LONG ANSWER TYPE QUESTIONS

Question 1. What is meant by a debenture? Explain the different types of debentures?
Answer Debenture: The word 'Debenture' has been derived from a Latin w'ord 'Debere' which means to borrow. Debenture is a written instrument acknowledging a debt under the common seal of the company. It contains a contract for repayment of principal after a specified period or at intervals or at the option of the company and for payment of interest at a fixed rate payable usually either half-yearly or yearly on fixed dates.
According, to Section 2(12) of The Companies Act, 1956 'Debenture' includes Debenture Stock, Bonds and any other securities of a company whether constituting a charge on the assets of the company or not. There are various types of Debentures.
(i) From Security Point of View :From security point of view debentures can be classified into two broad categories naked or simple debentures and Mortgaged debentures.
(a) Naked or Simple Debentures :Naked or Simple Debentures are those debentures which do not carry any security in respect of repayment of interest or the principal. The general solvency of the company is the only security for the holders of simple debentures.
(b) Mortgaged Debentures: Mortgaged Debentures are the debentures which are secured by a charge on the asset or properties of the company. The debenture holders have the right to recover their principal amount as well as unpaid interest out of the assets mortgaged by the company.

In case of mortgage debentures, a company may prefer to appoint trustees who will hold the property given by way of security in trust for the benefits of debentures holders.

(ii) From Permanence Point of View From Permanence point of view the debentures may be Redeemable or Irredeemable debentures.
(a) Redeemable Debentures Redeemable debentures provide for the payment of principal amount on the expiry of certain period. Redeemable debentures can be reissued even after they have been redeemed until they have been cancelled.
(b) Irredeemable Debentures Irredeemable Debentures are retained as a part of the permanent capital structure during the life time of the company. Such debt becomes due for payment only when the company goes into liquidation or when the payment of interest is not made regularly.

The company has the option of cancelling its liability to the debenture holders at any time by giving due notice to them.

(iii) From Priority Point of View :From this point of view the debentures may be First and Second debentures.
(a) First Debentures :First Debentures are those debentures which are paid first before any payment is made to another type of

debentures.
(b) Second Debentures: Second Debentures are those debentures which are paid after making the payment of first debentures.
(iv) From Recording Point of View :From recording point of view debentures can be classified into two categories bearer and registered debentures.
(a) Bearer Debentures :Bearer Debentures are transferable per bearer without endorsement and they are just like bearer cheques or government currency notes. They are treated as negotiable instrument and transferable by mere delivery. It is not necessary that transfer of such debentures should be registered with the company. The interest is paid to the holder irrespective of identity.
(b) Registered Debentures: Registered debentures are made out in the name of a particular person who is registered by the company as a holder and are transferable in the same way as shares.
The payment of interest and repayment of capital is made to those whose name are registered with the company and duly entered in the register of debenture holders.
(v) From Conversion Point of View: From conversion point of view debentures may be convertible or non-convertible.
(a) Convertible Debentures :Convertible debenture holders are given an option to convert them into equity or preference shares at a stated rate of exchange after a certain period. Convertible debentures are very popular these days with the companies as it provides them a major source of permanent working capital. It also provides safety, liquidity, capital appreciation and assured return to the investors.
(b) Non-Convertible Debentures: Non-convertible debentures are not convertible into equity or preference shares afterwards.

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