

Chapter 11: Company Accounts Part - 2 (Accounting for Debentures)

Question: 1

Answer in a sentence only.
What is meant by debenture?

Solution

Debentures are debt funds issued in the form of certificate under the common seal of a company. The certificate contains the details about rate of interest for the specified period, repayment of principle and the schedule of interest payments.

Question: 2

Answer in a sentence only.
What do you mean by Bearer Debenture?

Solution

Debentures that are transferable by mere delivery are known as bearer debentures. The name and address of the holder of a bearer debenture is not registered with the company. Interest on such debentures is paid only to those holders who produce interest coupons attached with these debentures.

Question: 3

Answer in a sentence only.
What is meant by 'Issue' of debentures for consideration other than cash?

Solution

Debentures can be issued for cash or for consideration other than cash. When debentures are issued to the vendors for purchase of assets, it is known as 'issue of debentures for consideration other than cash'. In other words, vendors are issued debentures for the amount due rather than making payment in cash. Such an issue can be made at a discount, at par or at a premium.

Question: 4

Answer in a sentence only.
What is meant by 'Issue of debenture at discount and redeemable at premium'?

Solution

When debentures are issued at a price below their face value, it is known as 'issue of debentures at discount'. 'Redemption of debentures at premium' implies that such debentures will be paid off a redemption price that is more than its face value. For example, a debenture with face value of Rs 10, issued at Rs 9 (issued at discount of Re 1) and redeemable at Rs 12 (redeemed at a premium of Rs 2).

Question: 5

Answer in a sentence only.
What is a 'Convertible Debenture'?

Solution

Those debentures that have an option/right to get converted into shares (either preference share or equity share) after a specified period are known as convertible debentures.

Question: 6

Answer in a sentence only.
What is meant by 'Mortgaged Debenture'?

Solution

The debentures that are secured by creating a charge on the assets of a company are known as mortgage debentures. Therefore, they are also known as secured debentures. The charge on the assets can be fixed, i.e. on some particular asset of the company or floating, i.e. on all the assets of the company in general.

Question: 7

Answer in a sentence only.
What is meant by redemption of Debentures?

Solution

Repayment of the principal amount of debentures is known as redemption of debentures. It can be at a premium, discount or par. The conditions about redemption are stipulated at the time of issue of debentures. That is, whether redemption is to be made at a price above its face value (at a premium), or at par, i.e. at face value, or at a price below the face value (i.e. redemption at discount) is decided at the time of issue of the debentures.

Question: 8

Answer in a sentence only.

What is meant by 'Premium on Redemption of debentures'?

Solution

When the debentures are repaid by paying a price that is more than their face value it is known as 'redemption of debentures at a premium'.

Question: 9

Answer in a sentence only.

What is meant by 'Irredeemable Debentures'?

Solution

Debentures that are not redeemable during the life time of a company are known as irredeemable debentures. Therefore, these are also known as perpetual debentures.

Question: 10

Answer in a sentence only.

What do you mean by 'Debenture Interest'?

Solution

Debenture interest is a charge against a company's profit, as it is an expense for the company. It can be paid monthly, quarterly or yearly, as defined in the terms and conditions of the issue.

Question: 11

Write one word/term/phrase which can substitute the following
The debentures where a charge is created on the assets of company.

Solution

Secured debentures

Explanation: Secured debentures are guarded by a charge on the company's assets. The charge can be fixed or floating. Fixed charge means that they are secured by a particular asset of the company and floating charge means that they are secured by all the assets of the company in general.

Question: 12

Write one word/term/phrase which can substitute the following
The debentures where no charge is created on the assets of company.

Solution

Unsecured debentures

Explanation: Debentures that are not secured by any security or do not have a charge on the assets are known as unsecured or naked debentures.

Question: 13

Write one word/term/phrase which can substitute the following
The acknowledgment of debt under common seal of company.

Solution

Debenture

Explanation: Debentures are debt funds issued in the form of certificates under the common seal of the company. The certificates contain the details about rate of interest for the specified period, repayment of principal and the schedule of interest payments.

Question: 14

Write one word/term/phrase which can substitute the following
The debentures of which payment is made on the expiry of specific period.

Solution

Redeemable debentures

Explanation: The debentures that are to be paid back after a specified period of time, as per the terms of the issue, are known as redeemable debentures. They can only be redeemed after the expiry of a specified period.

Question: 15

Write one word/term/phrase which can substitute the following
The debentures of which the payment is not made until the winding up of company.

Solution

Irredeemable debentures

Explanation: Debentures that are not redeemable during the life time of a company are known as irredeemable debentures. These are also known as perpetual debentures.

Question: 16

Write one word/term/phrase which can substitute the following
The debentures which are converted in to shares.

Solution**Convertible debentures**

Explanation: Debentures that have an option/right to be converted into shares (either preference or equity shares) after a specified time period are known as convertible debentures.

Question: 17

Write one word/term/phrase which can substitute the following
The debentures which are not converted into shares.

Solution**Non-Convertible debentures**

Explanation: Debentures that do not carry the option/right to be converted into equity shares after the specified period of time are known as non-convertible debentures.

Question: 18

Write one word/term/phrase which can substitute the following
The debentures which are registered in the register of company.

Solution**Registered debentures**

Explanation: Debentures that are not transferable by mere delivery are known as registered debentures. The names and addresses of holders of these debentures are recorded with the company. Such debentures can be transferred only through the execution of a proper transfer deed.

Question: 19

Write one word/term/phrase which can substitute the following
The debentures which are transferred by way of delivery.

Solution**Bearer debentures**

Explanation: Debentures that are transferable by mere delivery are

known as bearer debentures. The names and addresses of the holders of such debentures are not registered with the company. Interest on these debentures is paid only to those holders who produce interest coupons attached with such debentures.

Question: 20

Write one word/term/phrase which can substitute the following
The issue of debentures more than face value of debentures

Solution

Issue of debentures at premium

Explanation: When debentures are issued at a price more than their face value, it is known as 'issue of debentures at premium'. For example, when a debenture of face value Rs 10 is issued at Rs 12, it is issued at a premium of Rs 2. The premium is credited to Securities Premium Account.

Question: 21

Select most appropriate alternative from those given below

_____ is acknowledgment of debt under common seal of company.

Options

- Share
- Debenture
- Cheque
- Bond

Solution

Debenture is acknowledgment of debt under common seal of company.

Explanation: Debentures are written acknowledgement of debt issued under the common seal of a company with fixed rate of interest to the debenture holders.

Question: 22

Select most appropriate alternative from those given below :

The issue of debenture at its face value is called the issue _____.

Options

- at par
- at discount
- at premium
- none of these

Solution

The issue of debenture at its face value is called the issue **at par**.

Explanation: When debentures are issued at their face value, it is known as 'issue at par'. In this case, issue price is equal to face value.

Question: 23

Select most appropriate alternative from those given below
 _____ debentures which are recorded in register of company.

Options

- Simple debentures
- Registered debentures
- Bearer debentures
- Open debentures

Solution

Registered debentures which are recorded in register of company.

Explanation: Those debentures for which the names and addresses of the debenture holders are recorded in a company's register are known as registered debentures. Such debentures are not transferable by mere delivery.

Question: 24

Select most appropriate alternative from those given below :

The issue of debentures less than the face value is called _____.

Options

- at par
- at premium

- at discount
- none of these

Solution

The issue of debentures less than the face value is called **at discount**.

Explanation: When debentures are issued at a price below their face value, it is known as 'issue of debentures at discount'. Such discount is debited to Discount on Issue of Debentures Account.

Question: 25

Select most appropriate alternative from those given below :

The debentures which are converted into shares is called_____.

Options

- converted debentures
- non-convertible debenture
- bearer debentures
- unsecured debentures

Solution

The debentures which are converted into shares is called **converted debentures**.

Explanation: The debentures that are issued with an option of being converted into equity shares or preference shares after the expiry of a certain specified period are known as convertible debentures.

Question: 26

Select most appropriate alternative from those given below :

The issue of debentures more than face value is called_____.

Options

- at par
- at discount
- at premium

- none of these

Solution

The issue of debentures more than face value is called **at premium**.

Explanation: When debentures are issued at a price more than their face value, it is known as 'issue of debentures at a premium'. Such a premium is credited to the Securities Premium Account.

Question: 27

Select most appropriate alternative from those given below :

_____ debentures of which the amount is repaid within specific period.

Options

- Redeemable
- Irredeemable
- Secured
- Non convertible

Solution

Redeemable debentures of which the amount is repaid within specific period.

Explanation: Debentures, on which the amount is to be paid back after a specified period of time, as per the terms of the issue, are known as redeemable debentures. They can only be redeemed after the expiry of a specified time period.

Question: 28

Select most appropriate alternative from those given below :

_____ debentures which are not secured against any charge on asset of the company.

Options

- Secured
- Unsecured

- Redeemable
- Convertible

Solution

Unsecured debentures which are not secured against any charge on asset of the company.

Explanation: The debentures that are not secured by any security or do not have a charge on the assets of a company are known as unsecured or naked debentures.

Question: 29

Select most appropriate alternative from those given below :

The interest on debentures is transferred to _____.

Options

- Debentures A/c
- Profit of Loss A/c
- Balance Sheet
- Debenture holders A/c

Solution

The interest on debentures is transferred to **Profit and Loss A/c**.

Explanation: Interest on debentures is an expense for a company. Debenture-holders are the creditors of the company and are paid a fixed rate of interest every year till redemption. Therefore, the interest expense is a charge against the profits and is debited to the Profit and Loss Account.

Question: 30

Select most appropriate alternative from those given below :

The debenture holder is _____ of the company.

Options

- debtor
- creditor

- owner
- supplier

Solution

The debenture holder is **creditor** of the company.

Explanation: Debentures are debt funds issued under the common seal of a company. These are issued for a specified period of time with a fixed rate of interest. Debenture-holders are regarded as the creditors of the company, as they have lent the amount to the company as a loan.

Question: 31

State to whether the following statement is True/False.

The debenture holder is owner of the company.

Options

- True
- False

Solution

False

Explanation: Debenture-holders are the creditors of a company. They get interest at a fixed rate, irrespective of whether the company makes profit or not. Unlike shareholders, they are not the owners of the company.

Question: 32

State to whether the following statement is True/False.

The acknowledgement of debt under common seal of company is termed as share.

Options

- True
- False

Solution

False

Explanation: The acknowledgement of debt under the common seal of a company is termed as debenture. Debentures carry a fixed rate of interest that is a charge against company profits. Debentures are paid back after the expiry of the specified term for which they were issued.

Question: 33

State to whether the following statement is True/False.

The amount of irredeemable debentures is not paid in the life time of the company.

Options

- True
- False

Solution

True

Explanation: Irredeemable debentures are not payable during the life time of a company. They are also known as perpetual debentures. They are paid only at the time of liquidation or in the event of winding up of the company.

Question: 34

State to whether the following statement is True/False.

The issue of debentures less than face value of debenture to termed as issue of debentures at discount.

Options

- True
- False

Solution

True

Explanation: When debentures are issued at a price less than their face value, it is known as 'issue of debentures at discount'.

Question: 35

State to whether the following statement is True/False.

The debentures are known as creditors ship capital of the company.

Options

- True
- False

Solution

True

Explanation: Debentures are debt instruments issued under the common seal of a company to its debenture holders. They are regarded as the creditors of the company as against the owners who are the 'equity shareholders'. Capital financed through debentures is known as debt capital or creditors' share capital of the company.

Question: 36

State to whether the following statement is True/False.

The unregistered debentures are known as naked debentures.

Options

- True
- False

Solution

True

Explanation: Unregistered debentures are also known as naked or bearer debentures. Such debentures are issued without any security, i.e. they do not have a charge on the assets of a company.

Question: 37

State to whether the following statement is True/False.

The rate of interest on debentures is attached to the debenture

Options

- True
- False

Solution

True

Explanation: Debentures are issued at a fixed rate of interest with payment of interest at regular intervals. However, repayment of principal amount is made only after the expiry of a specified period.

Question: 38

State to whether the following statement is True/False.

Unsecured debentures are safer than secured debentures.

Options

- True
- False

Solution

False

Explanation: Unsecured debentures are issued without any security or charge, whereas secured debentures are issued with security or charge (floating or fixed) on the assets of a company. Therefore, secured debentures are more secure because if a company defaults in paying interest, the debenture-holders may sell off the assets in order to recover their dues.

Question: 39

State to whether the following statement is True/False.

The issue of debenture more than face value is termed on issue of debentures at par.

Options

- True
- False

Solution

False

Explanation: Issue of debentures at a price more than their face value is

known as 'issue of debentures at a premium'. The amount of a premium so received is credited to the Securities Premium Account.

Question: 40

State to whether the following statement is True/False.

Premium on issue of debentures is recorded on the asset side of balance sheet.

Options

- True
- False

Solution

False

Explanation: The premium received on the issue of debentures represents the excess amount received over and above the face value of the debentures. It is a capital gain for the company. Therefore, it is shown on the Liabilities side of the Balance Sheet under the head "Reserves & Surplus".

Question: 41

Amar Ltd. issued 10,000 12% Debentures of Rs 100 each payable Rs 30 on application and remaining amount on allotment. The public applied for Rs 9,000 debentures which were fully allotted and on the relevant allotment money duly received. Give journal entries in the books of Amar Ltd.

Solution

Book of Aman Ltd.

Journal Entry

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Bank A/c Dr. To Debenture Application A/c (Debenture application received on 9,000, 12% Debentures of Rs 30 each)		270,000	270,000
	Debenture Application A/c Dr.		270,000	270,000

	To 12% Debentures A/c (Debenture application money transferred to 12% Debenture A/c)			
	Debenture Allotment A/c Dr. To 12% Debentures A/c (Debenture allotment due on 9,000 12% Debenture of Rs 70 each)		630,000	630,000
	Bank A/c Dr. To Debenture Allotment A/c (Debenture allotment money received)		630,000	630,000

Question: 42

Tanagi Ltd. issued Rs 10,000 12% debentures of Rs 100 each at a discount of 5% Payable as follows:

On Application Rs 40

On Allotment Rs 55

Show journal entries assuming that all the installments were duly collected. Also show the relevant portion of the balance sheet.

Solution

Books of Tanagi Ltd.

Journal Entry

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Bank A/c Dr. To Debenture Application A/c (Debenture application received on 10,000 12% Debentures of Rs 40 each)		400,000	400,000
	Debenture Application A/c Dr. To 12% Debentures A/c (Debenture application money transferred to 12% Debenture A/c)		400,000	400,000
	Debenture Allotment A/c Dr. Discount on Issue of Debentures		550,000 50,000	600,000

	To 12% Debentures A/c (Debenture Allotment due on 10,000 12% Debenture of Rs 55 each, issued @ discount of 5%)			
	Bank A/c To Debenture Allotment A/c (Debenture Allotment received on 10,000, 12% Debentures of Rs 55 each)	Dr.	550,000	550,000

Balance Sheet of Tanaji Ltd.

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
<u>Secured loans :</u> 12% Debentures	10,00,000	Cash at Bank	9,50,000
		<u>Miscellaneous Exp. - Discount on Issue of Debentures</u>	50,000
	10,00,000		10,00,000

Working Notes :

Face value of Debenture = Rs. 100

Discount (100 x 5%) = Rs. 5

∴ Issue Price = Rs.95

Question: 43

Archana Ltd. issued 2,000 10% Debentures of Rs 100 each at a premium of Rs 10 per Debenture payable as follows:

On Application : Rs. 50

On Allotment : Rs. 60 (Premium included Rs. 10)

The Debentures were fully subscribed and all money was duly received.

Pass Journal entries and show how the amounts appear in Balance Sheet.

Solution

Books of Archana Ltd.

Journal Entry

Date	Particulars	L.F.	Debit Amount	Credit Amount
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			(Rs.)	(Rs.)
	Bank A/c To Debenture Application A/c (Debenture application money received on 2,000, 10% Debentures of Rs 50 each)	Dr.	100,000	100,000
	Debenture Application A/c To 10% Debentures A/c (Debenture application money transferred to 10% Debenture A/c)	Dr.	100,000	100,000
	Debenture Allotment A/c To 10% Debentures A/c To Securities Premium A/c (Debenture allotment due on 2,000 shares of Rs 60 each including premium of Rs 10 each)	Dr.	120,000	100,000 20,000
	Bank A/c To Debenture Allotment A/c (Debenture allotment money received)	Dr.	120,000	120,000

Balance Sheet of Archana Ltd.

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
<u>Reserves and Surplus</u> Securities Premium	20,000	Cash at bank	220,000
<u>Secured Loan</u> 10% Debentures	200,000		
	220,000		220,000

Working Note:

Face value of a Debenture = Rs. 100

Securities Premium = Rs.10

∴ Issue Price = Rs. 110.

Note : As per the textbook solution 2,500, 10% Debentures were issued but according to the question 2,000, 10% Debentures were issued. Therefore, our solution is as per the information provided in the question.

Question: 44

Amar Ltd. purchased assets of the book value of Rs 99,000 from Abhi Ltd. It was agreed that purchase consideration to be paid by issuing 11% Debentures of Rs 100 each Assume debentures have been issued.

1. At par
 2. At Discount of 10% and
 3. At Premium of 10%
- Record necessary journal entries

Solution**Books of Amar Ltd.****Journal Entry**

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Sundry Assets A/c Dr. To Abhi Ltd. (Assets purchased from Abhi Ltd.)		99,000	99,000
	On Issue of Debentures at Par Abhi Ltd. Dr. To 11% Debentures A/c (990, 11% Debentures issued @ Rs 100 each for purchases consideration of Rs 100 each)		99,000	99,000
	On Issue of Debenture @ 10% Discount Abhi Ltd. Dr. Discount on Issue of Debentures A/c Dr. To 11% Debentures A/c (1,100, 11% Debentures issued @ Rs 100 each (including discount of 10%) for purchase consideration of Rs 99,000)		99,000 11,000	110,000
	On Issue of Debentures at Premium of 10% Abhi Ltd. Dr. To 11% Debentures A/c To Securities Premium A/c (900, 11% Debentures issued @ Rs 110 (including premium of 10%) for purchase consideration of Rs 99,000)		99,000	90,000 9,000

Working Notes:

WN1: Calculation of Number of Debentures, when Debentures issued at Discount of 10%

Number of Debentures Issued

= Amount Payable/(Face Value - Discount) Per Debenture

= $99,000/100 - 10(100 \times 10\%)$

= 1100 Debentures.

WN2: Calculation of Number of Debentures, when Debentures issued at Premium of 10%

Number of Debentures Issued

= Amount Payable/(Face Value + Premium) Per Debenture

= $99,000/100 + 10(100 \times 10\%)$

= 900 Debentures.

Question: 45

Dinesh Ltd. Issued 10,00,000 6% Debentures on 1st April, 2010. Interest is paid on 30 sept., 2010 and 31st March, 2011.

Record necessary journal entries assuming that income tax is deducted at 30% of the amount of interest.

Solution

Books of Dinesh Ltd.

Journal Entry

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
2010 Apr.01	Bank A/c Dr. To Debenture Application and Allotment A/c (Debenture application and Allotment received on 10,000 6% Debentures of Rs 100 each)		10,00,000	10,00,000
Apr.01	Debenture Application and Allotment A/c Dr. To 6% Debentures A/c (Debenture application and		10,00,000	10,00,000

	allotment transferred to 6% Debenture A/c)			
Sept.30	Debenture Interest A/c Dr. To Income Tax Payable A/c To Debentureholders A/c (Amount of interest due on debenture and TDS)		30,000	9,000 21,000
Sept.30	Debentureholders A/c Dr To Bank A/c (Interest paid to Debenture holder)		21,000	21,000
2011 Mar.31	Debenture Interest A/c Dr. To Income Tax Payable A/c To Debentureholders A/c (Amount due on Debenture and TDS)		30,000	9,000 21,000
Mar.31	Debentureholders A/c Dr. To Bank A/c (Interest paid to Debenture Holder)		21,000	21,000
Mar.31	Income Tax Payable A/c Dr. To Bank A/c (Income Tax paid)		18,000	18,000
Mar.31	Profit and Loss A/c Dr. To Debenture Interest A/c (Interest on Debenture transferred to Profit and Loss A/c)		60,000	60,000