

REDEMPTION OF DEBENTURES

Meaning : Redemption of debentures means repayment of the due amount of debentures holders. It may be at par or at premium.

Time of Redemption:

- **At maturity :** When repayment is made at the date of maturity of debentures which is determined at the time of issue of debentures
- **Before maturity :** If articles of association and terms of issue mentioned in prospectus allows, then a company can redeem its debentures before maturity date

Redemption Methods

- **Redemption in Lump-sum :** When redemption of all debentures is made at the expiry of a specific period, as per the terms of issue.
- **Redemption by draw of lots :** In this method a certain proportion of debentures are redeemed each year being selected by draw of lots.
- **Redemption by purchases in open market :** If articles of association of a company authorize, it may purchase its own debentures from open market i.e. stock exchange
- **By Conversion into shares or other securities.**

Sources of Redemption of Debentures

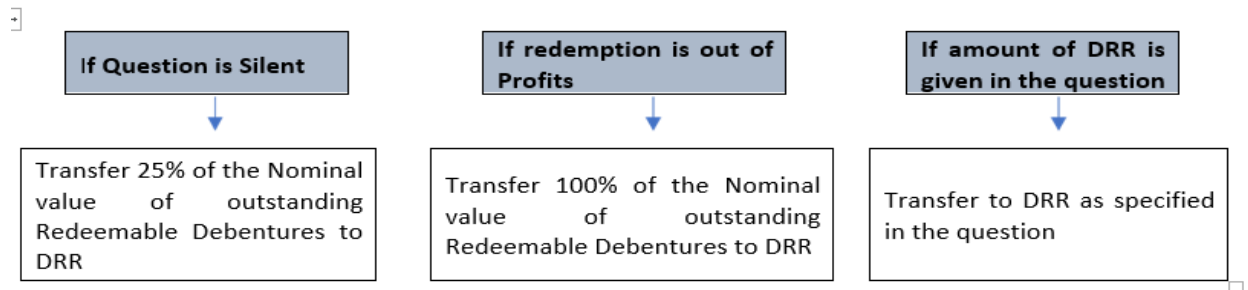
- Proceeds from fresh issue of Share Capital or Debenture holder.
- From accumulated profit.
- Proceeds from sale of fixed assets.
- A company may purchase its own debentures out of its surplus funds.

Two terms which are used in the redemption of debentures :

1. **Redemption out of capital :** When a company has not used its reserves or accumulated profits for redemption of its debentures, it is called redemption out of capital, Redemption only out of capital is not possible now as The Companies Act 2013 prescribes (other than those exempted from creating DRR) to transfer amount of profits available for Dividend as per rule 18(7) of companies Act 2013.
2. **Redemption out of profit :** Redemption out of profit means that adequate amount of profits is transferred to DRR A/c from Statement of Profit & Loss before the redemption of debenture commences. In this case Companies transfer 100% of Nominal value total Redeemable debentures to DRR before dividend payouts to shareholders.
3. **Redemption out of profit and capital:** It means redemption partially out of profits and partially out of capital. Here the company does not transfer 100% of nominal values of outstanding debentures to DRR out of surplus profits available for payment as dividend.

Debenture Redemption Reserve (DRR)

- Section 71 (4) of the companies Act, 2013. requires the company to create DRR out of the profits available for dividend and the amount created in DRR shall not be utilized for any purpose except redemption.
- Rule 18 (7) of Companies (share capital and Debentures) Rules, 2014 requires the following Companies shall transfer at least 25% of the nominal value of the outstanding debentures to DRR-
 - NBFCs registered with RBI
 - Financial institutions other than all India Financial Institutions regulated by RBI
 - Housing finance companies registered with National Housing Bank.
 - Any other company (whether listed or unlisted), DRR to be created for both public and private placed debenture.
- **Exemption to create DRR:-**
 - All India Financial Institutions regulated by RBI.
 - Banking Companies.
- **DRR can be created out of the below reserves:**
 - General Reserves
 - Dividend Equalization Reserves
 - Balance in P&L A/c
- **DRR is a specific reserve.** A company can utilize DRR only for redemption of Debentures.
- DRR is not required to be created on fully convertible debentures. And where the debentures are partly convertible, DRR is created on the non- convertible part of Debentures.
- Amount to DRR may be transferred by a Company in lump sum or in parts, but the minimum amount (25%) Of the face value of the outstanding debentures is credited to DRR before Redemption begins.



Journal Entry for Creating DRR

| Particulars | DR | CR |
|---|-------|-------|
| General Reserve A/c Dr | | |
| Dividend Equalization Reserve Ac DR | | |
| Surplus in P&L A/c Dr. | | |
| To DRR (Being the amount transferred to DRR) | | |

- Debentures having been redeemed, DRR is transferred to General Reserve.
- The company has 2 options to transfer DRR to GR:
 - Transfer proportionate amount after every redemption from DRR to GR, or
 - Transfer entire DRR to GR after all the Debentures are redeemed.

- DRR is shown under the main head 'Shareholders funds' and sub head 'Reserves and Surplus' in Balance Sheet.
- **Journal Entry for Transferring DRR to GR:**

| Particulars | DR | CR |
|--|-------|-------|
| Debenture Redemption Reserve A/c DR To General Reserve (Being the amount proportionate to debentures redeemed transferred from DRR to GR transferred to DRR) | | |

Debenture Redemption Investment (DRI) :

- As per rule 18 (7) (c), every company required to create / Maintain DRR shall invest or deposit before 30th April in specified securities a sum which shall not be less than 15% of the nominal value of debenture maturing or payment during the year ending 31st March of the next year.
- Specified Securities for DRI:
 - Deposits with any scheduled bank free from any charge
 - Unencumbered securities of Central Govt. and State Govt.
 - Unencumbered securities and bonds of Indian Trust Act.

Journal Entry for investment (DRI)

| Particulars | DR | CR |
|---|-------|-------|
| DRI Dr | | |
| To Bank | | |
| Being the investment made @ 15% in specified securities | | |

- DRI is to be made by only those Companies who are required to create DRR.
- DRI is not required for fully convertible Debentures and if the debentures are partly convertible, DRI is made of an amount to at least equal to 15% of the non- convertible portion only.

1)

Issue

| | | |
|---------------------------------|--|------------------------------|
| On receipt of application money | Bank A/c Dr. To Debenture Application A/c | With the appl money received |
|---------------------------------|--|------------------------------|

Allotments

| | | |
|----------------------------|--|---|
| On allotment of Debentures | Debenture Appl A/c Dr. To X% Debentures A/c | With Application Money on allotted deb. |
| | Debenture Appl Dr. | |

| | | |
|--|---|---|
| On refund of Excess Application Money | To Bank A/c | With the appl money refunded on rejected applications |
| On adjustment of excess App. Money with allotment | Debenture Appl Dr. To Debentures Allotment A/c | With surplus money adjusted with allotments |
| On Allotment being called | Debenture Allot A/c Dr. To X% Debentures A/c | With the Allotment money due on allotments |
| On receipt of allotment money | Bank A/c Dr To Debenture Allot A/c | With the Allotment money received on allotments |
| On calls being made | Debenture calls A/c Dr. To X% Debentures A/c | With the call money due on allotments |
| On receipt of calls money | Bank A/c To Debenture calls A/c | With the call's money received |
| When interest is Due on Debentures | Debentures Interest A/c Dr. To Debentures holder A/c To Income Tax/ TDS Payable A/c | (Gross Interest) (Net Interest) (Income Tax Deducted) |
| When Interest is paid to debenture Holders | Debentures Holder A/c Dr. To Bank A/c | (With Net Interest) |
| On payment of Income Tax to Government | Income Tax /TDS Payable A/c Dr. To Bank A/c | (TDS Amount) |
| On Transfer of Interest on Debenture to statement of profit and Loss A/c | Statement of Profit and Loss Dr. To Debenture Interest A/c | (Amount of gross Interest) |

Redemption

| | | |
|---|--|---|
| Creation of DRR @ 25% before redemption | General Reserve A/c Dr Dividend Equalization Reserve A/C Dr. Surplus in P&L A/c Dr. To DRR (Being the amount transferred to DRR) | 25 %/100% of the nominal value of debentures |
| On creation of DRI @ 15% | DRI Dr To Bank | Being the investment made @ 15% in specified securities |
| Sale of investments at the time of redemption | Bank Dr To DRI | Being the investment sold |
| On redemption of Debentures |% Debentures A/c Dr. To Debenture Holders A/c | With Nominal value of Debentures |
| For payment to Debenture holders | Debenture Appl Dr. To Bank A/c | Total amount paid |
| On movement of DRR to GR after redemption | Debenture Redemption Reserve A/c DR To General Reserve | |

2)

Issue

| | | |
|--|--------------|------------------------------|
| | Bank A/c Dr. | With the appl money received |
|--|--------------|------------------------------|

| | | | |
|---------------------------------|--|---|--|
| On receipt of application money | To Debenture Application Allotment A/c | & | |
|---------------------------------|--|---|--|

Allotments

| | | | |
|--|---|---|------------------------------------|
| Issued at par, redeemable at premium | Debenture Application Allotment A/c | & | With the appl money received |
| | Loss on issue of Debentures A/c Dr. | | With Prem. payable at redemption |
| | To ...% Debentures A/c | | With Nominal Value of Debenture |
| | To Premium on redemption of Deb A/c | | With Prem payable at redemption |
| issued at discount, redeemable at premium | Debenture Application Allotment A/c | & | With the appl money received |
| | Discount on issue of Debentures A/c | | With Discount on issue |
| | Loss on issue of Debentures A/c Dr. | | With Premium payable at redemption |
| | To ...% Debentures A/c | | With Nominal Value of Debenture |
| | To Premium on redemption of Deb A/c | | With Premium payable at redemption |
| issued at Premium, redeemable at premium | Debenture Application Allotment A/c | & | With the appl money received |
| | Loss on issue of Debentures A/c Dr. | | With Premium payable on redemption |
| | To ...% Debentures A/c | | With Nominal Value of Debenture |
| | To Securities premium A/c | | With premium received on issue |
| | To Premium on redemption of Deb A/c | | With Premium payable at redemption |
| When interest is Due on Debentures | Debentures Interest A/c Dr. | | (Gross Interest) |
| | To Debentures holder A/c | | (Net Interest) |
| | To Income Tax/ TDS Payable A/c | | (Income Tax Deducted) |
| When Interest is paid to debenture Holders | Debentures Holder A/c Dr. To Bank A/c | | (With Net Interest) |
| On payment of Income Tax to Government | Income Tax /TDS Payable A/c Dr. To Bank A/c | | (TDS Amount) |
| On Transfer of Interest on Debenture to statement of profit and Loss A/c | Statement of Profit and Loss Dr. To Debenture Interest A/c | | (Amount of gross Interest) |

Redemption

| | | | |
|---|---|--|--|
| Creation of DRR @ 25% before redemption | General Reserve A/c Dr Dividend Equalization Reserve A/C Dr. Surplus in P&L A/c Dr. To DRR | | 25 %/100% of the nominal value of debentures |
|---|---|--|--|

| | | |
|---|---|---|
| | (Being the amount transferred to DRR) | |
| On creation of DRI @ 15% | DRI Dr To Bank | Being the investment made @ 15% in specified securities |
| Interest received on Securities invested | Bank A/c Dr | Net interest earned |
| | TDS collected (Receivable) A/c Dr | TDS deducted on Interest earned |
| | To Interest earned on securities <i>(to be calculated for the no of months for which investment was done)</i> | Gross Interest earned |
| | | |
| Sale of investments at the time of redemption | Bank Dr To DRI | Being the investment sold |
| On redemption of Debentures at premium |% Debentures A/c Dr. | With Nominal value of Debentures |
| | Premium on redemption of Debentures A/c Dr | Premium od redemption |
| | To Debenture Holders A/c | Gross amount payable |
| For payment to Debenture holders | Debenture Holders Dr. To Bank A/c | Total amount paid (including premium) |
| On movement of DRR to GR after redemption | Debenture Redemption Reserve A/c DR To General Reserve | |