon at 10%)	Dr. 1,00,000	10,000 90,000
4.	June 30	Debentureholders A/c To Bank A/c (Being the payment of interest for first half-year)	Dr. 90,000	90,000
5.	June 30	TDS Payable A/c To Bank A/c (Being Income Tax TDS from Debenture Interest paid to Govt.)	Dr. 10,000	10,000
6.	Dec 31	Debenture Interest A/c To TDS Payable A/c To Debentureholders A/c (Being interest due for next 6 months and TDS thereon at 10%)	Dr. 1,00,000	10,000 90,000
7.	Dec 31	Debentureholders A/c To Bank A/c (Being the payment of interest for second half-year)	Dr. 90,000	90,000
8.	Dec 31	TDS Payable A/c To Bank A/c (Being Income Tax TDS from Debenture Interest paid to Govt.)	Dr. 10,000	10,000
9.	Dec 31	Profit and Loss A/c To Debenture Interest A/c ($\text{₹ } 1,00,000 + \text{₹ } 1,00,000$) (Being the transfer of Debenture Interest to Profit and Loss Account)	Dr. 2,00,000	2,00,000