

1. Details of Module and its structure

Module Detail	
Subject Name	Accountancy
Course Name	Accountancy 04 (Class XII, Semester – 2)
Module Name/Title	Redemption of Debentures – Basics Concepts & Redemption by Lump Sum Payment Method – Part 5
Module Id	leac_20205
Pre-requisites	Knowledge about Issue of Shares; Basics of Issue of Debentures
Objectives	After going through this lesson, learners will be able to understand the following: <ol style="list-style-type: none">1. Meaning of Redemption of Debentures2. Sources of Redemption of Debentures3. Methods of Redemption of Debentures4. Provisions related to DRR & DRI5. Redemption of Debentures by lump sum payment on maturity.
Keywords	Redemption of Debentures; Sources of Redemption; Methods of Redemption; DRR; DRI;

2. Development Team

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1. Meaning of Redemption of Debentures

Redemption of debentures
refers to
REPAYMENT TO DEBENTUREHOLDERS
or
DISCHARGING THE LIABILITY ON ACCOUNT OF DEBENTURES
in accordance with the terms of issue.

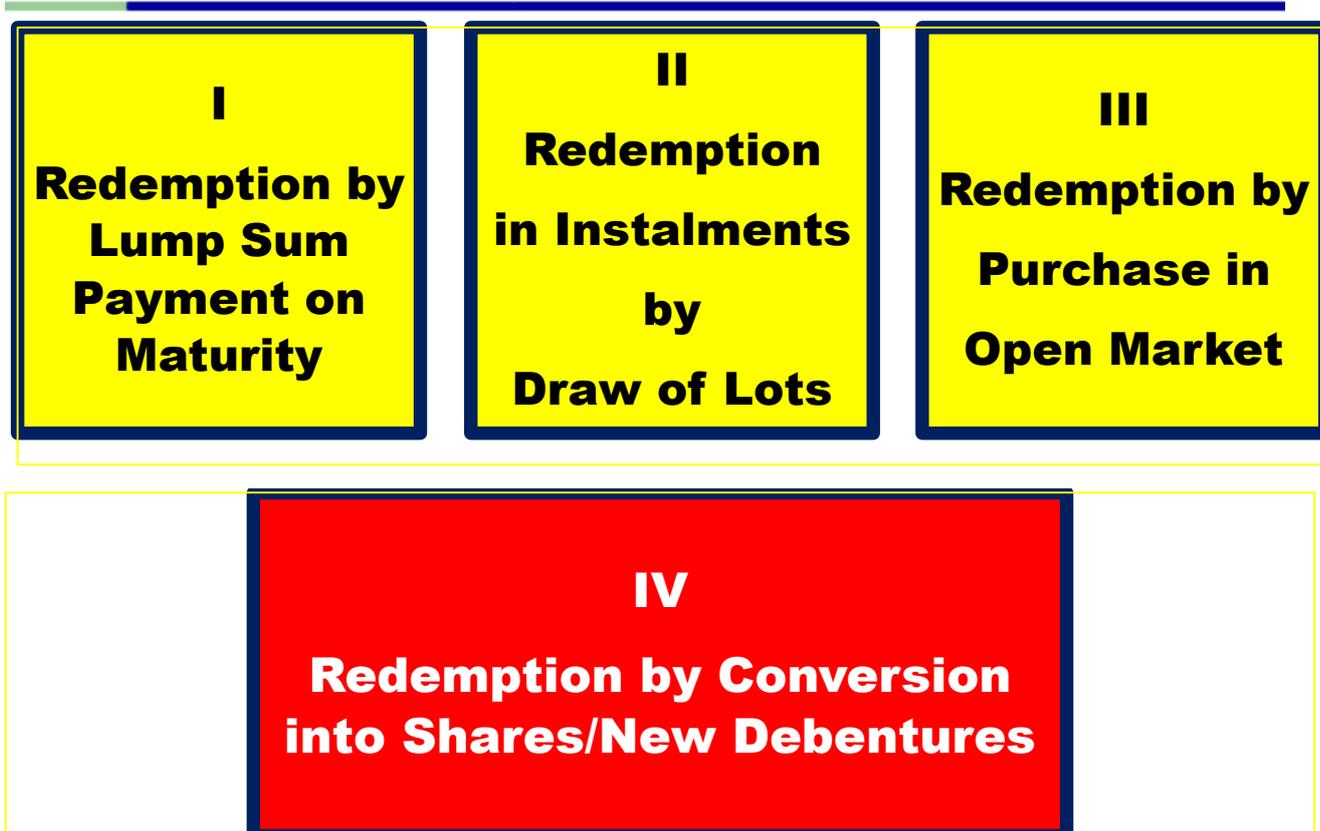
2. Sources of Redemption of Debentures



A	PROFITS	Redemption Out of Profits
B	CAPITAL	Redemption Out of Capital
C	COMBINATION OF PROFITS & CAPITAL	Redemption Partly Out of Profits & Partly Out of Capital

3. Methods of Redemption of Debentures

Following are the four methods by which debentures can be redeemed:



Note: First three methods involve Outflow of Cash & require to meet certain special provisions. Whereas, in fourth method there is no movement of cash.

Method 1 – Redemption by Payment in Lump Sum on Maturity:

- ⇒ Lump Sum means in Single Instalment.
- ⇒ When a company redeems debentures by paying full amount to debenture holders on maturity, it is termed as ‘Redemption of debentures by Lump Sum Payment’.

Method 2 – Redemption in Instalments by Draw of Lots:

- Under this method, redemption of debentures is made in instalments on the specified dates during the tenure of the debentures.
- Total debenture are divided into certain instalments considering the life of debentures.
 - Actual debentures redeemable in each instalments are identified by means of drawing of lot out of the debentures outstanding.

Method 3 – Redemption by Purchase of Own Debentures in Open Market:

When a company purchases its own debentures for the purpose of cancellation, such an act of purchasing and cancelling the debentures is termed as ‘Redemption of Debentures by Purchase in Open Market’.

Method 4 – Redemption of Debentures by Conversion into Shares or new Debentures:

A company can redeem its debentures by converting them into shares or new class of debentures.

- ⇒ If debenture holders find that the offer is beneficial to them, they can exercise their right of converting their debentures into shares or new class of debentures.
- ⇒ In this case new shares or debentures can be issued at Par, at a premium or at a Discount*.
(*only Debentures can be issued at discount)
- ⇒ It should be noted that only **Actual Proceeds** i.e. the actual amount received towards the Face Value of debentures should be considered for ascertaining the number of Shares to be issued for the debentures to be converted.

Situation (a) - If 1,000 9% Debentures of ₹100 each were issued at par

Actual Proceeds towards Face Value of Debentures are $1,000 \times 100 = ₹ 1,00,000$

Situation (b) - If 1,000 9% Debentures of ₹100 each were issued at 10% discount

Actual Proceeds towards Face Value of Debentures are $1,000 \times 90 = ₹ 90,000$

Situation (c) - If 1,000 9% Debentures of ₹100 each were issued at 20% premium

Actual Proceeds towards Face Value of Debentures are $1,000 \times 100 = ₹ 1,00,000$

- Note:**
- i. Actual Proceeds are considered only if Debentures are converted into Shares before the Maturity Date.
 - ii. If Debentures are Converted into shares on their maturity date then we will take the amount as per the condition of Redemption.

Note:

i. Time of redemption of debentures: Generally, debentures are redeemed on due date but a company may redeem its debentures before maturity date, if its articles provides so.

ii. Odd one out : Redemption by Conversion into Shares or new class of Debentures is an odd one out

method. In other three methods payment is made to debentureholders in one or the other way whereas, in fourth method payment is not made at all.

4. Provisions related to DRR & DRI

☆ **DEBENTURE REDEMPTION RESERVE (DRR)**

It is a special reserve created out of distributable profits* for the purpose of redemption of debentures. (* profits available for distributing as dividend.)

- This reserve (if required) can be created at any time before the redemption of debentures begins, in a single instalment or in several instalments.
- This reserve cannot be used for any purpose other than Redemption of Debentures.

☞	Are all companies bound to create DRR for Redemption?
	No, Following table shows companies required to create DRR & companies exempted:

As per the prevailing rule {Rule 18(7) (b) of the Companies (Share Capital and Debentures) Rule 2014}:

Following companies are REQUIRED TO CREATE DRR (For Public Issue)	Following companies are EXEMPTED FROM CREATING DRR (For both Public Issue & Private Placement)
<p style="text-align: center;">UNLISTED COMPANIES (other than NBFCs and HFCs registered with RBI)</p> <p>➤ They are required to create DRR which shall not be less than 10% of the Nominal value of Outstanding Debentures.</p>	<p>i. All India financial institutions registered with RBI, ii. Banking companies, iii. NBFCs registered with Reserve bank of India, iv. Housing Finance companies registered to the National Housing bank; & v. Other LISTED COMPANIES</p>
<p>☞ These companies cannot redeem debentures fully Out of Capital.</p>	<p>☞ These companies can redeem debentures ‘Out of Capital’.</p>
<ul style="list-style-type: none"> • But these companies are not required to create DRR, in case of Convertible Debentures or Partly Convertible (to the extent they are convertible). 	<p>vi. Unlisted Companies (other than i & ii i.e. AIFIs and Banking Co.s) are also exempted but only in case of Privately placed debentures.</p>
<p><i>For Unlisted Companies (other than NBFCs & HFCs) it is compulsory to create minimum 10% DRR. But as such there is no upper limit, if they wish they can create even 100% DRR i.e. companies can redeem debentures fully out of profits.</i></p>	

#1 Distributable Profits include, General Reserve, Surplus i.e. Balance in Statement of P & L, Dividend Equilisation Reserve and any other reserve which is available for distribution as dividend.

AT ANY TIME BEFORE REDEMPTION

To create Debenture Redemption Reserve (DRR), following Journal Entry will be passed for:

Transfer of 'Divisible Profits' to DRR

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
	Surplus i.e. Balance in Statement of Profit & Loss A/c Dr. General Reserve A/c Dr. To Debenture Redemption Reserve A/c (Being profits / free reserve transferred to DRR.)			

* Even 'Dividend Equalisation Reserve can be used to create DRR (If available & if required.)

IMMEDIATELY AFTER REDEMPTION

After redemption, balance of Debenture Redemption Reserve (DRR) is transferred to General Reserve by passing the following journal entry:

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being proportionate DRR transferred to General Reserve.)			

Note: Unless and until Debentures are redeemed, balance in DRR is shown under the head 'Shareholders Funds' and sub-head 'Reserves and Surplus'.

☆ DEBENTURE REDEMPTION INVESTMENT (DRI)

It is a special investment made to ensure some liquidity (funds) at the time of redemption.

Debenture Redemption Investment is made

On or before 30th April,

minimum 15% of Nominal Value of Debentures

DUE FOR REDEMPTION	
During the financial year	
Must be Invested in Specified Securities.	
☞	Are all the companies bound to purchase Specified Securities for DRI?
	Not all but most of the Listed & Unlisted Companies (excluding those governed by RBI & National Housing Bank) are required to make DRI.

Following table shows companies required to purchase DRI & companies exempted:

As per the prevailing rule {Rule 18(7)(b) of the Companies (Share Capital and Debentures) Rule 2014}:

Category 'A'^{#1} COMPANIES REQUIRED TO CREATE DRI (For Public Issue)	Category 'B'^{#1} COMPANIES EXEMPTED FROM CREATING DRI
<p>1. Listed Companies (other than AIFIs and Banking Companies) (for Public Issue & Private Placement)</p> <ul style="list-style-type: none"> - NBFCs registered with RBI - HFCs registered with National Housing Bank - Other Listed Companies <p>2. Other Unlisted Companies (other than NBFCs and HFCs)</p>	<p>1. AIFIs regulated by RBI</p> <p>2. Banking Companies</p> <p>3. Unlisted Companies (For Private Placement) (other than AIFIs and Banking Companies)</p> <ul style="list-style-type: none"> - NBFCs registered with RBI - HFCs registered with National Housing Bank

Companies bound to make DRI have to invest or deposit the required amount on or before April 30. This sum shall not be less than 15% of the amount of debentures maturing during the year ending on March 31 of the next year.

This investment (DRI) can be made in anyone or more of the following:

- (i) Deposit with any scheduled bank, free from any charge or line;
- (ii) Securities of the Central Government or of any State Government;
- (iii) Securities mentioned in sub clauses (a) to (d) and (ee) of section 20 of the Indian Trusts Act, 1982;
- (iv) Bonds issued by any other company which is notified under sub clause (f) of section 20 of the Indian Trusts Act, 1982;
- (v) The amount invested or deposited as above shall not be used for any purpose other than for redemption of debentures maturing during the year referred above;

★ Securities Exchange Board of India (SEBI) ensures transfer of divisible profit equal to minimum 10% of

Outstanding Debentures to DRR & Purchase of DRI Securities not less than 15% of debentures due for redemption in a financial year, to protect the interest of Debenture holders.

5. Redemption of Debentures by Lump Sum payment on maturity

When company pays the whole amount in lump sum on maturity, it is termed as 'Redemption by Lump Sum on Maturity'.

In this method following journal entries are recorded in the books of a company:

PROCESS OF REDEMPTION INCLUDES FOLLOWING STEPS



Step	Journal Entries		
①	Transfer the required amount to Debenture Redemption Reserve (DRR)		
	General Reserve A/c Dr. Surplus i.e. Balance in Statement of P & L Dr. To Debenture Redemption Reserve (DRR) A/c (Reserves/profits transferred to DRR.)		
②	Investment in Specified Securities to fulfil the condition of DRI		
	Debenture Redemption Investment A/c Dr. To Bank A/c (Investment made in specified securities equal to 15% of Debentures due for redemption in financial year.)		
③	Sell Investment (DRI) or Realise Debenture Redemption Investment Deposits		
	Bank A/c Dr. To Debenture Redemption Investment A/c (Specified securities sold or deposits realized for redemption.)		
④	Make Redemption Due		
	<u>If debentures are redeemed at Par</u> % Debentures A/c Dr. To Debentureholders A/c (...% Debentures due for redemption at par.)	<u>If debentures are redeemed at Premium</u> % Debentures A/c Dr. Premium on Redemption of Debenture A/c Dr. To Debentureholders A/c (...% Debentures due for redemption at ...% premium.)	
⑤	Make Payment to Debentureholders		

	Debentureholders A/c To Bank A/c (Payment made to debentureholders.)	Dr.		
⑥ Close DRR A/c by Transferring the balance to General Reserve A/c				
	Debenture Redemption Reserve A/c To General Reserve A/c (DRR A/c closed by transferring to general reserve.)	Dr.		

ILLUSTRATION 1 (Assuming DRR & DRI are not required)

Give the necessary journal entries at the time of redemption of debentures in each of the following cases.

i. On 1 st April, 2015 X Ltd. issued 5,000, 9% debentures of ₹100 each at par and redeemable at par at the end of 5 years, out of capital.
ii. On 1 st April, 2016 X Ltd. issued 1,000, 12% debentures of ₹100 each at par. These debentures are redeemable at 10% premium at the end of 4 years.
iii. On 1 st April, 2016 X Ltd. issued 8% debentures of the total face value of ₹1,00,000 at premium of 5% to be redeemed at par at the end of 4 years.
iv. On 1 st April, 2015 X Ltd. issued ₹1,00,000, 11% debentures at a discount of 5% but redeemable at a premium of 5% at the end of 5 years.

SOLUTION:

Case i. On 1st April, 2015 X Ltd. issued 5,000, 9% debentures of ₹100 each at par and redeemable at par at the end of 5 years, out of capital.

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020 Mar 31	9% Debentures A/c To Debentureholders A/c (5,000 9% debentures due for redemption at par.)		5,00,000	5,00,000
Mar 31	Debentureholders A/c To Bank A/c (Payment made to debentureholders.)		5,00,000	5,00,000

Case ii. On 1st April, 2016 X Ltd. issued 1,000, 12% debentures of ₹100 each at par. These debentures are redeemable at 10% premium at the end of 4 years.

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020	12% Debentures A/c Dr.		1,00,000	
Mar 31	Premium on Redemption of Debentures A/c Dr. To Debenture holders A/c		10,000	1,10,000
	(1,000 12% debentures due for redemption at premium.)			
Mar 31	Debenture holders A/c Dr. To Bank A/c		1,10,000	1,10,000
	(Amount paid to debenture holders.)			

Case iii. On 1st April, 2016 X Ltd. issued 8% debentures of the total face value of ₹1,00,000 at premium of 5% to be redeemed at par at the end of 4 years.

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020	8% Debentures A/c Dr.		1,00,000	
Mar 31	To Debenture holders A/c			1,00,000
	(₹1,00,000 8% debentures due for redemption at 5% premium.)			
Mar 31	Debenture holders A/c Dr. To Bank A/c		1,00,000	1,00,000
	(Amount paid to debenture holders.)			

Case iv. On 1st April, 2015 X Ltd. issued ₹1,00,000, 11% debentures at a discount of 5% but redeemable at a premium of 5% at the end of 5 years.

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020	11% Debentures A/c Dr.		1,00,000	
Mar 31	Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c		5,000	1,05,000
	(₹1,00,000 8% debentures due for redemption at 5% premium.)			
Mar 31	Debentureholders A/c Dr. To Bank A/c		1,05,000	1,05,000
	(Amount paid to debentureholders.)			

ILLUSTRATION 2

XYZ Ltd. issued 200, 11% debentures of ₹ 100 each on April 01, 2017 at discount of 10% redeemable at premium of 10%.

Debentures are to be redeemed in lump sum at the end of 4th year.

The company has invested requisite amount in specified securities. Pass the necessary journal entries for issue and redemption if:

Case (a) XYZ Ltd. is a listed company **Case (b)** XYZ is "other unlisted" company.

Note: 1. Listed Companies are not required to create DRR but they must invest 15% of nominal value of debentures due for redemption in specified securities (DRI).

2. Other Unlisted companies are required to create minimum 10% DRR.

3. If a company decides to carry out redemption 'Out of Profits', it will create DRR equal to 100% of Nominal Value of Debentures.

SOLUTION:

Common Journal Entries for Issue of Debentures for all type of companies

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2017	Bank A/c Dr.		18,000	
Apr 1	To Debenture Application and Allotment A/c (Application money received on 200 debentures @ ₹90 each.)			18,000

Apr 1	Debenture Application and Allotment A/c	Dr.	18,000	
	Discount on issue of Debenture A/c	Dr.	2,000	
	Loss on issue of Debenture A/c	Dr.	2,000	20,000
	To 11% Debentures A/c			2,000
	To Premium on Redemption of Debentures A/c			
(Issue of Debentures at 10% discount and redeemable at 10% premium.)				

(a) XYZ Ltd. is a Listed Company – Journal Entries for Redemption of Debentures

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020 Apr 30	Debenture Redemption Investment A/c Dr. To Bank A/c (15% of ₹20,000, nominal value of debentures invested.)		3,000	3,000
2021 Mar 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investments sold at the time of redemption of debentures)		3,000	3,000
Mar 31	11% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (2,000 11% Debentures due on redemption at 10% premium.)		20,000 2,000	22,000
Mar 31	Debentureholders A/c Dr. To Bank A/c (Amount paid to Debentureholders)		22,000	22,000

(b) If 'XYZ Ltd.' is an Unlisted Company – Journal Entries for Redemption of Debentures

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2020 Mar 31	Surplus, i.e., Balance in Statement of Profit & Loss Dr. To Debenture Redemption Reserve A/c (DRR created @ 10% of outstanding debentures)		2,000	2,000
2020 Apr 30	Debenture Redemption Investment A/c Dr. To Bank A/c (15% of ₹20,000, nominal value of debentures invested.)		3,000	3,000
2021 Mar 31	Bank A/c Dr. To Debenture Redemption Investment A/c (Investments sold at the time of redemption of debentures)		3,000	22,000
Mar 31	11% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (2,000 11% Debentures due on redemption at 10% premium.)		20,000 2,000	22,000
Mar 31	Debentureholders A/c Dr. To Bank A/c (Amount paid to Debentureholders)		22,000	22,000
Mar 31	Debenture Redemption Reserve A/c Dr. To General Reserve (DRR Account closed by transferring to General Reserve.)		2,000	2,000

ILLUSTRATION 3.

1st April, 2015 VK Ltd., an 'other listed company' issued 60,000 9% debentures of ₹ 100 each at par redeemable at the end of **four and a half years** at a premium of 20%.

On this date there existed a balance of ₹ 5,00,000 in Securities Premium Reserve Account.

The company transferred the required amount to Debenture Redemption Reserve in 3 equal instalments on March 31, 2017, 2018 and 2019.

It invested in specified securities (DRI) the required amount on 1st April of the financial year in which debentures were redeemed.

Record the necessary journal entries for redemption process. Also show journal entry for writing off 'Loss on Issue of Debentures'.

SOLUTION:

JOURNAL

DATE	PARTICULARS	LF	DR. Amt. in ₹	CR. Amt. in ₹
2016				
Mar 31	Securities Premium Reserve A/c Dr. Statement of Profit & Loss Dr. To Loss on Issue of Debentures A/c (Loss on issue of debentures written off.)		5,00,000 7,00,000	12,00,000
2017				
Mar 31	Surplus i.e. Balance in Statement of P & L Dr. To Debenture Redemption Reserve A/c (Profits transferred to DRR.)		2,00,000	2,00,000
2018				
Mar 31	Surplus i.e. Balance in Statement of P & L Dr. To Debenture Redemption Reserve A/c (Profits transferred to DRR.)		2,00,000	2,00,000
2019				
Mar 31	Surplus i.e. Balance in Statement of P & L Dr. To Debenture Redemption Reserve A/c (Profits transferred to DRR.)		2,00,000	2,00,000
2019				
April 1	Debenture Redemption Investment A/c Dr. To Bank A/c (15% of ₹60,00,000, nominal value of debentures invested.)		9,00,000	9,00,000
2019				
Sep 30	Bank A/c Dr. To Debenture Redemption Investment A/c		9,00,000	9,00,000

	(Investments sold for redemption of debentures)			
Sep 30	9% Debentures A/c Dr.	60,00,000		
	Premium on Redemption of Debentures A/c Dr.	12,00,000		
	To Debentureholders A/c			72,00,000
	(60,000 9% Debentures due on redemption at 20% premium.)			
Sep 30	Debentureholders A/c Dr.	72,00,000		
	To Bank A/c			72,00,000
	(Amount paid to Debentureholders)			
Sep 30	Debenture Redemption Reserve A/c Dr.			
	To General Reserve		6,00,000	
	(DRR Account closed by transferring to General Reserve.)			6,00,000

Note: 1. Full amount of 'Loss on Issue of Debentures A/c' is written off in the year of issue, using Securities Premium Reserve to the extent of availability and excess by debiting Statement of P & L.