

Accounting For Issue of Debentures

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Debentures – Meaning

- A debenture is an instrument issued by a company under its common seal as acknowledgment of a debt. It contains a contract for repayment of the principal amount on or before a specified date and for payment of interest at a fixed rate until the principal sum is repaid.
- According to Section 2 (12) of the Companies Act, 'debenture' includes "debenture stock, bonds and any other security of a company whether constituting a charge on the assets of the company or not".

Features of Debentures

- (i)* A certificate acknowledging the debt owned by a company to the person named therein.
- (ii)* Promise to repay the principal amount on or before a specified date.
- (iii)* Promise of periodic payment of interest at a fixed rate.
- (iv)* Precise details of the security, if any.

Types of Debentures

(1) On the basis of security:

- (i) Secured Debentures and
- (ii) Unsecured debentures,

(2) On the basis of Redemption:

- (i) Redeemable and
- (ii) Non – redeemable debentures,

(3) On the basis of Records:

- (i) Registered debentures and
- (ii) Bearer debentures and

(4) On the basis of Convertibility:

- (i) Convertible debentures – Fully Convertible and Partly Convertible
- (ii) Non- convertible debentures.

Types of Debentures

(5) On the basis of Priority:

- (i) First Debentures, and
- (ii) Second Debentures

(6) On the basis of coupon rate:

Usually debentures are issued with a specified rate of interest, which is called as coupon rate.

- (i) Debentures with fixed coupon rate,
- (ii) Debentures with floating coupon rate, and
- (iii) Zero coupon bond.

Terms of Issue of Debentures

- **Face Value or Nominal Value:**
Nominal value of debentures determined by the Company and mentioned on the face of debenture certificate.
- **Issue Price :** The price at which debentures are issued by the company.
- **Issue at Par**
Issue Price = Face Value
- **Issue at Premium**
Issue Price > Face Value
- **Issue at Discount**
Issue Price < Face Value

Terms of Redemption

- **Redemption at Par**

When debentures are redeemable at Face Value

- **Redemption at Premium**

When debentures are redeemable at an amount more than Face Value

Subscription of Public Issue of Debentures

- **Full Subscription**

No. of Debentures Applied = No. of Debentures issued/offered

- **Under Subscription**

No. of Debentures Applied < No. of Debentures issued/offered

- **Over Subscription**

No. of Debentures Applied > No. of Debentures issued/offered

Issue of Debentures for Cash at Par Redeemable at Par

1. For receiving application money

Bank A/c	Dr.
To Debenture Application A/c	

(Being application money received)

2. On allotment for transferring application money to Debentures account

Debentures Application A/c	Dr.
To Debentures A/c	

(Being application money transferred to Debentures A/c)

3. On allotment-for making due allotment money

Debentures Allotment A/c

Dr.

To Debentures A/c

(Being allotment money made due on ... debentures @
Rs. ..per debentures)

4. For receiving allotment money

Bank A/c

Dr.

To Debentures Allotment A/c

(Being allotment money received)

5. For making due call money

Debentures Call A/c Dr.

To Debentures A/c

(Being call money made due on... Debentures @ Rs... per debenture)

6. For receiving call money

Bank A/c Dr.

To Debentures Call A/c

(Being call money received)

Issue of Debentures at Premium Redeemable at Par

- *(i) When premium has been called on application*
the application money will consist of debenture money and premium. The amount received as premium should be credited to '**Security Premium Account.**' On allotment, application money will be transferred as:

Debentures Application A/c	Dr.
To Debentures A/c	
To Securities Premium A/c	

(Being application money transferred to debentures and security premium A/c)

Issue of Debentures at Premium Redeemable at Par

(ii) If the premium is called along with allotment money,

then entry for making due allotment money will be:

Debentures Allotment A/c Dr.

To Debentures A/c

To Securities Premium A/c

(Being allotment money, including premium made due)

Issue of Debentures at Premium Redeemable at Par

(iii) If the premium is demanded along with call money, the entry for making due call money will be:

Debentures	Call A/c	Dr.
	To Debentures A/c	
	To Securities Premium A/c	

(Being call money including premium made due)

Note:

Normally, it is mentioned in the question as to when premium is receivable - on application or on allotment or on call. If not mentioned, it is assumed that the premium is due along with allotment money.

Issue of Debentures at Discount Redeemable at Par

The amount of discount is recorded at the time of allotment, therefore the following entries should be passed for making allotment money due:

Debentures Allotment A/c Dr.

Discount on Issue of Debentures A/c Dr.

To Debentures A/c

(Being amount made due on allotment and adjusted discount)

Issue of Debentures for Cash at Par Redeemable at Premium

1. For receiving application money

Bank A/c Dr.
To Debenture Application A/c

(Being application money received)

2. On allotment for transferring application money to Debentures account

Debentures Application A/c Dr.
Loss on Issue of Debentures A/c Dr.
To Debentures A/c
To Premium on Redemption of Debentures A/c

(Being application money transferred to Debentures A/c and made provision for premium on redemption)

Issue of Debentures for Cash at Discount Redeemable at Premium

1. For receiving application money

Bank A/c **Dr.**

To Debenture Application A/c

(Being application money received)

2. On allotment for transferring application money to Debentures account

Debenture Application A/c **Dr.**

Discount on Issue of Debentures A/c **Dr.**

Loss on Issue of Debentures A/c **Dr.**

To Debentures A/c

To Premium on Redemption of Debentures A/c

(Being application money transferred to Debentures A/c, and made provision for premium on redemption)

Issue of Debentures as Collateral Security

- Debentures issued as collateral security means issue of debentures as a subsidiary or secondary security in addition to principal security for taking a loan.
- No interest is payable on such debentures.
- When loan is repaid the debentures issued as collateral security shall be released by the lender.
- If company fails to repay the loan and the lender is unable to recover the loan amount from the principal security, he can sell these debentures in the open market to realize his loan.

Accounting for Issue of Debentures as Collateral Security

(1) When no entry is passed:

In this case, the fact is disclosed in the balance sheet of the company that the loan is secured and the debentures have been issued as collateral security.

(2) When a company records the debentures issued as collateral security, following entry is passed:

Debenture Suspense A/c Dr.
 To Debentures A/c

(Being debentures issued as collateral security)

Note: *Debenture Suspense A/c is shown in the Balance Sheet of the company, under the head 'Other Non-Current Assets'.*

Issue of Debentures for consideration other than cash

- *A company can issue Debentures for purchase of an asset or for purchase of business.*
- ***(a) Entry for purchase of a fixed asset***

Fixed Assets A/c Dr.
To Vendor's A/c

(Being fixed assets purchased from vendor)

Notes: Vendor's A/c is credited with the amount of Purchase consideration.

- **(b) For purchase of business:**

Sundry Assets A/c

Dr.

Goodwill A/c (ii)

Dr.

To Sundry Liabilities A/c

To Vendor's A/c (i)

To Capital Reserve A/c (iii)

(Being business purchased)

Notes:

- (i) Vendor's A/c is credited by **purchase consideration**.
- Purchase consideration, if not given in the question, it will be equal to **net assets, i.e., Assets minus Liabilities**.
- (ii) If purchase consideration is given and it is more than net assets, then the difference shall be debited to **Goodwill A/c**.
- (iii) If purchase consideration is given and it is less than net assets, then the difference shall be credited to **Capital Reserve A/c**.

- ***For issue of debentures to vendors***

- (a) Issue of debentures at par:***

Vendor's A/c Dr.

To Debentures A/c

(Being debentures issued to vendor at par)

- (b) Issue of debentures at premium:***

Vendor's A/c Dr.

To Debentures A/c

To Securities Premium A/c

(Being debentures issued to Vendor at premium)

(c) Issue of debentures at discount:

Vendor's A/c Dr.
Discount on Issue of Debentures A/c Dr.
 To Debentures A/c

(Being debentures issued to vendor at discount)

Note : A working note should be prepared to calculate number of debentures to be issued.

$$\text{Number of debentures to be issued} = \frac{\text{Amount Payable}}{\text{Issue Price}}$$

Writing off discount/loss on issue of debentures

- Discount/loss on issue of debenture is a loss of capital nature and therefore be written off over a reasonable period. It can be written off by debiting to Securities Premium Account or to Capital Reserve Account.
- Alternatively discount/loss on issue of debentures can be gradually charged to the Profit and Loss A/c over the period of life of debentures.
- **For writing off discount/loss on issue of debentures following entry is passed:**

Security Premium A/c	Dr.
or Profit & Loss A/c	Dr.
To Discount/Loss on Issue of Debentures A/c	
(Being discount/loss on issue of debentures written off)	

Discount/Loss on issue of debentures – Amount to be written off

Fixed instalment method. This method is applied when debentures are redeemable in lump sum at the end of the specified period. In this case, the total amount of discount/loss on issue of debentures is spread equally over the period of life of debentures. Amount to be written off every year is calculated as under:

$$\frac{\text{Total Discount or Loss on Issue of Debentures}}{\text{Life of Debentures (No. of Years)}}$$

Writing off discount/loss on issue of debentures

Proportionate method. This method is applied when debentures are redeemable in instalments by annual drawings. In this case, the total amount of discount/loss on issue of debentures is spread over the period of debentures in the ratio in which the amount of debentures has been used in various years.

A company issued 10% Debentures of Rs. 3,00,000 at a discount of 2%, repayable by draw of lots in 3 equal instalments starting from the end of 1st year. Calculate the amount of discount to be written off every year.

Year	Outstanding Amount of Debentures	Ratio	Discount to be written off
1	3,00,000	3	$6,000 \times \frac{3}{6} = 3,000$
2	2,00,000	2	$6,000 \times \frac{2}{6} = 2,000$
3	1,00,000	1	$6,000 \times \frac{1}{6} = 1,000$
	Total	6	

Interest on debentures

1. When Interest becomes due:

Interest on Debentures A/c	Dr. (Total amt. due)
To Income Tax Payable (TDS) A/c	
To Debentureholders A/c	

1. For payment of interest to Debentureholders

Debentureholders A/c	Dr.
To Bank A/c	

Interest on debentures

3. When Income Tax Payable (TDS) is paid

Income Tax Payable (TDS) A/c Dr.

To Bank A/c

4. For closing Interest on Debentures A/c

Profit and Loss A/c Dr.

To Interest on Debentures A/c

Interest Accrued and Due and Interest Accrued but Not Due

- **Interest Accrued and Due** - When due date expired

Interest on Debentures A/c Dr.

 To Outstanding Interest on Deb. A/c

- **Interest Accrued but Not Due** - When due date not expired

Interest on Debentures A/c Dr.

 To Accrued Interest on Deb. A/c

Note: Both are shown in “Other Current Liabilities” in B/S.