



What are Debentures?

Debenture is a written instrument acknowledging a debt under the common seal of the company. It is derived from a Latin word called 'Debere' which means to borrow.

Difference between Shares and Debentures

The differences between shares and debentures are as follows:

Shares	Debentures
Share is a representation of ownership in a company. It is a part of owned capital.	Debentures are acknowledgement of debts. It is a part of borrowed capital.
The return on shares is called dividend	The return on debentures is called interest
They are not returned during the life cycle of the company	They are repaid on expiry of the time period, since they come with a deadline
Shareholders enjoy voting rights	Debenture holders do not enjoy voting rights
They cannot be converted into debentures	They can be converted into shares

Types of Debentures

1. From the point of view of Security

a. Secured Debentures- Those debentures where a charge is created on the assets of the company for the purpose of payment in case of default are called secured debentures.

b. Unsecured Debentures- They do not have a specific charge on the assets of the company

2. From the point of view of Tenure

a. Redeemable Debentures- Those debentures which are payable on the expiry of the specific period either in lump sum or in installments during the life time of the company

b. Irredeemable Debentures- These debentures are repayable on the winding-up of a company or on the expiry of a long period

3. From the point of view of Convertibility

a. Convertible Debentures- Debentures which are convertible into equity shares or in any other security either at the option of the company or the debenture holders are called convertible debenture.

b. Non-Convertible Debentures- The debentures which cannot be converted into shares or in any other securities are called non-convertible debentures.

4. From Coupon Rate Point of View

a. Specific Coupon Rate Debentures- These debentures are issued with a specified rate of interest, which is called the coupon rate.

b. Zero Coupon Rate Debentures- These debentures do not carry a specific rate of interest. In order to compensate the investors, such debentures are issued at substantial discount and the difference between the nominal value and the issue price is treated as the amount of interest related to the duration of the debentures.

5. From the point of view of Registration

a. Registered Debentures- Those debentures in respect of which all details including names, addresses and particulars of holding of the debenture holders are entered in a register kept by the company.

b. Bearer Debentures- The debentures which can be transferred by way of delivery and the company does not keep any record of the debentures are called bearer debentures.

Issue of Debentures

● Issue of Debentures for Cash

A. If whole amount is received in one installment

- (i) On receipt of the application money
Bank A/c Dr.
To Debenture Application & Allotment A/c
- (ii) On Allotment of debentures
Debenture Application & Allotment A/c Dr.
To Debentures A/c

B. If debenture amount is received in two installments

- (i) On receipt of application money
Bank A/c Dr.
To Debenture Application A/c
- (ii) For adjustment of applications money on allotment
Debenture Application A/c Dr.
To Debentures A/c
- (iii) For allotment money due
Debenture Allotment A/c Dr.
To Debentures A/c
- (iv) On receipt of allotment money
Bank A/c Dr.
To Debenture Allotment A/c

C. If debenture money is received in more than two installments Additional entries

- (i) On making the first call
Debenture First Call A/c Dr.
To Debentures A/c
- (ii) On the receipt of the first call
Bank A/c Dr.
To Debenture First Call A/c

- **Issue of Debentures at a discount-** When a debenture is issued at a price below its nominal value, it is said to be issued at a discount.
- **Debentures Issued at Premium-** A debenture is said to be issued at a premium when the price charged is more than its nominal value.

Over Subscription

When the number of debentures applied for is more than the number of debentures offered to the public, the issue is said to be over subscribed.

Issue of Debentures for Consideration Other than Cash

Sometimes a company purchased assets from vendors and instead of making payment in cash issues debentures for consideration thereof.

1. On purchase of assets

Sundry Assets A/c Dr.
To Vendor's

2. On issue of debentures

- (a) At par
Vendors Dr.
To Debentures A/c
- (b) At premium
Vendors Dr.
To Debentures A/c
To Securities Premium Reserve A/c
- (c) At a discount
Vendors Dr.
Discount on Issue of Debenture A/c Dr.
To Debentures A/c

Issue of Debentures as a Collateral Security

A collateral security may be defined as a subsidiary or secondary or additional security besides the primary security when a company obtains a loan or overdraft from a bank or any other financial Institution. Debentures issued as collateral security can be dealt within two ways in the books of the company:

First Method- No entry is made in the books of accounts since no liability is created by such issue. However, on the liability side of the balance sheet, below the item of loan, a note to the effect that it has been secured by issue of debentures as a collateral security is appended.

Second Method- The issue of debentures as a collateral security may be recorded by means of journal entry as follows:

- i. *Issue of 10,000, 9% debentures of Rs. 100 each as collateral security for bank loan of Rs. 10,00,000.*

Debenture Suspense A/c	Dr.	10,00,000	
To 9% Debentures A/c			10,00,000

- ii. *For cancellation of 9% debentures as collateral security on repayment of bank loan.*

Terms of Issue of Debentures

The following are the terms of Issue of Debentures to be followed:

(i) Issued at par and redeemable at par

- (a) Bank A/c Dr.
To Debenture Application & Allotment A/c
(Receipt of application money)
- (b) Debenture Application & Allotment A/c Dr.
To Debentures A/c
(Allotment of debentures)

(ii) Issued at discount and redeemable at par

- (a) Bank A/c Dr.
To Debenture Application & Allotment A/c
(Receipt of application money)
- (b) Debenture Application & Allotment A/c Dr.
Discount on Issue of Debentures A/c Dr.
To Debentures A/c
(Allotment of debentures at a discount)

(iii) Issued at a premium and redeemable at par

- (a) Bank A/c Dr.
To Debenture Application & Allotment A/c
(Receipt of application money)
- (b) Debenture Application & Allotment A/c Dr.
To Debentures A/c
To Securities Premium Reserve A/c
(Allotment of debentures at a premium)

(iv) Issued at par and redeemable at a premium

(a) Bank A/c	Dr.
To Debenture Application & Allotment A/c	
(Receipt of application money)	
(b) Debenture Application & Allotment A/c	Dr.
Loss on Issue of Debentures A/c	Dr. (with premium on redemption)
To Debentures A/c	(with nominal value of debenture)
To Premium on Redemption of Debenture A/c	(with premium on redemption)
(Allotment of debentures at par and <u>redeemed</u> at a premium)	

(v) Issued at a discount and redeemable at a premium

Bank A/c	Dr.
To Debenture Application & Allotment A/c	
(Receipt of application money)	
Debenture Application & Allotment A/c	Dr.
Loss on Issue of Debentures A/c	Dr. (with discount on issue plus premium on redemption)
To Debentures A/c	(with nominal value of debenture)
To Premium on Redemption of Debentures A/c	(with premium on redemption)
(Allotment of debentures at a discount and redeemable at premium)	

(vi) Issued at a premium and redeemable at a premium

Bank A/c	Dr.
To Debenture Application & Allotment A/c	
(Receipt of application money)	
Debenture Application & Allotment A/c	Dr.
Loss on Issue of Debentures A/c	Dr. (with premium on redemption)
To Debentures A/c	(with nominal value of debenture)
To Securities Premium Reserve A/c	(with premium on issue)
To Premium on Redemption of Debentures A/c	(with premium on redemption)

Interest on Debentures

Interest on debenture is a charge against the profit of the company and must be paid whether the company has earned any profit or not. The following journal entries are made in the books of the company under various circumstances:

- When interest is due*

Debenture Interest A/c	Dr.
To Income Tax payable A/c	
To Debenture holders A/c	

(Amount of interest due on debenture and tax deducted at source)
- For payment of interest to debenture holders*

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

(Amount of interest paid to debenture holders)
- On transfer debenture Interest Account to statement of Profit and Loss*

Statement of Profit and Loss	Dr.
To Debenture Interest A/c	

(Debenture interest transferred to profit and loss A/c)
- On payment of tax deducted at source to the Government*

Income Tax Payable A/c	Dr.
To Bank A/c	

(Payment of tax deducted at source on interest on debentures)

Writing Off Discount/Loss on Issue of Debentures

Discount or loss can be written-off from securities premium reserve.
 Securities Premium Reserve A/c Dr. [If exists to the extent of balance]
 Statement of Profit and Loss Dr.

To Discount/Loss on Issue of Debentures A/c
 (Discount/Loss on issue of debentures written-off)

Redemption of Debentures

The following are the methods of redemption of debentures:

- **Payment in lump sum-** The company redeems the debentures by paying the amount in lump sum to the debenture holders at the maturity based on the terms of issue. The following journal entries are made in this case:

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.
 Premium on Redemption of Debentures A/c Dr.
 To Debenture holders

Debenture holders Dr.
 To Bank A/c

- **Payment in installments-** The redemption of debentures is made in installments on the specified date during the tenure of the debentures. The journal entries in this case is as follows:

- (a) Debentures A/c Dr.
 To Debenture holders A/c
- (b) Debenture holders A/c Dr.
 To Bank A/c

- **Purchase in the open market-** An act of purchasing and cancelling the debentures constitutes redemption of debentures by purchase in the open market.

a) 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
 Debentures A/c Dr.
 To Bank A/c
 To Profit on Redemption of Debentures A/c
- 2. On transfer of Profit on Redemption
 Profit on Redemption of Debenture A/c Dr.
 To Capital Reserve

b) If 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

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