

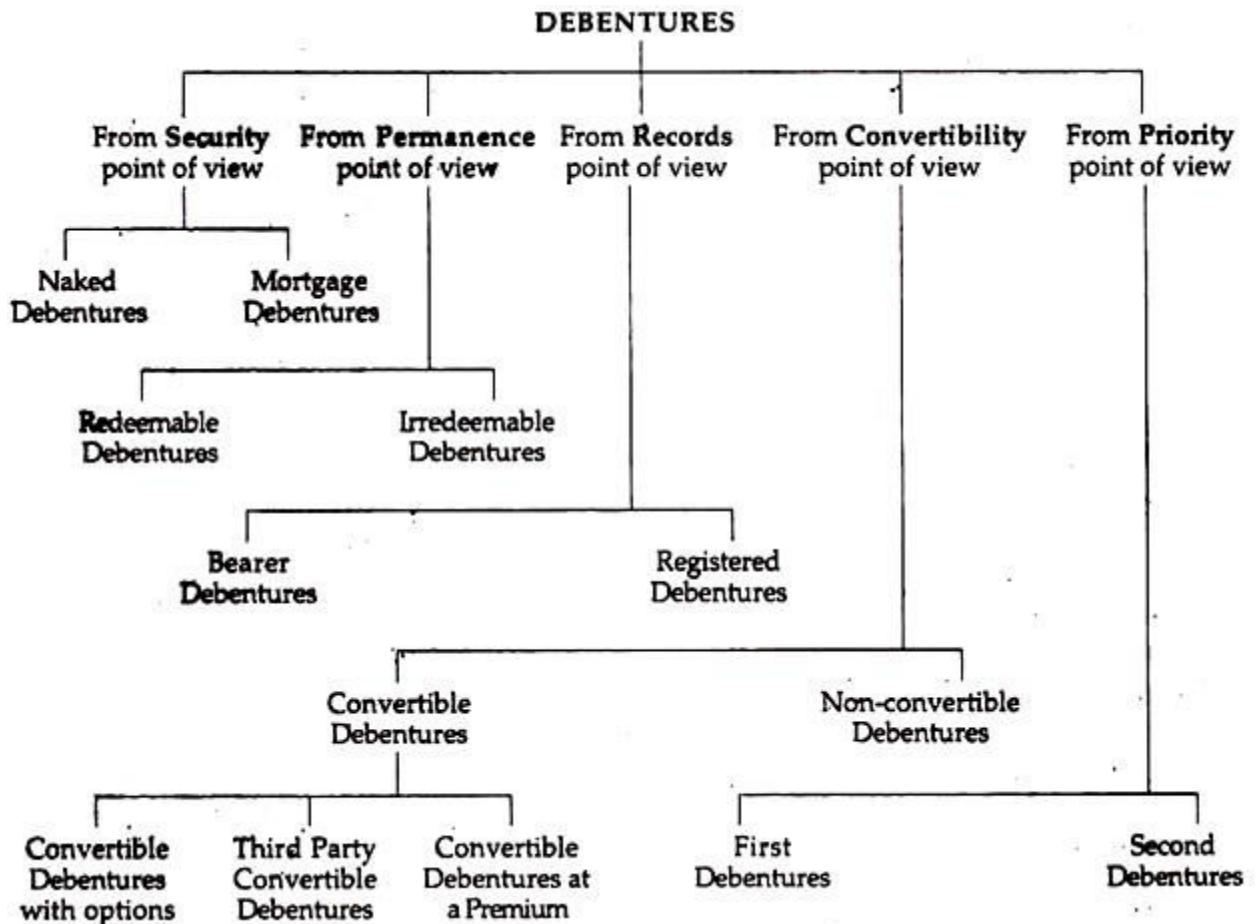


# Issue of Debentures

# 9

## CHAPTER

1. **Debenture** : It is an instrument acknowledging a debt issued the common seal of the company. It specifies nominal/par value of debenture, the rate of interest to be paid, periodicity of payment, the tenure of debentures and terms of redemption.
2. **Bond**:It is also an instrument of acknowledgement of debt. Bond is similar to debenture in terms of contents and texture. However, bonds can be issued without pre-determined rate of interest.
3. **Debentures are classified from various points of view, such as:**



**(a) From Security point of view:**

1. Naked Debentures/Unsecured: When Debentures are issued without any security (i.e., unsecured debentures) in respect of interest or the repayment of the principal, they are called Naked Debentures. Solvency of the company is the only security.
2. Mortgage Debentures/Secured Debentures: When debentures are secured by a charge (fixed charge when a particular asset is mortgaged and floating charge when general assets are mortgaged) on the assets of the company, these are known as Mortgage Debentures.

**(b) From Permanence point of view:**

1. Redeemable Debentures: These are those which are redeemed either at par or at a discount or at a premium after the expiry of the stipulated period; maximum period is 20 years. The same can be reissued even after redemption if not cancelled.

2. Irredeemable on Perpetual Debentures: These debentures are not redeemed until and unless the company goes into liquidation. At present, in our country, these Debentures cannot be issued as per Companies Act.

**(c) From Records point of view:**

1. Bearer Debentures: These debentures are just like negotiable instruments and are transferable by simple delivery, i.e., transfer of debentures is not to be registered with the company. Interest is paid at the end of the stipulated period to the persons who will possess them. In short, interest is paid to the holders irrespective of identity.
2. Registered Debentures: Here, the transfer of debentures will be effected on execution of a transfer deed or interest is payable or the repayment of debentures is made to that person whose name is registered in the books of the company. Registered Debentures can be transferred but the same has to be registered again. However, Registered Debentures are not negotiable instruments. It contains a commitment to pay the principal as well as interest.

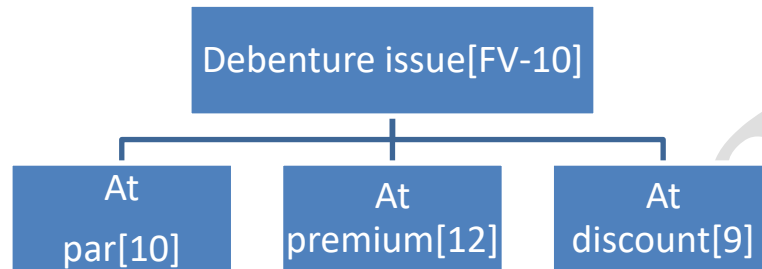
**(d) From Convertibility point of view:**

1. Convertible Debentures: Sometime debentures can be converted into preference shares or equity shares at a fixed rate of exchange after a certain period. Such debentures are called convertible debentures, These debentures are very popular in our country. After conversion the holders become the owner and ceases to be a lender.
2. Non-Convertible Debentures: These debenture holders have no right to convert their debentures to either equity or preference shares.

**(d) From Priority point of view:**

1. First Debentures: These debentures are those which are repaid before the other debentures are paid.
2. Second Debentures: These debentures are those which are paid after the first debentures are paid.
4. **Issue of debentures:** Debentures, whether issued for cash or otherwise, may be issued at
  - (i) **At Par:** These are said to be issued at par when the issue price and face value of the debentures is same.

- (ii) **At Premium:** These are said to be issued at a premium when the issue price is more than the face value.
- (iii) **At Discount:** These are said to be issued at a discount when they are issued at a price below its nominal or face value.



### 5. Issue of Debentures for Cash

Accounting treatment of issue of debentures can be discussed under two heads

- (i) When Debenture Amount is Received in Lumpsum  
(If the full amount is payable along with application)

Transaction	Entry
On Receipt of Application Money	Bank A/c Dr. To Debenture Application and Allotment A/c
At par	Debenture Application and Allotment A/c Dr. To X % Debentures A/c
At premium	Debenture Application and Allotment A/c Dr. To X % Debentures A/c To Securities Premium Reserve A/c
At Discount	Debenture Application and Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To X % Debentures A/c
On Refund of Excess Application Money	Debenture Application and Allotment A/c Dr. To Bank A/c

- (ii) When Debenture amount is received in instalments

On receipts of applications	Bank A/c Dr. To Debenture Application A/c
On acceptance of applications	Debenture Application A/c Dr. To % Debenture A/c

On adjustment of excess debenture application money	Debenture Application A/c Dr. To Debenture allotment A/c
On refund of excess debenture application money	Debenture application A/c Dr. To Bank A/c
On making allotment money due	<b>At par</b> Debenture Allotment A/c Dr. To X % Debentures A/c  <b>At Premium</b> Debenture Allotment A/c Dr. To X % Debentures A/c To Securities Premium Reserve A/c  <b>At discount</b> Debenture Allotment A/c Dr. Discount on issue of Debentures A/c Dr. To X % Debentures A/c
On receipt of allotment money	Bank A/c Dr. To Debenture Allotment A/c
On making calls	Debenture call A/c Dr. To % debentures a/c
On receipt of call money	Bank A/c Dr. To Debenture call A/c

#### 6. Issue of Debentures for Consideration other than cash

When debentures are issued to vendors against purchase of assets or against purchase of business, it is termed as issue of debentures for consideration other than cash.

In this case, consideration for issue of debentures is not cash but the assets or business.

On Purchase of assets or business	<ul style="list-style-type: none"> <li><b>When assets are purchased</b></li> </ul> Sundry Assets A/c Dr. To Vendor's A/c
	<ul style="list-style-type: none"> <li><b>When business is purchased</b></li> </ul> Sundry assets A/c Dr. Goodwill A/c* To Sundry Liabilities A/c To Vendor's A/c To Capital Reserve A/c*
On issue of debentures	<ul style="list-style-type: none"> <li><b>When debentures are issued at par</b></li> </ul> Vendor's A/c Dr. To X % Debentures A/c
	<ul style="list-style-type: none"> <li><b>When debentures are issued at premium</b></li> </ul> Vendor's A/c Dr. To X% Debentures A/c To Securities Premium Reserve A/c
	<ul style="list-style-type: none"> <li><b>When debenture are issued at discount</b></li> </ul> Vendor's A/c Dr. Discount on Issue of Debentures A/c Dr. To X% Debentures A/c

**(i) Issue of Debentures to Promoters**

Formation Expenses/ Incorporation Cost/Goodwill A/c Dr.  
To % Debentures A/c

**(ii) Issue of Debentures to Underwriters**

Making underwriting expenses due	Underwriting Expenses A/c Dr. To Underwriters A/c
Issuing debentures to underwriters	Underwriters A/c Dr. To % Debentures A/c
	Statement of Profit and Loss Dr. To Underwriting Expenses A/c

**7. Issue of Debentures as collateral Security:** When a company takes a loan, it may provide primary security on its assets. However, the lending institution may insist on some more assets as secondary or collateral security.

In such a situation, the company may issue debentures to the lender as secondary or collateral security such an issue of debentures is known as 'debentures issued as collateral security'.

Debentures issued as collateral security can be dealt in two ways:

- (i) **First Method** (Without passing any journal entry)  
 in this method, no journal entry is passed in the books for issue of debentures as collateral security. However, the fact that debentures have been issued as collateral security is disclosed in the balance sheet by way of information below debentures, which are shown as long-term borrowings under non-current liabilities or as short-term borrowings under current liabilities.
- (ii) **Second Method** (withy journal entry)  
 Debentures issued as collateral security may be recorded in the books of accounts. Following journal entry will be passed for issue of debentures as collateral security:

Debenture Suspence A/c	Dr.	[This appears on Assets side]
To % Debentures A/c		[This appears on liabilities side]

When the loan is paid, the above entry is cancelled by passing its reverse entry. In balance sheet, debentures issued as collateral security must be shown separately from other debentures.

8. **Interest on Debentures:** Interest on debentures is considered as an expense. It profits of the company and is payable irrespective of the fact whether there are profits or not.

Entries for interest on debentures as follows

When Interest is due	Debentures Interest a/c To Debentureholders' A/c To TDS/Income Tax Payabl A/c	Dr.	[With gross interest] [with net interest][with income tax deducted]
When interest is paid	Debentureholders' A/c To Bank or Cash A/c	Dr.	[with net interest]
On payment of income tax to government	TDS/Income Tax payable A/c To Bank A/c	Dr.	[with net amount of income tax deducted at source]
On transfer of interest on debentures	Statement of profit and loss To debenture interest A/c	Dr.	[with the amount of interest]

## 9. Various Cases from the Point of view of Redemption

As the issue can be made at par, at premium or at discount, the redemption of debentures can be either at par or at premium. Combining various conditions/terms of issue and redemption of debentures, there may be following possibilities:

When debentures are issued at par and redeemable at par, i.e. redeemable value is equal to the face value	Bank A/c                      Dr. To Debenture Application A/c
	Debenture Application A/c Dr. To % Debentures A/c
When debentures are issued at par and redeemable at premium, i.e. in excess of nominal value	Bank A/c                      Dr. To X% Debentures A/c
	Debenture Application A/c Dr. Loss on issue of debentures A/c                      Dr. To X% Debenture A/c To Premium on Redemption of Debentures A/c
When debentures are issued at a discount and are redeemable at par	Bank A/c                      Dr. To Debenture Application A/c
	Debenture Application A/c Dr. Discount on issue of Debentures A/c                      Dr. To X% Debentures A/c
When debentures are issued at a discount and are redeemable at premium	Bank A/c                      Dr. To Debenture Application A/c
	Debenture Application A/c Dr. Discount on Issue of Debentures                      Dr. Loss on issue of Debentures Dr. To X% Debentures A/c To Premium on Redemption of Debentures A/c
	Debenture Application A/c                      Dr. Loss on Issue of Debentures A/c                      Dr.  To X% Debentures A/c To Premium on Redemption of Debentures A/c
When debentures are issued at a premium and redeemable at par	Bank A/c                      Dr. To Debenture Application A/c
	Debenture Application A/c n Dr. To X% Debentures A/c To Securities Premium Reserve A/c



When debentures are issued at a premium and are redeemable at premium	Bank A/c                      Dr. To Debenture Application A/c
	Debenture Application A/c    Dr. Loss on issue of debentures A/c    Dr. To X% Debentures A/c To Securities Premium Reserve A/c To Premium on Redemption of Debentures A/c

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