

Redemption of Securities

S3 BBA - Corporate Accounting - Module III

S3 BCOM – Corporate Accounting – Module I

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In the slides to come

- Redemption of debentures
- Methods of redemption
- Accounting for debenture redemption
- Redemptions of preference shares
- Rules and Accounting

Redemption of Debentures

- Redemption of debentures refers to extinguishing or discharging the liability on account of debentures in accordance with the terms of issue.
- In other words redemption of debentures means repayment of the amount of debentures by the company.

Methods of Redemption of Debentures

- 1. Payment in lump sum
- 2. Payment in instalments
- 3. Purchase in the open market
- 4. By conversion into shares or new debentures

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- Payment in lump sum : The company redeems the debentures by paying the amount in lump sum to the debentureholders at the maturity thereof as per terms of issue.
 - Payment in instalments : Under this method, normally redemption of debentures is made in instalments on the specified date during the tenure of the debentures.

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- Purchase in the open market: Under this method, normally redemption of debentures is made by purchasing own debentures from the market by using accumulated profits of the company.
 - 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.

2.12 Redemption by Payment in Lump Sum

When the company pays the whole amount in lump sum, the following journal entries are recorded in the books of the company:

1. *If debentures are to be redeemed at par*

(a) Debentures A/c	Dr.
To Debentureholders	

(b) Debentureholders	Dr.
To Bank A/c	

2. *If debentures are to be redeemed at premium*

(a) Debentures A/c	Dr.
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Premium on Redemption of Debentures A/c	Dr.
To Debentureholders	

(b) Debentureholders
To Bank A/c

Dr.

Illustration 21

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

1. X Ltd. issued 5,000, 9% debentures of Rs. 100 each at par and redeemable at par at the end of 5 years out of capital.
2. X Ltd. issued 1,000, 12% debentures of Rs. 100 each at par. These debentures are redeemable at 10% premium at the end of 4 years.
3. X Ltd. issued 12% debentures of the total face value of Rs. 1,00,000 at premium of 5% to be redeemed at par at the end of 4 years.
4. X Ltd. issued Rs. 1,00,000, 12% debentures at a discount of 5% but redeemable at a premium of 5% at the end of 5 years.

Solution:**Journal**

<i>Date</i>	<i>Particulars</i>	<i>L.F.</i>	<i>Debit Amount (Rs.)</i>	<i>Credit Amount (Rs.)</i>
1.	9% Debentures A/c Dr. To Debentureholders A/c (Amount due on redemption debentures)		5,00,000	5,00,000
	Debentureholders A/c Dr. To Bank A/c (Payment made to debentureholders)		5,00,000	5,00,000
2.	12% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders (Amount due on redemption of debentures)		1,00,000 10,000	1,10,000
	Debentureholders A/c Dr. To Bank A/c (Payment made to debentureholders)		1,10,000	1,10,000

3.	12% Debentures A/c	Dr.	1,00,000	
	To Debentureholders A/c (Amount due on redemption)			1,00,000
	Debentureholders A/c	Dr.	1,00,000	
	To Bank A/c (Payment made to debentureholders)			1,00,000
4.	12% Debentures A/c	Dr.	1,00,000	
	Premium on Redemption of Debentures A/c	Dr.	5,000	
	To Debentureholders A/c (Amount due on redemption of debentures)			1,05,000
	Debentureholders A/c	Dr.	1,05,000	
	To Bank A/c (Payment made to debentureholders)			1,05,000

2.12.2 Redemption by Payment in Instalments

When, as per terms of the issue, the debentures are to be redeemed in instalments beginning from a particular year, the actual debentures to be redeemed are selected usually by draw of lots. At the time of redemption, the following journal entries will be recorded.

- | | | |
|-----|-------------------------|-----|
| (a) | Debentures A/c | Dr. |
| | To Debentureholders A/c | |
| (b) | Debentureholders A/c | Dr. |
| | To Bank A/c | |

Illustration 23

JK Ltd., a listed company, issued 6,000, 12% Debentures of 50 each at a premium of 5% on April 1, 2014. Interest on these debentures is payable annually on 31st March each year. The debentures are redeemable at par in four equal installments at the end of third, fourth, fifth and sixth year

You are required to pass journal entries at the time of issue and redemption of debentures in the books of the company.

Solution:**Books of JK Ltd.
JOURNAL**

<i>Date</i>	<i>Particulars</i>	<i>L.F.</i>	<i>Dr. (Rs.)</i>	<i>Cr (Rs.)</i>
2014 April, 1	Bank A/c Dr. To Debenture Application and Allotment A/c (Application money received on debentures)		3,15,000	3,15,000
April, 1	Debenture Application and Allotment A/c Dr. To 12% Debentures A/c To Securities Premium Reserve (Debenture Application money transferred to debentures and securities premium reserve)		3,15,000	3,00,000 15,000
2015 March, 31	Debenture Interest A/c Dr. To Debentureholders A/c (Interest due on debentures)		36,000	36,000
March, 31	Debentureholders A/c Dr. To Bank A/c (Payment of Interest)		36,000	36,000

2016					
March, 31	Debenture interest A/c Debentureholders A/c (Interest due on debentures)	Dr.	36,000		36,000
March, 31	Debentureholders A/c To Bank A/c (Interest due on debentures)	Dr.	36,000		36,000
2017					
March, 31	Debenture interest A/c Debentureholders A/c (Interest due on debentures)	Dr.	36,000		36,000
March, 31	Debentures A/c. To Debentureholders A/c (6000 = 1,500 debentures due on redemption)	Dr.	75,000		75,000
March, 31	Debentureholders A/c To Bank A/c (Amount paid to debentureholders including interest)	Dr.	1,11,000		1,11,000

2018 March, 31	Debentures Interest A/c To Debentureholders A/c (Interest due on 4,500 debentures)	Dr.	27,000	27,000
March, 31	12% Debentures A/c To Debentureholders A/c (6000 = 1,500 debentures due on redemption)	Dr.	75,000	75,000
March, 31	Debentures Holders A/c To Bank A/c (Amount paid to debentureholders including interest)	Dr.	1,02,000	1,02,000
2019 March, 31	Debentures Interest A/c To Debentureholders A/c (Interest due on 3000 debentures)	Dr.	18,000	18,000
March, 31	12% Debentures A/c To Debentureholders A/c (6000 = 1,500 debentures due on redemption)	Dr.	75,000	75,000
March, 31	Debentureholders A/c To Bank A/c (Amount paid to be debentureholders including interest)	Dr.	93,000	93,000

March, 31	Debentures Interest A/c To Debentureholders A/c (Interest due on 1,500 debentures)	Dr.	9,000	9,000
March, 31	12% Debentures A/c To Debentureholders A/c (6000 = 1,500 debentures due on redemption)	Dr.	75,000	75,000
March, 31	Debentureholders A/c To Bank A/c (Amount paid to debentureholders including interest)	Dr.	84,000	84,000

2.13 Redemption by Purchase in Open Market

When a company purchases its own debentures in the open market for the purpose of immediate cancellation, the purchase and cancellation of such debentures are termed as redemption by purchase in the open market. The advantage of such an option is that a company can redeem the debentures at its convenience whenever it has surplus funds. Secondly, the company can purchase them when they are available in market at a discount.

When the debentures are purchased from the market at a discount and cancelled, the journal entries are recorded as follows :

- 1. On purchase of own debentures for immediate cancellation*
Debit: Debentures A/c
Credit: Dr.
 To Bank A/c
 To Profit on Redemption of Debentures A/c
- 2. On transfer of Profit on Redemption*
Debit: Profit on Redemption of Debenture A/c
Credit: Dr.
 To Capital Reserve

In case, the debentures are purchased from the market at a price which is above the nominal value of debenture, the excess will be debited to loss on redemption of debentures. The journal entry in that case will be

- | | | |
|----|---|-----|
| 1. | Debentures A/c | Dr. |
| | Loss on Redemption of Debentures A/c | Dr. |
| | To Bank A/c | |
| 2. | Statement of profit and loss | Dr. |
| | To Loss on Redemption of Debentures A/c | |

Illustration 28

X Ltd. purchased its own debentures of Rs. 100 each of the face value of Rs. 20,000 from the open market for cancellation at Rs. 92. Record necessary journal entries.

Solution:**Books of X Limited
Journal**

<i>Date</i>	<i>Particulars</i>	<i>L.F.</i>	<i>Debit Amount (Rs.)</i>	<i>Credit Amount (Rs.)</i>
(1)	Debentures A/c Dr. To Bank A/c To Profit on Redemption of Debentures A/c (Own debentures purchased at Rs. 92 from the market)		20,000	18,400 1,600

(2)	Profit on Redemption of Debenture A/c To Capital Reserve (Transfer of profit on cancellation of debentures to capital reserve)	Dr.		1,600	1,600
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* Alternatively, the following two journal entries may be passed:

<i>Date</i>	<i>Particulars</i>	<i>L.F.</i>	<i>Debit Amount (Rs.)</i>	<i>Credit Amount (Rs.)</i>
	Own Debentures A/c To Bank A/c (Purchased its own debentures of Rs. 20,000 @ Rs. 92 each)		18,400	18,400
	Debentures A/c To Own Debentures A/c To Profit on Redemption of Debentures A/c (Own debentures purchased being cancelled)		20,000	18,400 16 00

2.14 Redemption by Conversion

As stated earlier the debentures can also be redeemed by converting them into shares or new debentures. If debentureholders find that the offer is beneficial to them, they will take advantage of this offer. The new shares or debentures may be issued at par, at a discount or at a premium.

Illustration 31

Arjun Plastics Limited redeemed 1,000, 15% debentures of Rs. 100 each by converting them into equity shares of Rs. 10 each at a premium of Rs. 2.50 per share. The company also redeemed 500 debentures by utilising Rs. 50,000 out of profit. Give the necessary journal entries.

Solution:

Books of Arjun Plastic Limited Journal

<i>Date</i>	<i>Particulars</i>	<i>L.F.</i>	<i>Debit Amount (Rs.)</i>	<i>Credit Amount (Rs.)</i>
	15% Debentures A/c To Debentureholders A/c (Amount due to debentureholders)	Dr.	1,00,000	1,00,000

Debentureholders A/c To Equity Shares Capital A/c To Securities Premium Reserve A/c (Issue of 800 equity shares at a premium of Rs. 2.50 per share)	Dr.	1,00,000	80,000 20,000
Debenture A/c To Debentureholders A/c (Amount due to debentureholders)	Dr.	50,000	50,000
Debentureholders A/c To Bank A/c (Payment to debentureholders)	Dr.	50,000	50,000

Redemption of preference shares Sec 80

- A company limited by shares if so *authorised by its Articles*, may issue preference shares which at the option of the company, are liable to be redeemed.
- the 'gap' created in the company's capital by the redemption of redeemable preference shares must be filled in by:
 - (a) the proceeds of a fresh issue of shares;
 - (b) the capitalisation of undistributed profits; or
 - (c) a combination of (a) and (b).

Accounting Entries

- 1. When new shares are issued at par

Bank Account Dr.

To Share Capital Account

(Being the issue of....shares of Rs... each for the purpose of redemption of preference shares, as per Board's Resolution No....dated.....).

-
- 2. When new shares are issued at a premium.

Bank Account Dr.

To Share Capital Account

To Securities Premium Account

(Being the issue of.....shares of Rs.... each at a premium of Rs....each for the purpose of redemption of preference shares as per Board's Resolution No.....dated.....)

-
- 3. When new shares are issued at a discount

Bank Account Dr.

Discount on Issue of Shares Account Dr.

To Share Capital Account

(Being the issue ofshares of Rs.....each at a discount of Rs..... each for the purpose of redemption of preference shares, as per Board's Resolution No...dated.....)

-
- 4. When preference shares are redeemed at par

Redeemable Preference Share Capital Account Dr.

To Preference Shareholders Account

- 5. When preference shares are redeemed at a premium

Redeemable Preference Share Capital Account Dr.

Premium on Redemption of Preference Shares Account Dr.

To Preference Shareholder Account

-
- 6. When payment is made to preference shareholders

Preference Shareholders Account Dr.

To Bank Account

- 7. For adjustment of premium on redemption

Profit and Loss Account Dr.

Securities Premium Account Dr.

To Premium on Redemption of Preference Shares Account

Illustration 1

Hinduja Company Ltd. had 5,000 8% Redeemable Preference Shares of Rs. 100 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of Rs. 10 each fully up at par. You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of Hinduja Company Ltd. Journal

Date	Particulars	Dr. (Rs.)	Cr. (Rs.)
	Bank A/c Dr. To Equity Share Capital A/c (Being the issue of 50,000 Equity Shares of Rs. 10 each at par for the purpose of redemption of preference shares, as per Board Resolution No....dated....)	5,00,000	5,00,000

8% Redeemable Preference Share Capital A/c Dr.	5,00,000	
To Preference Shareholders A/c (Being the amount payable on redemption of preference shares transferred to Preference Shareholders Account)		5,00,000
<hr/> Preference Shareholders A/c Dr.	5,00,000	
To Bank A/c (Being the amount paid on redemption of preference shares)		5,00,000
<hr/>		

Illustration 3

G India Ltd. had 9,000 10% redeemable Preference Shares of Rs. 10 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of Rs. 10 each fully paid up at a discount of 10%.

You are required to pass necessary Journal Entries including cash transactions in the books of the company.

Solution

In the books of G India Limited Journal

Date	Particulars	Dr. (Rs.)	Cr. (Rs.)
	Bank A/c Dr.	90,000	
	Discount on Issue of Shares A/c Dr.	10,000	
	To Equity Share Capital A/c		1,00,000
	(Being the issue of 10,000 Equity Shares of Rs.10 each at a discount of 10%, as per Board's Resolution No..... Dated.....)		

10% Redeemable Preference Shares Capital A/c	Dr.	90,000	
To Preference Shareholders A/c			90,000
(Being the amount payable on redemption of preference shares transferred to Preference shareholders A/c)			
<hr/>			
Preference Shareholders A/c	Dr.	90,000	
To Bank A/c			90,000
(Being the amount paid on redemption of preference shares)			
<hr/>			

Note

When shares are redeemed by issuing shares at a discount, the proceeds from new issue must be sufficient to cover the face value of shares redeemed. Here, face value of shares to be redeemed is Rs. 90,000. Proceeds from each new share is Rs. 9 (Rs.10 – 10 x 10% discount). Therefore, the number of new shares to be issued = $\text{Rs. } 90,000 / \text{Rs. } 9 = 10,000$ shares.

Illustration 6

The Balance Sheet of XYZ as at 31st December, 2005 *inter alia* includes the following:

	Rs.
50,000, 8% Preference Shares of Rs.100 each, Rs. 70 paid up	35,00,000
1,00,000 Equity Shares of Rs. 100 each fully paid up	1,00,000
Securities Premium	5,00,000

Capital Redemption Reserve	20,00,000
General Reserve	50,00,000

Under the terms of their issue, the preference shares are redeemable on 31st March, 2006 at 5% premium. In order to finance the redemption, the company makes a rights issue of 50,000 equity shares of Rs. 100 each at Rs. 110 per share, Rs. 20 being payable on application, Rs. 35 (including premium) on allotment and the balance on 1st January, 2007. The issue was fully subscribed and

Allotment made on 1st March, 2006. The money due on allotment were received by 31st March, 2006. The preference shares were redeemed after fulfilling the necessary conditions of Section 80 of the Companies Act, 1956. The company decided to make minimum utilisation of general reserve.

You are asked to pass the necessary Journal Entries and show the relevant extracts from the balance sheet as on 31st March, 2006 with the corresponding figures as on 31st December, 2005.

Solution

Journal

		Rs.	Rs.
8% Preference Share Final Call A/c To 8% Preference Share Capital A/c (For final call made on preference shares @ Rs. 30 each to make them fully paid up)	Dr.	15,00,000	15,00,000

Bank A/c To 8% Preference Share Final Call A/c (For receipt of final call money on preference shares)	Dr.	15,00,000	15,00,000
Bank A/c To Equity Share Application A/c (For receipt of application money on 50,000 equity shares @ Rs. 20 per share)	Dr.	10,00,000	10,00,000

Equity Share Application A/c To Equity Share Capital A/c (For capitalisation of application money received)	Dr.	10,00,000	10,00,000
Equity Share Allotment A/c To Equity Share Capital A/c To Securities Premium A/c (For allotment money due on 50,000 equity shares @ Rs. 35 per share including premium of Rs. 10 per share)	Dr.	17,50,000	12,50,000 5,00,000

Bank A/c	Dr.	17,50,000	
To Equity Share Allotment A/c (For receipt of allotment money on equity shares)			17,50,000
<hr/>			
8% Preferences Share Capital A/c	Dr.	50,00,000	
Premium on Redemption of Preference Share A/c	Dr.	2,50,000	
To Preference Shareholders A/c (For amount payable to preference shareholders on redemption at 5% premium)			52,50,000
<hr/>			

Securities Premium A/c To Premium on Redemption A/c (For writing off premium on redemption of preference shares)	Dr.	2,50,000	2,50,000
<hr/> General Reserve A/c To Capital Redemption Reserve A/c (For transfer of CRR the amount not covered by the proceeds of fresh issue of equity shares i.e., 50,00,000 – 10,00,000 – 12,50,000)	Dr.	27,50,000	27,50,000

Preference Shareholders A/c To Bank A/c (For amount paid to preference shareholders)	Dr.	52,50,000	52,50,000
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Balance Sheet (extracts)

	As at 31.3.2006	As at 31.3.2005
<i>Share Capital:</i>		
Issued, Subscribed and Paid up:		
1,00,000 Equity Shares of Rs. 100 each fully paid up	1,00,000	1,00,000

50,000 Equity Shares of Rs. 100 each Rs. 45 paid up	22,50,000	-
50,000 8% Preference Shares of Rs. 100 each, Rs. 70 called up	-	35,00,000
<i>Reserves and Surplus:</i>		
Capital Redemption Reserve	47,50,000	20,00,000
Securities Premium	7,50,000	5,00,000
General Reserve	22,50,000	50,00,000

Note

Amount received (excluding premium) on fresh issue of shares till the date of redemption should be considered for calculation of proceeds of fresh issue of shares. Thus, proceeds of fresh issue of shares are Rs. 22,50,000 (Rs. 10,00,000) application money plus Rs. 12,50,000 received on allotment towards share capital).

Thank You

- [YouTube.com/abbasvattoli](https://www.youtube.com/abbasvattoli)